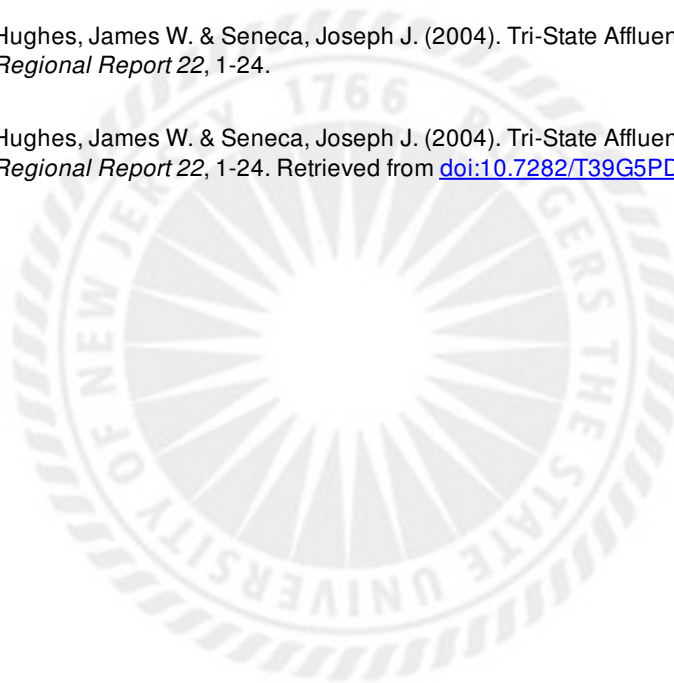


## Tri-State Affluence: Losing by Winning

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# Rutgers

## Regional Report

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### **Tri-State Affluence: Losing by Winning**

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If the states of Connecticut, New Jersey, and New York seceded from the United States and became a separate nation, they would likely form the wealthiest nation on earth, challenged only by Luxembourg.<sup>1</sup> (Perhaps this new principality could be called “New Yoconsey,” an amalgamation derived from selected extracts of New York, Connecticut, and New Jersey.) The three states encompass not only one of the greatest concentrations of affluence in America but of global wealth as well. Moreover, this tri-state affluence actually has an even smaller geographic footprint and is centered in a cluster of wealthy counties in the metropolitan region surrounding and including New York City.

But affluence brings with it burdens and consequences as well, particularly if a region is part of a large nation that is, in general, less well economically endowed. Given the progressive nature of federal and state income tax systems, the three states and their highest-income counties are critical pillars for federal and state budgets. Consequently, there are disproportional flows of income tax dollars out of affluent jurisdictions. Connecticut, New Jersey, and New York serve as significant “cash cows,” providing disproportional shares of federal tax revenues to support federal spending. Similarly, in addition to their disproportionate support of federal spending, the affluent counties of the region also serve as “cash calves” for their respective states’ spending.

But this is a mixed blessing for the state and local governments receiving this largesse because when income growth falters, the tax revenue generation process also works in reverse. Recent income volatility in New York City—stemming from overdependence on cyclical Wall Street—generated income—and in New Jersey, where income growth sagged badly in its affluent counties during the 2000–02 post-bubble economy—contributed significantly to revenue shortfalls and ongoing fiscal stress.

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<sup>1</sup> This estimation is based on the use of purchasing power parities (PPI) instead of exchange rates in order to consistently reflect the real differences between nations. See Organization for Economic Cooperation and Development, “National Accounts of OECD Countries” (Paris, France), annual.

## Executive Summary

Connecticut, New Jersey, and New York serve as an income dynamo, a reality evident in a range of income statistics.

- In 2003, Connecticut’s per capita income ranked first among the 50 states (36 percent higher than that of the nation). New Jersey ranked second, while New York ranked fifth.
- Median household and median family income statistics present only slightly different rankings (New Jersey replaces Connecticut as number one) but produce the same conclusion. There is no other cluster of contiguous states in the country remotely comparable to the high-income position of the tri-state area. Moreover, the scale and depth of the affluence is also unparalleled.
- While the three states accounted for 10.8 percent of the nation’s total population in 2003, they had 13.1 percent of the nation’s total personal income. The tri-state area has not only proportionately more higher-income individuals but plenty of them! This agglomeration of income constitutes the most potent multistate consumer market in the country.

High levels of income have several important fiscal consequences that follow from a progressive federal income tax and expenditure system.

- The benefits of affluence are obvious, but there are consequences: The three states pay disproportionate shares of federal income and employment taxes. While the three states contained 10.8 percent of the nation’s population in 2003, they paid 15.1 percent of total federal individual income and employment taxes, the direct result of higher incomes and progressive federal income tax rates.

- If the federal income and employment tax payments of the three states were equivalent to their national population shares, significant sums would remain in their economies. In New Jersey, \$26 billion would have been retained in the state in 2003, an amount greater than the state's fiscal year 2003–04 budget! New York would have “saved” \$35.4 billion, while Connecticut would have retained \$11 billion.
- Thus, the tri-state area pays nearly 40 percent more in federal individual income and employment taxes compared to what its population share alone would indicate. Connecticut and New Jersey actually pay 50 percent more! While these tax “overages” support important public expenditures, they also represent a draining of fiscal resources that can have negative consequences for the individual state economies if federal expenditures in the region do not compensate for the region's disproportionate tax shares.
- Unfortunately, relatively low levels of federal expenditures in the region have led to persistent and significant “balance-of-payment deficits” with the federal government. New Jersey and Connecticut have consistently ranked fiftieth and forty-ninth, respectively, among the states in the ratio of federal spending to federal tax collections. Considerable income tax revenues flow out of the tri-state area and are dispersed throughout the country and beyond.
- To the degree that these streams of funds support important and effective federal programs, this progressive flow of resources from the region represents a *responsibility* of affluence. However, to the degree these funds are used for outright subsidies to various industrial sectors or inefficient transfers to other states and regions based not on economic merit but political heft, then the tri-state region's economy is weakened significantly.
- There is intense economic competition among the states. Affluence and a negative flow of federal funds translate into higher costs of doing business in Connecticut, New Jersey, and New York,

placing the region at a competitive disadvantage. The three states have an economic base that is the envy of the country. It is not surprising that other regions of the country, with the assistance of the federal “surpluses” they receive, are intensively attempting to create economic climates and supporting infrastructure to attract economic activity away from the tri-state region.

Affluence is not evenly distributed across the states' economic and demographic landscapes. Most of the high income is concentrated within the three states in eight counties in the metropolitan region centered around and including Manhattan. In 2002, all eight counties ranked in the top 20 counties nationally according to per capita income.

- Manhattan (New York County) had the highest per capita income of any county in the nation, a level 2.7 times higher than that of the United States. The other top 20 regional counties were Fairfield (6), Morris (7), Westchester (8), Somerset (11), Hunterdon (12), Bergen (15), and Nassau (18).
- Three diminutive nonmetropolitan counties outside the tri-state region ranked in the top five counties in the nation. If the rankings excluded these counties, the tri-state region would have six of the nine highest per capita income metropolitan counties in the United States, an unparalleled metropolitan concentration of income!

Another consequence of affluence is the variability of income tax revenues with respect to changes over the business cycle. Economic well-being, as measured by income, does not rise steadily year after year. Higher-income states, and particularly higher-income counties, tend to have greater volatility in income-growth patterns over the business cycle than the nation as a whole.

- For example, in the 1996–2000 period of strong national economic gains, income growth in the region's eight affluent counties significantly outperformed the nation. However, during the 2000–02 period of national economic weakness,

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income growth in these same counties significantly underperformed the nation, with two counties—Somerset and Manhattan—actually experiencing *declines* in both per capita and total personal income.

- In general, affluent areas disproportionately benefited in the boom/bubble years (1996–2000) and disproportionately suffered in the post-boom/bubble years (2000–02). It was this type of income boom–bust cycle that produced the income tax volatility that contributed to the recent and ongoing severe fiscal problems of New York City and New Jersey.

This volatile correlation between income and tax revenues has significant public policy ramifications. For example, in New Jersey, much attention has been focused on the overdependence on property taxes, but little concern has been raised more generally regarding the implications of sensitivity of income tax revenues to the business cycle.

- The boom years produced extraordinary income tax revenue growth that was quickly and *permanently* embedded in the New Jersey state budget. The cessation and reversal of that income growth—particularly in the state’s affluent counties—culminated in immediate and severe fiscal crisis.
- The subsequent structural deficit then led to increases in tax rates that have implications for long-term economic growth and the overall competitiveness of the state’s economy.

New Jersey’s dependence on the cyclically fluctuating income emanating from its affluent counties is paralleled by equivalent situations in New York and Connecticut. Thus, an examination of New Jersey’s pattern of revenue and expenditure flows among its regions and counties proves instructive.

- Just as the nation is highly dependent on Connecticut, New Jersey, and New York to produce income tax “surpluses,” so too is New Jersey dependent on six counties to do its income-

tax “heavy lifting”—Morris, Somerset, Hunterdon, Monmouth, Mercer, and Bergen. This is similar to the roles played by Fairfield County in Connecticut, and Manhattan (New York County) and Nassau County in New York.

