PART II

EXPLANATION OF RECEIPT ESTIMATES

EXPLANATION OF RECEIPT ESTIMATES

In accordance with the requirements of Article VII of the State Constitution and section 22 of the State Finance Law, there is submitted herewith an explanation of the receipt estimates by fund type.

These estimates have been prepared by the Division of the Budget with the assistance of the Department of Taxation and Finance and other agencies concerned with the collection of State receipts. To the extent they are material, income sources not noted below are discussed in the presentations of the agencies primarily responsible for executing the programs financed by such receipts.

CASH RECEIPTS
ALL GOVERNMENTAL FUNDS
2002-2003
(millions of dollars)

	General Fund	Special Revenue Funds	Capital Projects Funds	Debt Service Funds	Total
Personal income tax	16,791	2,664	0	4,243	23,698
User taxes and fees	7,063	506	1,010	2,225	10,804
Sales and use tax	6,328	362	0	2,106	8,796
Cigarette and tobacco taxes	446	0	0	0	446
Motor fuel tax	0	69	356	119	544
Motor vehicle fees	67	75	470	0	612
Highway Use tax	0	0	147	0	147
Alcoholic beverages taxes	180	0	0	0	180
Alcoholic beverage control license fees	42	0	0	0	42
Auto rental tax	0	0	37	0	37
Business taxes	3,380	1,035	568	0	4,983
Corporation franchise tax	1,407	205	0	0	1,612
Corporation and utilities tax	860	231	0	0	1,091
Insurance taxes	704	72	0	0	776
Bank tax	409	72	0	0	481
Petroleum business tax	0	455	568	0	1,023
Other taxes	743	0	112	336	1,191
Estate tax	701	0	0	0	701
Gift tax	7	0	0	0	7
Real property gains tax	5	0	0	0	5
Real estate transfer tax	0	0	112	336	448
Pari-mutuel taxes	29	0	0	0	29
Other taxes	1	0	0	0	1
Total Taxes	27,977	4,205	1,690	6,804	40,676
Miscellaneous receipts	2,091	9,570	1,678	807	14,146
Federal grants	0	31,684	1,567	0	33,251
Total	30,068	45,459	4,935	7,611	88,073

CASH RECEIPTS
ALL GOVERNMENTAL FUNDS
2003-2004
(millions of dollars)

	General Fund	Special Revenue Funds	Capital Projects Funds	Debt Service Funds	Total
Personal income tax	15,791	2,835	0	5,457	24,083
User taxes and fees	7,897	601	1,074	2,244	11,816
Sales and use tax	7,178	400	0	2,244	9,822
Cigarette and tobacco taxes	419	0	0	0	419
Motor fuel tax	0	105	403	0	508
Motor vehicle fees	68	96	486	0	650
Alcoholic beverages taxes	184	0	0	0	184
Highway Use tax	0	0	147	0	147
Alcoholic beverage control license fees	48	0	0	0	48
Auto rental tax	0	0	38	0	38
Business taxes	3,395	1,022	566	0	4,983
Corporation franchise tax	1,382	188	0	0	1,570
Corporation and utilities tax	755	205	0	0	960
Insurance taxes	872	105	0	0	977
Bank tax	386	65	0	0	451
Petroleum business tax	0	459	566	0	1,025
Other taxes	784	0	112	338	1,234
Estate tax	752	0	0	0	752
Gift tax	0	0	0	0	0
Real property gains tax	4	0	0	0	4
Real estate transfer tax	0	0	112	338	450
Pari-mutuel taxes	27	0	0	0	27
Other taxes	1	0	0	0	1
Total Taxes	27,867	4,458	1,752	8,039	42,116
Miscellaneous receipts	5,970	10,396	2,690	694	19,750
Federal grants	645	34,921	1,621	0	37,187
Total	34,482	49,775	6,063	8,733	99,053

CASH RECEIPTS
ALL GOVERNMENTAL FUNDS
2004-2005
(millions of dollars)

	General Fund	Special Revenue Funds	Capital Projects Funds	Debt Service Funds	Total
Personal income tax	18,520	2,998	0	5,944	27,462
User taxes and fees	8,340	695	1,084	2,364	12,483
Sales and use tax	7,666	454	0	2,364	10,484
Cigarette and tobacco taxes	424	107	0	0	531
Motor fuel tax	0	134	411	0	545
Motor vehicle fees	25	0	481	0	506
Alcoholic beverages taxes	183	0	0	0	183
Highway Use tax	0	0	152	0	152
Alcoholic beverage control license fees	42	0	0	0	42
Auto rental tax	0	0	40	0	40
Business taxes	3,739	1,091	610	0	5,440
Corporation franchise tax	1,746	238	0	0	1,984
Corporation and utilities tax	657	191	18	0	866
Insurance taxes	912	109	0	0	1,021
Bank tax	424	72	0	0	496
Petroleum business tax	0	481	592	0	1,073
Other taxes	762	0	112	349	1,223
Estate tax	730	0	0	0	730
Gift tax	0	0	0	0	0
Real property gains tax	3	0	0	0	3
Real estate transfer tax	0	0	112	349	461
Pari-mutuel taxes	28	0	0	0	28
Other taxes	1	0	0	0	1
Total Taxes	31,361	4,784	1,806	8,657	46,608
Miscellaneous receipts	2,087	11,478	2,431	647	16,643
Federal grants	0	34,425	1,840	0	36,265
Total	33,448	50,687	6,077	9,304	99,516

CASH RECEIPTS
GENERAL FUND
2002-2003 THROUGH 2004-2005
(millions of dollars)

	2002-2003 Actual	2003-2004 Estimated	2004-2005 Recommended	2004-2005 Compared with 2003-2004
Personal income tax	16,791	15,791	18,520	2,729
User taxes and fees	7,063	7,897	8,340	443
Sales and use tax	6,328	7,178	7,666	488
Cigarette and tobacco taxes	446	419	424	5
Motor fuel tax	0	0	0	0
Motor vehicle fees	67	68	25	(43)
Alcoholic beverages taxes	180	184	183	(1)
Alcoholic beverage control license fees	42	48	42	(6)
Auto rental tax	0	0	0	0
Business taxes	3,380	3,395	3,739	344
Corporation franchise tax	1,407	1,382	1,746	364
Corporation and utilities tax	860	755	657	(98)
Insurance taxes	704	872	912	40
Bank tax	409	386	424	38
Petroleum business tax	0	0	0	0
Other taxes	743	784	762	(22)
Estate tax	701	752	730	(22)
Gift tax	7	0	0	0
Real property gains tax	5	4	3	(1)
Pari-mutuel taxes	29	27	28	1
Other taxes	1	1	1	0
Total Taxes	27,977	27,867	31,361	3,494
Miscellaneous receipts	2,091	5,970	2,087	(3,883)
Federal Grants	0	645	0	(645)
Total	30,068	34,482	33,448	(1,034)

CASH RECEIPTS
SPECIAL REVENUE FUNDS
2002-2003 THROUGH 2004-2005
(millions of dollars)

	2002-2003 Actual	2003-2004 Estimated	2004-2005 Recommended	2004-2005 Compared with 2003-2004
Personal income tax	2,664	2,835	2,998	163
User taxes and fees	506	601	695	94
Sales and use tax	362	400	454	54
Motor fuel tax	69	105	107	2
Motor vehicle fees	75	96	134	38
Business taxes	1,035	1,022	1,091	69
Corporation franchise tax	205	188	238	50
Corporation and utilities tax	231	205	191	(14)
Insurance taxes	72	105	109	4
Bank tax	72	65	72	7
Petroleum business tax	455	459	481	22
Total Taxes	4,205	4,458	4,784	326
Miscellaneous receipts	9,570	10,396	11,478	1,082
Federal grants	31,684	34,921	34,425	(496)
Total	45,459	49,775	50,687	912

CASH RECEIPTS
CAPITAL PROJECTS FUNDS
2002-2003 THROUGH 2004-2005
(millions of dollars)

	2002-2003 Actual	2003-2004 Estimated	2004-2005 Recommended	2004-2005 Compared with 2003-2004
User taxes and fees	1,010	1,074	1,084	10
Motor fuel tax	356	403	411	8
Motor vehicle fees	470	486	481	(5)
Highway Use tax	147	147	152	5
Auto Rental Tax	37	38	40	2
Business taxes	568	566	610	44
Corporation and utilities tax	0	0	18	18
Petroleum business tax	568	566	592	26
Other taxes	112	112	112	0
Real estate transfer tax	112	112	112	0
Total Taxes	1,690	1,752	1,806	54
Miscellaneous receipts	1,678	2,690	2,431	(259)
Federal grants	1,567	1,621	1,840	219
Total	4,935	6,063	6,077	14

CASH RECEIPTS
DEBT SERVICE FUNDS
2002-2003 THROUGH 2004-2005
(millions of dollars)

	2002-2003 Actual	2003-2004 Estimated	2004-2005 Recommended	2004-2005 Compared with 2003-2004
Personal income tax	4,243	5,457	5,944	487
User taxes and fees	2,225	2,244	2,364	120
Sales and use tax	2,106	2,244	2,364	120
Motor fuel tax	119	0	0	0
Other taxes	336	338	349	11
Real estate transfer tax	336	338	349	11
Total Taxes	6,804	8,039	8,657	618
Miscellaneous receipts	807	694	647	(47)
Total	7,611	8,733	9,304	571

ECONOMIC BACKDROP

OVERVIEW

Following six quarters of uncertain fortune, the U.S. economy finally appears to be on a sustainable expansionary path. The 20 months following the end of the 2001 recession represent one of the most unusual recovery periods of the postwar era, combining high productivity gains with low output growth and falling employment. The recovery exhibited sporadic signs of life — growth in real U.S. GDP of 4.7 percent in the first quarter of 2002, a rise in industrial production for every month between January and June 2002, and rising employment toward the end of 2002, including the addition of 158,000 jobs in January 2003 — but never gained momentum. However, by the summer of 2003, an array of indicators showed broad-based strength and, finally, a sustained rise in employment. Indeed, the third quarter of 2003 produced the fastest quarterly growth rate in real GDP in almost 20 years.

Why did the U.S. economic recovery take so long to find its footing? Since the simultaneous collapse of equities and the high-tech sector in 2000, the national economy absorbed three additional but distinct shocks: the September 11 terrorist attacks, a string of corporate governance scandals, and the war in Iraq and its aftermath. These events created an environment of uncertainty that lengthened the period of adjustment for the business sector from the unrealistic expectations of the late 1990s. However, the mood of the business sector contrasted starkly with the behavior of households. Thus, declining employment and an absence of business spending coincided with record-breaking sales in the interest-sensitive housing and auto markets.

Following an unusually sluggish recovery period, the U.S. economic expansion now appears to be on track. Low interest rates, low inflation, a booming housing market, and expansive fiscal policy combined in the middle of 2003 to increase confidence within the business sector, which has finally demonstrated a long-awaited impetus to spend. Moreover, the Federal Reserve has signaled a willingness to remain accommodative and fiscal policy will remain expansionary throughout 2004. Consequently, the Budget Division believes that the U.S. economy is soundly upon a path of sustainable growth. Strong real GDP growth of 4.7 percent is projected for 2004, following growth of 3.1 percent for 2003.

The New York State economy is slowly emerging from recession. A number of indicators and business sentiment surveys show that the overall State economy is indeed at a turning point. Though the legacy of the September 11 attack is still evident in New York City, where employment remains down on a year-over-year basis, employment losses have stabilized and growth is evident in some sectors. Moreover, with the first sustained rise in equity prices in three years and low interest rates, the profit outlook for the finance industry has brightened. Total New York wages are expected to grow 5.1 percent in 2004, the best performance in four years. State nonagricultural employment is projected to rise 0.8 percent in 2004, slightly below projected growth for the nation of 1.1 percent.

THE NATIONAL ECONOMY

The recession of 2001 and the ensuing recovery were atypical of the postwar period. The seeds of past recessions were often sown by an overheating economy and accelerating inflation, which induced the Federal Reserve to put on the brakes by raising interest rates.[1] Higher rates would in turn reduce household demand and a recession would eventually follow. Although the Federal Reserve's rate hikes during the second half of 1999 and the first half of 2000 did engender a mild downturn in the interest rate-sensitive areas of spending in

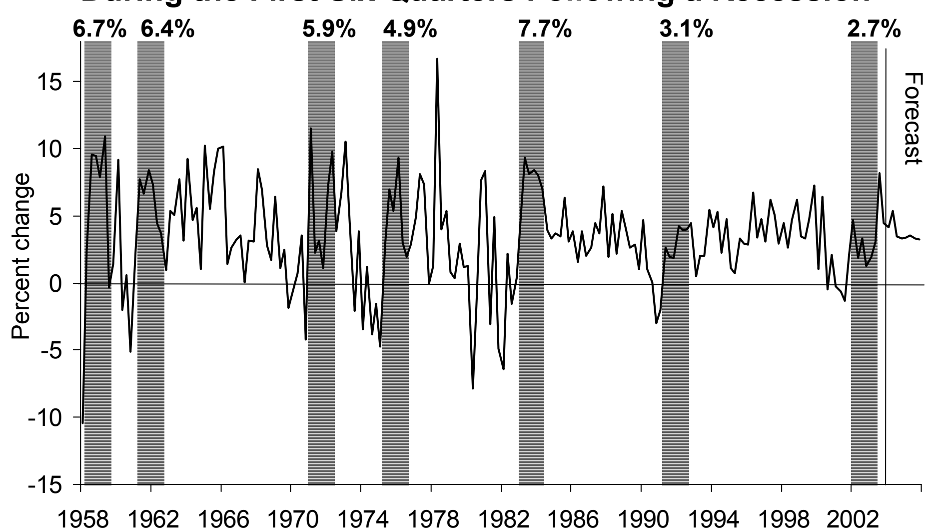
[1] Of course, each business cycle has its own unique traits, often related to idiosyncratic shocks such as the oil price increases in the 1970s.

2000 — indeed, revised data indicate that real U.S. GDP fell 0.5 percent during the third quarter — the overall impact of the monetary tightening was expected to be relatively mild, perhaps another "soft landing" as the Federal Reserve had successfully engineered in 1994-95. However, hopes for a soft landing dimmed after September 11, and, unlike in the typical postwar case, the business sector led the economy into a full-fledged recession. Nevertheless, the 2001 recession was mild as measured by the decline in real output, largely due to the rapid response of monetary policy to the slowdown. Had the Federal Reserve not cut rates early and sharply starting in January 2001, stimulating activity in the housing and auto markets, the recession would likely have been both deeper and more prolonged.

Though the 2001 recession was mild, the early stage of the recovery was unusually weak, comparable only to the beginning of the 1990s expansion (see Figure 1). No sooner did the recession end than a series of corporate governance scandals dealt a blow to an economy still reeling from September 11. Later in 2002, the economy was further shaken by the emerging conflict with Iraq. These events had the effect of delaying the rebound that typically occurs in the early stages of an economic recovery. Falling equity prices and global uncertainty focused the business sector on improving profits by cutting costs at the expense of both employment and investment growth. Moreover, the fact that consumption never actually declined during the recession meant less pent-up demand entering the recovery. This resulted in slow growth combined with falling employment through the second quarter of 2003. However, with inventories now sufficiently pared, business sector confidence increasing, low interest rates and fiscal stimulus in place, and a global economy on the verge of a rebound, the U.S. economic recovery finally appears to be on track.

Figure 1

Real U.S. GDP Growth During the First Six Quarters Following a Recession



Note: Shaded areas represent the six quarters following the last seven US recessions, excluding the 1980 recession; numbers above bars show average annualized rate of quarterly job growth over the six quarters.
Source: Economy.com.

Because the usual economic rebound following a recession was delayed, all of the risks inherent in forecasting at or near business cycle turning points apply today. The lags with which economic data become available and the extent to which these data subsequently get revised are important parts of the problem. When the economy turns downward, preliminary attempts to measure economic activity tend to overestimate the strength of the economy. The opposite is often true for the recovery phase. Moreover, as the last two years have demonstrated, the economy is particularly vulnerable to shocks during a recovery. This is partly due to the fragility of business sentiment and consumer confidence at this stage of the business cycle. Finally, the impact of changes in public policy, such as the tax cuts passed in 2003, are notoriously difficult to estimate, both with respect to timing and magnitude. The size of the impact depends on how much consumers choose to spend and when. Moreover, Federal legislation passed in May 2003 reduced income tax rates retroactively to January of that year. The timing of the stimulus then depends on how workers adjust their behavior in response to the new tax schedules.

Table 1 shows Blue Chip consensus forecasts for real GDP growth (GNP if prior to 1992) published in January for the year just started and compares those forecasts to the actual growth rates for the same year. The "actuals" shown in the table are based on the very first estimate of the fourth quarter released by the U.S. Bureau of Economic Analysis (the "advance release"), since it is difficult for forecasters to anticipate future revisions in the underlying economic data. As Table 1 indicates, when the economy turns down, economists tend to overestimate real output growth and as the economy turns up they tend to underestimate growth.[2] The most recent recession and subsequent recovery are good examples. The January 2001 Blue Chip consensus forecast was 1.5 percentage points higher than the actual for that year, while the forecast for 2002 was 1.3 percentage points too low. These data suggest that there may be a tendency to underestimate the strength of the economic rebound that is now underway.

TABLE 1
FORECASTING ACCURACY NEAR TURNING POINTS

Forecast Year	Current Year Output Forecast	Actual (Advance Release)	Error
1980-1982 Recessions			
1980	-1.0	-0.1	-0.9
1981	0.7	2.0	-1.3
1982	0.3	-1.8	2.1
1983	2.5	3.3	-0.8
1984	5.8	6.8	-1.0
1990-1991 Recession			
1990	1.0	0.9	0.1
1991	0.0	-0.7	0.7
1992	1.6	2.1	-0.4
1993	2.9	2.9	-0.1
2001 Recession			
2001	2.6	1.1	1.5
2002	1.1	2.4	-1.3
2003	2.8	3.1	-0.3

Note: The error is defined as forecast minus actual.
Source: Blue Chip Consensus, January, various years; Federal Reserve Bank of Philadelphia.

The evidence presented below suggests that the current recovery will be sustained throughout the forecast period. The climate of uncertainty appears to have subsided and business confidence appears to be improving. The rebuilding of inventories is likely to require increased demand for workers. Firms are already starting to replace obsolete computer equipment and there is evidence that capacity shortfalls may be emerging in other areas. Moreover, equity prices are rising in response to brisk profit growth and monetary policy is expected to remain accommodative. Rising household demand is expected to be supported by rising employment and incomes, buttressed by the continued impact of the 2003 tax cuts. Finally, the combined impact of a moderately falling dollar and accelerating growth for the world economy is expected to increase the demand for U.S. exports, although on balance, the trade deficit is projected to widen in 2004.

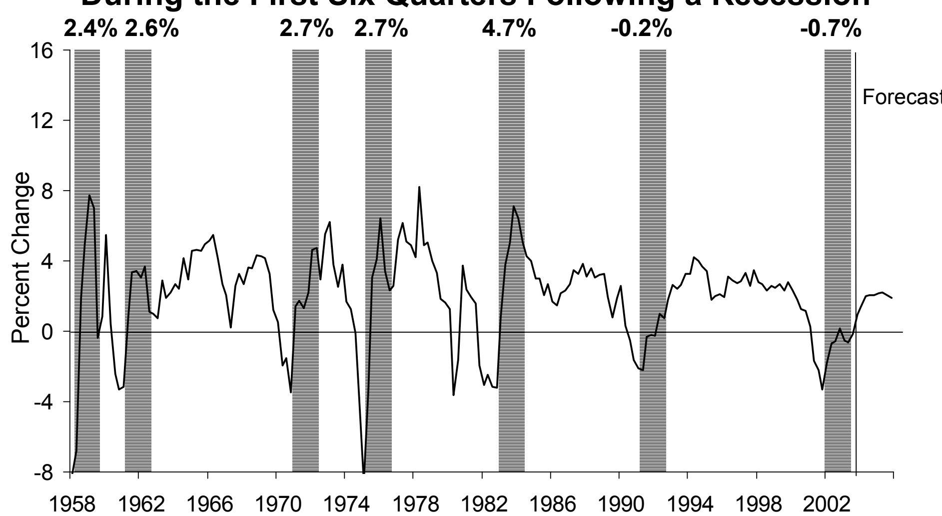
[2] The 1980 recession is not as much of an exception as it appears, since it lasted only through the first six months of the year.

The Longest Labor Market Turning Point

Although the National Bureau of Economic Research (NBER) Business Cycle Dating Committee declared November 2001 as the trough of the 2001 recession, U.S. employment continued to decline during most of 2002 and 2003. This fact distinguishes the beginning of the current recovery from most prior postwar recoveries (see Figure 2). Although the aftermath of the 1990-91 recession has often been referred to as a "jobless" recovery, payroll survey data indicate that the 2001 recession was followed by a "job-loss" recovery (see Box 1). More than two years after the November 2001 trough, private sector employment is still almost one million below its November 2001 level (see Table 2). Indeed, this lengthy period of job declines led the Committee to wait an unusually long 20 months before declaring a trough at November 2001. Many factors contributed to the economy's continued loss of jobs during the recovery. However, the shocks the economy sustained during the period — September 11, corporate governance scandals, and the war in Iraq — and the uncertainty they engendered, appear to be the most important explanation and the one best supported by the data. With the impact of these shocks now dissipating, the environment is likely to be much more favorable to job growth going forward.

Figure 2

Private Nonfarm Employment Growth
During the First Six Quarters Following a Recession



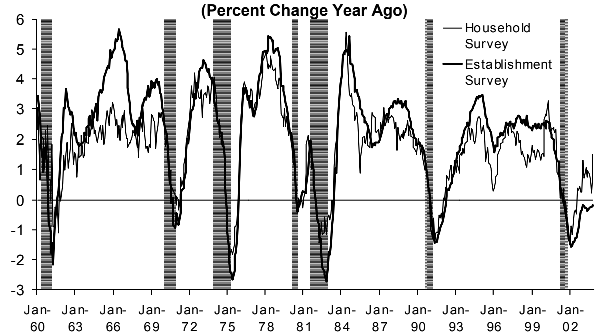
Note: Shaded areas represent the six quarters following the last seven US recessions, excluding the 1980 recession; numbers above bars show average annualized rate of quarterly job growth over the six quarters.
Source: Economy.com.

BOX 1
THE EMPLOYMENT PUZZLE

Two startlingly different portraits of national employment emerge when comparing two alternative sources of data published by the U.S. Bureau of Labor Statistics. The source most often cited by economists who forecast employment is the Establishment Survey, which samples the payroll reports of about 400,000 firms across the country under the Current Employment Statistics (CES) program. Since it is an enumeration of jobs, an individual with two jobs would be counted twice. An alternative measure of employment comes from the Current Population Survey (CPS) of about 60,000 households, commonly known as the household survey, which is the primary data source for labor force and unemployment rate data. Because the CPS is most concerned with the employment status of a member of a household, an individual with more than one job is counted only once.

The chart below indicates that it is not unusual for these two data sources to diverge substantially in their measure of job growth. Although on average, payroll employment tends to grow faster, during and immediately following a recession, household survey employment tends to exhibit the higher growth rate. This has been true for all recessions since World War II, and the current post-recession period is no exception. Thus, historical evidence suggests that the more rapid pace of employment growth exhibited by the household survey data can be expected to be matched, and eventually surpassed, by faster growth on a payroll basis, once the recovery has gathered steam.

Total U.S. Employment
Establishment and Household Surveys
(Percent Change Year Ago)



Note: Establishment survey data suggest that employment has fallen since the recession officially ended. However, according to the household survey, employment grew during the same period.
Source: Economy.com.

However, the magnitude of the difference since the end of the 2001 recession has been substantially larger than the historical norm of about one-half of one percentage point. In fact, the difference between the two measures recently exceeded one percentage point, a magnitude reached briefly only twice during the postwar period. This difference has persisted for more than a year, a duration that is unparalleled in the last 45 years.

The current recovery has been labeled a “job-loss recovery,” for until the last few months, employment as measured by the payroll survey continued to decline even after output growth had resumed. This is the worst post-recession job performance since World War II; only the recovery from the 1990 recession is at all comparable, and in that case employment growth hovered around zero but did not decline. In contrast, the household survey data indicate that employment has been trending upward since early 2002 and currently exceeds its prior 2000 peak. Even after adjusting for the design differences between the two surveys, a discrepancy of 2.2 million jobs remains. The most recent household survey data indicates that by December 2003, civilian employment was 840,000 above its March 2001 level.

Several explanations for the source of the difference have been advanced. One is that in an effort to minimize costs, firms may be hiring more individuals on a contract basis to avoid commitments and fringe benefit costs. If such individuals were self-employed, they would be counted in the household data, but not in the payroll count. It has also been suggested that the Census Bureau has been overestimating immigration, and therefore the entire population, since the most recent decennial census.[1] Since population estimates are used to inflate the household survey results to population totals, an overestimate of the population would produce an overestimate of employment as well.

[1] The Federal Reserve Board, “The Jobless Recovery”, remarks by Governor Ben S. Bernanke at the Global Economic and Investment Outlook Conference, Carnegie Mellon University, Pittsburgh, Pa., November 6, 2003 at <http://www.federalreserve.gov/boarddocs/speeches/2003/2003110662/default.htm>.

TABLE 2
CHANGE IN U.S. EMPLOYMENT 25 MONTHS AFTER BUSINESS CYCLE TROUGH

Trough Date	Cumulative Change in Employment Since Trough: Level (000s)		Percent Change	
	Total	Private	Total	Private
Oct-45	5888	6157	15.3%	18.8%
Oct-49	5199	4543	12.1%	12.3%
May-54	3618	3080	7.4%	7.3%
Apr-58	3446	2882	6.8%	6.7%
Feb-61	2766	2108	5.2%	4.7%
Nov-70	4861	4007	6.9%	7.0%
Mar-75	5081	4760	6.6%	7.7%
Jul-80	(480)	8	-0.5%	0.0%
Nov-82	7317	7012	8.2%	9.6%
Mar-91	1681	1231	1.5%	1.4%
Nov-01	(776)	(907)	-0.6%	-0.8%

Source: Economy.com.

The reason most often cited for the "job-loss recovery" is the particularly high productivity growth experienced during and after the 2001 recession. Figure 3 shows average productivity growth over the first six quarters after each of the last seven recessions (excluding the short 1980 recession). The figure indicates that productivity growth during the period was robust, but not unprecedented. Indeed, the productivity growth observed during the six months following the 2001 recession might be identified as a return to normalcy following the exceptionally low productivity growth rates that followed the recession of 1990-91.

It has also been suggested that when the unemployment rate fell to 3.9 percent in the middle of 2000, employment had risen to a level that the economy could not sustain over the long run. Believing that the 1990s "New Economy" expansion would be virtually endless, firms hired more workers than long-term conditions could justify. However, "over-hiring" alone cannot justify the decline in employment experienced during the current expansion. By one definition, the sustainable level of employment is the level that is consistent with a 5 percent unemployment rate and a 67 percent labor force participation rate.[3] By that standard, the high level of employment attained at the expansionary peak was indeed unsustainable. However, the current employment level remains over 3 million below the sustainable level so defined. In addition, a comparison of actual employment with the Budget Division's estimate of potential employment indicates that the degree of over-hiring just prior to the 2001 recession was less than that which occurred before the 1990-91 recession.

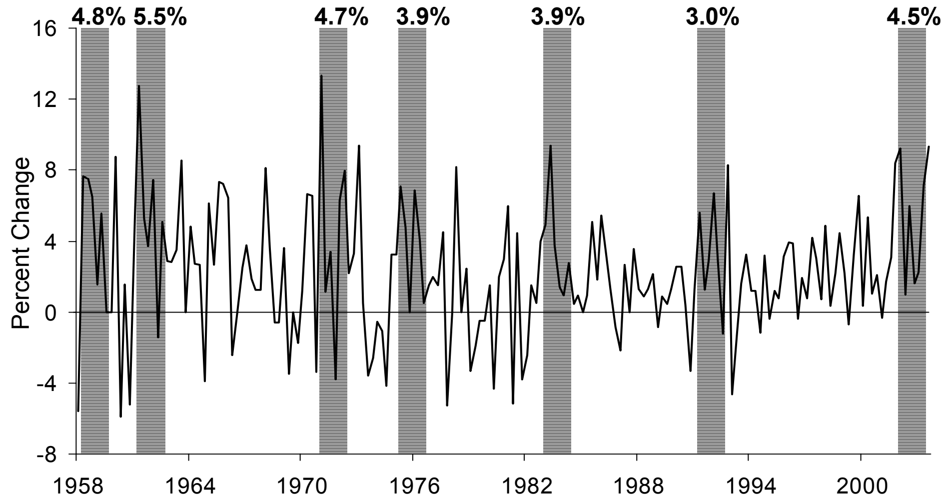
One study proposes structural change in the labor market as another explanation for the job-loss recovery.[4] Starting from the premise that industry restructuring often accelerates during a recession, the study's authors define job losses that occurred during the recession as permanent if they occurred within industries that continued to lose jobs during the expansion. In contrast, losses from industries that subsequently resumed growth are deemed to be temporary. The authors judge a large percentage of the job losses that occurred during the 2001 recession to have been permanent, forcing those who were laid off to find jobs in other industries. Thus, they conclude that structural change was a major contributor to the recent "job-loss recovery."

[3] See remarks by Governor Ben S. Bernanke delivered on November 6, 2003: <http://www.federalreserve.gov/boarddocs/speeches/2003/200311062/default.htm>

[4] See Erica L. Groshen and Simon Potter, "Has Structural Change Contributed to a Jobless Recovery?" Federal Reserve Bank of New York, *Current Issues in Economics and Finance*, Vol. 9, no. 8, August, 2003.

Figure 3

Nonfarm Business Productivity Growth During the First Six Quarters Following a Recession



Note: Productivity is measured as output per hour. Shaded areas represent the six quarters following the last seven US recessions, excluding the 1980 recession; numbers above bars show average rate of annualized quarterly growth over the six quarters.
Source: Economy.com.

The structural change argument raises the question as to why a relatively mild recession in terms of output growth would generate such a large degree of restructuring. In addition, the business sector underwent a substantial restructuring during and after the 1990-91 recession, but the economy still gained over one million jobs by the end of the second year of the recovery. This explanation also fails to address the uneven pattern of growth across industries during the recession. For example, the simultaneous decline of manufacturing jobs and increase in mortgage-lending jobs may not signal a restructuring as mush as the fact that while the manufacturing sector was in a recession, the housing sector was booming. Indeed, that boom has begun to ebb; the number of jobs in credit intermediation decreased in November for the second consecutive month, reflecting the falling demand for mortgage refinancing services. From July 2000 through September 2003, the industry had added a total of 251,000 jobs. From this evidence it appears that the simultaneous job losses from manufacturing and gains in mortgage lending represent the unique business cycles in those industries rather than restructuring.

It has also been suggested that the increasing globalization of the economy contributed to the job-loss recovery, an explanation that is closely related to the restructuring argument. It is true that a growing magnitude of the goods purchased in the U.S. is imported. In 1947, the ratio of imported goods to total goods output, both adjusted for price changes, was 6.8 percent. That ratio rose to 11.3 percent in 1967 and to 35.6 percent in 2003. However, due to the cyclical nature of international trade, imports actually fell during the recession and the early part of the recovery (see Figure 18).

The increasing cost of worker benefits has also been linked to job losses. Since 1980, the wage and salary portion of total compensation has risen 146 percent while the benefits portion has grown 216 percent, largely due to the rising cost of healthcare. This trend might induce reluctance among firms to hire permanent full-time workers, particularly during a time of uncertainty about business conditions. Firms might prefer to hire temporary workers, make existing employees work longer hours, or outsource to developing countries where wages are much lower. However, temporary help services employment also fell during much of the first

15 months of the recovery, and the average length of the private sector workweek has been remarkably stable.[5] Moreover, there is to date no evidence that the degree of outsourcing is sufficient to explain more than a small portion of the joblessness of the last two years.

Although all of the above factors may have contributed to the loss of over one million jobs in the 20 months following the official end of the 2001 recession, perhaps the most powerful factor is the financial and geopolitical uncertainty that clouded the business climate. The increased volatility in several key economic indicators during the first six quarters of the economic expansion strongly underlines the substantial uncertainty of the economic environment. As Figure 4 indicates, the perception of the business climate tends to be associated with the decision to create and eliminate jobs.[6] The business climate soured in the wake of September 11 and the corporate governance scandals that followed, with job losses intensifying at the end of 2001 and early 2002. Toward the middle of the year, the rate of job loss fell and even turned to gains in the fall. However, the run-up to the war in Iraq had a negative impact on business sentiment and those meager job gains became losses once again at the end of 2002 and the first half of 2003. As indicated in Figure 5, the uncertain climate similarly affected all areas of private business spending, including investment in equipment, software, and inventories.

With the nation becoming acclimated to long-term military engagement and the winding down of new announcements of corporate malfeasance, both business sentiment and consumer confidence appear to be on the upswing.[7] In addition, fiscal policy stimulus helped the third quarter of 2003 put forth the best economic performance in almost 20 years and a strong fourth quarter is expected as well. Additional fiscal policy stimulus in 2004 combined with continued accommodative monetary policy should ensure that, absent any further shocks, the recovery will continue to gain momentum and that the demand for labor will increase. The Budget Division is forecasting growth in U.S. employment of 1.1 percent for 2004, following a decline of 0.2 percent for 2003.