- Higher-income counties and regions generate even higher amounts of state income tax revenues. Since state income tax revenues are highly responsive to changes in income, this sensitivity applies symmetrically to both increases and decreases in income.
- Thus, when the economy and the stock market inevitably falter and income growth slows or actually becomes negative, there is a shock to the system. The euphoria of the large fiscal dividends that New Jersey derives from riding the sensitivity of tax revenues to income up the business cycle confronts the hard reality that this same sensitivity works in reverse.
- A similar but less extreme pattern is evident with sales taxes. Higher-income counties and regions generate higher amounts of state sales tax revenues, although not to the extent of income taxes.
- The other side of the fiscal equation concerns the progressivity of state expenditures on education and other forms of state aid. The broad general pattern is that the higher-income and higher income–taxed counties receive disproportionately lower levels of state aid, while the reverse is true for lower-income counties.
- Thus, there is a significant net flow of resources from high-income counties and regions to lower-income counties and regions in New Jersey. However, the ability to maintain this progressive expenditure pattern is jeopardized when income growth slows or turns negative.

The analysis of this report documents the region’s high levels of income concentrated in a relatively small number of counties. These income levels

generate significant tax revenues for federal, state, and local governments. But a progressive federal tax structure, combined with relatively low levels of federal spending in the region, yields persistent negative federal fiscal balances for the three states. Similar dependencies on high-income counties for tax yields within each of the states generate budget windfalls when income growth rates boom but budget shortfalls when income growth falters. Since public expenditures typically rise to peak tax-revenue levels and are difficult to reduce when revenues fall, there is a tendency to raise tax rates over time. This, in turn, further increases the volatility of the tax base and the ability of the states to sustain, as in the case of New Jersey, progressive expenditure programs.

## The Enviable Position of Being Number 1!

Several basic measures amply document the three states' dominant national income position (table 1).<sup>2</sup> In 2003, Connecticut's per capita income (\$43,173) ranked number one among the 50 states in the country and was 36 percent higher than that of the United States (\$31,632). New Jersey (\$40,427) ranked second, with a per capita income 28 percent higher than the nation's, while New York (\$36,574) ranked fifth.<sup>3</sup> There is no other cluster of contiguous states remotely comparable to the high-income position of the tri-state area.<sup>4</sup>

Median household and median family income statistics present slightly different rankings but yield the same conclusion (table 1). New Jersey (\$58,588) ranked number one among the 50 states in median household income in 2003, a level 34 percent higher than that of the United States (\$43,564). Connecticut (\$56,803) ranked third, while New York (\$46,195) ranked seventeenth.<sup>5</sup> Median family income in 2003 reveals a nearly identical profile. Top-ranked New Jersey had a median of \$70,263, a level also 34 percent higher than that of the nation (\$52,273), while Connecticut (\$69,917) ranked as the second-highest state. Similarly, New York's median family income (\$55,309) ranked sixteenth, slightly better than its household income ranking of seventeenth.

While these three measures document the *relative* affluence of Connecticut, New Jersey, and New York, they do not do justice to the scale or depth of that affluence. As shown in table 2, the three-state area contained 10.8 percent of the nation's population in 2003 (31.3 million persons out of 290.8 million) but accounted for a much higher 13.1 percent of the nation's total personal income (\$1.2 trillion out of \$9.2 trillion). The three states not only have proportionately larger shares of higher-income individuals, but they also have a lot of them! In the aggregate, this agglomeration of income constitutes the most potent multistate consumer market in the country.

### The Consequences of Affluence

Affluence, however, brings with it not only benefits but consequences. Because of their high incomes, Connecticut, New Jersey, and New York pay disproportionate shares of federal income and

<sup>2</sup> Per capita income is a statistical average calculated by dividing the total personal income by the population. As with any average, it can be greatly affected by extreme values. The median household and median family income statistics are derived from Bureau of Census survey data and represent the middle, or typical, case of the survey distribution—that is, 50 percent have higher incomes and 50 percent have lower incomes. Households are defined as either single persons or groups of unrelated persons occupying a dwelling unit. Families comprise two or more related individuals occupying a dwelling unit.

<sup>3</sup> Massachusetts (ranked third at \$39,815) and Maryland (ranked fourth at \$37,331) separated New York from Connecticut and New Jersey.

<sup>4</sup> Technically, high-income Massachusetts shares borders with both Connecticut and New York. However, Massachusetts's center of wealth lies at its eastern end, far from that of Connecticut, New Jersey, and New York.

<sup>5</sup> New York's higher ranking in per capita income compared to the other two income measures is due to its large number of very-high-income individuals. While these individuals raise the per capita average, they essentially have no impact on the median (i.e., the family or household in the middle of the income distribution).

**Table 1**  
**Recent Income Levels: Connecticut, New Jersey, and New York, 2003**

	2003		2003		2003	
	<u>Per Capita Income</u> Level	Rank	<u>Median Household Income</u> Level	Rank	<u>Median Family Income</u> Level	Rank
U.S. Total	\$31,632		\$43,564		\$52,273	
Connecticut	43,173	1	56,803	3	69,917	2
New Jersey	40,427	2	58,588	1	70,263	1
New York	36,574	5	46,195	17	55,309	16
<b>Ratio: State to Nation</b>						
Connecticut	1.36		1.30		1.34	
New Jersey	1.28		1.34		1.34	
New York	1.16		1.06		1.06	
Source: U.S. Census Bureau, 2003 American Community Survey. U.S. Bureau of Economic Analysis.						

employment taxes. While the three states had 10.8 percent of the nation's population and 13.1 percent of its total personal income in 2003, they paid 15.1 percent of total federal individual income and employment taxes (table 2). This disproportionately high total tax payment is the result of relatively high income levels in general and progressive tax rates in particular—that is, the tri-state area has proportionately more people in the higher federal income tax brackets. The area pays nearly 40 percent more in individual income and employment taxes compared to its population share. Connecticut and New Jersey pay 50 percent more; New York pays 32 percent more. In other words, the three states serve as the nation's "cash cows."

If the federal income and employment tax burdens of the three states were equivalent to their national population shares, significant sums would remain in each state's economy. For example, if New Jersey's share of the national tax burden in 2003 were the same as its population share of 3.0 percent, its federal tax payments would be roughly \$50.5 billion instead of its actual 4.5 percent tax share paid of \$76.2 billion. The approximately \$26 billion that would remain in the state is greater than the state's 2003–04

budget (\$24.1 billion)! Similarly, New York would "save" \$35.4 billion (\$111.1 billion instead of \$146.5 billion), while Connecticut would "save" \$11.0 billion (\$20.2 billion instead of \$31.2 billion) if their tax burdens were based on population shares alone.

Consequently, high personal incomes combined with relatively low levels of federal expenditures in the region lead to significant "balance-of-payment deficits" with the federal government (table 3). According to the Washington, D.C.-based Tax Foundation, for every federal tax dollar collected in New Jersey in 2002, the state received only 62 cents in federal spending, a level that was actually down from 66 cents in 1992, fully a decade earlier. In both years, these "returns" were the largest shortfalls (or the smallest "return" on a federal tax dollar) of any state. New Jersey ranked last among all the states. Connecticut was similarly positioned, ranking forty-ninth in both years, and its return also worsened, from 68 cents to 65 cents. New York fared somewhat better; its 85 cents return ranked fortieth in 2002, the same ranking as in 1992, when it had an 86 cents return. Thus, the region's deficits with the federal government have been both persistent and growing.

**Table 2**  
**Population, Personal Income, and Federal Income and Employment Taxes**  
**United States, Connecticut, New Jersey, and New York, 2003**

	Population		Personal Income		Federal Individual Income and Employment Taxes	
	Total	Share of Nation	Total (in \$000)	Share of Nation	Total (in \$000)	Share of Nation
United States Total	290,809,777	100.0%	\$9,199,007,802	100.0%	\$1,683,184,679	100.0%
Three-State Area	31,311,883	10.8	1,201,463,057	13.1	254,037,003	15.1
Connecticut	3,483,372	1.2	150,387,093	1.6	31,288,964	1.9
New Jersey	8,638,396	3.0	349,223,572	3.8	76,240,503	4.5
New York	19,190,115	6.6	701,852,392	7.6	146,507,536	8.7

*Note:* Percentages may not add due to rounding.  
*Source:* U.S. Bureau of Economic Analysis; Internal Revenue Service.

In sharp contrast, New Mexico ranked number one in both years, and its per-tax-dollar return increased between 1992 and 2002. New Mexico received \$2.08 in federal spending for every federal tax dollar collected in 1992. This return rose by 14 percent to \$2.37 by 2002. Thus, states such as New Mexico are federal tax benefit “winners,” while states like New Jersey and Connecticut are the biggest “losers.” Considerable income tax revenues flow out of the tri-state area and are dispersed throughout the country and beyond.<sup>6</sup>

## Metropolitan-Area Income Concentration

**A**ffluence and wealth are not evenly distributed within Connecticut, New Jersey, and New York.

Most of the high income is concentrated within the three states in eight counties in the metropolitan region, centered around and including Manhattan (see figure 1). All eight counties ranked in the top 20 counties nationally according to per capita income (table 4). Four of these eight counties are in the top 10; six are in the top 12.