Improved prospects for employment growth will provide a boost to income growth as well. Wages and salaries are projected to grow 4.4 percent in 2004, following growth of only 2.1 percent in 2003. Total personal income is expected to grow 4.7 percent in 2004 following growth of 3.3 percent in 2003, outpacing growth in wages alone due to strong expected growth in several of the non-wage components of personal income including transfer payments, proprietors' income, and dividends. The forecasts for personal income and wage growth are below their respective historical averages (see Table 10), largely due to low inflation.

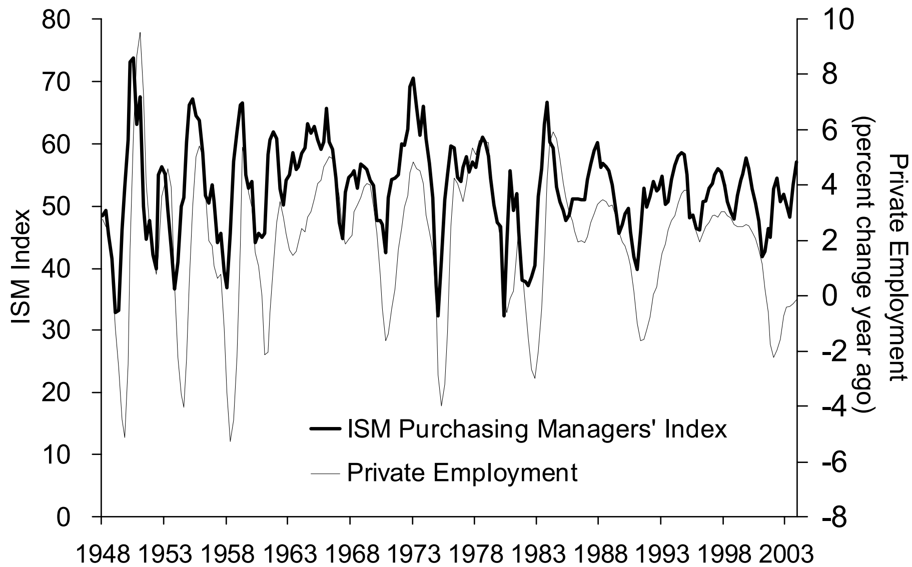
[5] For a comment on the BLS measure of the length of the average workweek, please see Stephen S. Roach, "The Productivity Paradox," *The New York Times*, November 30, 2003, Section 4.

[6] The Institute for Supply Management's (ISM) manufacturing Purchasing Managers' Index is a composite index based on seasonally adjusted diffusion indexes for five indicators: new orders, production, employment, supplier deliveries, and inventories. Based on qualitative response data collected from member firms, these indexes can be interpreted as indicators of manager sentiment. A statistical analysis indicates that private sector employment and the ISM manufacturing index are significantly related.

[7] It remains to be seen if the mutual fund scandal will have a disruptive effect on financial markets or simply be taken in stride.

Figure 4

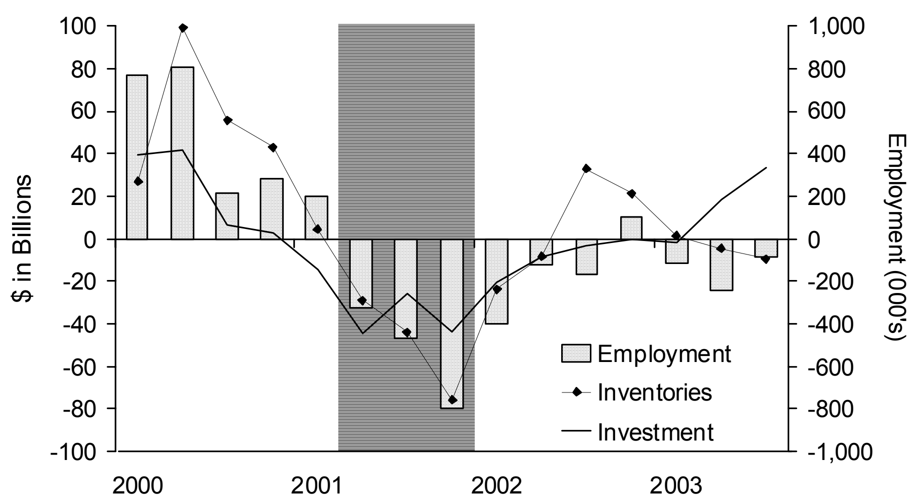
Business Confidence and Private Sector Employment



Source: Economy.com.

Figure 5

Changes in Employment, Nonresidential Fixed Investment, and Business Inventories



Note: Shaded areas represent the three quarters of the 2001 recession according to NBER.
Source: Economy.com.

Business Spending Due for a Rebound

The delayed rebound in economic activity is just as evident in investment spending as in employment. The two most important factors explaining the unusual behavior of business investment during the early phase of the current expansion are the excess capacity left over from the investment boom of the late 1990s and the extraordinary level of uncertainty facing those making capital investment decisions. Business investment appears finally to have begun to recover, with back-to-back increases in the second and third quarters of 2003. Given the short investment cycle for computers and related equipment, and the aging of the rest of the capital stock, we can expect sustained increases in business investment spending during the forecast period. This growth will be supported by continued low interest rates and tax investment incentives due to expire at the end of 2004.

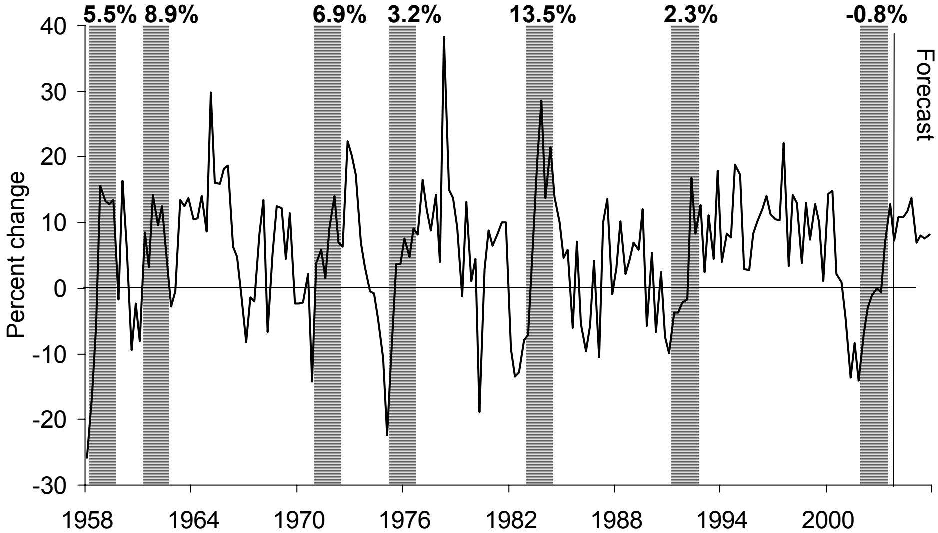
In analyzing business spending behavior over the long run, it is assumed that firms choose a level of investment that achieves an optimal relationship between the stock of capital and the level of output or sales.[8] If the business sector's outlook for economic growth improves, then firms will expect to produce more output, which in turn requires more capital, and investment spending will rise. Since, in the short-run, the capital stock can be adjusted only gradually, firms are continually making adjustments to get closer to the optimal relationship between capital and output. The short-run behavior of investment also varies with the cost of acquiring and using capital goods. The latter factor, commonly referred to as the user cost of capital, is affected by prices of new investment goods, inflation-adjusted borrowing costs, equity prices, the rate of capital depreciation, and the extent to which the tax code subsidizes or penalizes investment. Investment thus depends on a combination of objective economic factors, such as interest rates and equipment prices, and more subjective and forward-looking factors, such as expectations for the future. All of these factors are important to understanding investment behavior prior to, during, and subsequent to the 2001 recession.

During the six quarters immediately following the 2001 recession, investment spending was weaker than during earlier postwar recoveries (see Figure 6). Prior to 1990, the typical post-World War II recession was led by declines in household spending in response to higher interest rates, particularly on housing and consumer durables. But as discussed below, household spending on homes and automobiles held up well during the 2001 downturn. The recessions of 1990-91 and 2001 were instead led by a decline in business spending, which continued to decline even after the NBER-designated trough date. However, the decline in nonresidential fixed investment during the most recent downturn was much sharper and more prolonged than in the early 1990s.

The investment boom of the late 1990s left significant excess capacity in its wake. By late 2000, the generalized sense of optimism that had pervaded the latter part of the 1990s was waning. Many firms had just completed their Y2K adjustments, and so their replacement cycles for computers and software suddenly lengthened. The Federal Reserve's interest rate increases in the second half of 1999 and the first half of 2000 combined with lower equity prices to raise the user cost of capital. As dot-coms and telecommunications providers failed, competitive pressures to maintain technological leadership faded and demand for additional technology investment declined. Under diminished expectations for future sales, what earlier had been perceived as a sound investment became "capacity overhang," inducing firms to curtail their investment spending.

[8] Optimal investment is the level that maintains the profit maximizing or cost minimizing capital output ratio. With a Cobb - Douglas production function, the optimal capital output ratio will be equal to the ratio of the price of output to the rental rate of capital. Given this optimal ratio, optimal investment varies with output growth and the rental rate of capital.

Figure 6
Growth in Nonresidential Fixed Investment
During the First Six Quarters Following a Recession



Note: Shaded areas represent the six quarters following the last seven US recessions, excluding the 1980 recession; numbers above the bars show the average annualized rates of quarterly growth over the six quarters.
Source: Economy.com.

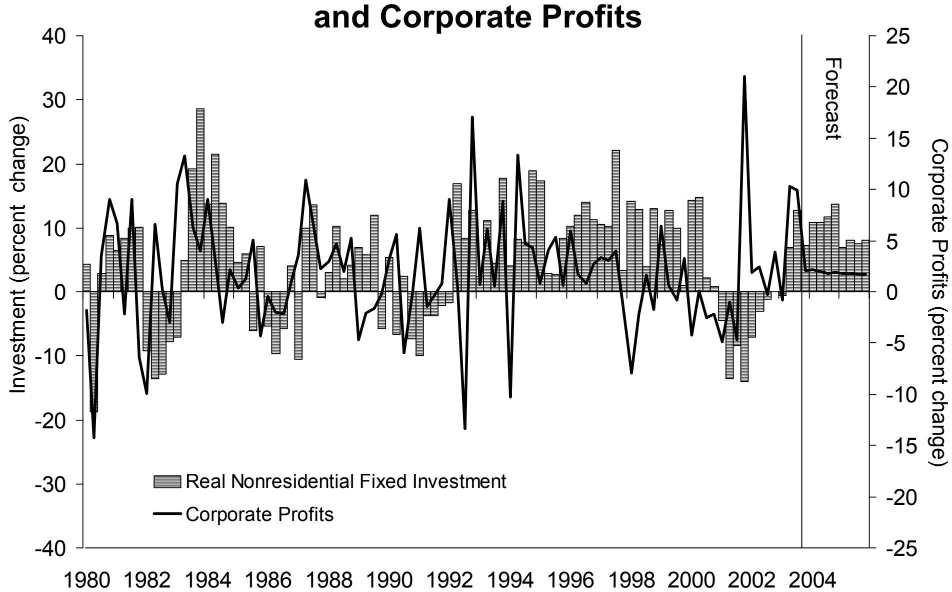
With each successive shock to the economy — the terrorist attacks of September 2001, revelations of corporate governance scandals, and the conflict in Iraq — the business climate deteriorated further, causing businesses to postpone capital spending. The positive investment growth of the fourth quarter of 2002 turned negative in the first quarter of 2003, as did inventories during the following quarter (see Figure 5). Investment was weak during the early phase of the recovery period despite federal tax policies designed to stimulate business spending.[9] The data indicate that business fixed investment remained weak until after the resolution of the Iraq crisis. Although econometric evidence suggests that profit growth tends to lead investment, the weakness during 2002 and early 2003 cannot be attributed to poor profits since corporate profits have exhibited robust growth since early 2002 (see Figure 7). This growth has been mainly due to aggressive cost cutting.

[9] The "Job Creation and Worker Assistance Act of 2002," (JCWA) signed into law in early March 2002, created a 30-percent first-year "bonus depreciation" on capital equipment acquired during the three years following September 11, 2001. This is in addition to regular depreciation. The law also allowed small businesses to expense the purchase of "qualified property" rather than depreciate it. For 2001 and 2002, up to $24,000 worth of depreciable assets could be expensed. The "Jobs and Growth Tax Relief Reconciliation Act of 2003" (JGTRRA), passed in May 2003, contained additional incentives for business investment, including a quadrupling of the amount of "qualified property" small businesses could expense and an increase in the rate of "bonus depreciation" to 50 percent for property acquired after May 5, 2003 and placed in service before January 1, 2004. Under the law, small businesses can now expense up to $100,000 in "qualified property" purchased through the end of 2005. The definition of "qualified property" was also amended to include off-the-shelf computer software.

In an attempt to quantify the extent of the capacity overhang in the U.S. economy, one study notes that during the 1961-1969 expansion, real business fixed investment increased 95 percent while real GDP increased 51 percent. During the 1982-1990 expansion, real investment rose 42 percent with real GDP rising about 37 percent. But during the expansion of 1991-2001, real business fixed investment climbed 113 percent while real GDP rose only about 39 percent.[10] Another study finds a substantial overhang only in telecommunications and information-processing equipment, and concludes that by 2002 what remained of the overhang was too small to significantly inhibit investment spending growth in the future.[11]

Figure 7

Growth in Real Nonresidential Fixed Investment and Corporate Profits



Note: Corporate profits growth rate is not annualized.
Source: Economy.com; DOB staff estimates.

Looking forward, several factors will help to insure that investment spending continues to grow. Interest rates are expected to remain relatively low. With business confidence increasing, firms can be expected to respond positively to fiscal policy incentives, such as bonus depreciation and full expensing. Real investment in computers and peripheral equipment has been growing since the fourth quarter of 2001, reflecting its unique replacement cycle. Indeed, as computers continue to account for an ever-increasing share of the capital stock, their accelerated pace of depreciation ensures that average investment growth will continue to grow over time. While investment in structures and other sectors has lagged, the aging of the existing capital stock suggests that capital shortfalls may be developing in some areas. Figure 8 compares actual and forecast values of private nonresidential investment in capital equipment, excluding computers and computer-related goods, to an estimate of the optimal level. The figure suggests that a situation of overcapacity has become one of undercapacity. Although excess capacity remains in select industries, it is deemed insufficient to significantly inhibit future growth. The Budget Division projects growth of 10.6 percent in real nonresidential fixed investment for 2004, following growth of 2.5 percent in 2003.

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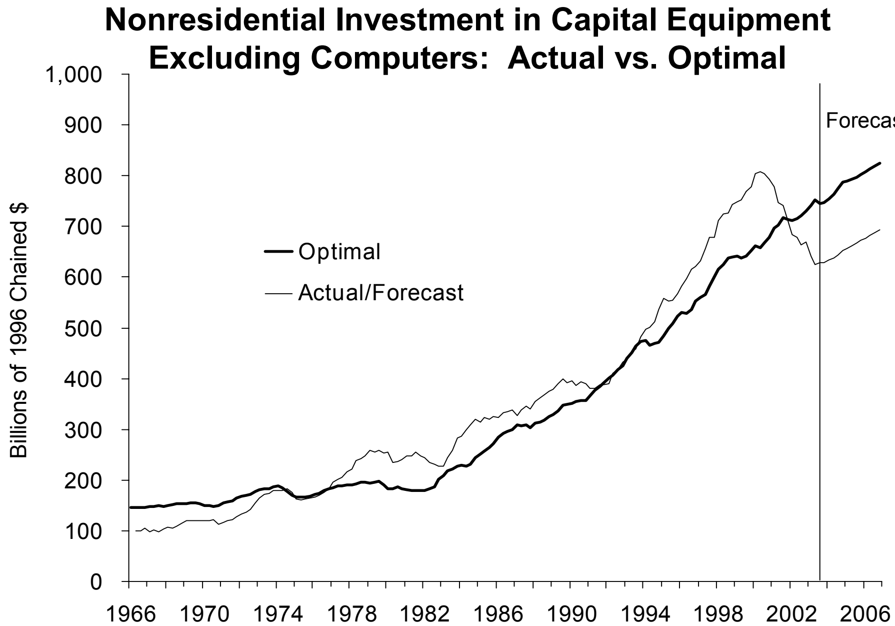
[10] Kevin L. Kliesen, "Waiting for the Investment Boom? It Might Be a While," *National Economic Trends,* May 2003, The Federal Reserve Bank of St. Louis.

[11] Eric French, Thomas Klier and David Oppedahl, "Is There Still an Investment Overhang, and if so, Should We Worry About It?" *Chicago Fed Letter*, Special Issue, Number 177a, May 2002, The Federal Reserve Bank of Chicago. The analysts use four methods to try to measure the extent of the capital overhang. One measure indicated no capital overhang, while the other three showed some overhang.

Figure 8



Source: Economy.com; DOB staff estimates.

Outlook For U.S. Corporate Profits And The Stock Market

Projected rates of investment growth will be supported by solid growth in corporate profits. As indicated in Figure 7, corporate profits from current production (including the capital consumption and inventory valuation adjustments) have been quite strong since the beginning of 2002. Indeed, corporate profits growth for 2002 was revised up by 9.7 percentage points during the most recent comprehensive revision of the National Income and Product Accounts (NIPA) data (see Box 2). On a year-over-year basis, corporate profits have exhibited strong growth for eight consecutive quarters. Early in 2002, profit growth was led by financial firms, which account for about 40 percent of total domestic corporate profits, and by wholesale and retail trade firms, which together account for about an additional 10 percent. Profits in other industries have been showing either low growth or declines, with durable manufacturing exhibiting the worst performance. Later in 2002 and early 2003, financial and trade firm profits deteriorated, while nondurable manufacturing and “other” industries started to improve. With productivity growth expected to remain robust, the Budget Division projects growth of 15.1 percent in corporate profits from current production for 2004, following growth of 18.7 percent in 2003.

BOX 2

2003 COMPREHENSIVE REVISION OF THE NATIONAL INCOME AND PRODUCT ACCOUNTS[1]

In December 2003, the Bureau of Economic Analysis released its 12th comprehensive revision of the national income and product accounts (NIPA). The comprehensive revision includes:

- changes in definitions and classifications, such as the recognition of implicit services provided by property and casualty insurance as services consumption and the allocation of a portion of implicit services provided by commercial banks to borrowers.
- introduction of new and improved methodologies and the incorporation of newly available and revised source data,
- presentational changes in the NIPA tables that reflect definitional changes.

The revised data do not paint a significantly different historical portrait of the major economic indicators, such as real output and personal income. The average growth rate of real output stayed at 3.2 percent for the period from 1929 to 2002. While real consumption and residential investment now appear to have grown faster than originally thought, exports and government expenditures grew more slowly.

Real output growth was revised down for 2002 by 0.3 percentage points, but was revised up by the same magnitude for 2001 (see table below). Real output declined during the first three quarters of 2001, consistent with prior estimates, although the biggest decline occurred during the third quarter of 2001, rather than the second quarter, as indicated by previous estimates (see graph below).

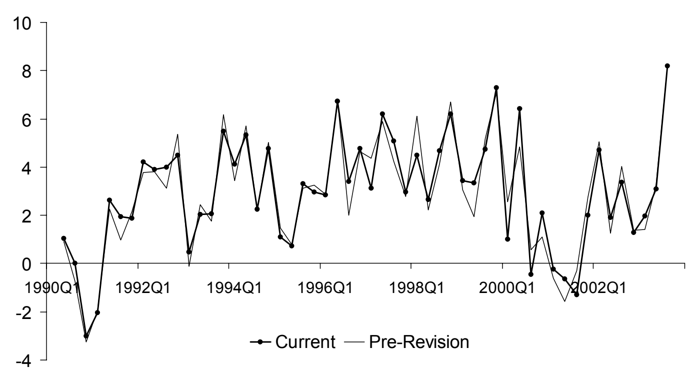
One of the most significant revisions was made to corporate profits. The 2002 growth rate was revised up from 8 percent to 17 percent. The large upward revision reflects improved methods of estimating the cost of stock options.

SELECTED NIPA REVISIONS

	Real GDP			Personal Income			Corporate Profits with IVA &CCA		
	Current	Pre-revision	Diff.	Current	Pre-revision	Diff.	Current	Pre-revision	Diff.
1999	4.4%	4.1%	0.3%	5.1%	4.9%	0.3%	6.2%	3.6%	2.6%
2000	3.7%	3.8%	-0.1%	8.0%	8.0%	0.1%	-3.9%	-2.2%	-1.7%
2001	0.5%	0.3%	0.3%	3.4%	3.3%	0.0%	-5.8%	-7.2%	1.4%
2002	2.2%	2.4%	-0.3%	2.3%	2.7%	-0.5%	17.4%	7.6%	9.7%

Note: Discrepancies are due to rounding.
Source: Economy.com.

NIPA Comprehensive Revision: Real GDP Growth
(percent change, annualized)



Source: Economy.com.

[1] For more information on 2003 Comprehensive revision, see <<www.bea.doc.gov/bea/dn1.htm>>.

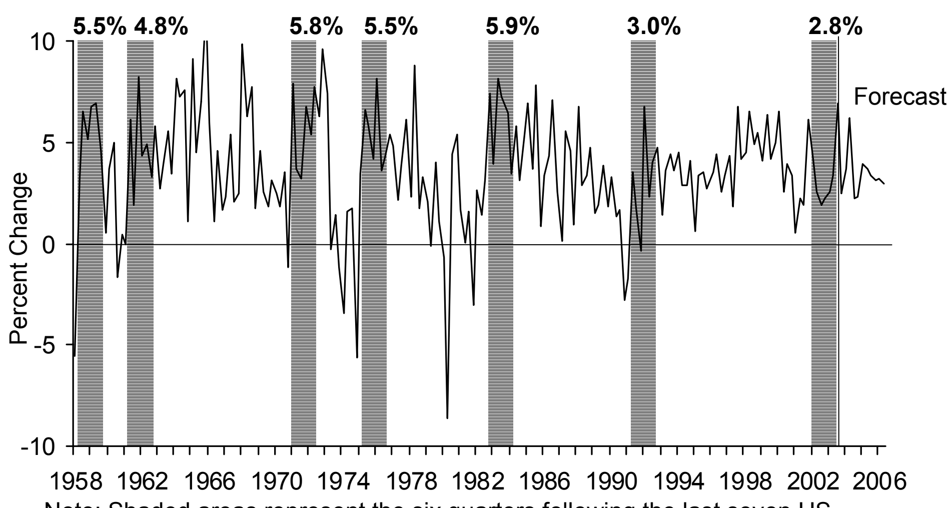
The growing profits depicted in Figure 7 were reflected in stock market growth long before other indicators. The stock market is typically viewed as a leading indicator, since equity prices represent how investors assess the long-term value of holding stocks, and are therefore forward looking. Consequently, equity values depend on present and expected future corporate profits, discounted by the interest rate. Solid growth in corporate profits going forward will continue to support the upward trend in equity values that dates back to the fall of 2002, although that trend was interrupted by the run-up to the war in Iraq. Since March 2003, equity prices have risen consistently. Continued low interest rates also bode well for equity values. For example, the rate on Baa corporate bonds is expected to rise only modestly through the forecast period from a near 40-year low of 6.8 percent in 2003 to 7.7 percent in 2005. The Budget Division projects that the stock market, as represented by Standard and Poor's 500 Index (S&P 500), will rise 15.6 percent in 2004, following a 3.2 percent decline for 2003.

Household Sector Spending Remains Solid

Unlike the typical postwar downturn, household sector spending held up extremely well during the 2001 recession. Much of that strength was the result of the interest rate cuts initiated by the Federal Reserve Board in January 2001, which stimulated both new home buying and a wave of mortgage refinancing. Fiscal policy stimulus and purchasing incentives offered by auto manufacturers immediately following September 11 were also factors. In contrast, consumption weakened during the period immediately following the recession (see Figure 9). Some of that weakness may have been due to the lack of pent-up demand following unusually strong spending during the recession.

Figure 9

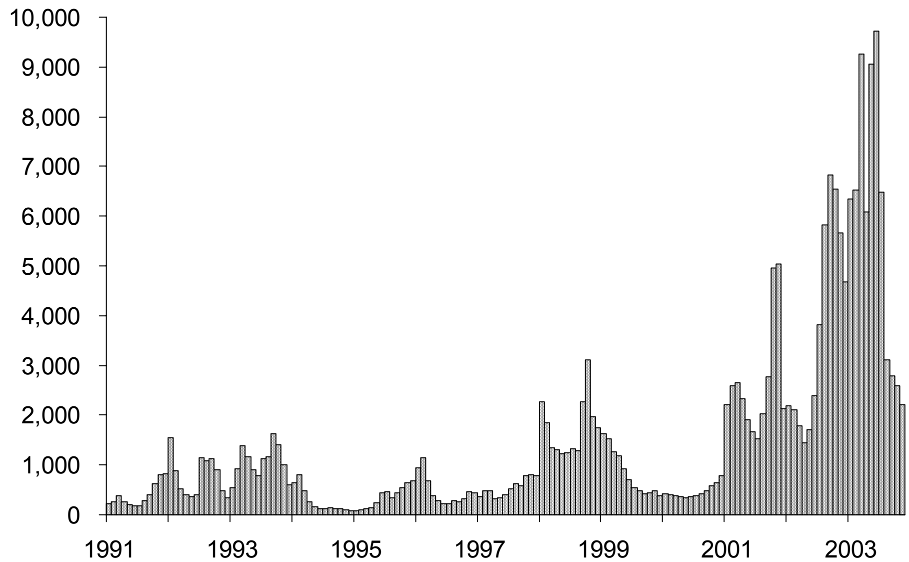
Consumption Growth
During the First Six Quarters Following a Recession



Note: Shaded areas represent the six quarters following the last seven US recessions, excluding the 1980 recession; numbers above the bars show the average annualized rates of quarterly growth over the six quarters.
Source: Economy.com.

Figure 10

Conventional Market Mortgage Refinance Index



Source: Economy.com.

With long-term interest rates expected to rise modestly over the course of 2004 and beyond, cash-outs from mortgage refinancing, which provided much support to consumption spending over the last three years, are expected to diminish. The Conventional Market Mortgage Refinance Index has declined more than 80 percent since its June 2003 peak (see Figure 10). Moreover, there is evidence that an increasing percentage of households are refinancing for the purpose of reducing their loan payments, rather than cashing out equity. The percentage of refinancings involving new loan amounts that are at least five percent higher than the original loan dropped from 63 percent in the second quarter of 2002 to 32 percent in the second and third quarters of 2003. Although lower monthly payments do imply more funds available for non-housing forms of consumption, the boost to consumption growth might be less than that from a direct extraction of equity. However, because of spending lags, the record cashout volume estimated for 2003 may continue to support consumption spending in 2004 as well (see Figure 11).

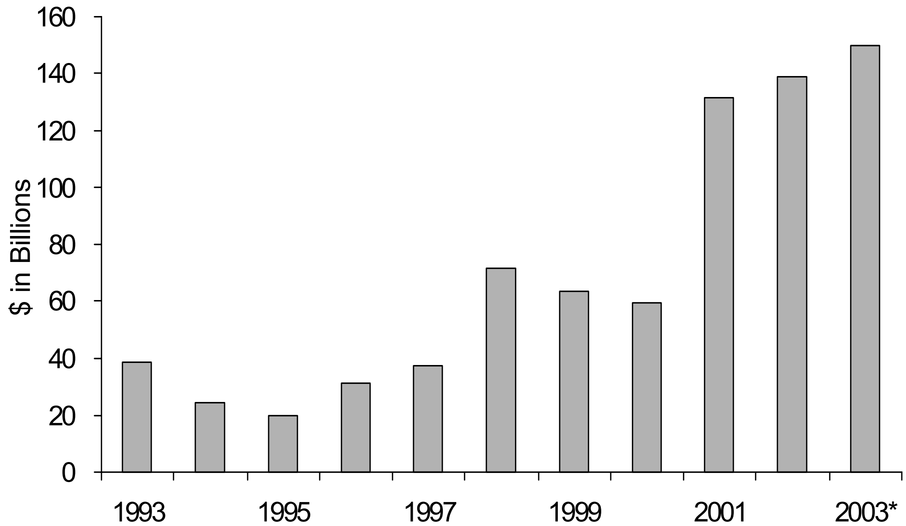
The continuing impact of the Jobs and Growth Tax Relief Reconciliation Act of 2003 (JGTRRA) will also support further consumption growth in 2004.[12] Although there is little consensus as to the impact of the 2001 tax cut on consumption spending, most analysts agree that JGTRRA is at least in part responsible for the economy's strong performance during the third quarter of 2003. Consumption spending rose 6.4 percent during the third quarter, the highest growth since the third quarter of 1997. The total annualized boost to disposable income from the tax cut is estimated at about $107 billion for the third quarter of 2003, more than half of which was due to the childcare credit refund. Evidence suggests that most of this additional income was actually spent by consumers during the third quarter of

[12] JGTRRA, valued at $350 billion by the Joint Committee on Taxation, provides tax relief to both consumers and businesses. The Act's provisions include an increase in the child care tax credit per child from $600 to $1000, an acceleration of the statutory reductions in individual income tax rates originally slated to go into effect in 2006, an acceleration of marriage penalty relief, reduction of other income tax rates, as well as an increase in the individual alternative minimum tax exemption. As many of the law's provisions were made retroactive to January 1, tax rebate checks related to the childcare credit were sent to qualified taxpayers for up to $400 for each child during last summer.

2003. An additional boost to disposable income of approximately $150 billion annualized is expected in the first half of 2004, when many taxpayers settle with the IRS, primarily in the February to April period.

Figure 11

Home Equity Cashed Out Through Refinancing



Note: Total includes first lien mortgages, second mortgages and consolidations.
*The year 2003 includes only three quarters of data.
Source: Freddie Mac.

The primary determinant of consumer spending is households' long-term expectation for disposable income. Therefore, how tax cuts affect the behavior of household spending depends primarily on household income and whether the cut is permanent or temporary. With many of the tax cut provisions not set to expire until the end of 2010, households are likely to perceive them as permanent and so their impact will be significant. Based on an analysis of Consumer Expenditure Survey data, the marginal propensity to consume averages about 60 percent, although it is much higher for low-income households and much lower for high-income households (see Table 3). With JGTRRA not set to expire until 2010, the Budget Division estimates that the 2003 tax cuts added $16 billion to real consumption during 2003, with most of that consumption spending occurring in the third quarter, and will add $44 billion to real consumption during 2004, with much of it concentrated in the second quarter (see Figure 12).

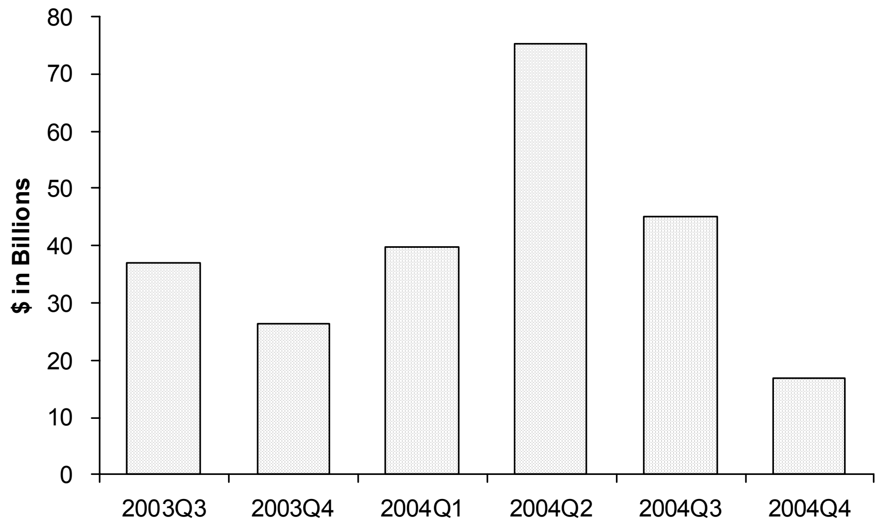
TABLE 3
MARGINAL PROPENSITY TO CONSUME
Consumer Expenditure Survey

Income Class	2000	2001
$7,000-29,000	70.0%	69.4%
$29,000-68,000	67.3%	65.7%
$68,000-143,000	38.9%	44.6%
$143,000 and Above	28.4%	30.8%

Note: Annual numbers are the average of quarterly MPCs.
Source: Consumer Expenditure Surveys, 2000 and 2001; DOB staff estimates.