But the rankings in table 4 still understate the economic potency of the eight regional counties because they include three extraordinarily small nonmetropolitan counties in the top five national counties: Teton, Wyoming; Pitkin, Colorado; and Loving, Texas. These three counties, with a combined population of less than 34,000 people, are special cases.<sup>7</sup> If the rankings are restricted to only metropolitan counties, then four of the tri-state region’s counties—Manhattan (New York), Fairfield (Connecticut), Morris (New Jersey), and Westchester (New York)—would rank in the top five counties in

<sup>6</sup> A recent book draws political conclusions from the uneven flows of federal subsidies (particular to various industries) and federal tax revenues among the states. See John Sperling, *The Great Divide: Retro vs. Metro America* (Sausalito, CA: PoliPoint Press, 2004), especially chapter 2.

<sup>7</sup> Loving County, Texas, is an oil- and gas-production center providing its 64 residents with a very high standard of living. The other two nonmetropolitan counties in table 4 are largely retreats for the rich and famous. Pitkin County, Colorado, is well-known for its world-class ski resorts, with Aspen its county seat. Teton County, Wyoming, is the location of the renowned community of Jackson Hole.

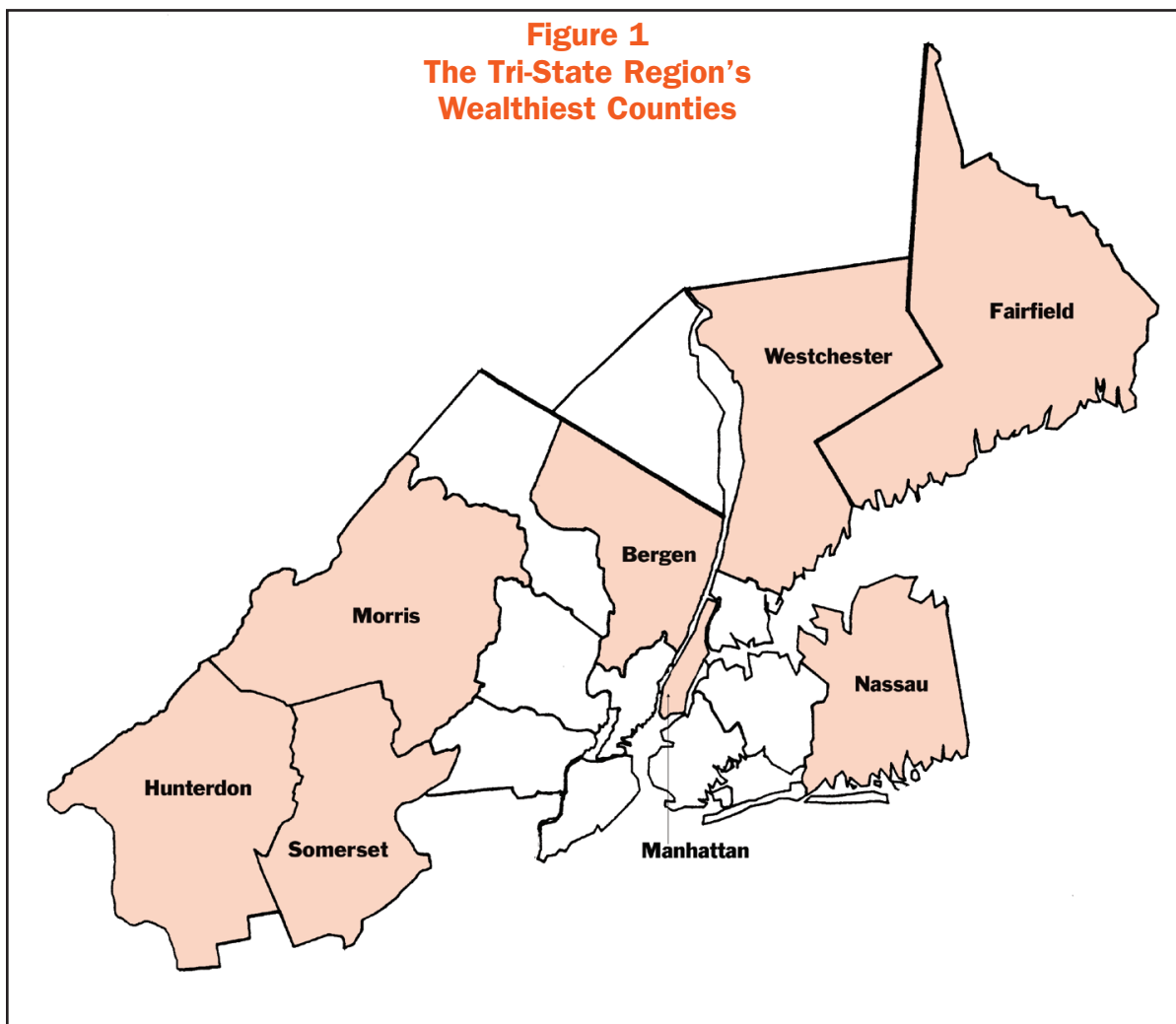


**Table 3**  
**Ratios of Federal Spending Per Dollar Tax Collected and State Ranking**  
**Connecticut, New Jersey, and New York**  
**1992 and 2002**

	Ratio		Rank	
	1992	2002	1992	2002
Connecticut	0.68	0.65	49	49
New Jersey	0.66	0.62	50	50
New York	0.86	0.85	40	40
<i>New Mexico</i>	2.08	2.37	1	1

Source: Tax Foundation, *Federal Tax Burdens and Expenditures by State*, Special Report No. 124, July 2003.

**Figure 1**  
**The Tri-State Region's**  
**Wealthiest Counties**



America, along with Marin (California).<sup>8</sup> Somerset and Hunterdon Counties in New Jersey would be ranked eighth and ninth. Thus, the tri-state region contains six of the nine highest per capita income metropolitan counties in the United States!

New York County (Manhattan) had the highest per capita income (\$84,591) of any county in the United States, a level 2.7 times greater than the national average (\$30,906).<sup>9</sup> Its total personal income, \$131.6 billion, was nearly double that of the second-highest county in the top 20—Nassau County, New York (\$66.4 billion). Affluent Manhattan, the well-to-do New York suburbs (Westchester and Nassau Counties), the prosperous Connecticut suburbs (Fairfield County), and the wealthy New Jersey suburbs (Morris, Somerset, Hunterdon, and Bergen Counties) stand as an unparalleled metropolitan concentration of income.<sup>10</sup>

### Advances and Setbacks

Economic well-being, as measured by income, does not rise steadily year after year. Between 1992 and 1996, per capita income in the United States grew at a modest 4 percent annual rate (table 5). With the exception of Nassau County, all of the high-ranking tri-state counties surpassed the national rate, led by Morris and Hunterdon Counties (5.5 percent each). Incomes nationwide advanced much more rapidly from 1996 to 2000, growing at a 5.9 percent annual rate, almost half again greater than the preceding four-year period. These were the economic Wonder Years, with a booming stock market, massive corporate investments in technology, and tight labor markets. Again, with the exception of Nassau County, every high-income county in the region outpaced the

nation, led by Hunterdon (8.8 percent) and Morris (8.5 percent).

But the economic bubble of the late 1990s burst, and the ensuing recession slowed income growth dramatically in the United States, causing an even more pronounced setback in the tri-state region. Per capita income grew by only 1.8 percent nationwide from 2000 to 2002, less than half the pace of the slow-growth 1992–96 period, and 70 percent below the annual increase of the 1996–2000 boom. During this time the region's high-income counties underperformed the nation, with three counties—Somerset (-1.9 percent), Manhattan (-0.7 percent), and Morris (-0.2 percent)—experiencing actual declines in per capita income. This reflected the economic aftershocks of the simultaneous bursting of the stock market and telecommunications bubbles.<sup>11</sup> Affluent areas disproportionately benefited in the boom/bubble years (1996–2000), then disproportionately suffered in the post-boom/bubble years (2000–02).

The same pattern was evident in total personal income growth: Modest advances in the 1992–96 period were followed by a surge between 1996 and 2000 and then a dramatic slowdown from 2000 to 2002. The region's high-income counties generally outperformed the nation for eight years (from 1992 to 2000) but trailed it in the 2000–02 period. Unprecedented losses in total personal income occurred in Somerset County (-0.5 percent) and Manhattan (-0.2 percent). Total personal income in Somerset increased by \$1.2 billion annually between 1996 and 2000; it then contracted by \$86 million annually between 2000 and 2002. Personal income in Manhattan grew by \$7.9 billion per year from 1996 to 2000; it subsequently declined by \$281 million per year in the 2000–02 period.

<sup>8</sup> Total personal income in six of the eight regional counties, led by Manhattan, dwarfs that of Marin County. Somerset's is roughly the same size; only Hunterdon's is appreciably smaller.

<sup>9</sup> New York County's extraordinary income level is a result of the sheer scale of its total personal income as well as its relatively small household size. According to *Census 2000*, Manhattan had 2.0 persons per household compared to 2.6 persons nationally. Nearly one-half (48 percent) of all households in Manhattan comprise a single person, compared to about one-quarter nationally (26 percent).

<sup>10</sup> For an analysis of the geographic distribution of New Jersey's income and property values, see James W. Hughes and Joseph J. Seneca, *The Emerging Wealth Belt: New Jersey's New Millennium Geography*, Rutgers Regional Report Issue Paper 17, September 1999.

<sup>11</sup> The largest county losses nationwide were in San Mateo County, California, and in Loving County, Texas—a consequence, respectively, of computer-technology trauma in Silicon Valley and of plunging energy prices.

**Table 4**  
**Per Capita Income: Top Thirty Counties, 2002**

Rank 2002	County	Per Capita Income, 2002	Ratio: County to Nation	Total Personal Income (\$000)	Population
	<b>United States</b>	<b>\$30,906</b>	<b>1.00</b>	<b>\$8,900,007,000</b>	<b>287,973,924</b>
1	* New York, New York	84,591	2.74	131,576,086	1,555,434
2	Teton, Wyoming	71,457	2.31	1,325,748	18,553
3	Pitkin, Colorado	69,681	2.25	1,040,685	14,935
4	* Marin, California	68,650	2.22	16,944,523	246,824
5	Loving, Texas	65,922	2.13	4,219	64
6	* Fairfield, Connecticut	59,727	1.93	53,432,682	894,622
7	* Morris, New Jersey	56,002	1.81	26,803,989	478,622
8	* Westchester, New York	55,522	1.80	52,073,719	937,894
9	* Arlington, Virginia	55,148	1.78	10,427,863	189,090
10	* Alexandria City, Virginia	55,071	1.78	7,155,850	129,938
11	* Somerset, New Jersey	55,057	1.78	16,942,242	307,722
12	* Hunterdon, New Jersey	55,050	1.78	6,974,002	126,685
13	* San Francisco, California	54,639	1.77	41,634,308	761,983
14	* San Mateo, California	53,315	1.73	37,338,895	700,341
15	* Bergen, New Jersey	52,867	1.71	47,286,982	894,454
16	* Fairfax, Ffx City + Falls Ch, Virginia	52,199	1.69	53,588,468	1,026,628
17	* Montgomery, Maryland	51,750	1.67	47,032,055	908,831
18	* Nassau, New York	49,543	1.60	66,351,279	1,339,265
19	Los Alamos, New Mexico	48,485	1.57	887,515	18,305
20	* Norfolk, Massachusetts	48,081	1.56	31,468,921	654,497
21	* Fulton, Georgia	47,478	1.54	38,921,017	819,777
22	* Montgomery, Pennsylvania	47,461	1.54	36,298,362	764,805
23	* Ozaukee, Wisconsin	47,418	1.53	3,979,542	83,924
24	* Oakland, Michigan	47,394	1.53	57,033,284	1,203,379
25	Nantucket, Massachusetts	47,104	1.52	492,757	10,461
26	* District of Columbia	46,800	1.51	26,636,320	569,157
27	* Chester, Pennsylvania	46,737	1.51	21,012,053	449,580
28	* Santa Clara, California	46,499	1.50	77,997,930	1,677,426
28	* Middlesex, Massachusetts	46,499	1.50	68,484,590	1,472,817
30	* Lake, Illinois	46,343	1.50	31,253,131	674,389

\*Metropolitan County. (A metropolitan county is one that contains a city of 50,000 or more persons or that shares more than 20 percent of its labor force with such a county.)

2002 ranking based on per capita income.

Source: U.S. Bureau of Economic Analysis.

**Table 5**  
**Annual Percentage Change: Per Capita and Total Personal Income, 1992-2002**

Rank 2002	County	Per Capita Income			Total Personal Income		
		1992- 1996	1996- 2000	2000- 2002	1992- 1996	1996- 2000	2000- 2002
	<b>United States</b>	<b>4.0%</b>	<b>5.9%</b>	<b>1.8%</b>	<b>5.4%</b>	<b>7.3%</b>	<b>2.8%</b>
1	* New York, New York	5.1	7.5	-0.7	5.8	7.9	-0.2
2	Teton, Wyoming	6.3	8.7	6.8	12.9	14.9	7.5
3	Pitkin, Colorado	5.2	12.9	2.3	8.2	13.6	2.9
4	* Marin, California	6.0	10.5	0.7	6.4	11.8	0.5
5	Loving, Texas	-0.5	46.6	-4.0	-3.9	17.7	-4.8
6	* Fairfield, Connecticut	4.3	8.2	0.6	5.0	9.3	1.2
7	* Morris, New Jersey	5.5	8.5	-0.2	7.1	10.0	0.6
8	* Westchester, New York	4.3	7.3	0.4	4.9	8.2	1.1
9	* Arlington, Virginia	3.8	6.7	5.7	5.0	7.8	5.6
10	* Alexandria City, Virginia	4.4	5.4	7.2	5.2	8.2	7.6
11	* Somerset, New Jersey	4.8	6.8	-1.9	7.5	9.9	-0.5
12	* Hunterdon, New Jersey	5.5	8.8	2.1	7.1	10.7	3.8
13	* San Francisco, California	4.5	11.4	-1.0	5.2	12.5	-1.9
14	* San Mateo, California	5.9	12.6	-4.8	7.1	13.7	-5.3
15	* Bergen, New Jersey	4.6	6.2	1.6	5.4	7.0	2.1
16	* Fairfax, Ffx City + Falls Ch, Virginia	3.9	7.5	2.2	5.6	9.9	3.2
17	* Montgomery, Maryland	3.5	6.4	2.1	4.9	8.6	4.0
18	* Nassau, New York	3.8	5.7	2.2	4.2	6.2	2.3
19	Los Alamos, New Mexico	2.9	4.9	8.2	3.2	4.8	8.2
20	* Norfolk, Massachusetts	4.9	8.5	1.3	5.7	9.1	1.6
21	* Fulton, Georgia	5.0	8.8	1.7	8.4	11.6	1.9
22	* Montgomery, Pennsylvania	3.8	5.7	1.6	5.1	6.8	2.6
23	* Ozaukee, Wisconsin	6.3	7.6	1.4	8.0	8.6	2.3
24	* Oakland, Michigan	6.1	6.7	0.3	7.4	7.5	0.6
25	Nantucket, Massachusetts	2.4	4.5	2.5	8.9	10.9	7.1
26	* District of Columbia	3.3	5.8	7.9	2.2	5.8	7.6
27	* Chester, Pennsylvania	5.1	7.3	0.3	6.9	9.4	1.9
28	* Santa Clara, California	4.9	15.2	-7.1	6.4	17.2	-7.3
28	* Middlesex, Massachusetts	4.6	9.0	0.2	5.2	9.9	0.3
30	* Lake, Illinois	4.5	5.8	0.1	7.3	8.5	2.1

\*Metropolitan County. (A metropolitan county is one that contains a city of 50,000 or more persons or that shares more than 20 percent of its labor force with such a county.)

2002 ranking based on per capita income.

Source: U.S. Bureau of Economic Analysis.

## Fiscal Consequences

The faltering of personal income growth has significant implications for income tax revenues. While much attention has been focused on the overdependence on property taxes in New Jersey, little concern has been raised more generally regarding the stability of income tax revenues and their sensitivity to the business cycle. A recent study of New York City’s tax system observed that the system has become less reliant on property and general sales taxes and more dependent on corporate and personal income taxes.<sup>12</sup> It concluded that this shift has made the city’s tax revenues less stable and more sensitive to cyclical swings, and that it caused income tax revenue to decline quickly and dramatically with the onset of the 2001 national recession. Since many public expenditure programs are difficult to reduce, particularly in the short term, New York City was forced to increase tax rates and take other extraordinary actions to close the fiscal gap created by the reduction in personal income tax revenues. In general, there has been a recurring cyclical pattern in New York City of economic booms, financial market collapses, and the subsequent stop-go effects on income tax revenues and rates. The study, in fact, recommended consideration of increasing the City’s reliance on the more persistent and stable property tax in order to mitigate the volatility of the City’s tax base!<sup>13</sup>

As shown earlier, the major swings in income growth rates were characteristic of the entire nation. But these changes were more extreme in many of the most affluent counties of the United States, particularly those of the tri-state region. While the state patterns show less volatility than counties, Connecticut, New Jersey, and New York all had larger variations than the nation as a whole (table 6). In the 1992–96 period, total personal income growth in the three states lagged the nation. One key reason was

the slower rate of population increase in the tri-state area compared to that of the nation, which produced a weaker demographic component of economic growth. However, from 1996 to 2000, despite this slower-growing population, Connecticut and New Jersey’s growth in total personal income surpassed that of the nation, and New York narrowed the difference between its income growth rate and the nation’s. In the 2000–02 period, all three states slipped significantly below the nation, although New Jersey exhibited the most competitive growth performance (2.0 percent versus 2.3 percent).

A significant implication of the slowdown in income growth is the echo effect this has on state fiscal conditions, particularly in light of the actual declines in income experienced by some of the formerly highest-income and fastest-income-growth counties in the region and nation. As shown in table 7, New Jersey’s gross income tax (GIT) revenues exploded at double-digit annual rates in fiscal years 1998 through 2001, averaging 13.5 percent per year for four consecutive years. This followed a slow-

**Table 6**  
**Percentage Change in**  
**Total Personal Income**  
**1992–2003**

	1992-1996	1996-2000	2000-2003
United States	5.4%	7.3%	2.3%
Three-State Area	4.3	6.9	1.6
Connecticut	3.9	7.7	1.6
New Jersey	4.9	7.6	2.0
New York	4.1	6.4	1.5

Source: U.S. Bureau of Economic Analysis.

<sup>12</sup> Jesse Edgerton, Andrew F. Haughwout, and Rae Rosen, “Revenue Implications of New York City’s Tax System,” *Current Issues in Economics and Finance*, Federal Reserve Bank of New York, Volume 10, Number 4, April 2004.