Figure 12

Projected Impact of the JGTRRA on Real Consumption



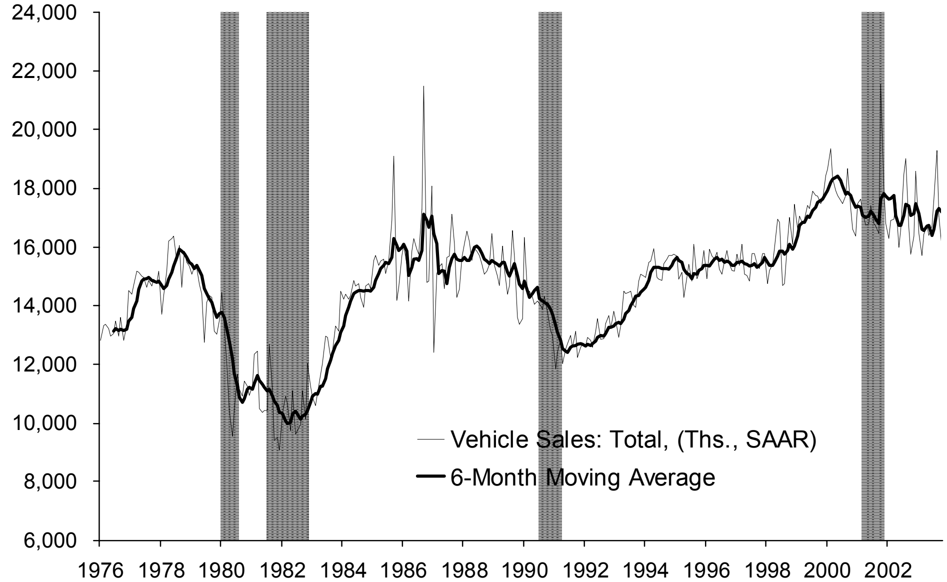
Note: JGTRRA refers to the "Jobs and Growth Tax Relief Reconciliation Act of 2003."
Source: Economy.com, Congressional Budget Office, U.S. Department of Treasury, DOB staff estimates.

After an especially strong third quarter due to the timing of the tax rebates, vehicle sales are expected to decline in the fourth quarter of 2003 (see Figure 13). However, the continuing impact of the tax cuts and the tail of the mortgage refinancing boom are expected to support strong durable goods sales during the first half of 2004. The timing of refund payments should produce particularly robust sales during the second quarter. Moreover, advancing employment and income growth should provide continued stimulus to household spending during the second half of the year and beyond. Overall, the cyclical component of real consumption, composed of vehicles and other durable goods, is expected to grow 7.4 percent in 2004, following growth of 6.5 percent in 2003. The less cyclical component of consumption, consisting of nondurable and services consumption, is projected to grow 3.2 percent in 2004, following growth of 2.5 percent in 2003, consistent with the projected growth in disposable income.

Households played a critical role in keeping the 2001 recession mild, not only through strong consumption spending, but also by supporting a booming housing market. Figure 14 shows the strength of the impact that the decline in mortgage rates has had on real fixed residential investment. Housing starts remain at record levels, despite the rise in mortgage rates since early 2003. However, with interest rates likely to rise further, and home prices at historically high levels, housing market growth is expected to moderate in 2004. The National Association of Realtors' Housing Affordability Index, which combines the impact of home prices, family incomes, and interest rates, remains at historically high levels, supporting the demand for housing. However, the index is expected to fall as interest rates and home prices continue to rise. The Budget Division expects real residential fixed investment to grow 5.5 percent in 2004, following growth of 9.0 percent in 2003.

Figure 13

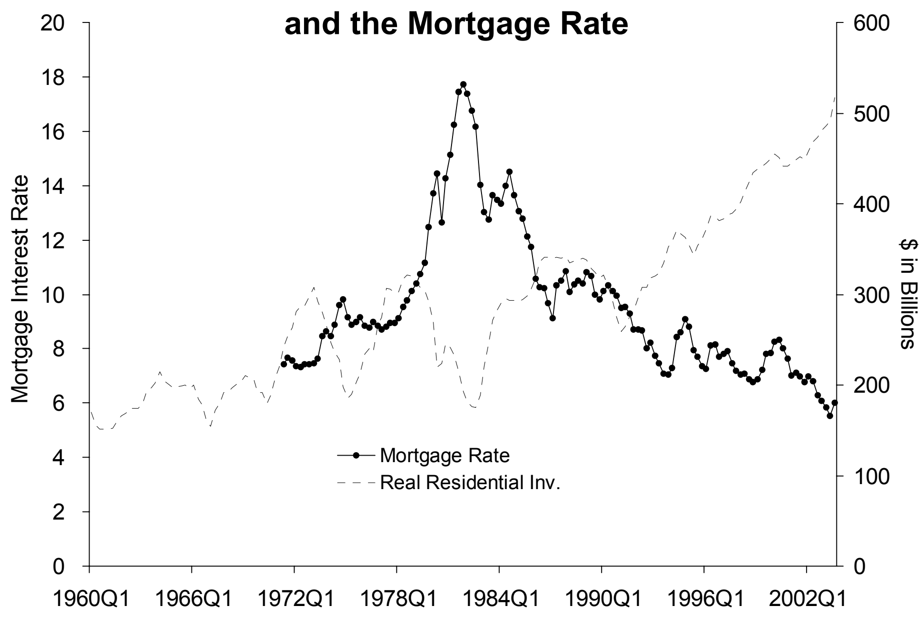
Vehicle Sales



Source: Economy.com

Figure 14

Real Residential Fixed Investment and the Mortgage Rate



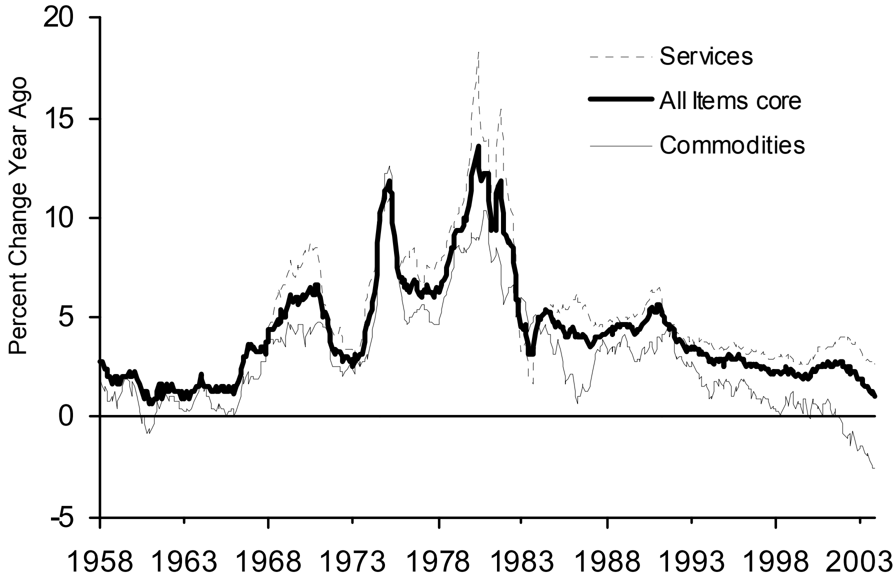
Source: Economy.com

Inflation and the Outlook on Monetary Policy

Inflation has been trending downward since the early 1980s. Recent trends in inflation, as measured by growth in the Consumer Price Index (CPI), have been dominated by weakness in the national and global economies, as well as turbulence in the energy market. For example, the rate of inflation fell from 3.4 percent in 2000 to 1.6 percent in 2002, primarily reflecting the contraction in economic activity. In contrast, the rise in inflation to 2.3 percent in 2003 is chiefly due to the rise in energy prices at the height of the Iraq conflict. Because of the volatility in food and energy prices, the movement in prices excluding these components, also known as the "core rate of inflation," is thought to give a truer picture of underlying price trends. The core rates of inflation for all items, commodities, and services appear in Figure 15. All have been trending downward since early 2002, with commodities prices actually exhibiting deflation on a year-over-year basis since the end of 2001.[13] Even medical care services inflation, which until about one year ago had been leading the services component of inflation upward, has moderated. Medical care services inflation averaged 4.5 percent in 2003, down from 5.1 percent for all of 2002.

Figure 15

Core CPI Inflation



Source: Economy.com.

What is the source of the disinflation in services prices and the deflationary trend in commodities? Inflationary pressures tend to be strongest during periods of expansion as the demand for labor and commodity resources increases. As the demand for labor weakens when the economy heads into recession, so does the pressure on employers to raise wages. Therefore, domestic inflation peaked along with the business cycle in early 2001. Moreover, with the increasing integration of the global economy, the U.S. downturn spread to our trading partners, reducing price pressures yet further. Because of the growing slack in the global economy, growth in the prices of traded goods has tended to be weaker than that of non-traded goods. Hence, one is more likely to observe deflation in the prices of commodities because they are traded more extensively.

Inflation rates tend to fall when there is spare capacity, even when the economy's rate of growth is strong. The degree of spare capacity rather than its rate of change is the more significant factor. A key measure of slack is the output gap, defined as the difference between actual and potential real GDP. Since potential GDP is unobservable, it must be estimated (see Box 3). The Budget Division currently estimates the economy's potential

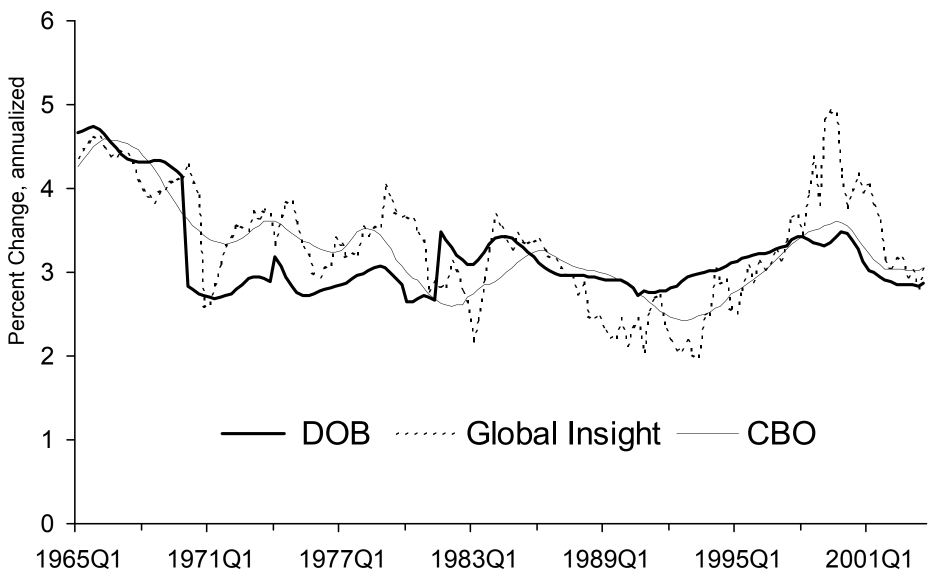
[13] Alternative measures of inflation include the price deflators associated with national output and its components. For example, the core deflator for personal consumption expenditures is reported to be closely monitored by the Federal Reserve Board. These measures are available on a quarterly basis, whereas the CPI is available monthly. However, the two sets of series tend to exhibit the same overall patterns.

growth rate to be about 3.0 percent (see Figure 16). A reduction in the size of the gap occurs when the growth rate of actual GDP exceeds the growth rate of potential GDP. With the economy's growth rate projected to exceed its potential in 2004, inflationary pressures can be expected to build from that source. Preliminary signals of such pressures have already emerged. For example, core wholesale finished goods prices, excluding food and energy, have begun to rise in recent months. Import prices have also been rising, due in part to the recent depreciation of the dollar.

Nevertheless, there are several reasons to expect inflation to remain low. The relatively strong output growth anticipated for 2004 will coincide with a significant degree of slack in the nation's labor market and industrial sector. The nation's unemployment rate is expected to fall only to 5.5 percent by the fourth quarter. An improving global economy will continue to sustain spare capacity as well. Moreover, the U. S. economy is expected to continue to exhibit high productivity growth. Finally, oil prices are expected to decline from recent levels. These factors will create countervailing downward pressures on inflation. On balance, the Budget Division believes that while the core rate of inflation will rise, an anticipated decline in energy prices will outweigh the impact of higher domestic and global growth, leading to slightly lower overall inflation for 2004. Consumer price inflation, as measured by growth in the CPI, is projected to fall to 1.8 percent from 2.3 percent in 2003.

Figure 16

Potential Real GDP



Source: Economy.com, Global Insight, Congressional Budget Office, DOB staff estimates.

The modest acceleration in the core rate of inflation projected for 2004 will induce the Federal Reserve to gradually increase the federal funds rate, after holding it steady at 1.0 percent since June 2003. The Budget Division uses a modified version of Taylor's monetary rule as a guide to forecasting changes in the Federal Reserve Board's federal funds policy target.[14] Taylor's rule is a federal funds rate reaction function that responds to both the deviation of inflation from its target level and the deviation of output growth from its potential level. We assume the Federal Reserve weighs deviations from its inflation target about twice as heavily as deviations from its output growth target, so the inflation deviation has a weight of 1 while the output-growth deviation has a weight of 0.5. In addition, the contemporaneous

[14] See John B. Taylor, "Discretion Versus Policy Rules in Practice," *Carnegie-Rochester Conference Series on Public Policy*, 39, 195-214, 1993.

value of inflation is replaced by an average of actual inflation for the past three quarters, estimated inflation for the current quarter, and expected inflation for one quarter ahead. A similar term is constructed for output growth.

BOX 3
THE DETERMINATION OF
POTENTIAL GROSS DOMESTIC PRODUCT

Potential Gross Domestic Product (GDP) is the level of output that the economy can produce when all available resources are being utilized at their most efficient levels. The economy can produce both above and below this level, but when it does so for an extended period, economic agents can expect inflation to either rise or fall, although the precise timing of that movement depends on many factors.

Some knowledge of the economy's productive capacity is fundamental to the decision-making process for households, firms, and the monetary authority. Households partially base their expectations surrounding their lifetime accumulation of wealth upon their estimates of the output potential of the economy. Firms choose a profit-maximizing level of labor and capital based on their estimates of the economy's long-run productive potential. An estimate of potential GDP also enables these agents to form expectations regarding the direction which inflation will take in the future. Such expectations might induce the central bank to shift the course of monetary policy.

Measurement of potential GDP requires a formalization of the aggregate production process. Economists refer to this formalization as an aggregate production function, which stipulates that total output is related to the amount of resources that are applied to production. The precise nature of the production function depends upon which sector of the economy one is trying to model.

Following the Congressional Budget Office (CBO), the Division of the Budget divides the economy into five sectors: nonfarm business, farm, government, nonfarm housing, and households and nonprofit institutions.[1] The nonfarm business sector is by far the largest sector of the economy, comprising 84.1 percent of total GDP during 2000. To model this sector, the DOB again follows CBO and adopts a neoclassical growth model incorporating three inputs to the production process: labor as measured by the number of hours worked, the capital stock, and total factor productivity.

Over the course of an economic expansion, we expect periods during which labor and capital are utilized in magnitudes that are above their most efficient levels. Similarly, during recessions, we expect periods when these inputs are underutilized. Therefore, we can adjust the inputs to the production process to their "potential" levels by removing the historical movements in these series that can be associated with the business cycle. To measure the total potential capital stock, DOB multiplies the U.S. Bureau of Economic Analysis' measure of the real capital stock by the capacity utilization rate, after removing the cyclical component of the latter series by using a methodology developed by the CBO. To measure the potential level of the number of hours worked, we remove the cyclical component using the same methodology.

To estimate the potential level of total factor productivity, the actual values of labor and capital are substituted into a fixed-coefficient production function, where a coefficient of 0.7 is applied to labor and 0.3 is applied to capital. The residual obtained by subtracting the value of output obtained from this substitution from the historical value of output is assumed to represent total factor productivity. Removing the business cycle component from this residual yields its potential level. Substituting the potential levels of all of the inputs back into the fixed-coefficient production function, where total factor productivity is given a coefficient of one, yields a measure of potential nonfarm business GDP. For the other sectors of the economy, the cyclical component is removed directly from the series itself in accordance with the method used by CBO.

[1] See "CBO's Method for Estimating Potential Output," Congressional Budget Office, October 1995, and "CBO's Method for Estimating Potential Output: An Update," Congressional Budget Office, August 2001.

Recently, with inflation rates generally declining throughout the major world economies and outright deflation existing for an extended period of time in Japan, the Federal Reserve has expressed grave concern about the dangers of deflation in the United States, as seen in the minutes released after recent meetings of the Federal Open Market Committee. Thus, the federal funds rate is expected to rise more slowly than a strict application of Taylor's Rule would suggest. Indeed, recent research finds that a policy based on a modified Taylor's Rule may be more effective when the federal funds rate gets close to its nominal zero-bound.[15] The Budget Division expects the federal funds rate to move up 75 basis points by the end of 2004, representing a continued accommodative stance by the Federal Reserve from a historical standpoint.

Outlook on Government Spending

Between the third quarter of 2001 and the third quarter of 2003, real federal government expenditures rose 17.6 percent. During the same period, defense spending was up 22.7 percent, mostly due to conflicts in Iraq and Afghanistan (see Figure 17). In September 2003, Congress approved $87 billion in additional funds for the war in Iraq, with a significant portion of the money to be allocated for military compensation and purchases of military equipment.[16] However, DOB does not estimate strong growth for the federal component of GDP for either the fourth quarter of 2003 or all of 2004, since the level of spending was already very high during 2003. In addition, some of the spending allocated to the reconstruction of Iraq will be accounted for in real GDP as imports.[17] The Budget Division projects growth of 3.7 percent in the Federal contribution to real GDP growth for 2004, following growth of 8.1 percent for 2003. Spending at the state and local level will be continue to be restrained due to the lag in the response of state and local government receipts to changes in the direction of the overall economy. The state and local government component of real GDP is expected to grow 1.6 percent for 2004, following growth of only 0.8 percent in 2003.

The Federal budget deficit is not expected to have a significant impact on interest rates in the near term. This implies no significant crowding out of private sector investment by the public sector borrowing needs over the immediate forecasting horizon. However, the long-term impact of the deficit on interest rates is expected to be upward. The Budget Division projects a rise in the 10-year Treasury rate to 4.7 percent in 2004 from 4.0 percent in 2003.

The International Economy

The increased synchronicity of global markets implies that the growing strength of the U.S. economy will act as a renewed engine of global growth. Indeed, the 11.0 percent growth in real exports in the third quarter suggests that this growth is finally becoming palpable (see Figure 18). Goods exports, which account for about two thirds of all real U.S. exports, grew 8.9 percent in the third quarter. Much of that growth was accounted for by the almost 20 percent growth in capital goods exports, a category which accounted for 41.5 percent of U.S. goods exports during the first ten months of 2003 (see Figure 19).

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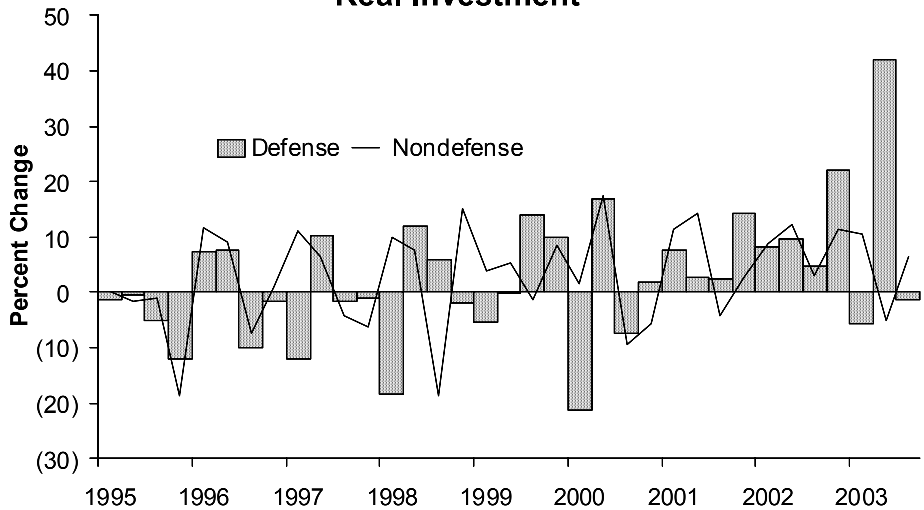
[15] See David L. Reifschneider and John C. Williams, "Three Lessons for Monetary Policy in a Low Inflation Era," *Finance and Economics Discussion Series*, 1999-44 (August).

[16] For more information see <<http://www.whitehouse.gov/omb/budget/amendments/supplemental_9_17_03.pdf>>.

[17] BEA includes military purchases abroad in a sub-category of "Imports of Services" called "Direct defense expenditures", which is defined as "Expenditures incurred by U.S. military agencies abroad, including expenditures by U.S. personnel, payments of wages to foreign residents, construction expenditures, payments for foreign contractual services, and procurement of foreign goods. Includes both goods and services that cannot be separately identified." For more information on this topic, see <http://www.bea.doc.gov/bea/newsrel/info0803.htm>.

Figure 17

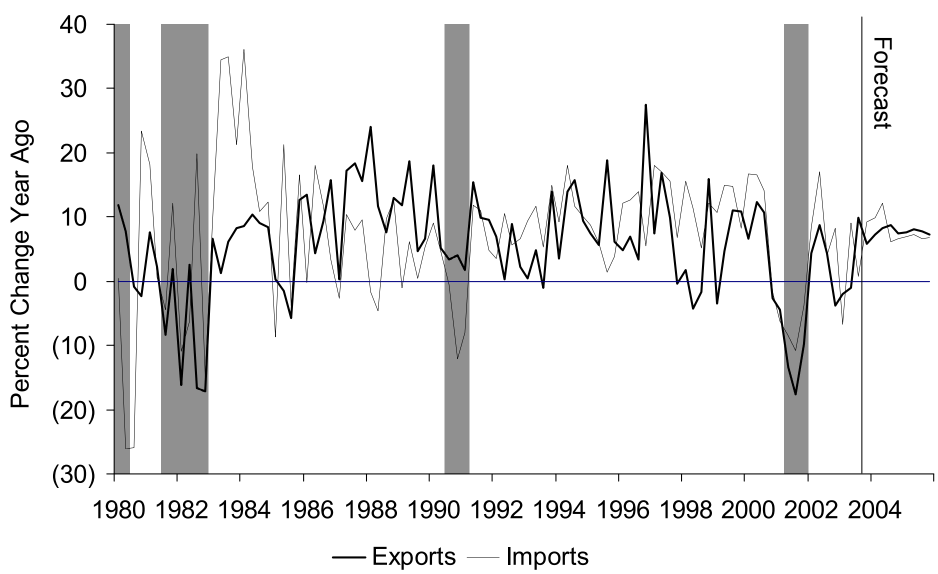
Real Federal Government Consumption Expenditures and Real Investment



Source: Economy.com

Figure 18

Real Import and Export Growth

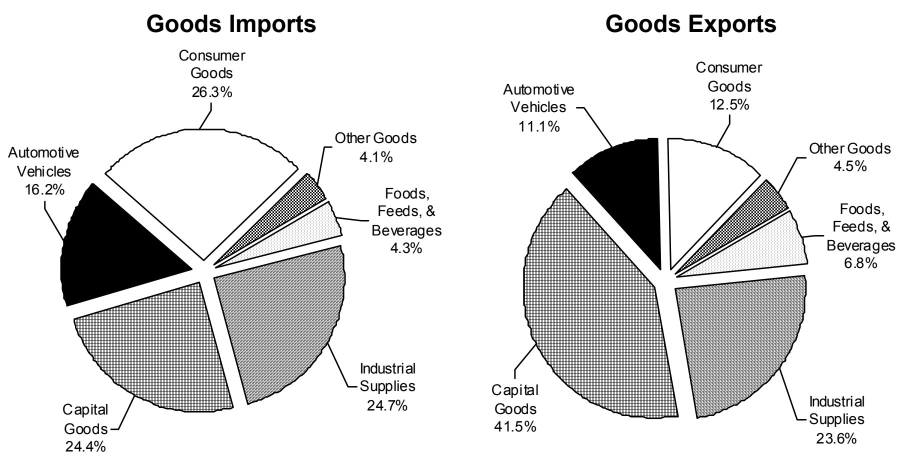


Note: Shaded areas represent US recessions.
Source: Economy.com; DOB staff estimates.

Although an increase in world demand for capital goods bodes well for global investment growth, growth rates are still well below potential. Table 4 displays a list of the nation's top 10 trading partners. These ten countries represent 68.8 percent of total U.S. imports and 66.3 percent of total U.S. exports in goods. Our largest trading partner, Canada grew 2.6 percent in the first quarter of 2003, but saw real GDP decline 0.3 percent in the second quarter, although final domestic demand grew a much stronger 2.9 percent. Like much of Latin America, the Mexican economy remains weak. One exception to the trend in Latin America is Chile, which saw average growth of over 3.0 percent for the first three quarters of 2003. China has averaged strong growth of 8.6 percent for the first three quarters of 2003, on a year-ago basis. While economic growth in Taiwan and South Korea has not been nearly as strong, both countries have seen solid improvement since the spring of 2003. After growing an anemic 0.9 percent in 2002, Euro area real GDP was virtually flat during the first two quarters of 2003. Euro area industrial production rose a mere 0.3 percent during the first eight months of 2003. Japan's economy has embarked upon a gradual recovery, characterized by increasing exports, business investment, and industrial production. However, housing investment and private consumption remain sluggish, and the decline in household income is only slowly reversing itself.

Figure 19

Composition of Real Imports and Exports of Goods by Principal End-Use Category for 2003



Note: Based on 10 months of data.
Source: U.S. Bureau of the Census.

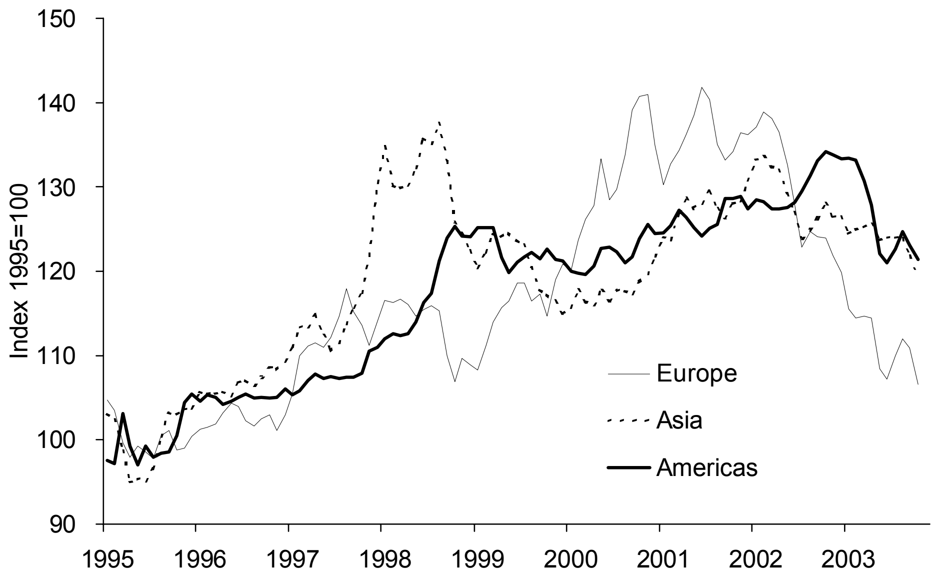
TABLE 4
TOP TEN TRADING PARTNERS OF THE U.S.
(Imports Plus Exports)

Country	YTD Through November 2003 ($ in Billions)
Canada	361.70
Mexico	215.82
China	164.28
Japan	155.39
Federal Republic Of Germany	87.99
United Kingdom	69.93
Republic of Korea	55.35
Taiwan	44.31
France	41.94
Malaysia	33.04

Source: U.S. Census Bureau.

The nation's foreign sector made a rare positive contribution to real GDP growth during the third quarter of 2003. Although the Budget Division is not forecasting an improvement in the U.S. trade deficit for the foreseeable future, the recent trend in the value of the dollar argues against too dramatic a deterioration in the U.S.'s net export position. Figure 20 shows trends in the trade-weighted value of the dollar against the currencies of three trading areas: Europe, the Americas, and Asia. The U.S. dollar has depreciated almost 12 percent against a trade-weighted measure of all foreign currencies since peaking in the first quarter of 2002, falling against all currencies except for several of our Asian trading partners, including China, Malaysia, and Hong Kong, nations that actively peg the values of their currencies to the U.S. dollar. As of the middle of 2002, the most recent period for which detailed data are available, both China and Hong Kong held particularly large portfolios of U.S. securities. We expect these two sets of countervailing forces to combine to allow a modest depreciation to continue, with a positive impact on U.S. export growth.

Figure 20
Trade Weighted Value of Dollar



Source: Economy.com.

With the U.S. economy exhibiting strong growth in the latter half of 2003 and into 2004, it will once again play the role of the global economy's growth engine. Holding other factors constant, this role suggests a continued widening of the nation's trade deficit for the foreseeable future, a trend that will only be cushioned by a modestly falling dollar. Although a large trade imbalance presents a currency risk, the strong growth in the U.S. economy relative to the rest of the world implies that the demand for U.S. dollar-denominated assets will remain strong, partially offsetting the forces driving down the value of the dollar. The Budget Division projects growth in real U.S. imports of 8.4 percent for 2004, following growth of 3.7 percent for 2003. Real U.S. exports are projected to grow 7.3 percent in 2004, following growth of 1.4 percent in 2003.

COMPARISON WITH OTHER FORECASTERS

Table 5 compares DOB's 2004 forecast for major U.S. indicators with those of other forecasting groups. Forecasts for real U.S. GDP growth range from a low of 4.3 percent (Economy.com) to a high of 4.9 percent (Macroeconomic Advisors). The Budget Division's forecast of 4.7 percent is in about the middle of the range. DOB's inflation forecast of 1.8 percent for 2004 is above the forecasters listed, but very similar to the Blue Chip Consensus. Unemployment rate forecasts for 2004 range from a low of 5.7 percent to a high of 6.1 percent. The Budget Division is at the low end of the range at 5.7 percent.

Table 10 and Table 11 present the Division of the Budget's baseline forecast for selected U.S. economic indicators. The Division's macroeconomic model underwent substantial revision in 2000. A brief description of the model is presented in Box 4.

TABLE 5
U.S. ECONOMIC FORECAST COMPARISON

	2003 (preliminary)	2004 (forecast)	2005 (forecast)	2006 (forecast)	2007 (forecast)
Gross Domestic Product (GDP) (1996 chain wt. percent change)					
DOB	3.1	4.7	3.5	3.3	3.1
Blue Chip Consensus	3.1	4.6	3.7	NA	NA
Economy.com	3.1	4.3	NA	NA	NA
Global Insight	3.0	4.7	3.8	3.3	3.3
Macroeconomic Advisers	3.1	4.9	4.2	3.7	3.0
Consumer Price Index (CPI) (percent change)					
DOB	2.3	1.8	2.1	2.3	2.4
Blue Chip Consensus	2.3	1.7	2.1	NA	NA
Economy.com	2.3	1.2	NA	NA	NA
Global Insight	2.3	1.3	1.6	1.7	2.1
Macroeconomic Advisers	2.3	1.2	1.5	1.8	1.9
Unemployment Rate (percent)					
DOB	6.0	5.7	5.2	5.0	5.1
Blue Chip Consensus	6.0	5.7	5.4	NA	NA
Economy.com	6.0	6.1	NA	NA	NA
Global Insight	6.0	5.7	5.4	5.5	5.5
Macroeconomic Advisers	6.0	5.8	5.2	4.9	4.9

Source: Projections for 2003-2007 by New York State Division of the Budget, January 2004; Blue Chip Economic Indicators, January 2004; Economy.com, Macro Forecast, January 2004; Global Insight, US Executive Summary, December 2003; and Macroeconomic Advisers, Economic Outlook, January 2004.

Risks to the U.S. Forecast

Although the Budget Division believes that the U.S. is on a sustainable growth path, that belief is contingent upon the absence of any further shocks to the economy. Unpredictable events such as a terrorist attack remain the biggest risk to the economic expansion. Such a shock could induce firms to postpone their spending and hiring plans again, reducing future investment and employment, which in turn could result in lower consumption growth. Moreover, a destructive attack on oil facilities abroad or a policy shift on the part of oil-producing nations could result in higher oil prices than anticipated, having adverse economic repercussions. Similarly, a corporate governance scandal of Enron proportions could dishearten investors, weakening equity prices and business and consumer spending.

If the Federal Reserve Board should initiate a policy of monetary tightening sooner than anticipated, growth could also be more restrained than expected. A significant risk of deflation has now receded, and the Federal Reserve has demonstrated in the past that it can swiftly shift course when it deems necessary. If households demonstrate a weaker response than expected to the fiscal stimulus provided by the tax cut, growth could be weaker than what is reflected in the forecast. In addition, with the personal savings rate now at a relatively low level, there is a risk of a "virtuous reform" by consumers to increase savings in order to readjust their balance sheets. The resulting decline in consumption growth could weaken corporate profits, which could in turn result in lower employment and investment growth. As discussed above, the dollar is at some risk of a sharp adverse reaction by foreign investors. A dollar collapse would impart a substantial inflationary impulse to the economy. This could well lead to higher interest rates and lower stock prices, both of which would constrict economic activity. This problem could be exacerbated by weaker-than-expected growth among the nation's trading partners, producing weaker export growth than projected.

On the other hand, an economic resurgence that moderately exceeds the Budget Division's expectations is also possible. A more rapid increase in export growth due to either a weakened dollar or faster global growth could generate a somewhat stronger increase in total output than expected. Similarly, lower inflation than expected, perhaps as a result of a substantial drop in the price of oil or stronger productivity growth than expected, could induce the Federal Reserve to postpone interest rate increases, resulting in stronger consumption and investment growth than projected. Moreover, strong productivity growth could result in higher real wages, supporting faster growth in consumer spending than expected.

BOX 4
THE DIVISION OF THE BUDGET
U.S. MACROECONOMIC MODEL

Macroeconomic modeling has undergone a number of important changes during the last 25 years, primarily as a result of developments in economic and econometric theory. These developments include the incorporation of both rational expectations and micro-foundations based on the long-run optimizing behavior of firms and households. In addition, analysts now employ more flexible specifications of behavioral relations within a vector autoregressive (VAR) model framework. Recent developments also include a more rigorous analysis of the time series properties of commonly used macroeconomic data series, as well as the implications of these properties for model specification and statistical inference. There has also been a significant improvement in the understanding of the long-run equilibrium relationships among macroeconomic data series and the predictive power of these relationships in constraining economic dynamics.

The Budget Division's U.S. macroeconomic model (DOB/U.S.) incorporates the theoretical advances described above in an econometric model used for forecasting and policy simulation. The model contains 98 core equations, of which 29 are behavioral. In addition, there are hundreds of auxiliary forecasting equations that incorporate the results from the core model as inputs. The current estimation period for the model is 1965:1 through 2002:3. Our analysis borrows heavily from the Federal Reserve Board model which was redesigned the during the 1990s using the most up-to-date advances in modeling techniques.[1] We are grateful to Federal Reserve Board economists for providing guidance and important insights as we developed the DOB/U.S. macroeconomic model.

In economic parlance, DOB/U.S. could be termed a neoclassical model. Agents optimize their behavior subject to economically meaningful constraints. Households exhibit optimizing behavior when making consumption and labor supply decisions, subject to a wealth constraint. Expected wealth is, in part, determined by expected future output and interest rates. Likewise, firms maximize profits when making labor demand and investment decisions. The value of investment is affected by the cost of capital, as well as expectations about the future path of output and inflation. The economy's long-run growth path converges to an estimate of potential GDP growth. Monetary policy is administered through adjustments to the federal funds rate, as guided by Taylor's Rule. Current and anticipated changes in this rate influence agents' expectations and the rate of return on various financial assets.

DOB/U.S. incorporates three key theoretical elements into this neoclassical framework: expectations formation, equilibrium relationships, and dynamic adjustments (movements toward equilibrium). The model addresses expectations formation by first assuming that expectations are rational and then specifying a common information set that is available to economic agents who incorporate all relevant information when forming and making their expectations. Long-run equilibrium is defined as the solution to a dynamic optimization problem carried out by households and firms. The model structure incorporates an error-correction framework that ensures movement back to long-run equilibrium.

The model structure reflects the microeconomic foundations that govern optimizing behavior, but is sufficiently flexible to capture the short-run fluctuations in employment and output caused by economic imbalances (such as those caused by sticky prices and wages). DOB/U.S. incorporates dynamic adjustment mechanisms that reflect the fact that while agents are forward looking, they do not adjust to changes in economic conditions instantaneously. The presence of frictions (costs of adjusting productive inputs, sticky wages, persistent spending habits) governs the adjustment of non-financial variables. These frictions, in turn, create imbalances that constitute important signals in the setting of wages and prices. In contrast, the financial sector is assumed to be unaffected by frictions due to the negligible cost of transactions and the presence of well-developed primary and secondary markets for financial assets.

[1] "A Guide to FRB/USA Macroeconomic Model of the United States," edited by F. Brayton and P. Tinsley. Federal Reserve Board, Version 1.0, October 1996.

THE NEW YORK STATE ECONOMY

The New York State economy is finally emerging from recession, a view supported by both the most recent economic data and the results of recently conducted business sentiment surveys. Current conditions are similar to what they were one year ago, when it looked like the State recovery would begin in earnest. However, the U.S. and global recoveries lost momentum as the nation was heading toward war, resulting in an unanticipated lengthening of the State's recession. With the uncertainty of that period now dissipating, the State economy is poised for its first annual increase in employment in four years.

Private sector employment growth for the first four quarters of the State recovery is projected at 0.5 percent.[18] Although this is below average growth for this stage in a recovery, it is stronger than the 0.1 percent growth that followed the 1989-92 State recession.

The recent upturn in financial market activity has improved prospects for bonuses and wages as well. Wage growth for 2004 is estimated at 5.1 percent, with much of this strength attributable to improved financial sector performance. Personal income is also expected to increase by 5.1 percent in 2004, primarily reflecting the strength in wage growth. A detailed analysis of employment and wage trends at the establishment level is presented below that supports the Budget Division's positive outlook for this year. A focus on the Manhattan economy, the center of economic dislocation for this past recession, suggests that although it is lagging much of the rest of the State, it has shown remarkable resiliency since the destruction of the World Trade Center on September 11, 2001.

Emerging from the 2001-03 Recession

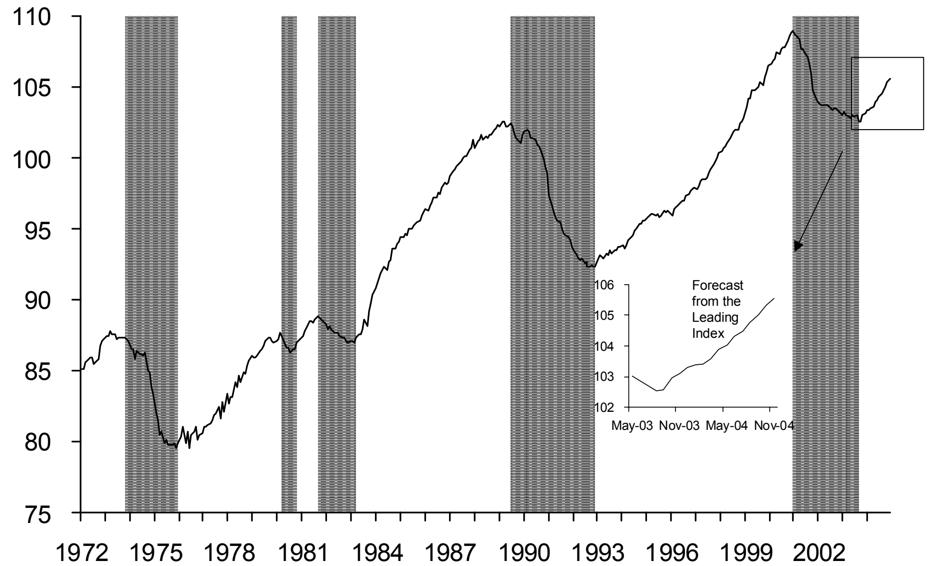
The tragedy of the September 11 terrorist attack is a haunting reminder of how an unexpected event can disproportionately affect the economy of a single state or region. Such events underline the importance of understanding each state's unique business cycle trends. The attack on the nation's and the world's financial capital — New York City — struck a severe blow to the State economy, a blow from which the State is still recovering. Although the national recession of 2001 officially ended in November of that year, the Division of the Budget believes that the State economy only emerged from recession in 2003, enduring a significantly longer downturn than the nation as a whole (see Box 5).

According to the New York State Index of Coincident Economic Indicators, the most recent recession started earlier in New York than in the nation and ended later, not unlike the recession of the early 1990s (see Figure 21). However, although the 2001-03 recession encompasses one of the most catastrophic events in the State's history, it was not as deep as the 1989-92 State recession that lasted more than three years and cost over 500,000 jobs. There are two striking differences between today's economy and that of the early 1990s. In contrast to the downsizing of the State's defense industry that eliminated hundreds of thousands of jobs a decade ago, the nation's defenses are now fully mobilized for the war on terrorism and the reconstruction of Iraq. Although little of the State's defense manufacturing sector survived the restructuring of the 1990s, the recent increase in Federal defense spending has benefited some of the State's manufacturing firms. But perhaps the more important difference pertains to the real estate market. In contrast to the market collapse that occurred in the early 1990s, the State's housing market has been booming and has cushioned the severity of the recession in many areas.

[18] The first four quarters of the current State expansion span the fourth quarter of 2003 and the first three quarters of 2004.

Figure 21

New York Index of Coincident Economic Indicators



Source: Economy.com; DOB staff estimates.

The New York State Index of Coincident Economic Indicators is used to date the State's distinct business cycle turning points. According to the Index, while the national economy was recovering in 2002 and the first half of 2003, the New York economy continued to decline until September 2003.[19] There are several reasons why the State's 2001-03 recession lasted so much longer than for the nation. Wall Street was at the center of the equity-price/high-tech collapse in early 2000 that ultimately precipitated the national downturn. The financial markets were a target of the far more destructive blow of September 11, and were hit once more with the collapse of the Enron Corporation and the string of corporate governance scandals that followed. The interruption of the national recovery due to the run-up to the war in Iraq further delayed the State's emergence from recession.

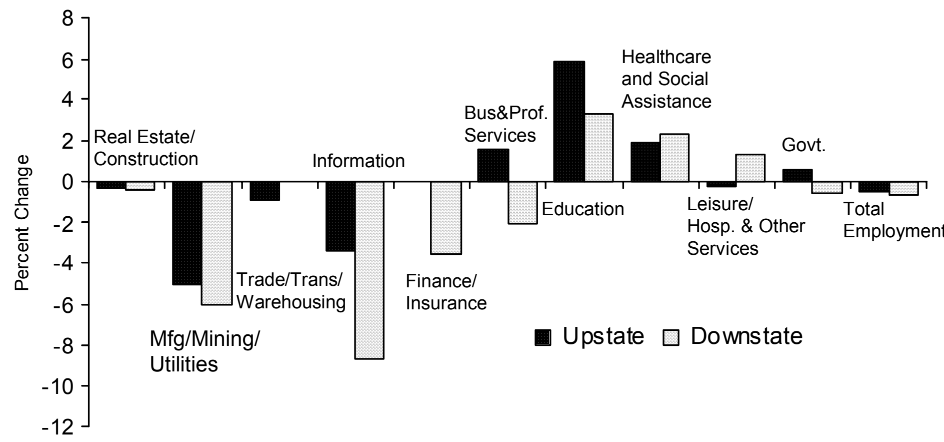
The impact of that delay was felt most acutely in New York City. Figure 22 compares employment growth for the 10-county downstate region for selected sectors with that of the rest of the State for the first half of 2003 relative to the same period in 2002. With Manhattan as the center of the State's economic downturn, the current recovery is clearly proceeding at disparate paces across the State's regions. The most recent Covered Employment and Wages (CEW) data available indicates that toward the end of the recession, the 10-county downstate region was still losing jobs at a slightly faster pace than upstate between the first half of 2002 and the first half of 2003, with downstate employment falling 0.7 percent, compared to a 0.5 percent decline upstate. While the greatest disparity now appears in the information sector, which includes the media and communications industries, large disparities also exist in the finance and insurance sector, and the business and professional services sectors. One area in which the downstate economy is doing better than upstate is in the leisure, hospitality and other services sector, which includes many of the travel and tourism industries such as accommodations, arts, and entertainment. This sector grew 1.3 percent downstate during the first half of 2003, but fell 0.2 percent upstate. The decline in manufacturing for both regions roughly reflects national trends.

[19] When the New York State Department of Labor releases its next benchmark revision of the Current Employment Statistics data in March 2004, the revised data may indicate that the State's recession ended either earlier or later in 2003.

Figure 22

Employment Growth: Upstate vs. Downstate

2003H1 over 2002H1



Note: Business and professional services includes NAICS broad sectors 54, 55 and 56; recreation and other services includes NAICS broad sectors 71, 72, and 81.
Source: NYS Department of Labor, CEW data.

The Budget Division's assessment that the State economy is now in recovery and will continue to expand throughout 2004 is supported by the results from two statewide surveys of business sentiment. A survey of New York businesses by the Econometric Research Institute at the University at Albany finds that 51 percent of the firms surveyed agreed that the New York State economy was still in recession as of October 2003, showing weak growth in both employment and wages and salaries. However, this number is significantly down from the 76 percent reported in April 2003 and from the post-US-recession high of 97 percent reported in January of 2002. The survey shows that while profits declined for 11.0 percent of establishments in 2003, 9.5 percent anticipate higher profits in 2004. Furthermore, 41.7 percent of establishments feel optimistic enough about the future to anticipate expanding over the next five years as compared to only 8.8 percent that expect to contract.[20]

Additional evidence indicating that the State economy is beginning to expand comes from the Empire State Manufacturing Survey conducted by the Federal Reserve Bank of New York. Perhaps the most positive part of the report is the nine consecutive increases in the General Business Conditions Index through December 2003. Its component indices also give rise to optimism. The manufacturing survey's inventory index has turned positive, implying that manufacturing firms are starting to restore their inventories. And while the survey's employment indices do not suggest outright job gains, they do show declining job losses.

The finance industry is expected to have its best profit performance in three years, and the travel and tourism industries, which were among those hardest hit by the events of September 11, have been steadily improving. The reconstruction of the World Trade Center site will provide an economic boost to lower Manhattan, while the expected improvement in the global economy should increase the demand for State-manufactured goods. All of this evidence suggests that the State economy is finally in recovery.

[20] These results are almost identical to those found in the October survey of 2002. At that time, the State economy had started to move in a positive direction but the crisis in Iraq in early 2003 may have put a damper on many firms' expansionary plans.

BOX 5
NEW YORK STATE INDICES OF COINCIDENT AND LEADING ECONOMIC INDICATORS

In the absence of an official mechanism for dating business cycles at the sub-national level, DOB staff constructed a New York State Index of Coincident Economic Indicators measuring overall economic conditions for New York.[1] The methodology used to construct the index is based on the Stock and Watson methodology and rests on the notion that co-movements in many macroeconomic time series can be captured by a single unobserved variable representing the overall state of the economy.[2] Four State data series — private sector employment, hours worked in the manufacturing sector, the unemployment rate, and sales tax receipts (as a proxy for retail sales) — are combined into a single index using the Kalman filter, a common approach to the estimation of unobserved variables.

Based on the DOB Coincident Index, five business cycles have been identified for New York since the early 1970s, as reported in the table below. A recession is judged to have begun if the DOB Coincident Index sustains three to five consecutive declines of significant depth. A similar approach is used to date business cycle troughs.

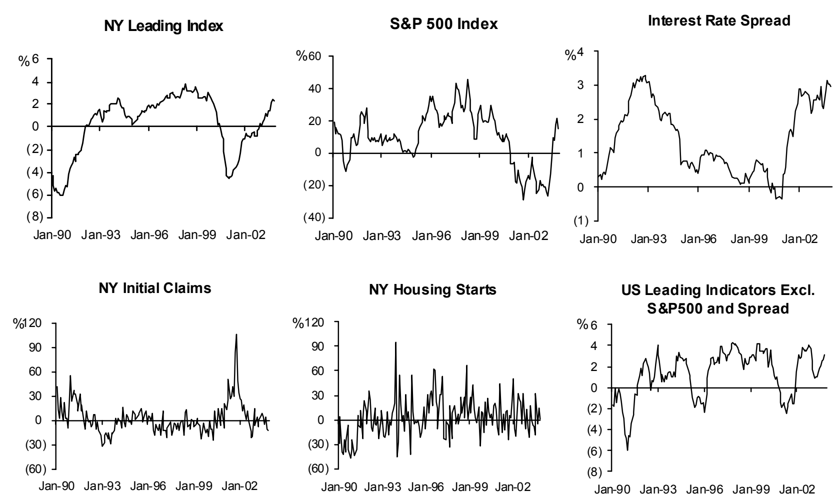
NEW YORK STATE BUSINESS CYCLES

Peak Date	Trough Date	Recession Length (in months)	Private Sector Job Losses
October 1973	November 1975	25	384,800
February 1980	September 1980	7	54,800
August 1981	February 1983	18	76,600
June 1989	November 1992	41	551,700
December 2000	August 2003	32	333,000

Source: DOB staff estimates.

In order to gauge the future direction of the State economy, the Budget Division produces the New York State Index of Leading Economic Indicators, which yields a forecast for the Coincident Index up to 12 months ahead. The forecasting model includes the following five leading economic variables in a vector autoregressive framework: the U.S. Index of Leading Economic Indicators (excluding stock prices and the interest rate spread), New York housing permits, New York initial unemployment insurance claims, stock prices, and the spread between the 10-year and one-year U.S. Treasury rates.

Variables Used in New York Index of Leading Indicators



Note: All percent changes are from prior year.
Source: Economy.com, DOB staff estimates.

[1] See R. Megna, and Q. Xu (2003). "Forecasting the New York State Economy: The Coincident and Leading Indicators Approach," *International Journal of Forecasting*, Vol 19, pp 701-713.
[2] Stock, J.H., and M.W. Watson (1991), "A Probability Model of the Coincident Economic Indicators," in K. Lahiri and G. H. Moore (eds.), *Leading Economic Indicators: New Approaches and Forecasting Records*, New York: Cambridge University Press, pp. 63-85.

Outlook for Employment

Total State nonagricultural employment is projected to rise 0.8 percent in 2004, following a 0.4 percent decline in 2003. The growth rate projected for the State for 2004 is slightly below the 1.1 percent expected increase for the nation as a whole. Private sector employment is projected to grow 0.9 percent in 2004, representing an increase of 60,200 jobs, following a 0.4 percent drop for 2003. Table 6 reports projected changes in employment for selected group of NAICS sectors. The greatest losses are expected to occur in the manufacturing sector, while the greatest rates of gain are expected to be experienced in the construction, educational and health services sectors. The State's average annual unemployment rate is expected to fall to 6.0 percent this year, a slight decrease from 6.2 percent in 2003. The unemployment outlook for this past recession compares favorably with the three previous recessions. The State's unemployment rate peaked at 10.3 percent in 1976, 8.6 percent in 1982-83, and again at 8.6 percent in 1992.

TABLE 6
CHANGE IN NEW YORK STATE EMPLOYMENT FOR 2004
SELECTED SECTORS

	Percent	Levels
Total Private	**0.9**	**60,200**
Utilities	(0.9)	(400)
Construction	5.3	17,200
Manufacturing and Mining	(3.4)	(21,100)
Wholesale Trade	0.4	1,500
Retail Trade	0.4	3,600
Transportation and Warehousing	0.6	1,400
Information	(2.1)	(5,700)
Finance and Insurance	0.4	2,300
Real Estate and Rental and Leasing	1.5	2,700
Professional, Scientific and Technical Services	1.7	8,300
Management and Admin. and Support Services.	1.2	6,400
Educational Services.	2.9	7,400
Healthcare & Social Assistance	2.1	23,400
Leisure, Hospitality and Other Services.	1.4	13,400
Government	**0.2**	**3,200**
Total	**0.8**	**63,400**

Note: Management and administration and support services includes NAICS sectors 55 and 56. Sum of sectors may not match the total due to rounding.
Source: NYS Department of Labor; DOB staff estimates.

Although State employment continues to be down on a year-over-year basis, current labor market dynamics support the expectation that employment will be on the rise by early 2004. The State labor market is extremely dynamic — even in the worst of times, new firms are created and existing firms add jobs. Though State private sector employment fell 2.4 percent in 2002, about 39.7 percent of establishments created jobs. As the New York State economy makes the transition from recession to recovery, the number of jobs being added by new firm startups and expanding firms is expected to grow, while the number of jobs being eliminated by firms shutting down and contracting firms is expected to fall. A detailed examination of establishment-level microdata indicates that this is exactly what we see. Box 6 describes the methodology used to perform the analysis.

BOX 6
ANALYZING PRIVATE SECTOR EMPLOYMENT DYNAMICS AT THE ESTABLISHMENT LEVEL

The expansion or contraction of an industry over time is usually measured by the net change or net growth in jobs. However, a look beneath the net numbers into the mechanics of job creation and destruction at the establishment level facilitates a deeper understanding of the underlying dynamics.[1] The data for this study derive from the Covered Employment and Wages (CEW), or ES-202, program.[2] These data include all establishments subject to Federal unemployment insurance laws and cover approximately 98 percent of all employment. For the second quarter of 2003, the most recent period for which data are available, the CEW data covered 538,609 private sector establishments in New York State and 6,811,662 private sector employees.

Establishment-level data facilitate the investigation of questions that cannot be addressed at the aggregate level. Such questions include whether the primary source of job creation is new firm startups or existing firms that have chosen to expand, or whether net employment growth is the result of an increase in the rate of job creation or a decrease in the rate of job destruction. Two industries may exhibit the same net change in employment but one may have a high job turnover rate, resulting from high gross rates of gains and losses, while the other may have a low turnover rate. Previous studies have found that high turnover rates tend to be associated with high net growth.[3] Hence, the underlying dynamics may give clues as to the near-term direction of the business cycle, and an industry that suddenly starts to experience an increase in firm startups or gross job creation may turn out be a leading industry in the economy's next growth phase. Moreover, one can also determine whether new jobs are being created in relatively high-wage or low-wage industries.

Because CEW data are not seasonally adjusted, comparisons over time should be restricted to the same quarter of various years. We, therefore, analyze job growth relative to the same quarter of the previous year. For example, the gross number of jobs created between the second quarter of 2002 and the second quarter of 2003 is constructed by adding together the number of jobs created by firm startups (firms which existed during the second quarter of 2003 but did not exist four quarters prior), by expanding firms that existed in both quarters, and through firm mergers and acquisitions. Between the second quarter of 2002 and the second quarter of 2003, a total of 1,034,882 jobs were created from these three sources. Comparability across industries requires normalizing by a common base. Because the jobs that were eliminated between the two quarters are no longer in the 2003 job count, we follow BLS and define the base as the average of the two quarters. Performing this calculation for the second quarter of 2003 produces the following:

$$\text{Gross rate of job gain} = \frac{\text{Startup gains} + \text{Existing firm gains} + \text{M\&A gains}}{\text{Base}} = \frac{1{,}034{,}882}{6{,}839{,}719} = 15.1\%$$

This result indicates that the State's gross rate of job creation for the second quarter of 2003 is 15.1percent.

We similarly construct a gross rate of job destruction by adding together employment at firms that existed in the second quarter of 2002 but not in the second quarter of 2003, jobs lost from contracting firms that existed in both quarters, and jobs lost due to a merger or acquisition. We then divide by the State's job base as defined above, which for the second quarter of 2003 yields:

$$\text{Gross rate of job loss} = \frac{\text{Shutdown losses} + \text{Existing firm losses} + \text{M\&A losses}}{\text{Base}} = \frac{1{,}090{,}995}{6{,}839{,}719} = 16.0\%$$

This result states that the gross rate at which jobs were lost between the two quarters is 16.0 percent.

(continued on next page)

[1] For a similar analysis for the U.S., see U.S. Bureau of Labor Statistics (BLS), "Business Employment Dynamics: First Quarter 2003," <http://www.bls.gov/news.release/pdf/cewbd.pdf>. This study examines CEW data aggregated across industries for the period from the first quarter of 1992 through the first quarter of 2003. The long length of the series permits seasonal adjustment, which in turn allows comparisons relative to the prior quarter. Analysis at the industry level precludes seasonal adjustment since establishment data classified under NAICS are not available for the period prior to the first quarter of 2000. Nevertheless, our findings are generally consistent with the results of the BLS study.

[2] For a detailed description of CEW data, see *2003-04 New York State Executive Budget*, Appendix II, p. 100.

[3] See R. Jason Faberman, " Job flows and labor dynamics in the U.S. Rust Belt." *Monthly Labor Review*, September 2002, Vol. 125, No. 9, pp. 3-10.

BOX 6 *(continued from previous page)*

For the second quarter of 2003, the gross rate of job destruction exceeded the gross rate of job creation. We refer to the net number of jobs lost as the job gap, which for the second quarter of 2003 totaled 56,114. The net change in employment can also be represented by a net index of job creation, constructed by dividing the gross rate of job gain by the gross rate of job loss. For the second quarter of 2003, this calculation yields:

$$\text{Net index of job creation} = \frac{\text{Gross rate of job gain}}{\text{Gross rate of job loss}} = \frac{15.1\%}{16.0\%} = 94.9\%$$

A net index value of exactly 100 percent implies a job gap of zero; a value above 100 percent indicates that employment is growing, while a value below 100 percent, as we see above, indicates a net job loss.

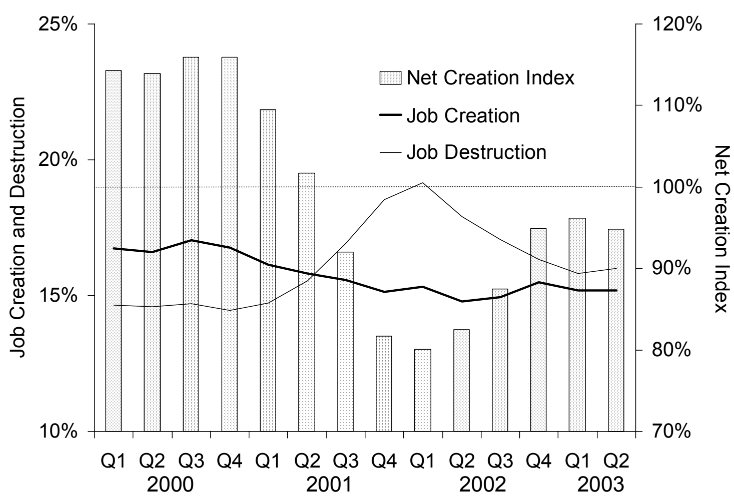
Clearly two industries could have similar values for the net index but have very different underlying dynamics. For example, by the second quarter of 2003, the construction sector and the transportation and warehousing sector had very similar net indices of job creation equal to 94.1 percent and 93.4 percent, respectively. However, underlying these numbers lie very different dynamics. As indicated in the table below, the construction sector has a much higher turnover rate than the transportation and warehousing sector. Understanding these differences have implications for fine-tuning the Budget Division employment forecast.

Employment Dynamics Comparison: 2003Q2

Sector (NAICS code)	Gross rate of job creation	Gross rate of job destruction	Net index of job creation
Construction (23)	20.1%	21.4%	94.1%
Transportation and Warehousing (48/49)	11.7%	12.5%	93.4%

The figure below plots the gross rates of creation and destruction (measured on the left scale) along with the net creation index (measured on the right scale) from the first quarter of 2000 to the second quarter of 2003, for the entire State private sector. The State economy was booming during 2000 and the first quarter of 2001, resulting in net index values well above 100 percent. In 2000, the gross job creation index averaged 17 percent, while the gross job destruction index averaged 14.8 percent. The net index averaged 115 percent, resulting in a net addition of 155,000 private sector jobs. On average, about one of every six jobs in 2000 was new relative to 1999.

Gross Job Creation and Destruction Indices



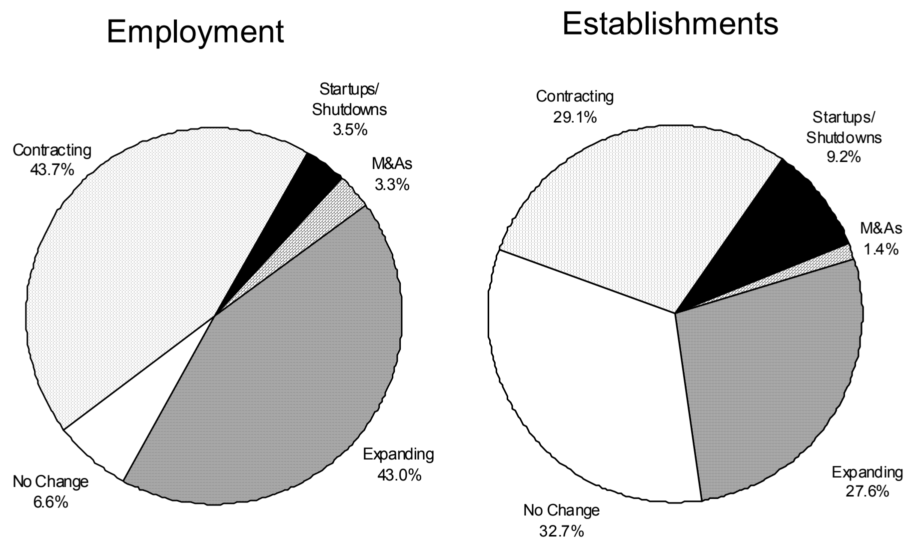
Source: Economy.com; DOB staff estimates.

By the third quarter of 2001, gross job destruction began to exceed gross job creation. However, the underlying dynamics indicate that the net decline in employment derived mainly from an acceleration in gross job destruction. Although gross job creation trended downward as of the first quarter of 2001, it is much flatter than the index of gross job destruction, indicating a relatively slow decline. However, the gross rate of job destruction rose steeply during the fourth quarter of 2001, reflecting the impact of September 11. The decline in the net index to 81.7 percent represents the loss of 236,500 jobs that occurred between the fourth quarter of 2000 and the fourth quarter of 2001.

Figure 23 shows the composition of the State's employment and establishment base as defined in Box 6 for the second quarter of 2003 by establishment type. Startups and shutdowns accounted for about 9.2 percent of the State's establishment base in the second quarter of 2003. Because these firms tend to be quite small, averaging only five employees, they accounted for only about 3.5 percent of the State's private sector employment base for that quarter. Indeed, startup firms did little more than replace firms that shutdown. Firms that were either acquired or absorbed by another firm account for 1.4 percent of the establishment base. The average size of these firms was about 23 employees and, therefore, account for 3.3 percent of employment.

Figure 23

Composition of State's Employment and Establishment Base 2003Q2



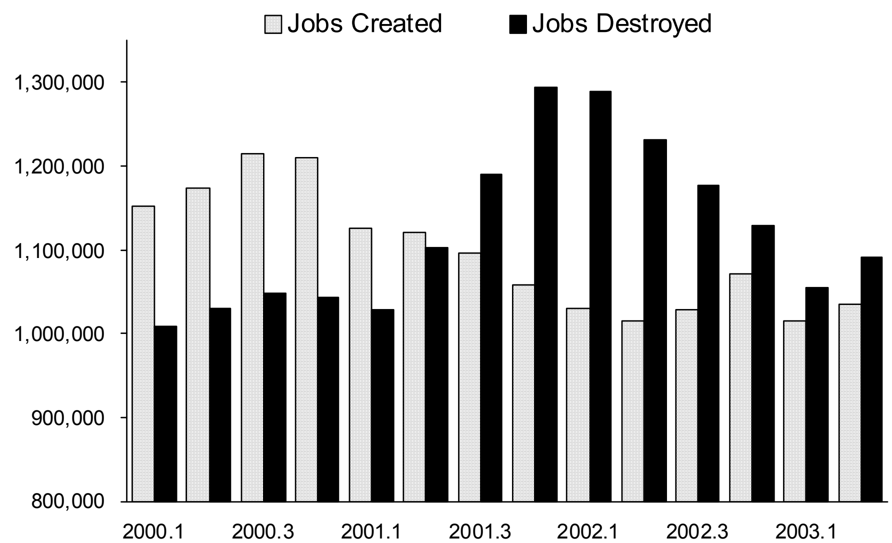
Source: NYS Labor Department; DOB staff estimates.

Existing firms account for an overwhelming proportion of both private sector establishments and employment — approximately 89.4 percent of the State's establishment base in the second quarter of 2003, and 93.2 percent of the job base. Existing firms are classified according to whether the firm expanded its workforce, reduced its workforce, or remained unchanged relative to the same quarter a year ago. As indicated in Figure 23, these types account for roughly equal shares of establishments but account for very different shares of employment. The average size of existing firms also varies by firm type, with those firms experiencing no change in employment averaging only three employees in 2002, expanding firms averaging 22 employees, and contracting firms averaging 18. Because existing firms account for so large a share of industry employment at any given point in time, they account for an overwhelming share of employment growth over time as well.

Figure 24 shows the gross numbers of jobs created and destroyed on a year-over-year basis for the period from the first quarter of 2000 through the second quarter of 2003. While the State economy was booming during the early part of the period, the gross number of jobs created well exceeded the gross number destroyed. However, the tide turned in the third quarter of 2001, with the number of jobs destroyed overtaking the number of jobs created. The full impact of September 11 is seen during the first quarter of 2002, when the gap between gross job destruction and creation is at its widest point. However, the job gap shows a narrowing trend after that, until a small widening in the second quarter of 2003, perhaps indicating the impact of the Iraqi conflict. The rate at which the job gap has narrowed supports the Budget Division forecast for positive year-over-year employment growth by the first quarter of 2004.

Figure 24

Job Creation and Destruction in New York



Source: NYS Department of Labor; DOB staff estimates.

Manufacturing

The long-term decline in New York manufacturing employment is expected to continue throughout the forecast period.[21] However, manufacturing's rate of job decline is projected to diminish over the course of 2004, with the improvement in both the U.S. and global economies, but only modestly. Manufacturing employment is expected to fall 3.4 percent in 2004, following a decline of 5.3 percent in 2003.