<sup>13</sup> A more general analysis indicated that reliance on property taxes by state and local governments increased significantly because of the 2001 recession. See Ray A. Smith, “Downturn Made States and Cities More Dependent on Property Taxes,” *Wall Street Journal*, August 24, 2004.

growth period (1994–97) that reflected declines in income tax rates as well as below-trend economic growth. The subsequent explosion in income tax revenues was the result of a surging stock market and accelerating economic growth.<sup>14</sup> However, the stock market bubble burst in 2001, and the resulting abrupt replacement of large capital gains with large capital losses, plus the broader national economic downturn, caused income tax revenues to plummet by 14.4 percent in fiscal year 2002. Double-digit rates of growth in tax revenue followed by a double-digit rate of decline represented nothing less than extreme fiscal shock for New Jersey. This shock then abated somewhat as revenues fell by “only” 1.5 percent in fiscal year 2003, reflecting the start of general, but weak, economic recovery in the second half of the year.

### New Jersey–New York Parallels

There is an intriguing parallel between New York’s dependence on volatile tax revenues derived from the income produced by financial activities (Wall Street) and New Jersey’s increasing fiscal dependence on the cyclically fluctuating income emanating from its affluent counties. In order to examine the potential problems caused by such cyclical effects, this study analyzes New Jersey’s revenue and expenditure flows among its counties at a single point in time. The purpose of this analysis is to document the extent of the state’s fiscal reliance on its high-income areas and to trace the flow of funds within the geographic regions of the state. Specifically, the analysis examines the sources by county of two key state taxes—the income and sales tax—and presents the allocation by county of state aid to school districts, municipalities, and county governments.

**Table 7**  
**Percentage Change in New Jersey**  
**Gross Income Tax Revenues**  
**1994–2003**

Fiscal Year	Percentage Change from Preceding Year
1994	3.4%
1995	1.6
1996	4.3
1997	1.9
1998	15.9
1999	13.1
2000	13.9
2001	10.9
2002	-14.4
2003	-1.5

Source: Office of Legislative Services, New Jersey Legislature.

### New Jersey Income and Sales Tax Revenues

Approximately 54 percent of annual New Jersey state tax revenues are generated from the state income tax and the state sales tax.<sup>15</sup> The state income tax is highly progressive, with rates that start at 1.4 percent for taxable incomes below \$20,000 and, effective in calendar year 2004, end with a top income tax levy of 8.97 percent on taxable incomes above \$500,000. Further, the definition of taxable income is broad, with few exemptions and deductions. The state sales tax rate, covering most consumer and intermediate goods, is 6 percent. The major consumer items exempt from the sales tax are food and clothing.

Given the diversity of economic conditions across New Jersey’s 21 counties, it is not surprising that state tax revenues vary significantly across regions and counties. Moreover, given the progressive nature of the income tax, there is a close correlation between income levels across counties and regions and income tax revenues. Sales taxes are also correlated with income levels but less so than income tax revenues.

<sup>14</sup> New Jersey taxes capital gains as ordinary income. Capital gains are not included in the total personal income or per capita income statistics.

<sup>15</sup> The Corporate Business Tax (CBT) provides approximately 10.8 percent of state revenues annually. The CBT is not included in this analysis because allocating business tax revenues by county is not meaningful since significant amounts of business tax revenues (e.g., from multistate, multinational corporations) are collected in complex ways.

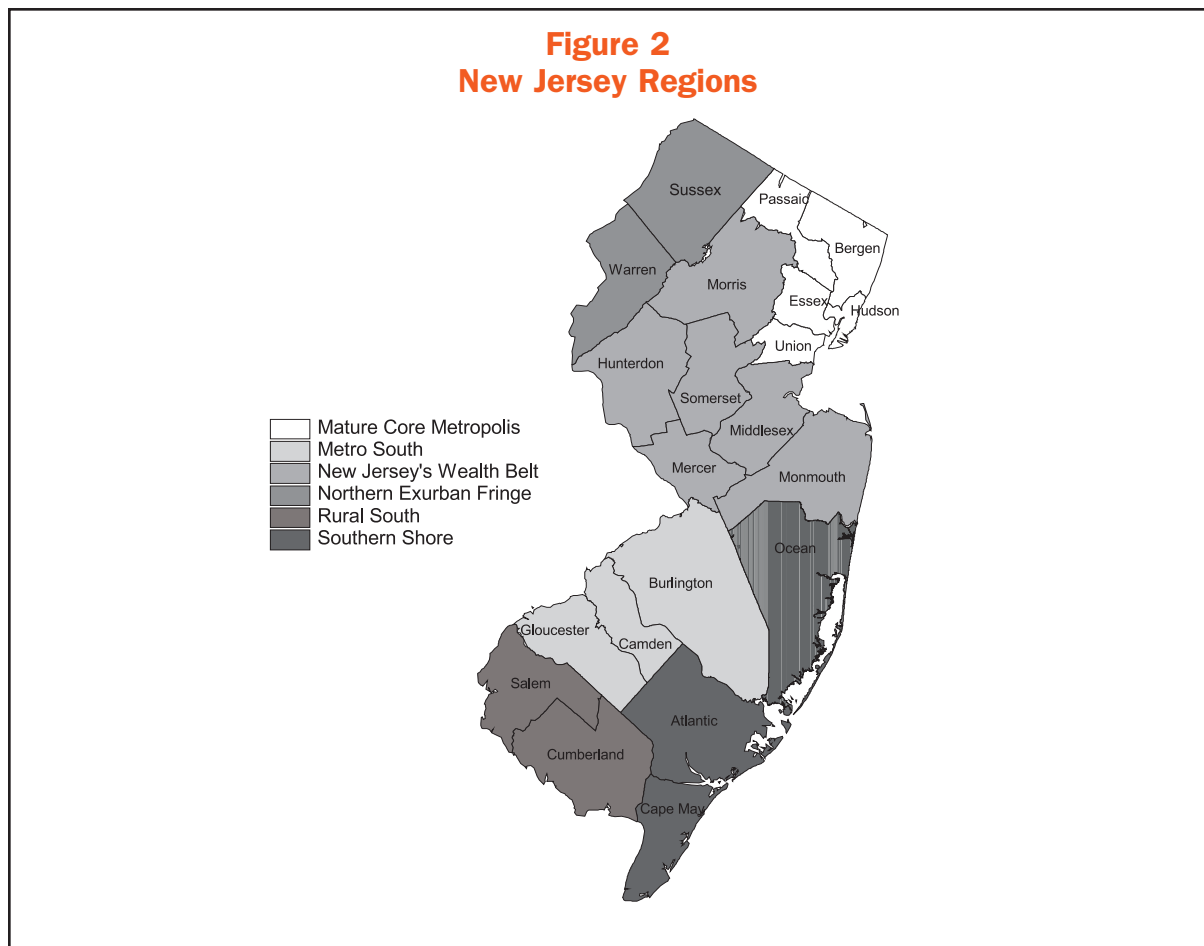
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Table 8 provides data on regional and county population share, income tax share, and sales tax share, along with revenue yields for these two taxes for fiscal year 2003. The 21 New Jersey counties are divided into six geographic regions (see figure 2).<sup>16</sup> Of the four New Jersey counties in the top 20 counties nationwide in per capita income, three (Hunterdon, Morris, and Somerset) are in the six-county New Jersey Wealth Belt, while the fourth (Bergen) is in the Mature Core Metropolis, a five-county region lying close to New York City.

In fiscal year 2003, the state income tax raised \$6.7 billion dollars in revenue.<sup>17</sup> The Wealth Belt

counties generated 43.7 percent (\$2.7 billion) of state income tax revenues compared to a population share of 31.2 percent. Morris and Monmouth Counties each provided 10 percent or more of state income tax revenues although accounting for only 5.6 percent and 7.3 percent, respectively, of the state's population. Relatively small Somerset County was *the* county "cash calf." Its income tax share (7.6 percent) was more than double its population share (3.6 percent).

Bergen County, in the Mature Core Metropolis, is the state's most populous county, accounting for 10.4 percent of the state's population. It generated 14.3



<sup>16</sup> The authors previously analyzed property values and income levels in New Jersey according to these six geographic subdivisions of the state. See "The Emerging Wealth Belt: New Jersey's New Millennium Geography," *op. cit.* The six geographic areas studied in that report are maintained in the current analysis.

<sup>17</sup> Using data on the allocation of income tax revenue by county for 2001, \$6.2 billion (or 92.5 percent) of the total fiscal year 2003 income tax revenue of \$6.7 billion can be assigned to county of origin. See New Jersey Division of Taxation, *2001 Annual Report*, and *2003 Annual Report*.

**Table 8**  
**Income and Sales Tax Revenues by Region and County, 2003**

Region/County	Population Share	Share of Income Tax	Income Tax Revenue (\$millions)	Share of Sales Tax	Sales Tax Revenue (\$millions)
<b>New Jersey Total</b>	<b>100.0%</b>	<b>100.0%</b>	<b>\$6,221.4</b>	<b>100.0%</b>	<b>\$3,678.4</b>
<b>Mature Core Metropolis</b>	<b>38.5</b>	<b>35.5</b>	<b>2,210.0</b>	<b>33.2</b>	<b>1,221.9</b>
Essex	9.2	8.6	533.4	6.0	220.1
Hudson	7.0	2.8	173.1	3.0	111.7
Union	6.1	6.1	379.2	6.1	225.1
Bergen	10.4	14.3	890.8	13.1	483.4
Passaic	5.8	3.8	233.4	4.9	181.7
<b>Northern Exurban Fringe</b>	<b>3.0</b>	<b>2.7</b>	<b>167.6</b>	<b>2.2</b>	<b>79.2</b>
Sussex	1.7	1.7	106.3	1.3	47.7
Warren	1.3	1.0	61.3	0.9	31.5
<b>New Jersey's Wealth Belt</b>	<b>31.2</b>	<b>43.7</b>	<b>2,716.0</b>	<b>40.3</b>	<b>1,483.4</b>
Hunterdon	1.5	2.7	167.4	2.2	81.6
Mercer	4.2	5.3	331.8	4.1	150.8
Middlesex	9.0	7.3	452.9	9.4	347.4
Monmouth	7.3	10.0	624.1	8.3	306.5
Morris	5.6	10.8	670.0	8.7	320.2
Somerset	3.6	7.6	469.8	7.5	276.8
<b>Metro South</b>	<b>14.2</b>	<b>10.3</b>	<b>637.7</b>	<b>12.1</b>	<b>444.7</b>
Camden	5.9	3.8	238.9	4.8	175.8
Burlington	5.1	4.6	286.8	4.9	180.9
Gloucester	3.1	1.8	111.9	2.4	88.0
<b>Southern Shore</b>	<b>10.5</b>	<b>6.8</b>	<b>420.8</b>	<b>10.7</b>	<b>394.7</b>
Atlantic	3.0	1.8	112.5	3.5	130.0
Cape May	1.2	0.8	50.7	1.6	60.3
Ocean	6.3	4.1	257.6	5.6	204.4
<b>Rural South</b>	<b>2.5</b>	<b>1.1</b>	<b>69.3</b>	<b>1.5</b>	<b>54.5</b>
Cumberland	1.7	0.7	45.9	1.1	39.1
Salem	0.8	0.4	23.4	0.4	15.5

*Note:* Figures may not sum due to rounding.  
*Source:* Division of Taxation, New Jersey Department of the Treasury.



percent of the state's income tax. However, its region as a whole, as well as all of the other regions except the Wealth Belt, had an income tax share below its population share. Hudson County, with a population share of 7.0 percent, generated only 2.8 percent of state income tax revenues. This differential made Hudson the major county income tax "winner," whereas Somerset was the major county "loser." In second place among the winners was rural Cumberland County, whose share of the income tax (0.7 percent) was far below that of its population share, while Morris was second among the "losers."

This pattern follows directly from the progressive rates of the state's income tax. The Wealth Belt counties, with their high average incomes, provided nearly 44 percent of state income tax revenues. This percentage will rise significantly in the future with the recently enacted increase in the top marginal income tax rate.

Just as the nation is highly dependent on Connecticut, New Jersey, and New York to produce income tax "surpluses," so too is New Jersey dependent on six counties to do the income tax "heavy lifting": Morris, Somerset, Hunterdon, Monmouth, and Mercer in the Wealth Belt, and Bergen in the Mature Core Metropolis. Similarly, Fairfield County performs a similar role in Connecticut, as do Manhattan and Nassau County in New York. Fairfield accounts for 25.9 percent of Connecticut's population but has 36.4 percent of the state's personal income and pays 41.4 percent of all state income taxes. Nassau's 7.0 percent share of New York's population is considerably less than its 9.7 percent share of personal income and its 12.8 percent share of state income taxes. The true fiscal behemoth, however, is Manhattan. While accounting for 8.1 percent of the state's population and 19.2 percent of the state's personal income, Manhattan produces 26.9 of New York State's state income tax revenue. Thus, Manhattan is an entire herd of "cash cows," a tax-revenue producer of monumental proportions!

Table 8 also provides similar data for the generation of sales tax revenues by region and county.<sup>18</sup> Not surprisingly, the Wealth Belt was the most significant revenue producer, generating 40.3 percent (\$1.48 billion) of the state's sales tax total (\$3.68 billion) while accounting for only 31.2 percent of the state's population. In general, the Wealth Belt generated somewhat less of a share of sales tax revenues (40.3 percent) than of income tax revenues (43.7 percent), but it again did the "heavy lifting." Among the non-Wealth Belt counties, it was Bergen in the Mature Core and Atlantic and Cape May in the Southern Shore resort region that had significantly higher sales tax shares relative to their population shares. However, sales taxes collected in resort counties were significantly increased by the spending of non-resident tourists.

Table 9 lists per capita income by region and county for 2002 (the latest data available) and the per capita income tax and sales tax revenues for 2003, along with their ratios to statewide averages. There is a close and progressive relation between per capita income and income taxes paid per capita. Not surprisingly, the Wealth Belt had the state's highest per capita income (\$45,539) of any region and also paid the state's highest per capita income taxes (\$1,007). However, while per capita incomes in the Wealth Belt were 15.4 percent higher than the statewide average, their per capita income taxes were 29 percent higher—almost double. This reflects the progressive nature of the state's income tax.

Morris County had the highest per capita income (\$56,002) of any county (42 percent higher than the state as a whole), while its per capita income taxes (\$1,387) were 77.8 percent higher. Similarly, Somerset County per capita income (\$55,057) was 39.5 percent higher than the statewide average, while its per capita income taxes (\$1,508) were 93.3 percent higher.<sup>19</sup>

In contrast to the Wealth Belt, the three southern regions had per capita incomes below the state average; nonetheless, their per capita income taxes

<sup>18</sup> Total state sales tax revenue in fiscal year 2003 was \$5.9 billion. The authors were able to allocate \$3.7 billion of this total (or 62.8 percent) to county of origin. A larger fraction of sales tax revenue (compared to income tax revenues) was not allocable to counties due to out-of-state sources (\$2.1 billion) and an unknown category (\$73.8 million). The Atlantic City Luxury Tax (\$5.6 million), which is dedicated to Atlantic City and County, was not included in the analysis.

<sup>19</sup> The difference in the date of the data may explain this since the income tax data are for 2003 and the income data are for 2002. Relative income levels for the 2003 tax year may have changed across some of the counties compared to 2002 levels.

**Table 9**  
**Per Capita Sales Tax and Income Tax by Region and County, 2003**

Region/County	Per Capita Income (2002) <sup>a</sup>	% of State Avg. (Per Capita Income)	Per Capita Income Tax	% of State Avg. (Income Tax)	Per Capita Sales Tax	% of State Avg. (Sales Tax)
<b>New Jersey Total</b>	\$39,461	100.0%	\$780 <sup>b</sup>	100.0%	\$426 <sup>c</sup>	100.0%
<b>Mature Core Metropolis</b>	39,957	101.3	664	85.1	367	86.2
Essex	38,312	97.1	670	85.9	276	64.9
Hudson	30,259	76.7	285	36.5	184	43.2
Union	39,889	101.1	716	91.8	425	99.8
Bergen	52,867	134.0	992	127.2	539	126.5
Passaic	31,323	79.4	468	60.1	365	85.6
<b>Northern Exurban Fringe</b>	35,642	90.3	644	82.5	304	71.4
Sussex	37,676	95.5	704	90.2	316	74.1
Warren	32,824	83.2	561	71.9	288	67.7
<b>New Jersey's Wealth Belt</b>	45,539	115.4	1,007	129.0	550	129.1
Hunterdon	55,050	139.5	1,305	167.3	636	149.4
Mercer	40,711	103.2	917	117.5	416	97.8
Middlesex	37,449	94.9	580	74.3	445	104.5
Monmouth	43,684	110.7	987	126.6	485	113.9
Morris	56,002	141.9	1,387	177.8	663	155.7
Somerset	55,057	139.5	1,508	193.3	888	208.6
<b>Metro South</b>	33,300	84.4	520	66.7	363	85.2
Camden	32,108	81.4	465	59.6	342	80.3
Burlington	36,513	92.5	645	82.8	407	95.6
Gloucester	30,265	76.7	419	53.8	330	77.4
<b>Southern Shore</b>	31,940	80.9	462	59.2	433	101.7
Atlantic	31,702	80.3	427	54.8	493	115.9
Cape May	34,879	88.4	497	63.8	592	139.0
Ocean	31,497	79.8	472	60.5	374	87.9
<b>Rural South</b>	26,806	67.9	324	41.5	255	59.8
Cumberland	25,856	65.5	307	39.4	262	61.4
Salem	28,977	73.4	361	46.3	239	56.0

Notes: <sup>a</sup> 2002 Per Capita Income county figures represent BEA data (regional figures are BEA total income figures divided by BEA population figures).

<sup>b</sup> The state average of \$780 used in calculating per capita income tax as a percentage of the state average is equal to the total income tax collected statewide for FY 2003 (including from "unknown" counties) divided by the total population (8,638,396).

<sup>c</sup> The state average of \$426 used in calculating per capita sales tax as a percentage of the state average is equal to the total sales tax attributable to specific counties (\$3,678,432,957) divided by the total population of the state (8,638,396). The total sales tax revenue collected by the state, including from unknown sources, out-of-state sources, and the Atlantic City Luxury Tax, totals \$5,856,357,246.