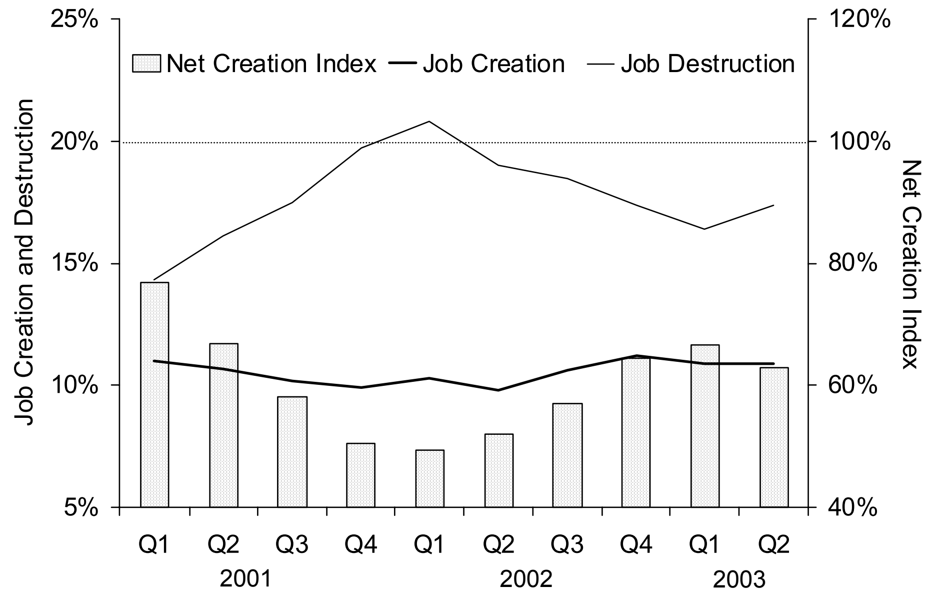
Since the mid-1970s, New York's comparative advantage has been shifting in favor of the production of services. Competitive pressures arising from increased globalization and rising productivity have resulted in the decline in State manufacturing employment each year since 1984. The rate of job loss from this sector accelerated during the recent recession, as it did during the earlier recessions of 1982 and 1991. As indicated in Figure 25, this acceleration was due to an increase in the gross rate of destruction, while the gross rate of job creation remained relatively flat.

The manufacturing sector lost 50,300 jobs in 2002, a decline of 7.2 percent, the fastest decline reported since the CEW program started in 1975. The rate of job loss eased somewhat in the first quarter of 2003, but rose slightly again in the second quarter. A total of 37,400 jobs were lost during the first half of 2003, a decline of 5.7 percent. The large size of the job gap during the first half of 2003 signals the likelihood that the State's manufacturing sector will continue to lose jobs in 2004.

[21] In evaluating the extent of the decline in manufacturing employment, care must be taken as to how jobs are classified. The number of jobs classified as manufacturing under the former SIC system is larger, and the decline more severe, than under the current NAICS system. For a detailed discussion, see *2003-04 New York State Executive Budget, Appendix II*, pp. 126-127.

Figure 25

Manufacturing



Source: NYS Department of Labor; DOB staff estimates.

Construction and Real Estate

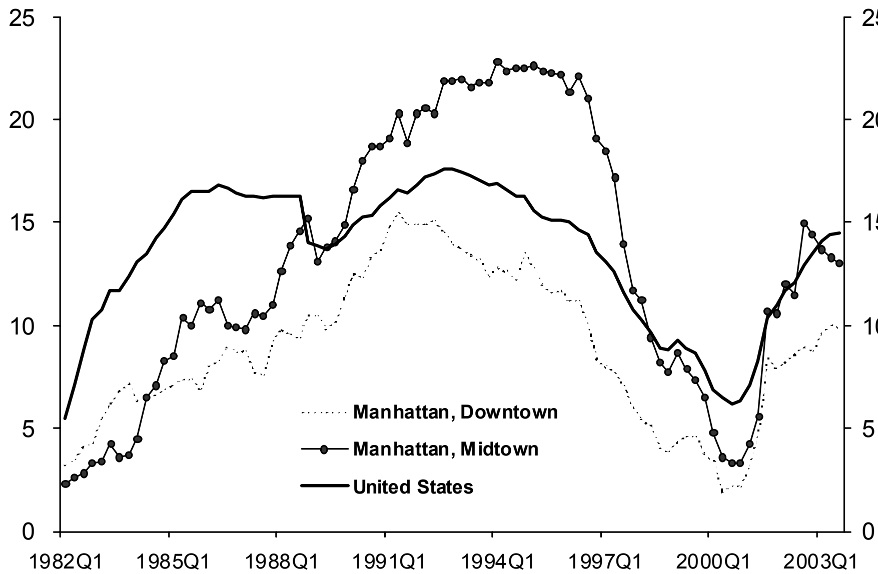
Construction employment is projected to rise 5.3 percent in 2004, following growth of 1.3 percent in 2003. Recent high levels of activity in the construction and real estate markets represent a key factor in distinguishing New York's 2001-03 recession from that of the early 1990s. State construction sector employment fell during all five years from 1989 to 1993, declining at double-digit rates in 1991 and 1992. In contrast, construction sector employment fell only 3.1 percent in 2002, due in part to the impact of historically low interest rates on the demand for housing. This same distinction between the two downturns can be observed in office vacancy rates as well (see Figure 26). Although vacancy rates in Manhattan have increased since 2000, they are far from the high rates attained during the early 1990s. Vacancy rates in midtown Manhattan fell during the second half of 2002 and the first three quarters of 2003.

Although construction employment continued to fall during the first half of 2003, the job gap has been gradually narrowing since the second quarter of 2002. By the second quarter of 2003, this sector's index of net job creation was 94.1 percent. The construction sector is expected to gain jobs during the second half of 2003 and grow briskly in 2004 and in the outyears. Contributing to these increases will be the reconstruction effort on the site of the World Trade Center. The groundbreaking for the "Freedom Tower" is scheduled for August 2004, with construction expected to be completed by September 11, 2008.

The real estate sector took a big hit after September 11, mainly because of an increased rate of job destruction. However, the industry bottomed out during the first quarter of 2002, and thanks to the housing boom of the last two years, the industry's index of net job creation exceeded 100 percent during the first half of 2003. Real estate rental and leasing sector employment increased 1.0 percent during the same period, due to a very strong housing market. Industry employment is expected to remain flat in 2004, as activity in the housing market begins to moderate.

Figure 26

Office Vacancy Rates



Source: Economy.com.

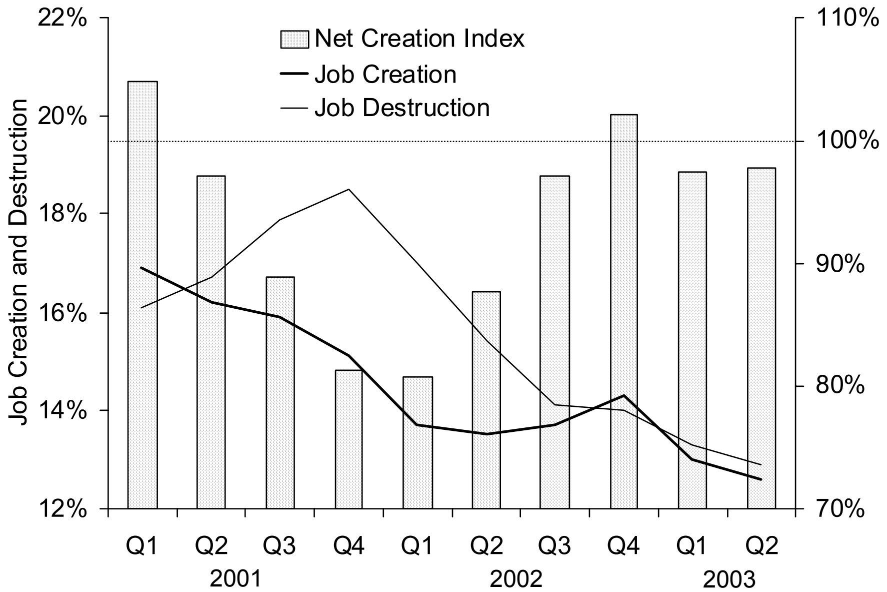
Trade, Transportation, and Warehousing

Both wholesale and retail trade employment are projected to grow 0.4 percent in 2004, following a decline of 0.7 percent and virtually no change, respectively, in 2003. The State's wholesale and retail trade sectors have suffered heavy job losses due to the long lasting impact of September 11 and the slow national economic recovery during 2002.

The wholesale trade sector has been dominated by job declines since early 2001. But wholesale trade lost 1,600 jobs in the first half of 2003, a decline of only 0.5 percent and a significant improvement from 2002. Wholesale trade is expected to be a net contributor to job growth in 2004 as the State and national economies improve. The job gap in the retail trade sector narrowed significantly during the second half of 2002 and remained small during the first half of 2003, lending support to the expectation that this sector will add jobs in 2004 (see Figure 27). By the first half of 2003, this sector's gross rate of job creation and destruction were well below the statewide average.

Transportation and warehousing employment, which tends to track the trade sectors very closely, is projected to increase 0.6 percent in 2004, following a decline of 0.8 percent for 2003. The impact of September 11 on employment is perhaps seen most dramatically in the transportation sector. The job gap in that sector was at its maximum during the first quarter of 2002, but has gradually narrowed since then, due primarily to a decline in the gross rate of job destruction. The substantial narrowing of the job gap in the State's transportation and warehousing sector suggests that employment in this sector is likely to grow in 2004.

Figure 27
Retail Trade



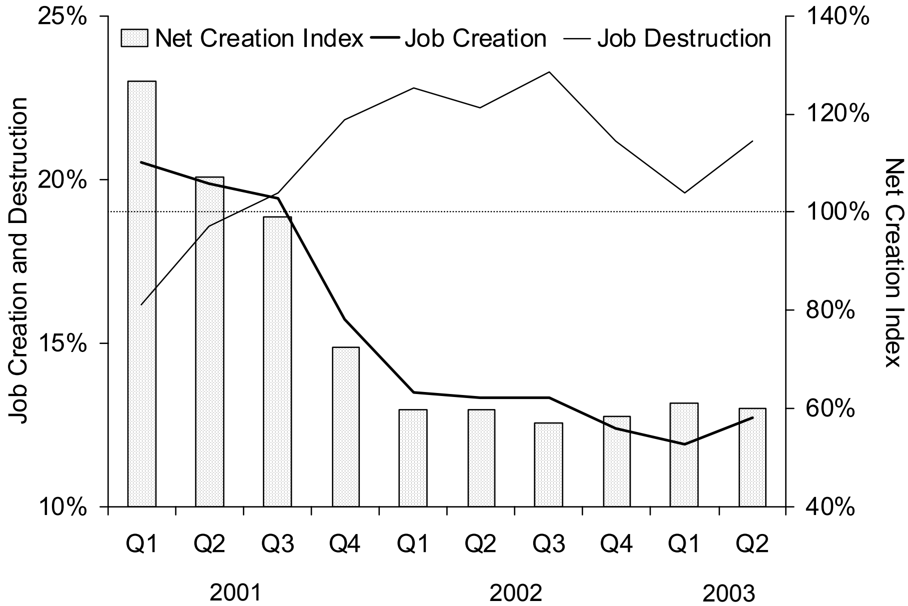
Source: NYS Department of Labor, DOB staff estimates.

Information (Media and Communications)

The Budget Division expects information sector employment to fall during 2004 at a rate of 2.1 percent, following a 6.1 percent decline in 2003. The information sector, which includes publishing, motion picture, broadcasting and telecommunications, is one of the most dynamic sectors in the State, exhibiting gross rates of job creation and destruction generally well above the statewide averages (see Figure 28). However, this sector has been in contraction since the start of the State's recession. Although the rate of contraction has stabilized, it continued to exhibit a wide job gap and a net job creation index of only about 60 percent during the first half of 2003.

Following the collapse of the "dot-com" sector in 2000 and 2001, the State's media services and telecommunications industries shed jobs at the highest rate of any sector in 2002. Employment in the information sector declined 8.8 percent, or by 28,500 jobs in 2002. The downward trend for this industry group continued during the first half of 2003. The State lost another 23,800 jobs, 7.9 percent, during the first two quarters of 2003 versus the same period of 2002. Almost 80 percent of these job losses occurred in the downstate region.

Figure 28
Information Services



Source: NYS Department of Labor, DOB staff estimates.

Finance and Insurance

The Budget Division expects finance and insurance sector employment to grow a modest 0.4 percent in 2004, following a decline of 1.5 percent in 2003. This forecast is consistent with a net job creation index value of close to 90 percent during the first half of 2003. The attacks of September 11, the national recession and corporate scandals all combined to have a significant impact on the State's financial sector. About 30,000 jobs in finance and insurance were lost in 2002, a decline of 5.4 percent. New York City more than accounts for these losses. This trend continued during the first half of 2003, with the securities industry losing another 13,400 jobs. However, as discussed below, these job losses lowered industry compensation costs and helped Wall Street firms to increase profits significantly in 2003. Industry employment is not expected to recover quickly. Indeed, in the aftermath of the stock market crash of 1987 and the recession of 1990-91, it took 10 years for the securities industry to return to its employment peak of 1987. Nevertheless, the narrowing of this sector's job gap during the first half of 2003 suggests it is reasonable to expect some growth in 2004.

Business and Professional Services

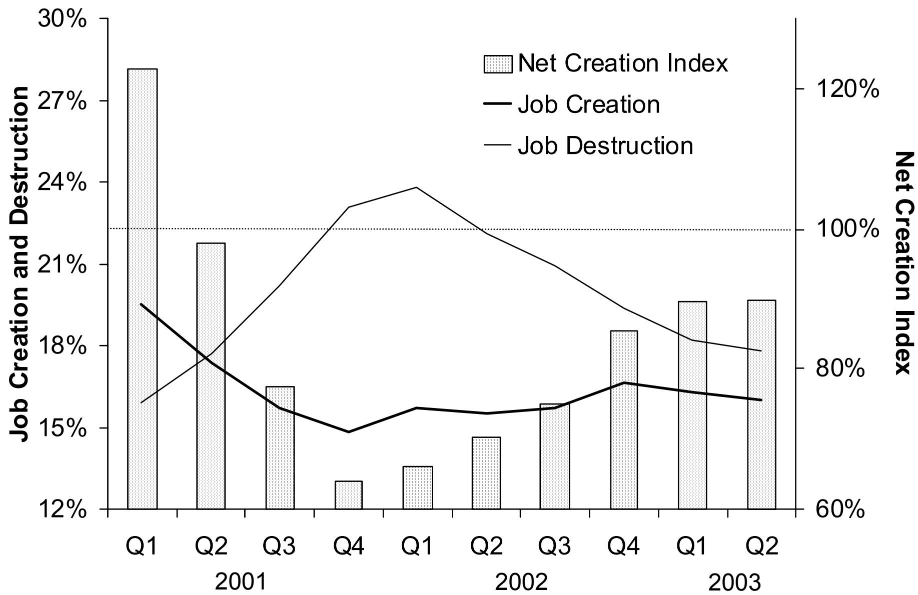
All of the State's business and professional services industries are expected to benefit from the strengthening national expansion in 2004. Professional and technical services industries are expected to grow 1.2 percent in 2004, following a decline of 0.8 percent in 2003, while management and administrative support services industries are expected to grow 1.7 percent in 2004, following a decline of 1.3 percent in 2003.

With the collapse of the high-tech bubble, the State's professional, scientific, and technical services industries saw a significant increase in the rate of gross job destruction during 2001 and early 2002 (see Figure 29). However, the job gap narrowed substantially in the first half of 2003, due primarily to a reversal of that trend, indicating that this sector is poised to grow in the near future.

The gross job destruction index rose swiftly in the management, administrative, and support services sectors in 2001, but the job gap had narrowed significantly by the fourth quarter of 2002. This sector contains temporary help services, one of the first types of employment to grow following a downturn. However, management services growth may have been stymied by the desire to avoid expanding management operations in New York in the wake of September 11.

Figure 29

Professional, Scientific & Technical Services



Source: NYS Department of Labor; DOB staff estimates.

Education and Healthcare

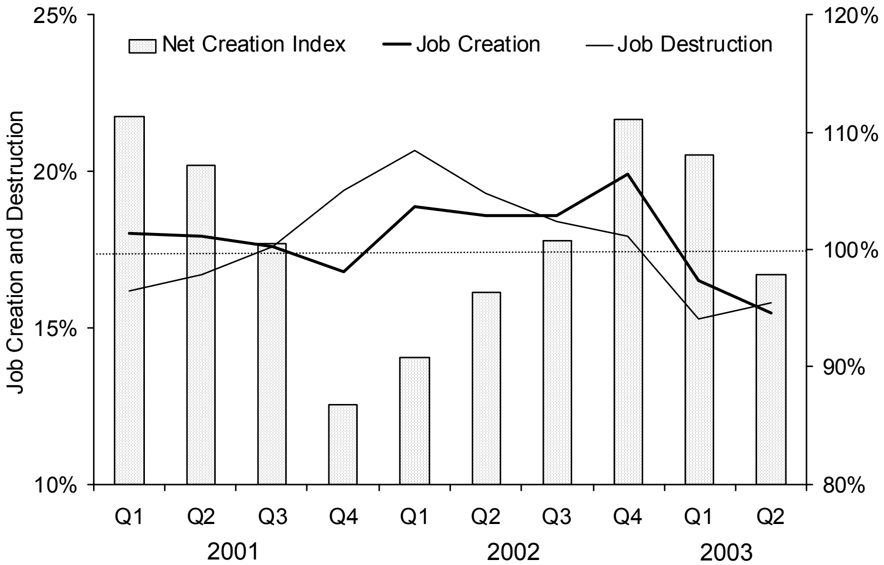
The Budget Division expects education and healthcare employment to grow 2.9 percent and 2.1 percent, respectively, for 2004. Education and healthcare services continued to grow throughout the recession, exhibiting net job creation indices remaining well above 100 percent. Education services grew 4.1 percent during the first half of 2003 compared to the same period in 2002, adding 10,400 jobs. Similarly, healthcare and social assistance services grew 2.1 percent during the first half of 2003, adding 23,600 jobs, following growth of 2.0 percent for 2002. The growth in the healthcare industry is expected to continue in line with the legislated expansion of government-sponsored healthcare programs and the rise in insurance premiums.

Leisure, Hospitality, and Other Services

The Budget Division expects leisure, hospitality, and other services employment to grow 1.4 percent in 2004, following growth of 0.9 percent in 2003. September 11 had a severe impact on these industries, particularly the arts and entertainment sectors. A steep increase in the rate of gross job destruction was experienced during the fourth quarter of 2001 and first quarter of 2002, although the sector began to bounce back soon thereafter (see Figure 30). This sector experienced a decline in gross job creation during the first two quarters of 2003, perhaps due to the climate of uncertainty engendered by the conflict in Iraq. Nevertheless, these sectors are expected to add jobs during the second half of 2003 and in 2004 as well.

Figure 30

Leisure, Hospitality and Other Services



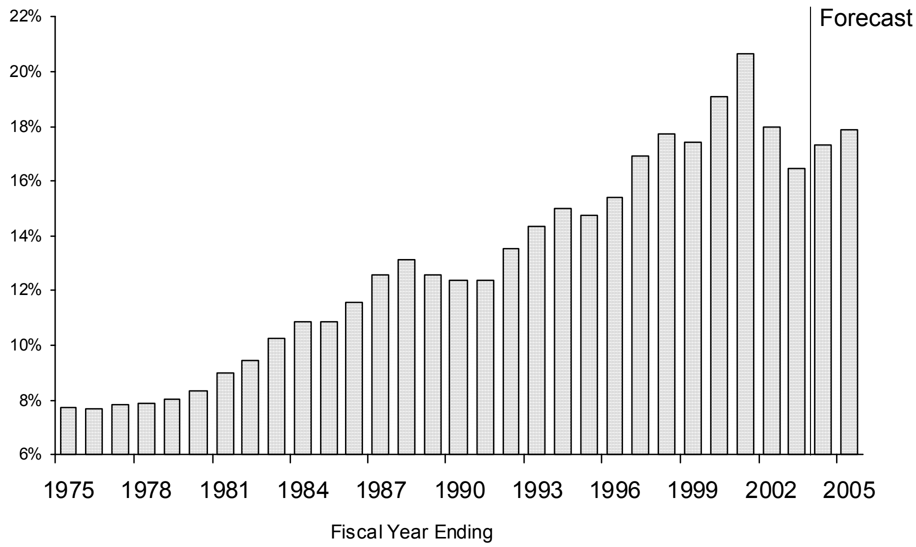
Source: NYS Department of Labor, DOB staff estimates.

The Securities Industry and the Stock Market

Because of the prominence of New York City in the world of finance, New York State revenues are profoundly affected by the fortunes of the financial markets. Figure 31 shows how finance and insurance sector wages have grown over time as a share of the State total. That share peaked at 20.6 percent during the 2000-01 State fiscal year, just as the stock market was beginning to collapse. In contrast, finance and insurance sector employment accounted for only 6.6 percent of total State employment during the same year. The financial markets affect employment and incomes in New York City and its surrounding suburbs, both directly, through compensation paid to finance sector workers and purchases made by finance sector firms, and indirectly, as finance sector workers spend their incomes on housing, entertainment, and other purchases. Finance sector workers are, on average, very highly compensated, as demonstrated by a comparison of their average wages to those of other New Yorkers (see Figure 32).

Figure 31

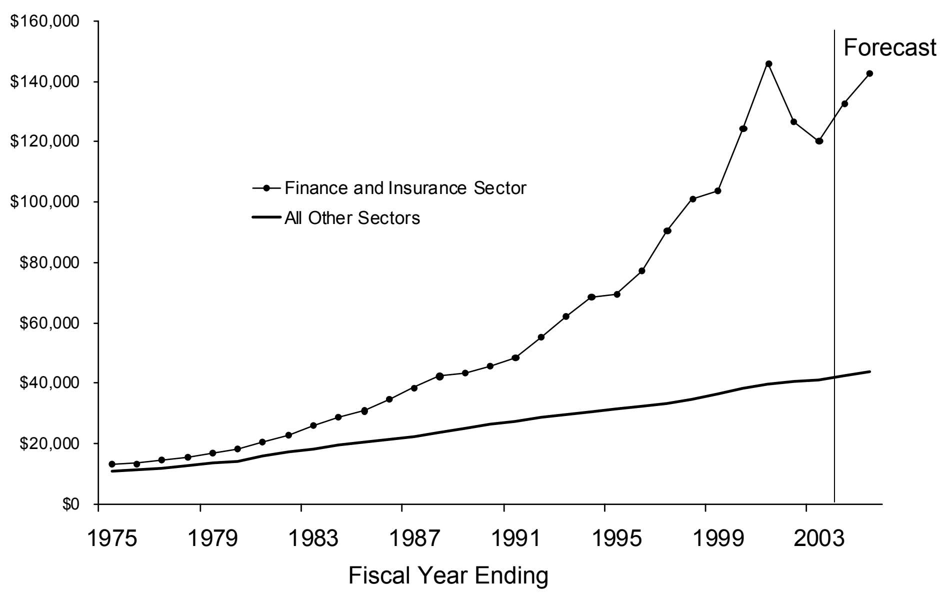
Finance and Insurance Sector Wages as Share of State Total



Source: NYS Department of Labor; DOB staff estimates.

Figure 32

Average Wages in New York



Source: NYS Department of Labor; DOB staff estimates.

The current bull market in equities has endured for over a year. Table 7 puts the current market in historical perspective. Since the end of World War II, there have been 10 bear markets, defined as a sustained drop in Standard and Poor's 500 Index (S&P 500) of about 20 percent or more. As seen in the table, each market cycle begins with a run-up in equity prices, or bull market, during which the market's previous high is reached and is eventually surpassed.

TABLE 7
BULL AND BEAR MARKETS

Price Run-Up	Peak Dates	Trough Dates	Percent Changes	Duration in Months	Market Hit Previous High: Dates	Market Hit Previous High: Months
(1)	(2)	(3)	(4)	(5)	(6)	(7)
	08/03/56	10/22/57	(21.5)	14.6	09/24/58	11.1
85.7%	12/12/61	06/26/62	(28.0)	6.5	09/03/63	14.2
78.8%	02/09/66	10/07/66	(22.2)	7.9	05/04/67	6.9
47.2%	11/29/68	05/26/70	(36.1)	17.9	03/06/72	21.4
73.5%	01/11/73	10/03/74	(48.2)	20.8	07/17/80	69.4
73.1%	09/21/76	03/06/78	(19.4)	17.5	08/15/79	17.3
58.9%	01/06/81	08/12/82	(25.8)	19.2	10/20/82	2.3
228.8%	08/25/87	12/04/87	(33.5)	3.4	07/19/89	19.5
64.8%	07/16/90	10/11/90	(19.9)	2.9	02/13/91	4.1
417.0%	03/24/00	10/09/02*	(49.1)	30.5	?	?

Note: To-date the S&P 500 has risen 44.7 percent since the October 9, 2002 trough, but would have to rise another 36 percent, or about 400 points to reach its prior peak.
Source: Economy.com.

As indicated in column (4) of Table 7, only the bear market of 1973-74 is comparable to the most recent one in terms of the percentage decline in prices. However, the 2000-02 bear market surpassed that of 1973-74 in length by almost one year, making it the longest bear market of the postwar period. Following most postwar bear markets, stock prices managed to attain their prior peaks within two years of the trough. However, it took almost six years after the 1973-74 bear market for stock prices to reach their former January 11, 1973, high. It is likely to take even longer for the market to return to its more recent March 2000 record level. As of January 6, 2004, the S&P 500 had risen 44.7 percent since the October 9, 2002, trough, but will have to rise another 36 percent, or about 400 points, before reaching its prior peak.

Equity market cycles tend to be accompanied by a rise and fall in securities industry employment, although typically with a lag. For example, in the bear market of 1973-1974, the State's securities industry lost 23 percent of its employment from February 1973 to October 1974. The record-setting bull market that lasted from October 1990 to March 2000 was the longest of the postwar period and characterized by the largest run-up in prices, 417 percent. It was also accompanied by a 50 percent increase in industry employment. However, since peaking in December 2000, State securities employment has fallen by about 18 percent. History suggests that it could take years, and perhaps intervening bull and bear markets, before employment recovers to the record levels reached in 2001.

Despite the recent improvement in the equity prices, the securities industry's most lucrative sources of income — initial public offerings (IPOs) and merger and acquisition activity — remain much reduced from their 2000 peaks. With secondary market prices still well below their 1999-2000 levels, firms are more reluctant to use equity financing to fund business expansion. The rebound from the market lows of October 2002 lost momentum as the nation began to head down the path toward war, resulting in a substantial weakening in the markets for IPOs and mergers and acquisitions in the first half of 2003. However, markets for these activities started to strengthen toward the end of that year.

True IPOs are projected to raise a total of $15.9 billion in 2003, a decline of 38.2 percent from the $25.8 billion raised in 2002.[22] However, the number of deals increased substantially over the course of the year. While only $2.4 billion was raised in the first half of 2003, deals valued at $13.5 billion were reported for the second half. Moreover, the industry reports a significant backlog in the pipeline entering 2004 worth $10.1 billion.

Most affected by the decline in the secondary equities market has been merger and acquisition activity. After peaking in number and value in 2000, the number of completed domestic mergers and acquisitions fell 34 percent in 2001 and another 52 percent in 2002. Completed domestic mergers and acquisitions saw a decline in value of about 60 percent in the three-year period from 2000 to 2002. For the first nine months of 2003, the number and value of completed U.S. mergers and acquisitions were the lowest since 1994. Because of the high fees involved, the decline in mergers and acquisitions represents a large revenue loss for the industry. However, like the IPO market, there appears to have been a rebound in this market toward the end of 2003, with announced deals valued at $119 billion reported for October, an increase of 330 percent from October 2002.

Debt underwriting activity was running at record levels in early 2003 due to declining interest rates, but showed some slowing toward the end of year. However, year-to-date debt underwriting is still projected to be up about 12 percent from 2002. Total corporate debt issuance is expected to reach about $2.9 trillion in 2003, versus nearly $2.6 trillion in 2002.

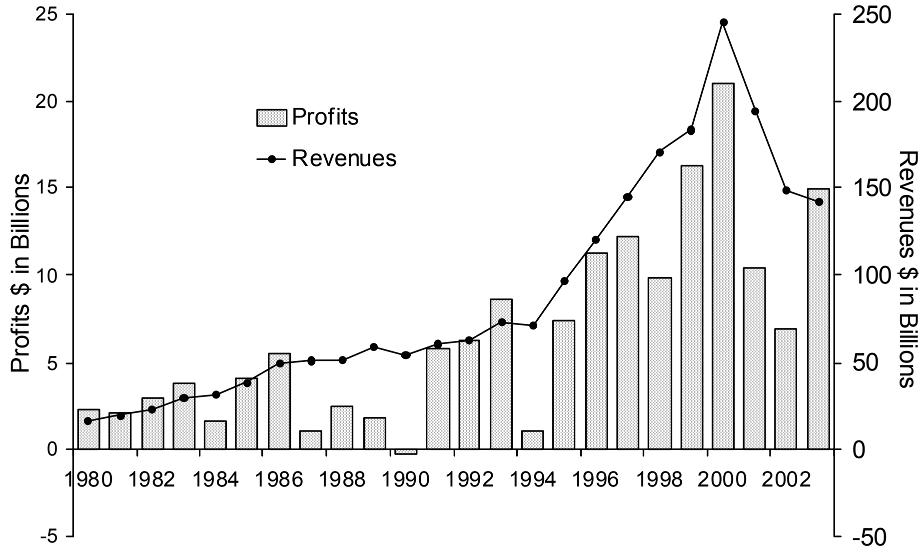
The combined effects of a weak start to the economic expansion, the decline in equity values, and national security concerns can be seen in the income levels of financial services firms. Pre-tax profits for the securities industry peaked at $21.0 billion in 2000, but fell 51 percent below that mark in 2001 (see Figure 33). Profits were only $6.9 billion in 2002. But, as indicated above, the improvement in both the economy and equities markets in the wake of the Iraq war has had a very positive impact, with securities industry profits of $15.0 billion now projected for 2003. However, much of this increase in profits has come about because of aggressive cost cutting by the industry. In fact, revenues generated for 2003 were about 4.5 percent below 2002, and 42.1 percent below 2000 levels.

In the wake of the economic downturn of 2001, the securities industry was able to cut expenses on gross interest and employee compensation. Due to the series of reductions in the federal funds rate that began in the first quarter of 2001 as the Federal Reserve sought to stimulate the economy, the gross interest expense of the industry fell an estimated 62 percent from 2000 to 2003. Reductions in personnel costs came from two sources: reductions in employment and reductions in compensation. Through the second quarter of 2003, the State's finance and insurance industry cut employment by 8.2 percent over a two-year period, eliminating 45,700 jobs. In addition, production payouts (payments tightly tied to revenue-generating activity) and bonuses (a more discretionary form of compensation) were reduced. Figure 34 shows that finance and insurance sector bonuses fell by about one-third in the 2001-02 fiscal year and are estimated to have fallen yet again in 2002-03.

[22] Securities Industry Association. True IPOs exclude closed-end funds.

Figure 33

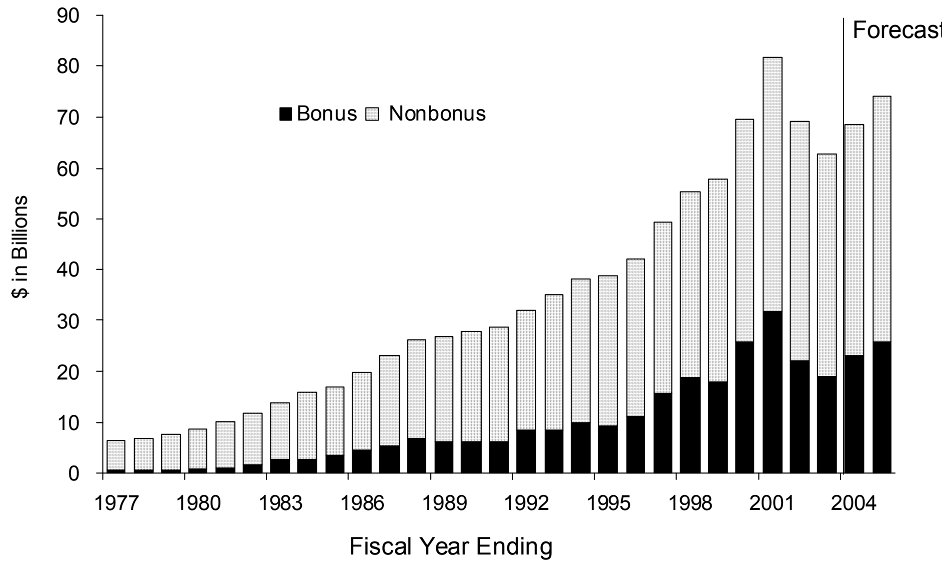
Securities Industry Profits and Revenues



Source: Securities Industry Association.

Figure 34

Total Wages in the Finance and Insurance Sector



Source: NYS Department of Labor; DOB staff estimates.