Source: New Jersey Department of the Treasury, Division of Taxation; U.S. Bureau of Economic Analysis.

were far below the state average. For example, the Metro South region had a per capita income (\$33,300) that was 84.4 percent that of the state, while its per capita income tax (\$520) was only 66.7 percent of the state average.

Thus, higher-income counties and regions generate even higher amounts of state income tax revenues. However, since state income tax revenues are highly responsive to changes in income, this sensitivity is applicable to both increases and decreases in income.<sup>20</sup> When stock markets and incomes fall, as they inevitably do, the euphoria of the large fiscal dividends that New Jersey derives from riding this sensitivity up the business cycle confronts the hard reality that all this works in reverse (see tables 6 and 7)!

Table 9 also provides similar data on the generation of sales tax revenues across regions and counties. The relation between per capita income and sales tax revenues is also a positive one albeit weaker than the relation with income taxes. The Wealth Belt was first in the state in sales taxes per capita (\$550, or 29.1 percent higher than the state as a whole), led by Somerset County (\$888). The Southern Shore was second-ranked (\$433 per capita), followed by the Mature Core Metropolis (\$367 per capita). Cape May County (Southern Shore) actually had a per capita sales tax (\$592) that was higher than that of the Wealth Belt. This is a tribute to the important role of summer tourism rather than robust spending by county residents. The Metro South region (\$363 per capita) and the Rural South region (\$255) had the state's lowest average per capita sales taxes. In general, sales tax revenues are related to income levels. Complicating this relationship, however, are

several factors: the exemptions for food and clothing; the fact that savings rise with income levels (and hence consumption expenditures, as a fraction of income, decline as income rises); and the complexities of collecting taxes on out-of-state purchases. Thus, the relation is not a statistically close one.<sup>21</sup>

### New Jersey School, Municipal, and County Expenditures

The New Jersey State Budget in fiscal year 2003–04 was \$24.1 billion. Of this total, 37.8 percent, or \$9.1 billion, was spent on school aid, municipal aid, and county aid. Table 10 provides data on the distribution of \$6.55 billion in school aid, constituting the largest single expenditure item in the state budget. The absolute level of school aid in New Jersey—particularly, the amount of expenditures per pupil across school districts—has been a contentious issue for more than a quarter of a century. The interpretation of the “thorough and efficient” education language in the state’s constitution has, over the years, through litigation, court decisions, and state legislation resulted in a complex system of financing for public schools. Some school districts receive all, or nearly all, of their resources from the state, whereas others are financed almost entirely from local sources. A consistent goal of the litigation has been to bring parity in educational opportunity, as measured by expenditures per pupil. Thus, state aid has disproportionately gone to low-income school districts in order to provide expenditure-per-pupil levels comparable to higher-income school districts.

Table 10 also provides data on the amount of state school aid received, the percentage of aid received, the percentage of total state enrollment, and state

<sup>20</sup> A regression was estimated between the log of state income tax revenues and the log of average per capita income across the state’s 21 counties. As expected, the correlation is extremely strong (adjusted R-square of .92), and the coefficient of the log of the income per capita variable is 2.03 and highly significant ( $t = 15.7$ ). The size of the coefficient indicates that for every 10 percent increase in county income per capita, income tax revenues increase by more than double that amount, or 20.3 percent.

<sup>21</sup> A regression between the log of sales tax revenue per capita and the log of income per capita across counties reveals a positive correlation (adjusted R-square of .59, although this correlation is significantly less than that of the income tax equation reported above). The coefficient of the log of the income per capita variable is 1.29 and significant ( $t = 5.4$ ). The size of the coefficient indicates there is a more than proportional relation between sales tax revenues and income changes, although less so than for income tax revenues. Specifically, a 10 percent increase in income per capita generates a 12.9 percent increase in sales tax revenues per capita.

school aid per pupil by region and county for 2003.<sup>22</sup> The broad general pattern is that the higher-income and higher income-taxed counties receive disproportionately lower levels of school aid, while the reverse is true for lower-income counties. The Mature Core Metropolis, with 36.6 percent of state enrollment, received 42 percent of state school aid in 2003. Four of the five counties in this region received a higher percentage of state school aid than they had of state enrollment. Bergen County, however, had a distinctly different pattern. It had 9.4 percent of state enrollment but received only 3.6 percent of state school aid.

The Wealth Belt Region contained 31.5 percent of state enrollment and received 22.2 percent of state school aid. Only Mercer County of the six counties in the region received proportionately more aid (4.5 percent) than it had in enrollment (4.4 percent). Several of the counties within the region had noteworthy differences between aid received and enrollment. Morris County, with 5.6 percent of enrollment, received 2.7 percent of state school aid. Somerset County had 3.7 percent of enrollment and received 1.8 percent of aid.

Of the remaining ten counties that constitute the four other regions, eight received either proportionately more aid, or the same proportion of aid, as their share of state enrollment. Ocean County received less aid (4.9 percent) than it had enrollment (5.8 percent), a result probably linked to the size of its retirement-age population. Sussex County received 1.8 percent of state aid but had 2.1 percent of state enrollment.

State school aid per pupil is listed in column four of table 10. As expected from the protocols that have evolved underlying the distribution of state school aid,

there is significant variation across counties. Cumberland County had the highest per pupil aid at \$9,910, or 206.8 percent of the state average. Hudson County aid per pupil was \$8,097, or 168.9 percent of the state average; Essex County aid per pupil was \$6,929, or 144.6 percent of the state average. At the other end, Bergen County had the lowest state aid per pupil—\$1,858, or 38.8 percent of the state average. The Wealth Belt counties, with the exception of Mercer County, were also all significantly below the state average aid per pupil.<sup>23</sup>

In calendar year 2003, the state also distributed \$1.8 billion in municipal aid and \$765.6 million in county aid (table 11). Municipal aid and county aid are allocated according to numerous criteria related to such factors as various service needs, income criteria, block grants, payments in lieu of taxes, property tax relief formulas, and energy tax receipts, among others. As a whole, this aid is a considerable sum: \$2.6 billion, or 10.8 percent of the state budget in fiscal year 2003. Because of the protocols for some of the distribution criteria, this aid may tend to be progressively distributed (i.e., proportionately more aid allocated to lower-income municipalities and counties), although large parts of it are allocated by population and by other factors not directly related to income levels.

Table 11 provides the regional and county distribution of this aid. Of the \$1.8 billion in municipal aid, 44 percent, or \$797.5 million, went to municipalities in the five counties of the Mature Core Metropolis. This region also received 46.7 percent, or \$357.8 million, of the total county aid of \$765.6 million. For perspective, the Mature Core Metropolis had 38.5 percent of the state's population in 2003

<sup>22</sup> This analysis is made at the county level. State school aid is distributed by school district and depends on factors specific to each district. These factors vary significantly within a county and, as a result, there is significant variation in school aid across districts within the same county. Thus, the regional and county data presented here represent only broad patterns in the allocation of total state school aid.

<sup>23</sup> A regression of the log of per capita county income on the log of state school aid per capita demonstrates the inverse relation that is embodied in the allocation protocols for state aid that are based on court decision and legislation. The adjusted R-square of .77 indicates a close correlation, and the coefficient of the log of per capita county income variable (-1.69) is negative and highly significant ( $t = -8.2$ ). The size of the coefficient means that a 10 percent increase in per capita county income results in a 16.9 percent decline in state aid per pupil.

**Table 10**  
**School Aid by County and Region, Calendar Year 2003**

Region/County	CY03 School Aid (\$millions)	Share of School Aid	Share of Enrollment	Per Pupil School Aid	% of State Avg.
<b>New Jersey Total</b>	\$6,552.6	100.0%	100.0%	\$4,793	100.0%
<b>Mature Core Metropolis</b>	2,752.3	42.0	36.6	5,499	114.7
Essex	872.7	13.3	9.2	6,929	144.6
Hudson	660.4	10.1	6.0	8,097	168.9
Union	448.1	6.8	6.2	5,251	109.6
Bergen	239.0	3.6	9.4	1,858	38.8
Passaic	532.1	8.1	5.8	6,730	140.4
<b>Northern Exurban Fringe</b>	212.0	3.2	3.4	4,512	94.1
Sussex	119.5	1.8	2.1	4,212	87.9
Warren	92.5	1.4	1.4	4,971	103.7
<b>New Jersey's Wealth Belt</b>	1,452.0	22.2	31.5	3,373	70.4
Hunterdon	53.8	0.8	1.6	2,386	49.8
Mercer	294.0	4.5	4.4	4,906	102.4
Middlesex	418.7	6.4	8.3	3,680	76.8
Monmouth	394.4	6.0	7.8	3,679	76.7
Morris	175.2	2.7	5.6	2,285	47.7
Somerset	115.9	1.8	3.7	2,301	48.0
<b>Metro South</b>	1,179.4	18.0	15.4	5,593	116.7
Camden	567.7	8.7	6.5	6,351	132.5
Burlington	357.3	5.5	5.4	4,801	100.2
Gloucester	254.4	3.9	3.4	5,404	112.7
<b>Southern Shore</b>	630.9	9.6	10.3	4,486	93.6
Atlantic	241.8	3.7	3.4	5,183	108.1
Cape May	69.8	1.1	1.1	4,611	96.2
Ocean	319.3	4.9	5.8	4,049	84.5
<b>Rural South</b>	326.0	5.0	2.8	8,638	180.2
Cumberland	255.7	3.9	1.9	9,910	206.8
Salem	70.3	1.1	0.9	5,890	122.9
<i>Note: Figures may not sum due to rounding.</i>					
<i>Source: New Jersey Department of Education; Division of Local Government Services, New Jersey Department of Community Affairs.</i>					

**Table 11**  
**Municipal and County Aid by County and Region, Calendar Year 2003**

Region/County	CY03 Municipal Aid (\$millions)	Share of Municipal Aid	CY03 County Aid (\$millions)	Share of County Aid
<b>New Jersey Total</b>	<b>\$1,811.4</b>	<b>100.0%</b>	<b>\$765.6</b>	<b>100.0%</b>
<b>Mature Core Metropolis</b>	<b>797.5</b>	<b>44.0</b>	<b>357.8</b>	<b>46.7</b>
Essex	230.6	12.7	120.0	15.7
Hudson	197.8	10.9	71.6	9.4
Union	127.9	7.1	46.4	6.1
Bergen	138.8	7.7	62.4	8.2
Passaic	102.5	5.7	57.4	7.5
<b>Northern Exurban Fringe</b>	<b>35.6</b>	<b>2.0</b>	<b>19.8</b>	<b>2.6</b>
Sussex	18.0	1.0	10.0	1.3
Warren	17.6	1.0	9.8	1.3
<b>New Jersey's Wealth Belt</b>	<b>546.8</b>	<b>30.2</b>	<b>178.8</b>	<b>23.4</b>
Hunterdon	21.2	1.2	6.5	0.9
Mercer	135.2	7.5	31.5	4.1
Middlesex	165.1	9.1	54.7	7.1
Monmouth	110.6	6.1	43.3	5.7
Morris	68.6	3.8	25.1	3.3
Somerset	46.2	2.5	17.6	2.3
<b>Metro South</b>	<b>240.2</b>	<b>13.3</b>	<b>122.0</b>	<b>15.9</b>
Camden	137.2	7.6	70.1	9.2
Burlington	66.5	3.7	33.4	4.4
Gloucester	36.6	2.0	18.5	2.4
<b>Southern Shore</b>	<b>137.6</b>	<b>7.6</b>	<b>60.3</b>	<b>7.9</b>
Atlantic	42.0	2.3	23.1	3.0
Cape May	23.9	1.3	9.6	1.3
Ocean	71.7	4.0	27.6	3.6
<b>Rural South</b>	<b>53.7</b>	<b>3.0</b>	<b>26.9</b>	<b>3.5</b>
Cumberland	28.4	1.6	17.0	2.2
Salem	25.2	1.4	9.9	1.3
<i>Note: Figures may not sum due to rounding.</i>				
<i>Source: Division of Local Government Services, New Jersey Department of Community Affairs.</i>				

(see table 8). The six-county Wealth Belt region received 30.2 percent, or \$546.8 million, of the total municipal aid, and 23.4 percent, or \$178.8 million, of the total county aid. This region had 31.2 percent of the state's population in 2003. The three-county Metro South region received 13.3 percent, or \$240.2 million, of the total municipal aid, and 15.9 percent of the total county aid. That region had 14.2 percent of the state's population in 2003. The three-county Southern Shore region received 7.6 percent, or \$137.6 million, of the total municipal aid, and 7.9 percent, or \$60.3 million, of the total county aid. In 2003, this region had 10.5 percent of the state's population.<sup>24</sup>

### Fiscal Flows and Balances

Finally, table 12 provides a summary of state revenues and state expenditures across regions and counties. It is important to recall that only two state taxes are included in the analysis, representing 54 percent of all state revenues, and that the expenditures analyzed—school aid, municipal aid, and county aid—represent 37.8 percent of the state budget. Other state revenues, and significant amounts of other state expenditures (e.g., transportation, human services, corrections) are not included, in part because their attribution to county of origin, or their assignment to county of benefit, cannot be made with accuracy or is not relevant. Nevertheless, for the major taxes and expenditure categories included in this study, table 12 lists the balance of fiscal flows across the regions and counties of New Jersey.

Because of the dominant relation between income tax liabilities and income levels, as well as the positive relation between income levels and consumer expenditures (and hence sales tax liabilities), the

high-income counties and regions generate disproportionate (to their population) shares of state income and sales taxes. The Wealth Belt region, with 31.2 percent of the population, generated 42.4 percent of state sales and income taxes in 2003. No other region generated an income and sales tax share equal to, or greater than, its population share. The Mature Core Metropolis generated 34.7 percent of state income and sales tax revenues and had 38.5 percent of the state's population. However, Bergen County, with a population share of 10.4 percent, generated 13.9 percent of state income and sales tax revenues. The Metro South region provided 10.9 percent of the state's income and sales tax revenues and had 14.2 percent of its population. The Southern Shore region generated 8.2 percent of state income and sales taxes and had 10.5 percent of the state's population.

State expenditures, with its largest component, school aid, closely correlated in its allocation to income levels, also followed a progressive relation. The Wealth Belt received 23.9 percent of total aid while providing 42.4 percent of state revenues. All other regions received more aid, as a percentage of the total, than they provided in income and sales taxes. The Mature Core Metropolis received 42.8 percent of state aid and provided 34.7 percent of state income and sales taxes. Bergen County, again, was the sole (and significant) exception in this region. It received 4.8 percent of total aid and provided 13.9 percent of state income and sales tax revenues. The Metro South region received 16.9 percent of the aid and provided 10.9 percent of state income and sales taxes. The Southern Shore region received 9.1 percent of state aid and generated 8.2 percent of the state income and sales taxes.

<sup>24</sup> A regression between the log of municipal aid per capita and the log of per capita income across the 21 counties indicated no statistical relation. This is in distinct contrast to the regression reported for state school aid. A regression between the log of county aid per capita and the log of per capita income was significant, although the relation was not particularly strong (adjusted R-square of .35). The coefficient of the income variable was -.936 and significant ( $t = -3.5$ ). The size of the coefficient indicates that a 10 percent increase in county per capita income results in a 9.36 percent decrease in county aid per capita.

**Table 12**  
**State Aid versus Income and Sales Tax by County and Region, 2003**

Region/County	Population Share	Share of State Income and Sales Taxes <sup>a</sup>	Share of Total State Aid <sup>b</sup>
<b>Total</b>	100.0%	100.0%	100.0%
<b>Mature Core Metropolis</b>	38.5	34.7	42.8
Essex	9.2	7.6	13.4
Hudson	7.0	2.9	10.2
Union	6.1	6.1	6.8
Bergen	10.4	13.9	4.8
Passaic	5.8	4.2	7.6
<b>Northern Exurban Fringe</b>	3.0	2.5	2.9
Sussex	1.7	1.6	1.6
Warren	1.3	0.9	1.3
<b>New Jersey's Wealth Belt</b>	31.2	42.4	23.9
Hunterdon	1.5	2.5	0.9
Mercer	4.2	4.9	5.0
Middlesex	9.0	8.1	7.0
Monmouth	7.3	9.4	6.0
Morris	5.6	10.0	2.9
Somerset	3.6	7.5	2.0
<b>Metro South</b>	14.2	10.9	16.9
Camden	5.9	4.2	8.5
Burlington	5.1	4.7	5.0
Gloucester	3.1	2.0	3.4
<b>Southern Shore</b>	10.5	8.2	9.1
Atlantic	3.0	2.4	3.4
Cape May	1.2	1.1	1.1
Ocean	6.3	4.7	4.6
<b>Rural South</b>	2.5	1.3	4.5
Cumberland	1.7	0.9	3.3
Salem	0.8	0.4	1.2

Notes: Figures may not sum due to rounding.  
<sup>a</sup> Total income and sales taxes equal \$9.89 billion.  
<sup>b</sup> Total state aid (school, county, and municipality) equals \$9.11 billion.  
Source: Division of Taxation, New Jersey Department of the Treasury; Division of Local Government Services, New Jersey Department of Community Affairs.



## Conclusion

**O**ne conclusion of this analysis, with all the caveats expressed about the data—including what is and what is not included, as well as the cautions about the relatively high level of geographic aggregation of the analysis—is that New Jersey's tax and expenditure system is progressive. While significant amounts of state aid are allocated *not* based on income, the progressive tax structure—and particularly the income tax, combined with the progressive distribution of school aid—results in a net flow of resources from high-income counties and regions to lower-income counties and regions.

A second conclusion is that the state's revenue stream, and its ability to pursue a progressive expenditure program, is significantly dependent on the tax revenue flows it receives from a core group of high-income counties. However, these very counties have recently experienced sharp declines in their rates

of income growth. The deep fiscal constraints faced by New Jersey in fiscal years 2002 and 2003 were, in significant part, the result of the falloff in income growth in the Wealth Belt counties of Hunterdon, Somerset, and Morris, and in Bergen County in the Mature Core Metropolis—all counties that had been major sources of the tax-revenue growth during the boom of the late 1990s. With large fixed-expenditure commitments, particularly with respect to school financing, New Jersey's budget is significantly vulnerable to the negative economic effects of a recession, such as the downturn of 2001, that affects large concentrations of high-income individuals living in a relatively few core high-income counties.

Similar conclusions apply to Connecticut and New York, although this analysis does not examine these two states with the same level of scrutiny as New Jersey. In terms of broad patterns, however, the fiscal dependence on, and the flow of funds from, their affluent county jurisdictions are substantially the same. ■

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