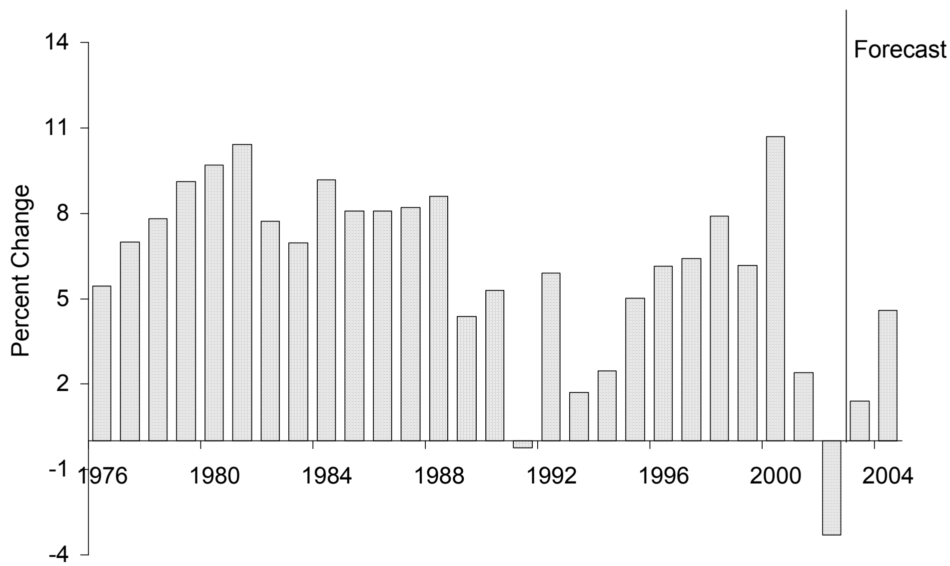
The combination of lower employment and lower compensation reduced total finance and insurance sector wages by 23.4 percent, from $81.9 billion in 2000-01 to $62.7 billion in 2002-03. The impact of these declines on finance and insurance sector wages as a share of the State total is clearly visible in Figure 31, while Figure 32 shows the concomitant impact on the industry average wage for both 2001-02 and 2002-03. However, with the industry's improved profit performance, compensation costs are expected to rise. The finance and insurance bonus share of total sector wages is expected to rise for both 2003-04 and the following year, though remaining below its former peak amount. As discussed above, sector employment is projected to grow in 2004 and a rising equity market is expected to result in higher production payouts and discretionary bonuses.

Outlook for Income

Growth in variable compensation and employment is expected to result in total wage growth of 5.1 percent for 2004, following an estimated increase of 1.8 percent for 2003 (see Figure 35). The strong growth in State wages, property income, and proprietors' income projected for 2004 will result in total personal income growth of 5.1 percent, following growth of 3.1 percent for 2003 (see Table 10).

Figure 35

New York State Wage Growth



Source: NYS Department of Labor; DOB staff estimates.

Because the state-level wage data published by BEA have proven unsatisfactory for the purpose of forecasting State personal income tax liability, the Budget Division constructs its own wage and personal income series based on CEW data. Moreover, because of the importance of trends in variable income — composed of bonus and stock options income — to the understanding of trends in State wages overall, the Budget Division has developed a methodology for decomposing its wage series into bonus and nonbonus wages. For a detailed discussion, see Box 7. The Budget Division's outlook for State income is based on these constructed series.

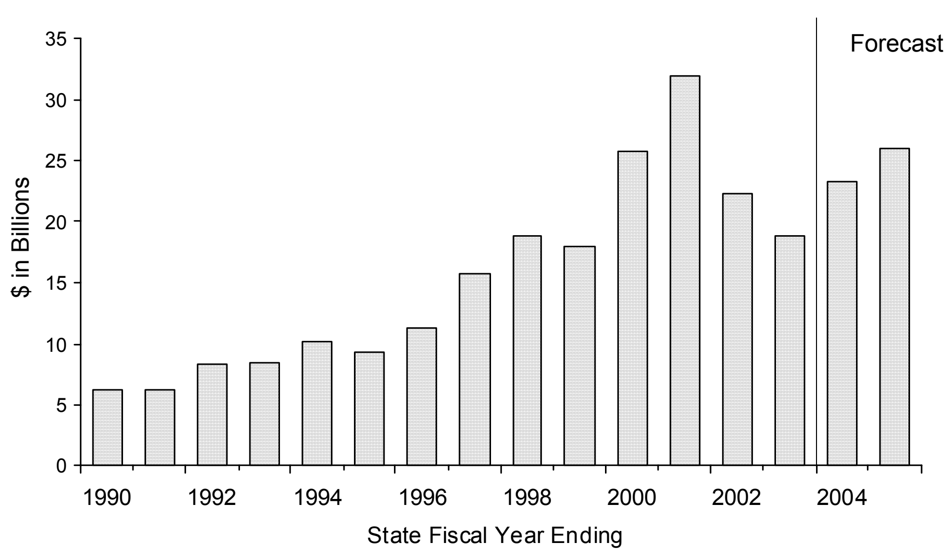
Variable Income Growth

Variable income is defined as that portion of wages derived primarily from bonus payments and stock incentive income, but also includes other one-time payments. As performance incentives for a given calendar year, firms tend to pay employee bonuses during either the fourth quarter of that year or the first quarter of the following year. Although stock options tend to be granted as part of a bonus package during the same quarters as the cash component, an employee may exercise that option, thus transforming it into taxable income, at different times. However, the concentration of variable income payments in the fourth and first calendar-year quarters makes the State fiscal year a logical period of analysis for discussing the determinants of variable income growth. Total State variable income is projected to rise 8.9 percent in the 2004-05 fiscal year, following growth of 15.2 percent in 2003-04. Growth in both years is more than accounted for by the finance and insurance sector, although bonus income in other sectors is expected to increase as well, with the exception of the information sector. On a calendar year basis, total State bonus income is expected to decrease 2.2 percent for 2003, followed by an increase of 12.7 percent for 2004.

Since 1990, there has been a substantial shift in the State's corporate wage structure away from fixed to performance-based pay. Figure 36 portrays how dramatically variable income paid to employees in the finance and insurance industry has grown since the early 1990s. The robust performance of security industry profits during 1999 and 2000 resulted in finance and insurance sector bonus growth of 43.5 percent and 23.7 percent in the 1999-2000 and 2000-01 State fiscal years, respectively, to levels that accounted for more than half of total bonuses paid in the State. An incentive-based payment structure allows employers to share with employees the risks of doing business and is particularly attractive to the securities industry, given the degree of volatility in industry profits. For example, when industry profits fell from $10.4 billion in 2001 to $6.9 billion in 2002, finance and insurance sector bonus income is estimated to have fallen 15.4 percent for the 2002-03 State fiscal year. In contrast, nonbonus income for this sector is estimated to have fallen only 6.4 percent, mainly due to the decline in employment.

Figure 36

New York State Finance and Insurance Sector Bonuses



Source: NYS Department of Labor; DOB staff estimates.

BOX 7
THE CONSTRUCTION OF NEW YORK STATE WAGES AND THE ESTIMATION OF VARIABLE INCOME

Trends in State wages are critical to an accurate analysis and forecast of personal income tax liability and collections. To improve the link between the economic and tax variables on a quarterly basis, the Division of the Budget (DOB) constructs its own wage series from the available primary data sources. This series differs from the data published by the U.S. Bureau of Economic Analysis (BEA).

The Division of the Budget uses only New York data to construct its State wage series. The primary source is data collected under the Covered Employment and Wages (CEW) Program. In contrast, the BEA uses national information to adjust the quarterly values for seasonal variation, as well as to ensure that state-level wages add up to national estimates. The consequence is often a significant difference between the two series in both the quarterly pattern and the annualized growth rates. For example, according to staff estimates based on the CEW data, wage growth rates for the first and second quarters of 2000, on a percent-change-year-ago basis, were 18.3 percent and 8.5 percent, respectively. The comparable growth rates originally published by the BEA were 2.4 percent and 5.4 percent. These estimates have since been revised up to 6.3 percent and 10.0 percent, respectively. However, the lack of timeliness in the revision process limits the usefulness of BEA for State forecasting purposes.

A comparison with yet another source of wage data also demonstrates the greater accuracy of the CEW data. Since the amount of wages withheld for personal income tax purposes varies systematically with wages itself, withholding data provide a useful guide for estimating State wage growth. For example, wages withheld during the first quarter of 2000 were 18.6 percent above withholding for the same quarter of the previous year. This estimate is much more consistent with the growth rate derived from the CEW data than with the BEA's estimate of 2.4 percent.

Once an entire year of CEW data becomes available, the BEA revises its state-level wage data to be more consistent with that data source. For this reason, the Division of the Budget's method performs well in anticipating the BEA's revised estimates of annual growth in New York wages. To make the actual magnitudes of the Division of the Budget's wage series more strictly comparable to the BEA wage series, noncovered and unreported legal wages must be added to wages taken directly from the CEW data. The addition of these components typically changes the annual growth rate for State wages by no more than two-tenths of one percentage point.

An increasing portion of New York State wages is paid on a variable basis, in the form of either bonus payments or proceeds derived from the exercise of stock options. Because no government agency collects data on variable income as distinct from ordinary wages, it must be estimated. The Division of the Budget derives its estimate of bonuses from firm-level data as collected under the CEW program. This method allows a large degree of flexibility as to when individual firms actually make variable income payments. However, as with any estimation method, some simplifying restrictions are necessary. DOB's method incorporates the assumption that each establishment makes variable income payments during at most two quarters of the year. However, the determination as to which quarters contain these payments is made at the firm level.

Firms report their wages to the CEW program on a quarterly basis. The firm's average wage per employee is calculated for each quarter. The average over the two quarters with the lowest average wages is assumed to reflect the firm's base pay, that is, wages excluding variable pay. If the average wage for either of the remaining quarters is significantly above the base wage, then that quarter is assumed to contain variable income.[1] The average variable payment is then defined as total average wage minus the base average wage, after allowing for an inflation adjustment to base wages. Total variable pay is then calculated by multiplying the average bonus payment by the total number of firm employees. It is assumed that only private sector employees earn variable pay.

[1] The threshold adopted for this purpose was 25 percent. However, the variable income estimates are fairly robust to even a five-percentage-point swing in this criterion.

The rapid run-up in finance and insurance bonuses was abruptly reversed during the 2001-02 State fiscal year when bonuses dropped 30.2 percent as a result of the national recession, the World Trade Center terrorist attack, and the downslide in equity prices. Securities industry profits further deteriorated in 2002, dropping 67.0 percent from their record 2000 level. With the recent rise in equity prices and the strong performance of the fixed income market, securities industry profits are projected to more than double in 2003.

However, the impact of this strong profit performance is likely to be tempered by relatively flat growth in revenues. Therefore, the Division of the Budget projects that variable income for the finance and insurance sector will grow 23.2 percent to $23.2 billion during the 2003-04 State fiscal year. Although this represents the highest bonus payout for this sector since the 2000-01 bonus season, it is still 27.3 percent below the record $31.9 billion estimated to have been paid out that year. Variable income for the sector is expected to rise 11.7 percent during 2004-05, bringing it back up to its 1999-00 level.

Nonbonus Wages

Unlike the variable component of income, nonbonus wages are driven largely by changes in employment and the nonbonus average wage, and are therefore relatively more stable. After adjusting for inflation, the nonbonus average wage for each of the State's industrial sectors is believed to have a stable long-run relationship with the real U.S. average wage. However, State real average wages can deviate from their long-run trend due to short-term fluctuations related to business cycles or shocks to the regional economy. Nonbonus average wages are projected to increase by 3.3 percent in calendar 2004, following estimated growth of 2.7 percent for 2003. With a positive boost from employment, total nonbonus wages are projected to grow 4.1 percent for 2004, following an increase of 2.3 percent for 2003.

Average Wage

For the first time in the history of CEW data, which begins in 1975, average wages in New York showed a decline in 2002. This was mostly due to the steep decline in bonuses. However, the increase in bonuses is expected to contribute to stronger growth in the State's overall average wage of 4.3 percent for 2004, following an estimated 2.2 percent increase for 2003. The 2004 forecast for average wage growth is significantly below its historical average due to low expected inflation. The Budget Division projects growth in the composite CPI for New York of 2.1 percent for 2004, following growth of 2.8 percent for 2003.

Nonwage Income

The Division of the Budget projects a 5.1 percent increase in the nonwage components of State personal income for 2004, following growth of 4.9 percent for 2003. The modest increase in growth for 2004 is attributable to higher growth in property income, transfer income and proprietors' income.

BOX 8
THE NEW YORK STATE DIVISION OF THE BUDGET'S
NEW YORK MACROECONOMIC MODEL

DOB's New York Macroeconomic model (DOB/N.Y.) attempts to capture the fundamental linkages between the New York and the national economies. Clearly, New York's economy depends on economic developments in the U.S. economy, usually expanding when the national economy is growing and contracting when the nation is in recession. However, this relationship is neither simple nor static. The growth rate of the State's economy can vary substantially in comparison to the nation. For example, during the 1990-91 national recession, the State's recession began noticeably earlier and ended significantly later than for the nation as a whole. Alternatively, during the early 1980's recession, the State's economy fared better than the nation.

The objective of DOB/N.Y. is to quantify the linkages between the national and State economies within an econometric modeling framework. DOB/N.Y. is a structural time series model with most of the exogenous variables derived from DOB/U.S. In general, the long-run equilibrium relationships between State and national economic variables are captured by a cointegration/error-correction specification, while the State's specific dynamics are modeled using a restricted vector autoregressive (RVAR) framework. DOB/N.Y. has four major components: a nonfarm payroll employment segment, a real nonbonus average wage segment, a bonus payment segment, and a nonwage income segment.

Employment

The national economy affects New York employment through two channels. First, if State employment growth for a specific sector is related to the growth of the U.S. employment in the same sector, U.S. employment for that sector is specified as an exogenous variable in the equation. Second, overall U.S. economic conditions, as measured by the growth of real U.S. GDP, is included either directly in the employment equations for some sectors or indirectly through the VAR relationships.

Intra-sectoral relationships for New York employment can be different from those for the nation as a whole. These relationships are captured in a restricted VAR model where the impact of one sector on other sectors is explicitly specified.

Average Real Nonbonus Wages

Our analysis suggests the existence of a long-run equilibrium relationship between real nonbonus average wage for most New York sectors and the national real average wage. Thus, the State average real nonbonus wage by sector is modeled in a cointegration/error-correction framework. This modeling approach is based on the belief that, in the long run, since both labor and capital are free to move in a market economy, regional differences in labor costs tend to disappear, though this process may take quite a long time. This formulation allows for short-run adjustments towards equilibrium, which describe the short-run dynamics of State-specific economic conditions.

Bonus Income

The DOB model for finance and insurance bonus income incorporates those factors that drive Wall Street profits: merger and acquisition activity, IPOs, and the volume of debt underwriting. Our analysis shows that bonuses paid in the State's other economic sectors tend to have long-term equilibrium relationships with those paid in the finance and insurance sectors; more technically, bonus payments in the financial services sector are cointegrated with bonuses paid in most other sectors. Consequently, the results from the finance and insurance sector bonus model are used to estimate bonuses paid in other sectors.

Nonwage Incomes and Other Variables

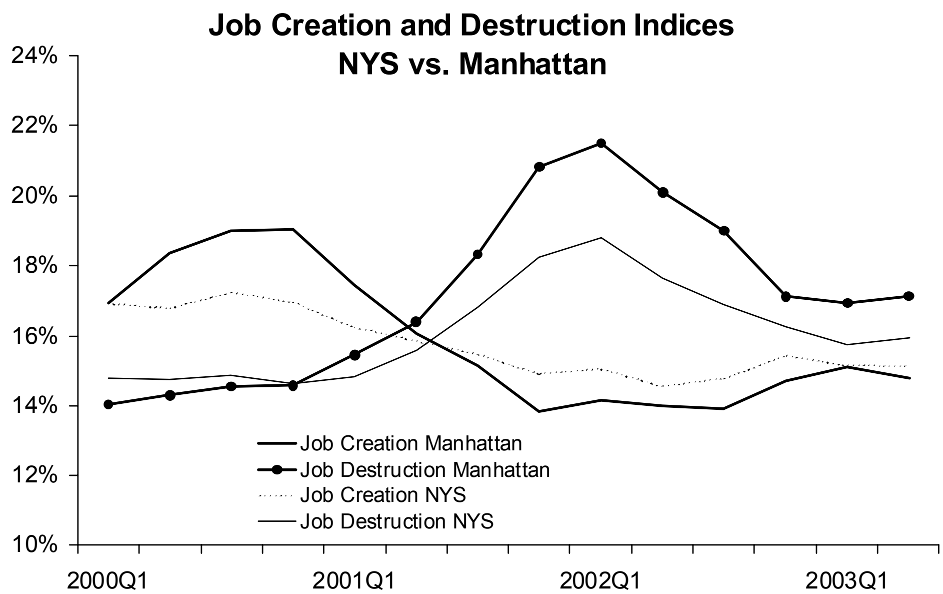
The New York nonwage components, except for the residence adjustment, are all driven by their national counterparts. The relationship is modeled as a change in the New York variable, as a function of a change in the U.S. nonwage counterpart ,along with lags of the independent and dependent variables as appropriate to account for short-term fluctuations.

Manhattan in the Eye of the Storm

Much of the growth in State incomes during the late 1990s was concentrated in industries with a strong presence in New York City, especially financial and information services. The recession and the tragedy of September 11 battered these sectors and the City employment picture. However, two years after the destruction of the World Trade Center, the City economy is well on the road to recovery. To examine the pace of the City's recovery from these events more closely, this section focuses on labor market dynamics in Manhattan since the start of the 2001-02 recession.

As the late 1990s boom was coming to a close in 2000, Manhattan's gross rate of job creation was strong and growing, while the gross rate of job destruction was relatively flat (see Figure 37). Manhattan was both creating jobs at a faster rate and was also losing jobs at a lower rate than the State overall. However, with Manhattan at the center of the State recession that started in January 2001, that trend reversed and employment began to fall. The gross rate of job creation started to decline in Manhattan in the first quarter of 2001, while gross job destruction started to rise. By the second quarter of 2001 — prior to September 11 — the rate of job destruction exceeded that of job creation, implying net losses.

Figure 37



Source: NYS Department of Labor; DOB staff estimates.

Following the attack on the World Trade Center, Manhattan's job gap widened dramatically. During the first quarter of 2002, 399,100 jobs were destroyed through firm shutdowns, mergers and acquisitions and the contraction of existing firms, while only 261,900 jobs were created through firm startups, mergers and acquisitions, and the expansion of existing firms. This resulted in a net job loss of almost 137,200 jobs.[23] More than half of the jobs lost in the State during that quarter were lost in Manhattan. Since then, the rate of job destruction in Manhattan has decelerated, though it continues to be driven by losses in contracting firms; the job creation index has shown modest improvement as well. Although Manhattan's job gap was still significantly larger than the statewide gap in the second quarter of 2003, it has narrowed substantially since the aftermath of September 11.

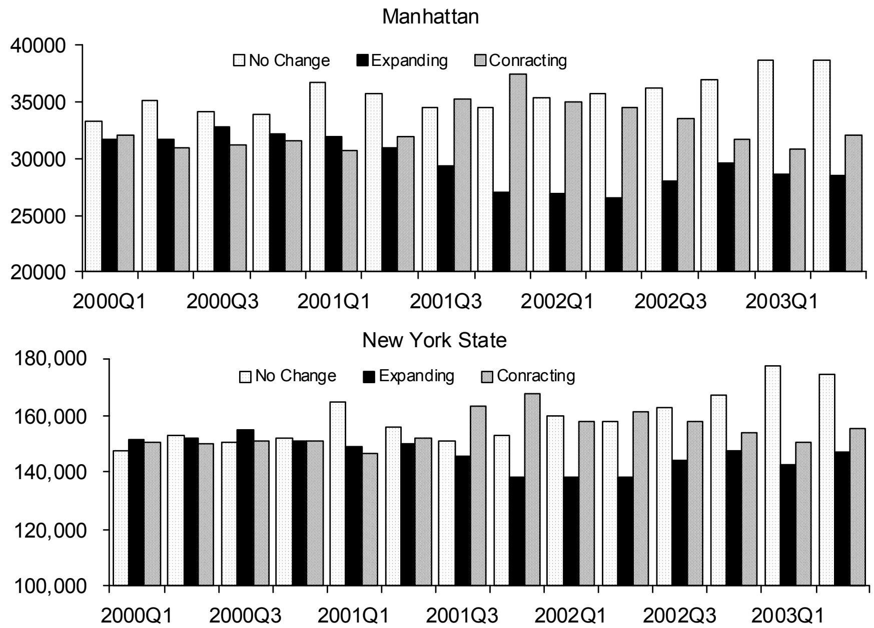
In Manhattan as elsewhere, labor market dynamics are dominated by existing firms. As indicated in Figure 38, the number of expanding firms in both Manhattan and the State continued to exceed the number of contracting firms until the second quarter of 2001.

[23] Many firms were temporarily relocated out of State immediately following the attack. Because many of these firms continued to participate in the State's Unemployment Insurance program, these relocated employees continued to appear in CEW data for New York. Therefore, CEW data may not reflect the full impact of September 11 on Manhattan employment.

However, with the onset of the State recession in early 2001, the number of contracting firms began to grow, peaking in the fourth quarter of that year, immediately following the attack. However, even during that quarter, the number of expanding firms in Manhattan was 72.2 percent as large as the number of contracting firms, an indicator of the dynamism of the Manhattan economy. Moreover, the rise in the number of expanding firms since the second quarter of 2002 clearly indicates a gradual improvement in business conditions since September 11.

Figure 38

Existing Firms in New York State and Manhattan



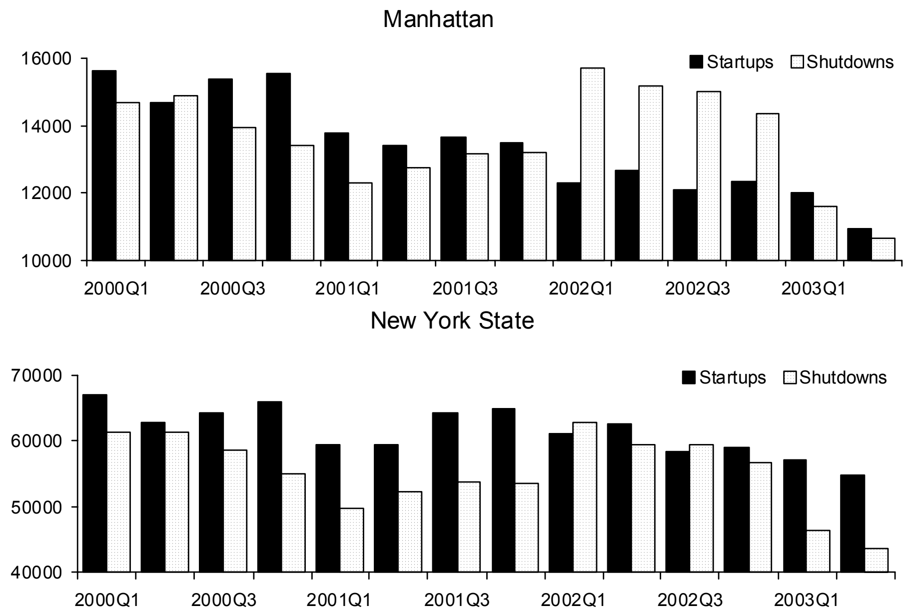
Source: NYS Department of Labor; DOB staff estimates.

The impact of the September 11 attack can be seen even more dramatically in firm startups and shutdowns. During almost every quarter in 2000 and 2001, the number of startups exceeded the number of shutdowns, in both Manhattan and the State overall (see Figure 39). However, this trend changed abruptly during the first quarter of 2002, when the number of shutdowns in Manhattan rose by 2500 compared to the prior quarter. Of this increase, about 60 percent occurred in just four sectors — professional and technical services, accommodations and food services, finance and insurance services, and the information sector — though these sectors accounted for only 32 percent of Manhattan's establishment base for the first quarter of 2002. The net number of firm shutdowns reached almost 3,400 during the first quarter of 2002, compared to only about 1,900 statewide. This fact implies a net increase in the number of firm startups outside of Manhattan.

The rise and fall in employment tends to follow the fortunes of existing firms. Figure 40 indicates that, following the September 11 attacks, job losses due to contracting firms peaked in Manhattan during the fourth quarter of 2001 at 258,400 (see Table 8). Employment losses due to firm shutdowns peaked in the following quarter, with half of the jobs lost, about 56,900, occurring in the finance and insurance, information, professional and technical services and accommodation and food services sectors.

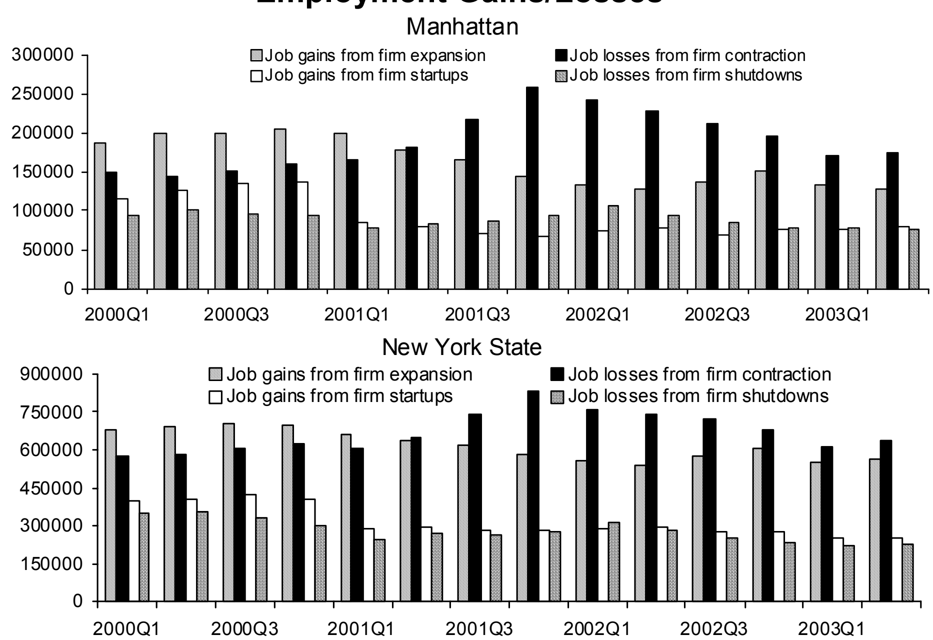
Although Manhattan — the epicenter of the 2001-03 contraction — lags much of the rest of the State, it is clearly on the road to recovery. By the first quarter of 2003, the number of firm startups exceeded shutdowns in Manhattan, due entirely to declines in firm shutdowns. These declines occurred in every sector of the economy except the utilities sector. And though Manhattan was still experiencing a net loss of jobs on a year-over-year basis in the second quarter of 2003, the extent to which the job gap has narrowed demonstrates the renewed vitality with which Manhattan is recovering from September 11.

Figure 39
Firm Startups and Shutdowns



Source: NYS Department of Labor; DOB staff estimates.

Figure 40
Employment Gains/Losses



Note: Compared to the same period of the prior year. Job gains and losses due to M&As and acquisitions are not included.
Source: NYS Department of Labor; DOB staff estimates.

TABLE 8
PRIVATE SECTOR JOB GAINS AND LOSSES IN NEW YORK AND MANHATTAN
(in thousands)

	New York State					Manhattan				
	Job Gains		Job Losses		Net Gains	Job Gains		Job Losses		Net Gains
	Expanding	Births	Contracting	Deaths	Losses	Expanding	Births	Contracting	Deaths	Losses
2000Q1	679.4	396.7	574.0	347.1	143.7	185.7	115.6	150.0	94.4	53.7
2000Q2	688.6	405.5	581.8	356.1	143.3	198.0	125.9	143.9	101.5	75.8
2000Q3	704.8	420.3	609.3	332.9	167.2	200.0	135.4	150.4	96.0	84.1
2000Q4	698.9	406.8	623.0	302.3	166.0	204.9	136.6	159.5	93.3	86.0
2001Q1	661.4	288.0	607.0	244.6	97.9	198.6	84.8	166.2	77.6	38.6
2001Q2	639.5	292.4	650.5	268.3	18.3	178.0	80.3	182.1	83.6	(6.5)
2001Q3	617.8	278.6	742.2	265.7	(95.5)	165.1	71.1	216.4	87.2	(60.7)
2001Q4	583.3	278.4	829.9	274.4	(236.5)	143.9	68.6	258.4	94.0	(134.4)
2002Q1	553.4	286.3	761.0	313.8	(256.9)	132.3	74.8	242.4	106.1	(137.2)
2002Q2	534.3	293.7	743.3	279.5	(215.2)	127.4	78.4	227.2	94.3	(113.1)
2002Q3	576.1	275.7	719.3	251.5	(147.3)	137.3	69.4	212.3	84.6	(92.9)
2002Q4	608.7	274.6	681.7	235.1	(57.4)	151.4	75.3	195.0	78.6	(44.2)
2003Q1	550.7	248.4	614.5	221.9	(32.0)	132.4	77.2	170.6	77.7	(28.2)
2003Q2	561.4	251.4	636.8	226.1	(56.1)	127.4	80.6	174.3	76.6	(41.9)

Note: Net gains and losses include net employment change due to mergers and acquisitions.
Source: NYS Labor Department; DOB staff estimates.

Risks to the New York Forecast

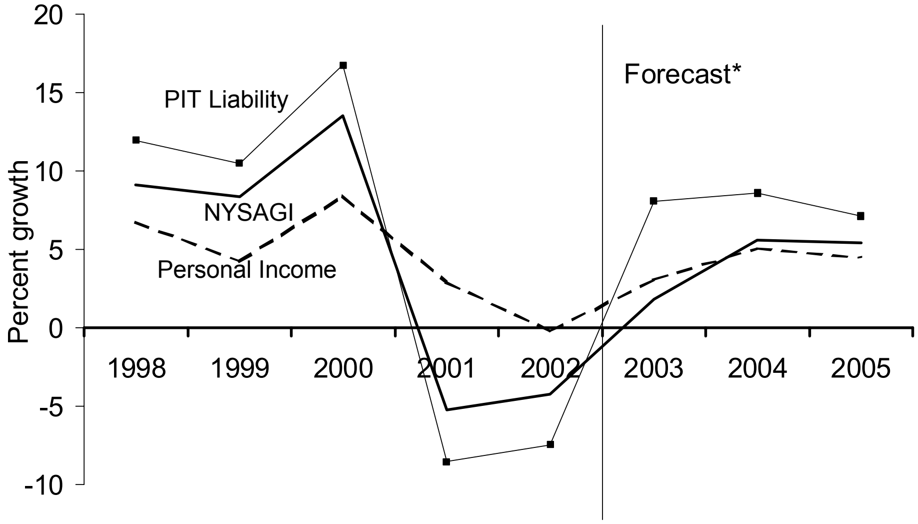
In addition to the risks described above for the national forecast, there are risks specific to the New York. Another attack targeted at New York City would once again disproportionately affect the State economy. Any other such shock that had a strong and prolonged impact on the financial markets would also disproportionately affect New York State, resulting in lower income and employment growth than reflected in the current forecast. In addition, if the national and world economies grow more slowly than expected, demand for New York State goods and services would also be lower than projected, dampening employment and income growth relative to the forecast. In contrast, should the national and world economies grow faster than expected, a stronger upturn in stock prices, along with increased activity in mergers and acquisitions and IPOs is possible, resulting in higher wage growth than projected.

The State's economic expansion is just starting to gain momentum, and as emphasized above, forecasting at or near a business cycle turning point is fraught with risk. Moreover, the financial markets, which are so pivotal to the direction of the downstate economy, are currently in a state of extreme flux. In the wake of several high-profile scandals, the pace of both technological and regulatory change is as rapid as it has ever been. These circumstances compound even further the difficulty in projecting industry revenues and profits.

SOURCES OF VOLATILITY IN THE INCOME TAX BASE — A RISK ASSESSMENT

As in many states, New York's revenue structure relies heavily upon the personal income tax (PIT). However, for a variety of reasons, PIT receipts can be extremely volatile, much more variable than conventional measures of personal income. This becomes readily apparent when comparing changes over time in actual liability with alternative indicators of the New York State income base (see Figure 41). PIT liability is the amount which State taxpayers actually owe based on total earnings during a given tax year.[24] New York State adjusted gross income (NYSAGI) is a measure of income from which total tax liability is ultimately determined and is derived from State tax returns. Personal income is a National Income and Product Accounts (NIPA) concept, measuring income derived from value added to current production.[25]

Figure 41
Indicators of New York State Tax Base
Growth Rate Comparison



* Growth rates for PIT liability and NYSAGI for 2002 are staff estimates.
Source: NYS Department of Taxation and Finance; Economy.com; DOB staff estimates.

It is evident in Figure 41 that PIT liability growth is much more variable than personal income, however defined. For example, in 2000, when all three indicators were on the upswing due to strong economic growth, personal income grew a historically robust 8.5 percent. Meanwhile, NYSAGI grew at an even stronger 13.5 percent, while PIT liability grew a remarkable 16.8 percent. When the national recession reversed this strong growth trend the following year, State personal income still grew, but at a much lower 3.0 percent. In contrast, NYSAGI fell 5.2 percent and PIT liability fell an even larger 8.5 percent. Similarly, with the New York economy still in recession in 2002, State personal income fell 0.2 percent, NYSAGI fell an estimated 4.2 percent, but PIT liability fell an estimated 7.4 percent. All three measures are expected to grow in 2003 and 2004 and past patterns suggest that NYSAGI can be expected to grow faster than personal income, while PIT liability can be expected to grow faster than both NYSAGI and personal income.

It is common to examine tax liability in terms of its sensitivity to changes in the economy and the tax base, or its "elasticity." For example, when the economy changes direction, personal income and particularly its largest component, wages, responds more strongly or "elastically" than indicators such as GDP and employment. Employers may drastically curtail or eliminate bonus payments in response to a poor performance by their firms that year. On the other hand, changes in firm employment levels are likely to occur more gradually.

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[24] For a more detailed discussion of personal income tax liability, see Tax Receipt Section "Personal Income Tax."
[25] For a discussion of how DOB constructs State personal income, see Box 8.

NYSAGI responds more elastically than personal income to economic upturns and downturns. This is because NYSAGI measures the taxable components of income, including items such as realized capital gains and losses. Since a capital gain or loss earned from the sale of a financial asset does not add to the value of current production, it is not included in the NIPA concept of personal income.[26] In 1999 and 2000, income from positive capital gains realizations grew an impressive 23.2 percent and 29.3 percent, respectively. However, the most recent data available show a 50.0 percent decline in capital gains realizations for 2001, and DOB's forecast suggests additional declines in capital gains of 31.0 percent in 2002 and 6.9 percent in 2003. With the dramatic rise in capital gains realizations during the late 1990s and 2000, and the equally dramatic declines in 2001 and 2002, the growth in taxable income became much more volatile than the growth in personal income as defined under NIPA. Unlike indicators such as GDP and employment, which have relatively stable bases, income from capital gains realizations can fall dramatically if taxpayers refrain from selling financial assets due to depressed market conditions or if taxpayers are carrying forward losses from prior years. Moreover, NYSAGI can fluctuate due to statutory changes in the definition of taxable income, and taxpayers' strategic responses to such changes.

Personal income tax liability is quite elastic with respect to changes in personal income measured either by NYSAGI or personal income as defined under NIPA, primarily due to the progressiveness of the State tax system. The volatile components of taxable income referred to above, such as bonuses and capital gains realizations, tend to be concentrated among the State's high-income taxpayers who are also taxed at the highest marginal tax rate. Growth in those components is liable to increase the average tax rate, while declines are liable to lower it. The movement of taxpayers across tax brackets as their incomes rise and fall is likely to amplify changes in average tax rates. Between 2000 and 2001, the decline in taxable income and the even larger decline in tax liability lowered the effective tax rate from 4.76 percent to 4.60 percent without any significant changes in tax law. The large 25.3 percentage point swing in PIT liability between 2000 and 2001 clearly indicates how radically tax liability can shift when the stock market fluctuates. For 2002, additional declines in capital gains and bonuses are estimated to have further eroded the effective tax rate to 4.44 percent, in part causing the estimated 7.4 percent decline in liability. For 2003 and 2004, DOB expects the effective tax rate to increase to 4.72 percent and 4.86 percent, respectively, as both the economy and equity markets improve and tax law changes are implemented. The increases in income tax rates imposed in 2003 will significantly increase the effective tax rates for high-income taxpayers.

The most volatile components of income can and have accounted for a large portion of the changes in NYSAGI. This fact poses significant risks to the Division of the Budget's personal income tax forecast. From Table 9 it can be determined that the increase in capital gains realizations of $14.5 billion accounted for 23.6 percent of the $61.4 billion increase in NYSAGI in 2000. For 2001, the decline in capital gains of $32 billion is larger than the estimated $27.0 billion decline in NYSAGI for that year, and the estimated decline of $9.9 billion in capital gains realizations accounted for almost 50 percent of the $20.4 billion decline in NYSAGI in 2002. Because so much of the fluctuation in New York State taxable income derives from financial market volatility, there is a large degree of risk surrounding forecasts for several components of taxable income and, ultimately, tax liability itself.[27] Therefore, the Budget Division has consistently maintained that a conservative approach to projecting these components is warranted.

[26] However, any transaction cost generated by such a sale would add value to current production and would therefore be included in personal income.

[27] For a discussion of the Budget Division's use of Monte Carlo simulations to compute confidence bands around forecasts, see *Executive Budget Presentation, 2002-03, Appendix II*, pp. 129-136. The confidence bands around this year's forecast are comparable to those estimated two years ago.

TABLE 9
CHANGES IN NYSAGI AND ITS MAJOR COMPONENTS

	1999	2000	2001	2002	2003	2004
NYSAGI						
Level in billions of $	453.1	514.5	487.5	467.1	475.6	502.3
$ Change	35.1	61.4	-27.0	-20.4	8.5	26.7
% Change	8.4	13.5	-5.2	-4.2	1.8	5.6
Wages						
Level in billions of $	328.9	368.2	376.2	363.9	370.4	389.2
$ Change	19.2	39.3	8.0	-12.2	6.5	18.7
% Change	6.2	12.0	2.2	-3.3	1.8	5.1
Capital Gains						
Level in billions of $	49.5	64.0	32.0	22.0	20.5	23.2
$ Change	9.3	14.5	-32.0	-9.9	-1.5	2.6
% Change	23.2	29.3	-50.0	-31.0	-6.9	12.9
Partnership/S corporation						
Level in billions of $	35.3	38.9	37.9	38.0	41.3	45.0
$ Change	4.6	3.6	-1.0	0.1	3.3	3.7
% Change	14.8	10.1	-2.6	0.2	8.7	9.1

Note: Discrepancies are due to rounding.
Source: NYS Department of Taxation and Finance; DOB staff estimates.

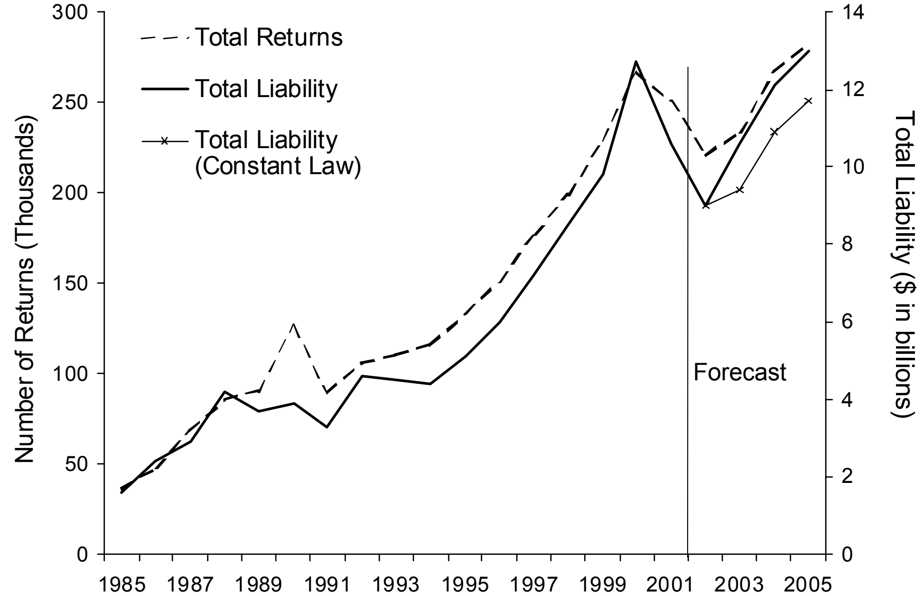
Changes in the State Distribution of Income

Given the progressive nature of the State's tax system, forecasting total income tax liability entails not only forecasting total income, but the distribution of income as well. Out-year estimation of the income distribution is especially risky since the share of income earned among the wealthiest taxpayers can fluctuate dramatically with such factors as the business cycle, the financial markets, and changes in federal and state tax treatment. The rising stock market created thousands of millionaires during the latter part of the 1990s, causing the share of total personal income tax liability accounted for by high-income taxpayers — those reporting taxable incomes of $200,000 or more — to grow rapidly during that period.[28] Approximately 8.9 million tax returns were filed in New York State for the 2001 tax year, reflecting an average annual growth of 1.9 percent since 1995. Over the same period, the number of high-income taxpayers grew from 133,000 to 251,000, reflecting an average annual growth of 15 percent (see Figure 42). In 2001, the most recent year for which detailed tax return data are available, these high-income taxpayers represented a mere 2.8 percent of all taxpayers, but they accounted for 35.0 percent of NYSAGI and 47.1 percent of personal income tax liability, or $10.6 billion out of a total of $22.4 billion (see Figure 43). In the peak year of 2000, high-income taxpayers represented 3.0 percent of all taxpayers but accounted for 50.8 percent of personal income tax liability.

[28] In 1995, 6,910 New York taxpayers had federal adjusted gross incomes of $1,000,000 or more. This number skyrocketed to 48,856 taxpayers in 2000. Between 1999 and 2000 alone, the number of millionaires almost doubled from 25,537 to 48,856.

Figure 42

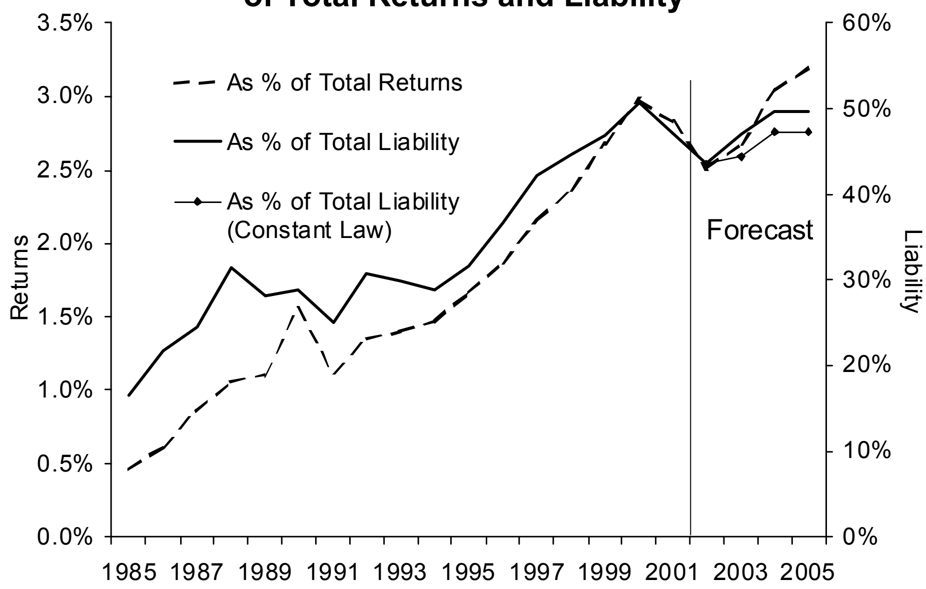
New York State High-Income Tax Returns



Source: NYS Department of Taxation and Finance; DOB staff estimates.

Figure 43

High-Income Taxpayers as Percent of Total Returns and Liability



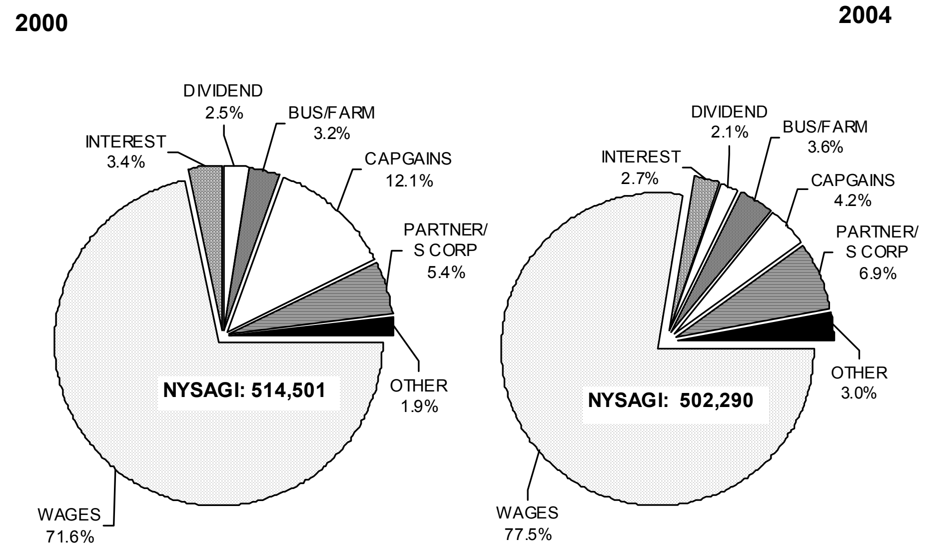
Source: NYS Department of Taxation and Finance; DOB staff estimates.

Figure 44 compares the composition of NYSAGI for all taxpayers for the peak tax year of 2000 to that for the 2004 tax year based on Budget Division projections. The figure shows a clear shift from net capital gains income to wage income. By 2004, estimated net capital gains income contributes only 4.2 percent to taxable income, down from a high of 12.1

percent in 2000. At the same time, the share of wages is expected to increase from 71.6 percent to 77.5 percent, which is close to the historical average of 80.0 percent between 1977 and 2000. Partnership income is expected to increase from 5.4 percent in 2000 to 6.9 percent in 2004.

Figure 44

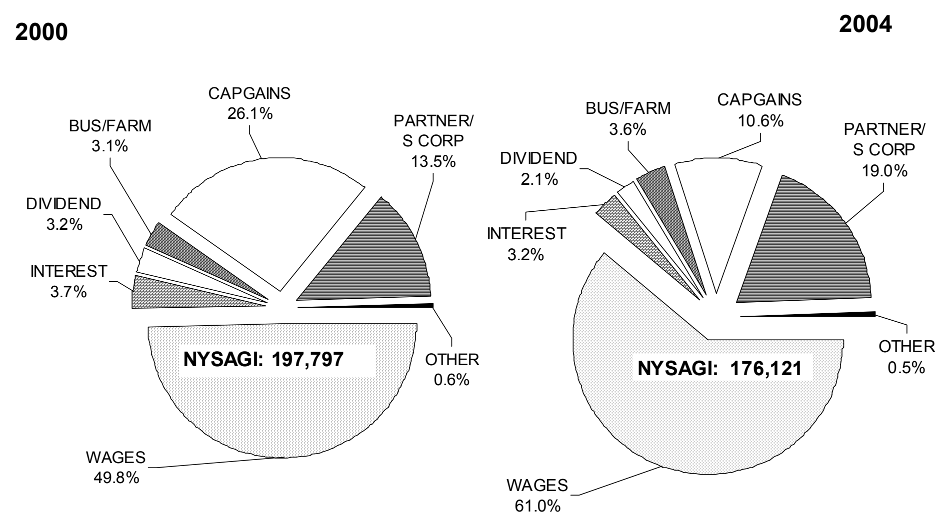
Composition of NYSAGI for All Taxpayers



Note: Both capital gains and partnership/S corporation gains income are net of losses.
Source: NYS Department of Taxation and Finance; DOB staff estimates.

Figure 45

Composition of NYSAGI for High-Income Taxpayers

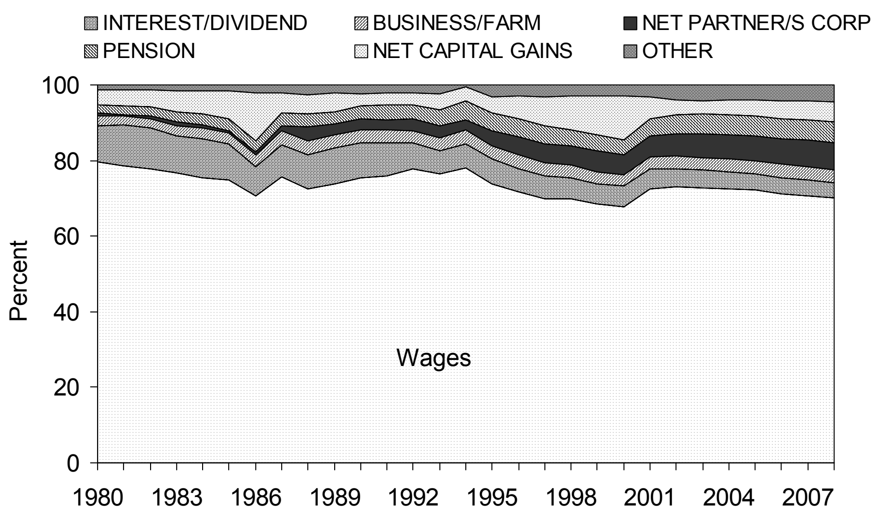


Note: Both capital gains and partnership/S corporation gains income are net of losses.
Source: NYS Department of Taxation and Finance; DOB staff estimates.

The composition of NYSAGI for high-income taxpayers differs noticeably from that of all other taxpayers (see Figure 44 and Figure 45). Moreover, as is evident from the most volatile components of NYSAGI, capital gains and partnership/S corporation income make up a much larger share among high-income taxpayers than for taxpayers overall, while the share of wages is considerably lower.[29] This volatility becomes apparent when comparing the composition of NYSAGI for high-income taxpayers between the 2000 and 2004 tax years. For high-income taxpayers, the share of capital gains realizations is projected to fall from 26.1 percent in 2000 to only 10.6 percent in 2004. Meanwhile, the shares for partnership/S corporation income and wages are projected to grow substantially.

There has been considerable shifting over time in the largest components of income as shares of total NYSAGI (see Figure 46). The shares for wages, interest, and dividend income show a downward trend. The share for business and farm income remains stable, while the shares for partnership/S corporation income and pension income have grown steadily. The share for capital gains is the most volatile, peaking in 1986 in response to tax law changes and growing rapidly with the stock market bubble between 1995 and 2000. After three consecutive years of decline, we expect the share of capital gains income to start growing again in 2004.

Figure 46
Major Components of NYSAGI as Percent of Total



Note: NYSAGI is measured gross of deductions.
Source: NYS Department of Taxation and Finance; DOB staff estimates.

The Major Components of NYSAGI

The Budget Division forecasts for the components of NYSAGI are based on detailed tax return data from a sample of State taxpayers through the 2001 tax year, made available by the New York State Department of Taxation and Finance. Although the measure of taxable wages derived from State tax returns does not precisely match the dollar amount derived from Covered Employment and Wages (CEW) data, they are believed to follow the same trend. Therefore, for a discussion of the Budget Division forecast for taxable wages, see "Outlook for Income" above.

[29] Although tax return data does not differentiate bonus income from nonbonus income, it can be surmised that bonus income represents a much larger share of taxable income among high-income taxpayers than among low-income taxpayers.

Positive Capital Gains Realizations

As discussed above, the volatility in capital gains realizations has accounted for a large share of the fluctuation in total NYSAGI in recent years. The Budget Division's forecasting model has attempted to capture the inherent volatility in this component of income by incorporating those factors that are most likely to influence realization behavior, such as expected and actual tax law changes and financial market activity for the contemporaneous period.[30] The model also includes prior year stock market activity to account for capital losses realized in past years. In any given tax year, taxpayers can only claim a net $3,000 ($1,500 if filing individually) in capital gains losses against ordinary income, but they can carry the remaining losses over an indefinite period in order to offset gains in future years. Although the model has performed well, DOB projections have always emphasized the high degree of uncertainty associated with any capital gains forecast.[31]

The most recent bear market for stocks was unprecedented in the period since World War II in both severity and duration, and was therefore accompanied by historically large capital losses. U.S. Department of Treasury Statistics of Income (SOI) data suggest that, at the national level, the loss carryover grew 45.9 percent in 2000, 81.5 percent in 2001 and another 52.6 percent in 2002. This compares to consecutive increases of 30.7 percent, 35.5 percent and 43.9 percent from 1974 to 1976, during and following the 1973-74 bear market, the only other multiyear downturn in equities in recent history. At the national level, an estimated $350 billion in realized losses has been carried forward from 2002 tax returns for use to offset taxable gains earned in 2003 and beyond. In contrast, in 1999, just prior to the bursting of the stock-market bubble, the loss carryover totaled $87 billion, a quarter of its current size. And while the ratio of the loss carryover — estimated for New York — to taxable net capital gains was 19.7 in 2000, by 2002 it had risen to an estimated 138.9, above the ratio attained during the 1973-74 bear market (see Figure 47). Because of the lack of historical experience, adjustments are made to the forecast for the period from 2003 to 2008 to more effectively account for the anticipated impact of accumulated losses. These adjustments are based on the ratio of losses to gains derived from national SOI data and applied to New York (see Figure 48).[32]

The Budget Division estimates three consecutive years of decline in capital gains realizations: 50.0 percent in 2001, 31.0 percent in 2002 and a smaller decline of 6.9 percent for 2003 (see Figure 49). Despite the recent upturn in stock market performance, taxable capital gains are still expected to decline in 2003 because of the large loss carryover. Subsequently, capital gains are predicted to improve rather quickly as the loss carryover dissipates. While the loss carryover adjustments depress growth rates in 2004 and 2005, the growth rate of capital gains realization increases as the magnitude of applied losses tapers off. Overall, the Budget Division expects that the capital gains share of total NYSAGI will rise to its historical average value by 2008 (see Figure 50).

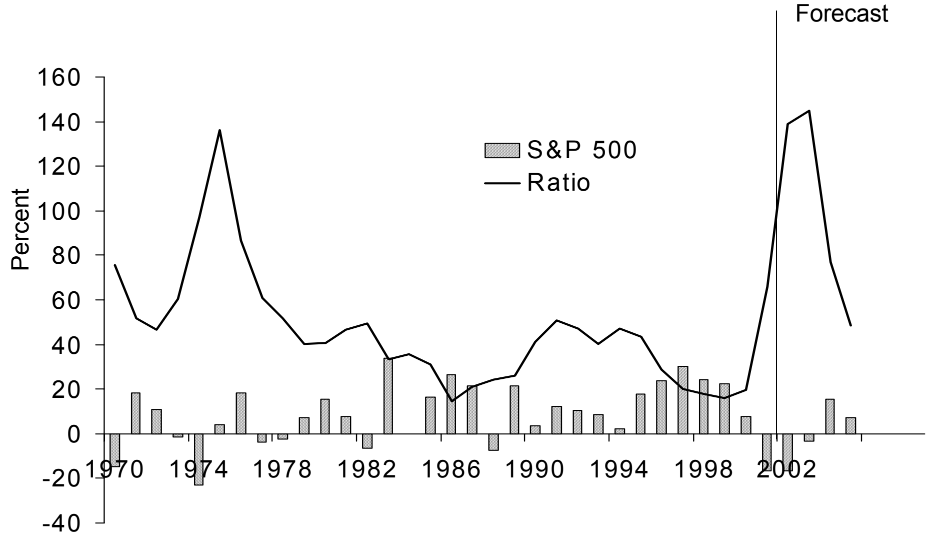
[30] For a discussion of DOB's traditional approach to modeling capital gains realizations, see L. Holland, H. Kayser, R. Megna and Q. Xu "The Volatility of Capital Gains Realizations in New York State: A Monte Carlo Study," *Proceedings, 94th Annual Conference on Taxation*, National Tax Association, Washington, DC, 2002, pp. 172-183.

[31] See *Executive Budget Presentation, 2002-03, Appendix II*, p. 131.

[32] Because the model cannot capture the full extent of the estimated value of the loss carryover, we perform manual adjustments to capital gains realizations. We estimate an unprecedented level of about $30 billion in losses. We assume that a little less than half that amount will be used to offset gains between 2003 and 2008. Positive taxable capital gains, gross of offsetting losses, provide an indication of the underlying performance of the stock market. However, these data are unavailable to researchers. Therefore, one should keep in mind that realized capital gains do not truly reflect the state of the markets until the loss carryover has sufficiently dissipated.

Figure 47

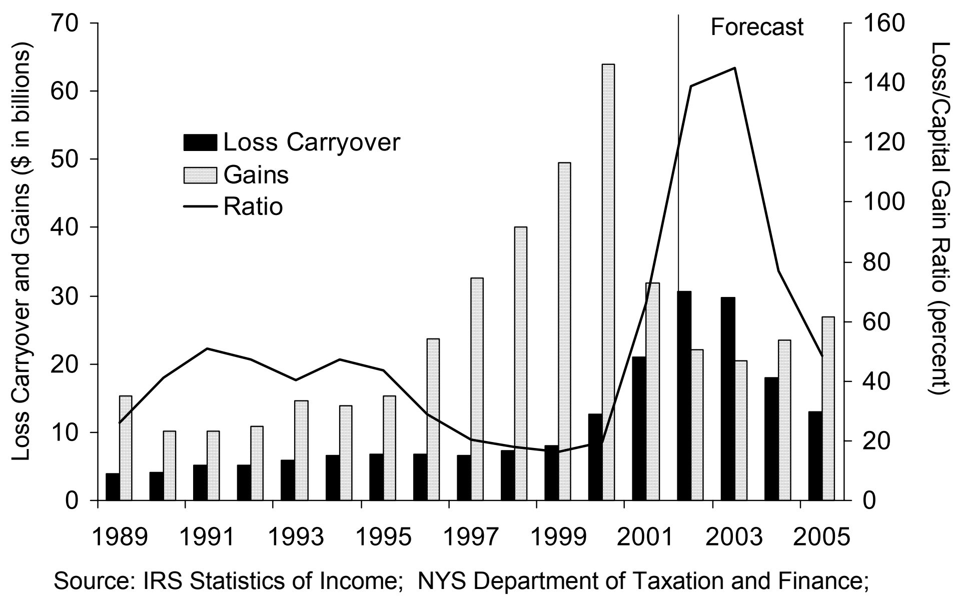
Ratio of Loss Carryover to Capital Gains Realizations and Growth in the S&P 500



Note: Forecast period for the S&P 500 starts in 2004.
Source: IRS Statistics of Income; DOB staff estimates.

Figure 48

Decomposing the Ratio of Loss Carryover to Capital Gains Realizations

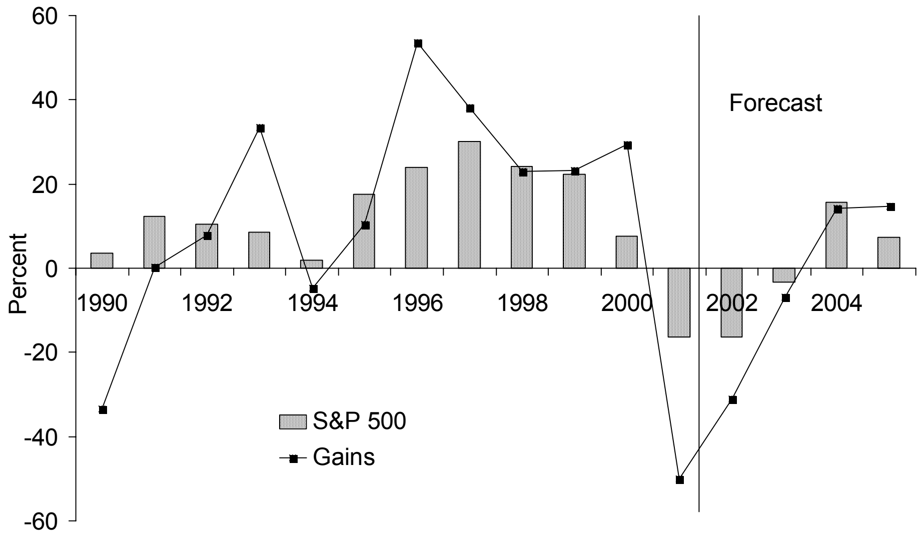


Source: IRS Statistics of Income; NYS Department of Taxation and Finance; DOB staff estimates.

The unprecedented size of the loss carryover poses significant risk for the out-year estimates of taxable gains. It is possible that larger amounts of accumulated losses will be applied to offset capital gains than anticipated in the forecast. The level of gains could also deviate from the forecast if the underlying assumptions about the economy and financial market conditions deviate from expectations. Historically, financial market conditions have been extremely difficult to predict in the short run, resulting in significant forecasting errors.

Figure 49

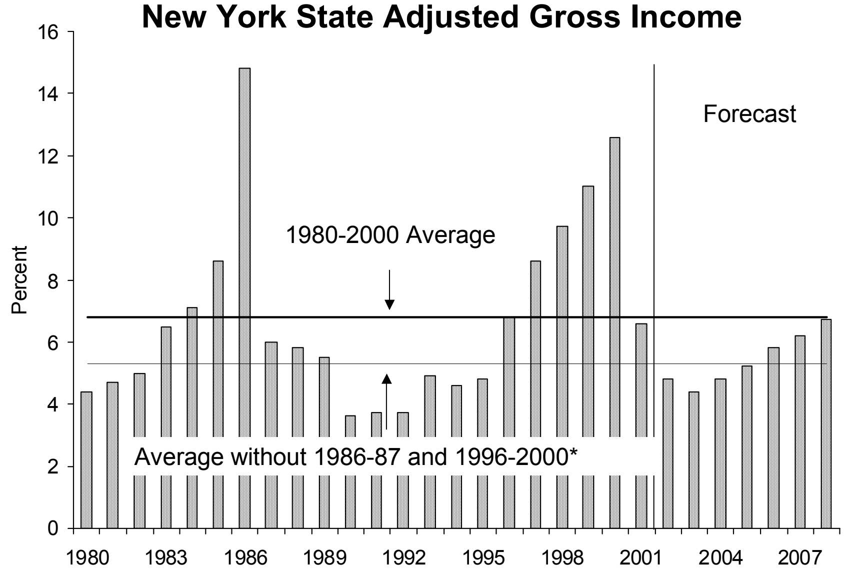
Growth in Capital Gains Realizations and S&P 500



Note: Forecast period for the S&P 500 starts in 2004.
Source: IRS Statistics of Income; NYS Department of Taxation and Finance; DOB staff estimates.

Figure 50

Capital Gains Realizations as Percent of Total New York State Adjusted Gross Income



*Adjustment to account for distortions from the 1986 tax reform and the speculative bubble of the late 1990s.
Source: NYS Department of Taxation and Finance; DOB staff estimates.

Rent, Royalty, Partnership, and S Corporation Income

Positive rent, royalty, estate, trust, partnership and S corporation income has become one of the largest components of NYSAGI, accounting for 7.6 percent in 2000 and an estimated 9.0 percent by 2004. The largest contributor to this component is partnership income, much of which originates within the finance and real estate industry and is therefore closely tied to both the overall performance of the economy and to the performance of the stock market. An almost equally large contributor is income from S corporation ownership. Selection of S corporation status allows firms to pass earnings through to a limited number of shareholders and to avoid corporate taxation. Over the years, rules governing which businesses can form S corporations have become less stringent, making this a very flexible business form; its use has increased dramatically. Empirical work confirms that the differential between personal income tax and corporate income tax rates can significantly affect election of S corporation status.[33] Consequently, DOB's forecast model includes the difference between the corporate franchise tax rate and the maximum marginal personal income tax rate, where the rates are composites of both State and Federal rates. The model also includes real U.S. GDP and the S&P 500. Together partnership income and S corporation income contribute more than 90 percent to this category's income total.

The DOB predicts that partnership and S corporation income will grow faster than other business income as the economy improves. While New York proprietors' income (which includes partnership income, S corporation income, and sole proprietorship income) grew at an average annual rate of 7.7 percent between 1978 and 2001, taxable partnership and S corporation income grew at a significantly faster rate of 9.7 percent. Some of this growth is due to past tax law changes and to easing of the requirements for forming S corporations. In the absence of further policy actions, it is expected that the growth rate will diminish but remain relatively high because its liability provisions and flexibility make S corporation status a continued favorite among new businesses. The Budget Division estimates that positive partnership and S corporation income increased slightly at a rate of 0.2 percent in 2002. As equity markets and the economy improve, growth in partnership and S corporation income is estimated at 8.7 percent in 2003, followed by growth of 9.1 percent in 2004.

Dividend Income

Dividend income is expected to rise and fall with the fortunes of publicly held U.S. firms, which, in turn, are expected to vary with the equity market and with the overall performance of the national economy. For example, during the State's last recession, dividend income declined for four consecutive years from 1989 to 1992. DOB's dividend model includes the S&P 500 equity market index and a recession dummy. Dividend income is also thought to be associated with firms' expectations pertaining to their future profitability, which is tied to the future strength of the economy. Interest rates can be interpreted as containing information about future prospects for the economy, because they contain inflation expectations, which, in turn, are shaped by expectations for the economy.

Historically, State dividend income growth has ranged from a decline of 6 percent in 1991 to an increase of 22 percent in 1981, proving growth to be much more variable than U.S. dividend income. This reflects the importance of factors influencing how taxpayers report their income, such as tax law changes, as well as changes in dividend payments by firms. The most obvious impact of a change in the tax law occurred in 1988, when reported dividend income grew 21.8 percent, followed by a decline of 2.6 percent in the next year. The Budget Division estimates dividend income to decline 4.6 percent in 2002 following a large decline of 19.3 percent in 2001. Dividend income is estimated to have exhibited slow positive growth of 0.9 percent in 2003, but is projected to grow a healthier 6.7 percent in 2004 due to a stronger economy and higher equity prices.

Interest Income

For a given amount of assets, an increase in interest rates will increase interest income. DOB's interest income forecasting model is based on this simple concept and accordingly

[33] See for example R. Carroll and D. Joulfaian "Taxes and Corporate Choice of Organizational Form," OTA Paper 73, Office of Tax Analysis, U.S. Treasury Department, Washington, DC, October 1997.

includes the 10-year Treasury rate. In addition, the overall trend in taxable interest income for New York is found to closely track that of U.S. interest income. However, taxable interest income for New York is much more volatile than the latter measure. For the period 1976 to 2001, the average growth rate for U.S. interest income was 8.9 percent, with a standard deviation of 7.6 percentage points. In contrast, New York's interest income as reported on returns over the same period averaged 6.0 percent growth, with a standard deviation of over 13.6 percentage points. Interest income fell 7.5 percent during 2001 due to the steep decline in interest rates during the year. Interest income is estimated to continue falling by 12.4 percent in 2002 and 5.1 percent in 2003 due to the continued decline in overall interest rates. Interest income is expected to fall modestly by 0.4 percent in 2004 before regaining positive growth in 2005.

Business and Farm Income

Business and farm income combines income earned and reported as a result of operating a business, practicing a profession as a sole proprietor, or from operating a farm. This component of income is expected to vary with the overall state of the State and national economies. Consequently, DOB's forecasting model includes real U.S. GDP, as well as New York State proprietors' income. Historically, business and farm income grows more slowly than proprietors' income, at an annual rate of about 6.5 percent compared with proprietors' income growth of 7.7 percent. The Joint Committee on Taxation (JCT) and the Congressional Budget Office (CBO) estimate that business income will be substantially lower in 2003-2005 because of the provisions of the Jobs and Growth Tax Relief Reconciliation Act of 2003 (JGTRRA).[34] Our estimates adjust for these provisions. The Budget Division estimates low growth of 2.9 percent in 2002, followed by a decline of 0.6 percent because of JGTRRA. For 2004, projections are for a growth rate more in line with history of 5.6 percent. There is a reasonable downside risk to our estimates for 2003 and 2004 because of the high estimates for revenue losses by JCT and CBO.

Pension Income

Pension income includes payments from retirement plans, life insurance annuity contracts, profit-sharing plans, military retirement pay, and employee savings plans. Pension income is linked to long-term interest rates, suggesting that firms base the level of pension and life-insurance benefits they offer to employees on their expectations of future profitability, which is tied to the future strength of the economy. Pension income has grown steadily over the years, although the growth rate has declined considerably over time despite an aging population. While the average annual growth rate between 1978 and 1989 was 13.4 percent, it fell to 7.3 percent between 1990 and 2001. This coincides with a decline in the 10-year Treasury rate from 10.3 percent in the earlier years to 6.5 percent in the later years. For pension income, DOB's forecasting model estimates 7.4 percent growth in 2002, followed by further growth of 5.1 percent and 5.2 percent for 2003 and 2004, respectively.

In summary, given the uncertainty surrounding such volatile components as capital gains realizations and the small number of taxpayers who account for the majority of this income, there exists significant risk to the Division of the Budget's personal income tax forecast. Some of this risk stems from the connection between revenues and the stock market, which is particularly difficult to forecast. The effect of the loss carryover and of yet unrealized losses on capital gains realizations could very easily exceed our current forecast. Should the momentum in GDP growth slow in 2004 relative to the forecast, business and farm income and partnership and S corporation income could be lower than expected. Rough estimates suggest that one percentage point shaved from GDP growth translates into a decline in NYSAGI of about $1 billion and a decline in PIT liability of about $50 million.

[34] See Congressional Budget Office, Congressional Budget Cost Estimate, H.R. 2, "Jobs and Growth Tax Relief Reconciliation Act of 2003," May 23, 2003.

TABLE 10
SELECTED ECONOMIC INDICATORS
(Calendar Year)

	2002 (actual)	2003 (estimate)	2004 (forecast)	2005 (forecast)	2006 (forecast)	2007 (forecast)	1976-2002 Average[2]
U.S. Indicators[1]							
Gross Domestic Product (current dollars)	3.8	4.7	6.3	5.4	5.2	5.2	7.1
Gross Domestic Product	2.2	3.1	4.7	3.5	3.3	3.1	3.2
Consumption	3.4	3.1	4.0	3.4	3.1	2.7	3.3
Residential Fixed Investment	4.9	9.0	5.5	(0.9)	(1.0)	(0.3)	3.8
Nonresidential Fixed Investment	(7.2)	2.5	10.6	9.3	8.8	8.9	5.2
Change in Inventories (dollars)	5.7	(1.3)	46.6	37.7	29.1	23.9	27.0
Exports	(2.4)	1.4	7.3	7.8	7.2	6.6	6.0
Imports	3.3	3.7	8.4	7.1	6.8	6.8	7.4
Government Spending	3.8	3.4	2.4	1.7	1.5	1.3	2.3
Corporate Profits[3]	17.4	18.7	15.1	7.5	7.2	6.3	7.3
Personal Income	2.3	3.3	4.7	5.3	5.5	5.5	7.3
Wages	0.6	2.1	4.4	5.9	5.8	5.4	7.0
Nonagricultural Employment	(1.1)	(0.2)	1.1	2.0	1.7	1.3	2.0
Unemployment Rate (percent)	5.8	6.0	5.7	5.2	5.0	5.1	6.4
S&P 500 Stock Price Index	(16.5)	(3.2)	15.6	7.5	7.2	7.1	10.3
Federal Funds Rate	1.7	1.1	1.2	3.0	4.6	5.1	7.1
Treasury Note (10-year)	4.6	4.0	4.7	5.6	6.4	6.7	8.2
Consumer Price Index	1.6	2.3	1.8	2.1	2.3	2.4	4.6
New York State Indicators							
Personal Income[4]	(0.2)	3.1	5.1	4.5	4.7	4.9	6.5
Wages and Salaries[4]							
Total	(3.3)	1.8	5.1	4.9	4.7	4.8	6.2
Without Bonus[5]	(0.8)	2.3	4.1	4.5	4.5	4.4	5.9
Bonus[5]	(19.0)	(2.2)	12.7	7.9	6.7	8.2	10.4
Wage Per Employee	(1.6)	2.2	4.3	3.7	3.6	3.8	5.4
Property Income	0.9	1.4	3.9	3.1	3.3	3.9	7.5
Proprietors' Income	4.2	7.1	7.7	5.8	7.1	6.9	8.6
Transfer Income	7.8	5.2	5.7	5.0	5.2	5.6	6.9
Nonfarm Employment[4]							
Total	(1.8)	(0.4)	0.8	1.1	1.1	1.0	0.8
Private	(2.4)	(0.4)	0.9	1.3	1.3	1.1	0.9
Unemployment Rate (percent)	6.1	6.2	6.0	5.7	5.5	5.6	6.7
Composite CPI of New York[5]	2.2	2.8	2.1	2.0	2.1	2.2	4.6
New York State Adjusted Gross Income							
Capital Gains	(31.0)	(6.9)	12.9	13.7	16.5	13.2	16.4
Partnership/ S Corporation Gains	0.2	8.7	9.1	9.3	9.4	8.2	11.9
Business and Farm Income	2.9	(0.6)	5.6	4.3	10.6	4.4	7.2
Interest Income	(12.4)	(5.1)	(0.4)	1.7	1.6	0.6	6.0
Dividends	(4.6)	1.0	6.7	6.5	6.1	4.7	5.8
Total NYSAGI	(4.2)	1.8	5.6	5.4	5.9	5.6	7.0

[1] All indicators are percent changes except change in inventories, the unemployment rate, and interest rates; all GDP components refer to chained 1996 dollars, unless otherwise noted.
[2] For the NYSAGI variables, averages are calculated using data through 2001. Partnership and S corporation gains data start in 1978.
[3] Includes inventory valuation and capital consumption adjustments.
[4] Nonagricultural employment, wage, and personal income numbers are based on CEW data.
[5] Series created by the Division of the Budget.
Source: Economy.com; NYS Department of Labor; NYS Department of Taxation and Finance; DOB staff estimates.

TABLE 11
SELECTED ECONOMIC INDICATORS*
(State Fiscal Year)

	2002-03 (actual)	2003-04 (estimate)	2004-05 (forecast)	2005-06 (forecast)	2006-07 (forecast)	1976-77 - 2002-03 Average
U.S. Indicators[1]						
Gross Domestic Product (current dollars)	4.0	5.4	6.1	5.3	5.2	7.1
Gross Domestic Product	2.4	3.9	4.5	3.4	3.2	3.1
Consumption	3.1	3.5	3.9	3.3	2.9	3.3
Residential Fixed Investment	5.6	10.0	3.0	(1.2)	(0.9)	3.5
Nonresidential Fixed Investment	(4.7)	5.3	10.8	8.7	9.0	5.2
Change in Inventories (dollars)	12.0	7.5	47.2	35.1	27.4	26.7
Exports	0.5	2.2	7.9	7.7	7.0	6.0
Imports	5.7	4.1	8.5	6.8	6.8	7.3
Government Spending	3.8	3.7	1.9	1.7	1.5	2.3
Corporate Profits[2]	14.3	25.3	10.5	7.4	7.1	6.9
Personal Income	2.6	3.6	4.9	5.4	5.4	7.3
Wages	1.1	2.4	4.9	6.0	5.7	6.9
Nonagricultural Employment	(0.8)	(0.1)	1.6	2.0	1.6	2.0
Unemployment Rate (percent)	5.8	6.0	5.6	5.1	5.0	6.3
S&P 500 Stock Price Index	(19.7)	9.8	11.4	7.3	7.3	9.8
Federal Funds Rate	1.5	1.1	1.5	3.5	4.8	7.1
Treasury Note (10-year)	4.3	4.2	4.8	5.9	6.5	8.2
Consumer Price Index	2.0	2.0	1.9	2.1	2.3	4.6
New York State Indicators						
Personal Income[3]	1.2	4.5	4.7	4.6	4.7	6.5
Wages and Salaries[3]						
Total	(1.2)	4.1	4.8	4.9	4.8	6.1
Without Bonus[4]	0.3	2.8	4.3	4.6	4.4	5.9
Bonus[4]	(11.7)	15.2	8.9	7.1	7.3	9.8
Wage Per Employee	(0.0)	4.2	3.9	3.7	3.6	5.3
Property Income	1.4	2.0	3.7	3.1	3.5	7.5
Proprietors' Income	5.1	8.1	6.5	6.3	7.1	8.4
Transfer Income	7.2	5.3	5.5	5.1	5.3	6.8
Nonfarm Employment[3]						
Total	(1.2)	(0.2)	0.9	1.2	1.1	0.8
Private	(1.7)	(0.2)	1.1	1.3	1.2	0.9
Unemployment Rate (percent)	6.2	6.2	6.0	5.6	5.5	6.7
Composite CPI of New York[4]	2.5	2.6	2.0	2.0	2.1	4.6

[1] All indicators are percent changes except change in inventories, the unemployment rate, and interest rates; all GDP components refer to chained 1996 dollars, unless otherwise noted.
[2] Includes inventory valuation and capital consumption adjustments.
[3] Nonagricultural employment, wage, and personal income numbers are based on CEW data.
[4] Series created by the Division of the Budget.
Source: Economy.com; NYS Department of Labor; DOB staff estimates.

RECENT TRENDS IN ALL FUNDS TAX RECEIPTS

SUMMARY

Growth in All Funds tax receipts has been very volatile over the past three decades, reflecting both underlying economic conditions and significant changes in tax policy. During the mid-1970s and early 1980s, tax revenue growth rates were quite high reflecting the inflationary environment of the times. Tax revenue growth in the mid-to-late 1980s was fueled by a bull market on Wall Street and large increases in real estate values. Tax growth dipped in the late 1980s, partly as a result of the implementation of a multi-year personal income tax cut program. The relatively small annual average growth in receipts during the 1990s was largely due to three factors: the severe economic downturn experienced in New York during the early 1990s, reduced inflation rates, and the significant tax reductions enacted over the 1995-2000 period. Most recently, the decline in tax receipts for 2001-02 and 2002-03 was directly related to the adverse effects of the national economic recession, the decline in stock market values, the disproportionate impact of the World Trade Center disaster on the New York economy and the continued impact of previously enacted tax reductions. The back-to-back decline in tax receipts was the first in many years, including the fiscally turbulent 1970s.

It is estimated that underlying receipts growth will remain relatively weak in 2003-04 as the continued impacts of recession, the aftermath of the equity market decline, and the events of September 11th continue to adversely affect receipts. However, base receipts growth will be supplemented by revenue actions taken with the 2003-04 Budget, including the temporary three-year increase in personal income tax rates and the two-year one quarter of one percent sales tax surcharge. Overall, tax receipts are expected to increase by 7.7 percent in 2003-04. Receipts increase by an estimated 5.2 percent when adjusting out the impact of law changes. Historically, tax receipt growth, adjusted for law changes, has lagged behind changes in economic conditions. This has been especially true for the current expansion as the lack of significant employment growth and the aftershocks of the 2001 recession continue to depress tax receipts growth before factoring in the impact of law changes.

As the negative influences acting on receipts growth subside, especially with respect to equity market conditions and the return to profitability in the financial services sector, the revenue picture is expected to brighten. Growth is expected to exceed historical averages as the economy revives in 2004-05 and 2005-06. Actual All Funds tax growth is projected to be 7.5 percent in 2004-05 and slow to just over 3 percent in 2005-06 and 2006-07 as the temporary tax increases are phased out. Adjusting for law changes, growth in tax receipts of 7 percent is projected for 2004-05 followed by estimated growth of approximately 5 percent in 2005-06 and 2006-07. Growth in estimated base receipts exceeds that of the historical period (1987-88 to 2002-03) by almost 2 percent.

IMPACT OF INFLATION

When receipts are adjusted for inflation, the impact of economic contractions becomes more apparent. There were significant consecutive declines in real receipts growth during the 1970s, as New York suffered through the deep mid-1970s recession and the oil shocks of 1973 and 1980. The negative growth rates in the late 1980s and early 1990s reflect the large 1987 personal income tax cut and the 1990 economic recession. The growth declines in the mid-1990s are due to slow economic growth in 1994 and 1995 and the multi-year tax reduction program started in 1995. The real declines in receipts for 2001-02 and 2002-03 are by far the most significant of the period and, again, reflect the impact of the national recession, the deflation in stock values, the adverse impact of September 11th, and the impact of previously enacted tax cuts. In fact, the 2001 recession had a far larger negative impact on tax receipts than any recession over the past 30 years. The first chart that follows shows that adjusting for tax policy changes and inflation, the decline in 2001-02 and 2002-03 was much more severe than for the other economic downturns of the previous three decades. It is expected that tax receipts, adjusted for inflation, will grow an average of 3.4 percent over the 2003-04 to 2006-07 period. This expected growth greatly exceeds historical averages. This is partly the result of law changes enacted in 2003-04. Adjusting for law changes, real base growth in tax receipts is estimated at 3.5 percent for this period, almost 3 percent higher than the average over the past 15 years.

SHIFTING TAX SHARES — IMPACT OF POLICY AND ECONOMICS

The series of charts and tables in this section detail both the shift in tax shares over time between the major tax sources and the growth in receipts for a selected set of primary tax sources both before and after adjusting for inflation. The inflation-adjusted charts also provide timeline indicators for major tax law changes, economic downturns and the recent stock market boom, all of which are major factors that have impacted receipts growth over the past 30 years.

The share of tax attributable to a major tax source is related to economic activity and tax policy shifts. For example, the temporary personal income tax and sales tax increases adopted last year, holding other factors constant, increase the share of the total for those taxes — for the years the increases are in effect. Other policy changes, when interacting with economic change, can have more long-term impacts on tax shares. For example, part of the increase in personal income tax share and decline in the corporate tax share in recent years can be traced to the movement of business income from the corporate to the individual income tax base. This movement was facilitated by State and Federal action allowing for the formation of Limited Liability Companies (LLC) and S corporations. These entities have many characteristics of a business but the flow of income to members (or shareholders) is taxed under the personal income tax. Over the past decade, the number of LLCs in New York has increased from zero in 1993 to over 150,000 in 2003. In addition, the growth in S corporations, which are companies with a small number of shareholders, has also been dramatic. New York first allowed S corporation status in 1981, but the number of S corporations grew dramatically in the 1990s. The combination of changing taxpayer behavior (filing status), aided by changes in policy facilitating the change in behavior, has resulted in significant changes in tax shares. In this case, the business share shrinks and the personal income tax share increases.

In other instances, changes in the economic environment can be so large as to conceal the impact of large tax policy shifts. For example, despite the significant income tax reductions of the late 1990s, income tax growth remained relatively high. This was the consequence of the rapid income growth associated with the large increases in financial service incomes. This shifted the income tax share upward despite the large reductions in income tax rates over the 1995-97 period.

Overall, there is a strong relationship between growth in the economy, as measured by personal income, and in tax receipts adjusted for law changes. The accompanying chart shows that growth in tax receipts responds positively to changes in personal income growth. The relationship is to be expected given the sensitivity of the personal income and sales tax to changes in economic conditions, and especially to changes in personal income. However, there is significant noise in this relationship, even after correcting for law changes, as unusual factors and changes in taxpayer behavior can disturb this relationship over time.

PERSONAL INCOME TAX

Personal income tax collections are strongly affected by both the economic cycle and changes in tax rates, as can be seen in the accompanying charts and tables. During periods of economic growth, collections from the income tax tend to increase more rapidly than the overall economy. During recessionary periods, income tax collections continue to increase but at a lower rate, with the exception of 2001-02 and 2002-03, when the September 11th attacks led to a more concentrated and lengthy economic impact in New York that depressed receipts. Lowering tax rates has the obvious effect of reducing growth in collections, holding economic factors constant, as can be seen during the tax cut programs of 1987-89 and 1995-97. The tax cuts of 1995-97 were overshadowed by strong wage growth, particularly in financial sector bonuses, and, as a consequence, tax collections growth remained robust.

The share of total tax receipts derived from the personal income tax has increased to historically high percentages in recent years, reaching 60 percent for the first time in 2000-01. In recent years, growth in employment and rapid increases in the income of high-income individuals drove the income tax share upward, while the share of most other tax sources has declined. (See Economic Backdrop section.) This upward shift in share was reversed in 2001-02 and 2002-03 as the income earned by high-income individuals in the form of bonuses, stock options, and taxable capital gains declined significantly, due to a depressed economy.

The estimated PIT share is expected to increase in 2003-04, reflecting improved economic conditions as well as the temporary increase imposed in 2003 in income tax rates for taxpayers over $150,000. As the New York economic recovery continues over the next few fiscal years, growth in wages and other personal income components and in capital gains are projected to accelerate. The temporary tax increase will be phased out in 2004-06. On net, personal income tax growth will average almost 6.8 percent over the 2003-04 to 2006-07 period, close to its historical average of 7.0 percent over the past three decades. With overall receipts expected to grow at a slower 5.5 percent average over the period, the income tax share will rise and again reach 60 percent of tax receipts by State fiscal year 2006-07.

USER TAXES AND FEES

User taxes and fees have declined as a share of total taxes since the early 1970s, reflecting, in part, that such taxes tend to be less sensitive to changes in the income of State residents than does the personal income tax. In addition, user taxes, such as the taxes on cigarettes, motor fuel and alcoholic beverages, are taxed at rates fixed in statute per quantity of the product consumed. These taxes are not very sensitive to overall price changes. As a result, during periods of economic expansion, they tend to grow more slowly than other tax sources that include price increases in their base and they tend to decline less rapidly during economic downturns. As a result, changes to the share of total taxes represented by user taxes is often a product of volatility in other more economically sensitive taxes. Therefore, given the current economic forecast, it is expected that the share of taxes derived from user taxes and fees will reach 27 percent of the total over the next two fiscal years. The percentage declines in 2005-06 and 2006-07 as the temporary surcharge is eliminated.

In general for this category, periods with low- or negative-growth rates coincide with recessionary periods (1980-82, 1990-92, 2001-02) or the first year of the exemption on clothes and shoes. Higher growth rates are associated with periods of recovery or sustained economic growth. User tax and fee growth averaged 4.4 percent over the 1973-74 to 2002-03 period. For the 2003-04 Budget planning horizon, average growth of 3.8 percent is assumed. The lower than average growth rate is due to a lower than average inflationary environment as well as the phasing out of the one quarter of one percent temporary tax increase imposed in 2003, the shifting of a portion of sales tax receipts to New York City beginning in 2005-06, partially offset by proposed changes to the sales tax clothing exemption.

BUSINESS TAXES AND OTHER TAXES

The business tax share of total taxes is very volatile, as a result of the significant variability of taxable business profits, but has declined in recent years due partially to reductions in tax rates and the base subject to tax. The volatility inherent in business taxes means that its share of total taxes fluctuates above and below average growth in an unpredictable manner.

The overall volatility of business tax collections is largely the result of intricacies of the tax law and timing issues associated with tax payments made by business taxpayers and more recently reflects the impact of significant tax reductions. Although collections tend to decline during periods of recession, some of the most significant periods of quarterly growth occurred during the recession from 1990 to 1992. The growth during this period is largely explained by the imposition of a 15 percent business tax surcharge between 1990 and 1993. Additionally, collections display significant volatility during periods of consistent economic growth. Collections displayed almost no growth during the Wall Street Boom of the late 1990s, which may be explained by aggressive tax planning by corporations, given Federal law changes at both the Federal and State level. In addition, a significant fraction of new businesses are being formed as LLC's or S corporations, and the income from these companies is primarily taxed under the personal income tax as discussed above. The graph and associated tables also reveal that the impact of tax cuts and tax increases tends to have a lagged effect on collections growth. Business tax growth averaged over 5 percent for the past 30 years. The 2004-05 Budget assumes growth of 3.4 percent over the 2003-04 to 2006-07 time frame.

The share of other taxes has been dominated by the repeal of the real property gains tax and the gift tax, and the reductions in the pari-mutuel tax and the estate tax. Average growth of 3.8 percent is expected for this tax category over the 2003-04 to 2005-06 period.

The following tables provide detail on historical growth in actual All Funds tax receipts. In addition, receipts are adjusted to show the impact of inflation on overall receipts and on major tax categories.

- All Funds Tax Receipts Growth – Actual and inflation adjusted levels and growth rates.
- Major Tax Groups Receipts Growth – Actual levels and growth by major tax source.
- Major Tax Groups Inflation Adjusted Receipts Growth – Inflation adjusted growth by major tax source.
- All Funds Receipts Shares – Share of total tax receipts by major tax source.
- Actual, Base and Inflation Adjusted Base Receipts Growth – Tax receipts growth adjusted for law changes.

ALL FUNDS TAX RECEIPTS GROWTH
(millions of dollars)

Fiscal Year	All Funds Tax Receipts[1]	Percent Change	All Funds Inflation Adjusted[2]	Percent Change
1972-73	7,806.5		18,484.4	
1973-74	8,186.6	4.9	17,995.7	(2.6)
1974-75	8,662.8	5.8	17,109.0	(4.9)
1975-76	9,421.5	8.8	17,237.2	0.7
1976-77	10,347.7	9.8	17,915.6	3.9
1977-78	10,505.4	1.5	17,061.1	(4.8)
1978-79	11,153.9	6.2	16,701.7	(2.1)
1979-80	12,137.6	8.8	16,174.4	(3.2)
1980-81	13,496.0	11.2	15,951.2	(1.4)
1981-82	15,143.3	12.2	16,353.5	2.5
1982-83	16,025.0	5.8	16,455.6	0.6
1983-84	18,644.3	16.3	18,511.6	12.5
1984-85	20,391.8	9.4	19,445.4	5.0
1985-86	22,571.8	10.7	20,817.9	7.1
1986-87	24,358.3	7.9	22,093.7	6.1
1987-88	25,858.9	6.2	22,539.9	2.0
1988-89	26,261.7	1.6	21,951.9	(2.6)
1989-90	28,050.4	6.8	22,345.0	1.8
1990-91	27,818.2	(0.8)	21,019.9	(5.9)
1991-92	29,846.6	7.3	21,763.3	3.5
1992-93	31,661.2	6.1	22,390.0	2.9
1993-94	33,026.2	4.3	22,716.7	1.5
1994-95	33,050.3	0.1	22,141.7	(2.5)
1995-96	33,927.1	2.7	22,112.0	(0.1)
1996-97	34,620.3	2.0	21,911.6	(0.9)
1997-98	35,920.6	3.8	22,294.7	1.7
1998-99	38,494.6	7.2	23,514.2	5.5
1999-2000	41,389.2	7.5	24,648.6	4.8
2000-01	44,657.9	7.9	25,718.4	4.3
2001-02	42,474.6	(4.9)	23,915.9	(7.0)
2002-03	39,627.0	(6.7)	21,893.4	(8.5)
2003-04*	42,692.4	7.7	23,077.0	5.7
2004-05**	45,913.2	7.5	24,038.3	5.6
2005-06**	47,386.4	3.2	24,278.3	1.1
2006-07**	49,048.5	3.5	24,772.0	1.1
Historical Average 1973-74 to 2002-03		5.7		0.7
Historical Average 1980-81 to 2002-03		5.4		1.4
Average Forecast 2003-04 to 2006-07		5.5		3.4
Average Recessionary Growth		4.9		(1.1)
Average Expansionary Growth		6.9		2.0

[1] Personal Income Tax defined as gross receipts less refunds — 2000-01 receipts reflect an adjustment for the timely payment of refunds.
[2] Receipts deflated by Consumer Price Index (CPI).
* Estimated.
** Projected.
Note: For law changes affecting amounts flowing into various funds, see individual sections.

MAJOR TAX GROUPS
(millions of dollars)

	All Funds Tax Receipts							
Fiscal Year	**Personal Income Tax[1]**	**Percent Change**	**User Taxes and Fees**	**Percent Change**	**Business Taxes**	**Percent Change**	**Other Taxes**	**Percent Change**
1972-73	3,211.9		2,978.7		1,282.6		333.3	
1973-74	3,432.0	6.9	3,137.9	5.3	1,296.1	1.1	320.6	(3.8)
1974-75	3,588.6	4.6	3,285.8	4.7	1,456.3	12.4	332.1	3.6
1975-76	3,948.8	10.0	3,437.8	4.6	1,699.0	16.7	335.9	1.1
1976-77	4,527.0	14.6	3,531.3	2.7	1,908.0	12.3	381.4	13.5
1977-78	4,506.2	(0.5)	3,710.2	5.1	1,998.8	4.8	290.2	(23.9)
1978-79	5,057.8	12.2	3,905.2	5.3	1,904.8	(4.7)	286.1	(1.4)
1979-80	5,780.0	14.3	4,129.6	5.7	1,973.3	3.6	254.7	(11.0)
1980-81	6,612.3	14.4	4,240.6	2.7	2,350.2	19.1	292.9	15.0
1981-82	8,034.0	21.5	4,434.8	4.6	2,392.1	1.8	282.4	(3.6)
1982-83	8,275.8	3.0	4,773.0	7.6	2,567.2	7.3	409.0	44.8
1983-84	9,374.0	13.3	5,476.4	14.7	3,203.9	24.8	590.0	44.3
1984-85	10,395.1	10.9	5,736.1	4.7	3,399.6	6.1	861.0	45.9
1985-86	11,582.3	11.4	6,319.4	10.2	3,606.1	6.1	1,064.0	23.6
1986-87	12,477.0	7.7	6,603.5	4.5	3,813.8	5.8	1,464.0	37.6
1987-88	13,569.3	8.8	7,071.9	7.1	3,923.5	2.9	1,294.2	(11.6)
1988-89	13,844.4	2.0	7,267.7	2.8	3,809.0	(2.9)	1,340.6	3.6
1989-90	15,301.0	10.5	7,857.5	8.1	3,725.8	(2.2)	1,166.1	(13.0)
1990-91	14,467.0	(5.5)	7,664.7	(2.5)	4,484.4	20.4	1,202.1	3.1
1991-92	14,942.6	3.3	8,093.4	5.6	5,699.0	27.1	1,111.6	(7.5)
1992-93	15,960.7	6.8	8,331.8	2.9	6,223.4	9.2	1,145.3	3.0
1993-94	16,502.0	3.4	8,597.6	3.2	6,798.3	9.2	1,128.3	(1.5)
1994-95	16,727.9	1.4	9,067.1	5.5	6,143.6	(9.6)	1,111.7	(1.5)
1995-96	17,398.5	4.0	9,152.7	0.9	6,240.1	1.6	1,135.8	2.2
1996-97	17,554.4	0.9	9,380.6	2.5	6,517.0	4.4	1,168.3	2.9
1997-98	18,289.0	4.2	9,722.4	3.6	6,585.6	1.1	1,323.6	13.3
1998-99	20,576.1	12.5	10,067.3	3.5	6,400.8	(2.8)	1,450.4	9.6
1999-2000	23,194.4	12.7	10,614.4	5.4	6,133.2	(4.2)	1,447.2	(0.2)
2000-01	26,942.5	16.2	10,669.5	0.5	5,846.2	(4.7)	1,199.7	(17.1)
2001-02	25,573.7	(5.1)	10,542.8	(1.2)	5,184.8	(11.3)	1,173.3	(2.2)
2002-03	22,648.4	(11.4)	10,804.3	2.5	4,983.2	(3.9)	1,190.5	1.5
2003-04*	24,660.0	8.9	11,815.4	9.4	4,983.0	(0.0)	1,234.0	3.7
2004-05**	26,769.0	8.6	12,481.3	5.6	5,439.5	9.2	1,223.4	(0.9)
2005-06**	28,356.0	5.9	12,135.0	(2.8)	5,597.3	2.9	1,298.1	6.1
2006-07**	29,500.0	4.0	12,479.5	2.8	5,691.2	1.7	1,377.8	6.1
Historical Average 1973-74 to 2002-03		7.0		4.4		5.0		5.7
Historical Average 1980-81 to 2002-03		6.4		4.3		4.6		8.4
Average Forecast 2003-04 to 2006-07		6.8		3.8		3.4		3.8
Average Recessionary Growth		5.8		3.5		7.1		1.9
Average Expansionary Growth		8.9		5.2		4.0		8.0

[1] Personal Income Tax defined as gross receipts less refunds – 2000-01 receipts reflect an adjustment for the timely payment of refunds.
* Estimated.
** Projected.
Note: For law changes affecting amounts flowing into various funds, see individual revenue sections.

MAJOR TAX GROUPS
(millions of dollars)

Inflation Adjusted All Funds Tax Receipts

Fiscal Year	Personal Income[1] Percent Change	User Taxes and Fees Percent Change	Business Taxes Percent Change	Other Taxes Percent Change
1973-74	(0.8)	(2.2)	(6.2)	(10.7)
1974-75	(6.1)	(5.9)	1.0	(6.9)
1975-76	1.9	(3.1)	8.1	(6.3)
1976-77	8.5	(2.8)	6.3	7.5
1977-78	(6.6)	(1.4)	(1.7)	(28.6)
1978-79	3.5	(3.0)	(12.1)	(9.1)
1979-80	1.7	(5.9)	(7.8)	(20.8)
1980-81	1.5	(8.9)	5.6	2.0
1981-82	11.0	(4.4)	(7.0)	(11.9)
1982-83	(2.0)	2.3	2.0	37.7
1983-84	9.5	10.9	20.7	39.5
1984-85	6.5	0.6	1.9	40.2
1985-86	7.8	6.6	2.6	19.5
1986-87	5.9	2.8	4.0	35.3
1987-88	4.5	2.9	(1.1)	(15.0)
1988-89	(2.2)	(1.4)	(6.9)	(0.7)
1989-90	5.3	3.0	(6.8)	(17.1)
1990-91	(10.3)	(7.5)	14.2	(2.2)
1991-92	(0.3)	1.9	22.6	(10.8)
1992-93	3.6	(0.2)	5.9	(0.1)
1993-94	0.6	0.4	6.3	(4.2)
1994-95	(1.3)	2.7	(12.0)	(4.0)
1995-96	1.2	(1.8)	(1.2)	(0.6)
1996-97	(2.0)	(0.5)	1.4	(0.1)
1997-98	2.2	1.6	(0.9)	11.1
1998-99	10.7	1.9	(4.3)	7.8
1999-2000	9.9	2.8	(6.6)	(2.7)
2000-01	12.3	(2.8)	(7.8)	(19.8)
2001-02	(7.2)	(3.4)	(13.3)	(4.4)
2002-03	(13.2)	0.5	(5.8)	(0.5)
2003-04*	6.8	7.2	(1.9)	1.7
2004-05**	6.6	3.7	7.1	(2.7)
2005-06**	3.8	(4.8)	0.8	3.9
2006-07**	1.6	0.5	(0.7)	3.7
Historical Average 1973-74 to 2002-03	1.9	(0.5)	0.0	0.8
Historical Average 1980-81 to 2002-03	2.4	0.4	0.6	4.3
Historical Average 1994-95 to 2002-03	1.4	0.1	(5.6)	(1.5)
Average Forecast 2003-04 to 2006-07	4.7	1.7	1.3	1.6
Average Recessionary Growth	(0.3)	(2.4)	1.0	(3.9)
Average Expansionary Growth	4.0	0.5	(0.8)	3.3

1 Personal Income Tax defined as gross receipts less refunds — 2000-01 receipts reflect an adjustment for the timely payment of refunds.
* Estimated.
** Projected.

ALL FUNDS TAX RECEIPTS

Fiscal Year	Personal Income Tax[1]	User Taxes and Fees	Business Taxes	Other Taxes
	Percent of All Funds Tax Receipts Accounted for By:			
1972-73	41.1	38.2	16.4	4.3
1973-74	41.9	38.3	15.8	3.9
1974-75	41.4	37.9	16.8	3.8
1975-76	41.9	36.5	18.0	3.6
1976-77	43.7	34.1	18.4	3.7
1977-78	42.9	35.3	19.0	2.8
1978-79	45.3	35.0	17.1	2.6
1979-80	47.6	34.0	16.3	2.1
1980-81	49.0	31.4	17.4	2.2
1981-82	53.1	29.3	15.8	1.9
1982-83	51.6	29.8	16.0	2.6
1983-84	50.3	29.4	17.2	3.2
1984-85	51.0	28.1	16.7	4.2
1985-86	51.3	28.0	16.0	4.7
1986-87	51.2	27.1	15.7	6.0
1987-88	52.5	27.3	15.2	5.0
1988-89	52.7	27.7	14.5	5.1
1989-90	54.5	28.0	13.3	4.2
1990-91	52.0	27.6	16.1	4.3
1991-92	50.1	27.1	19.1	3.7
1992-93	50.4	26.3	19.7	3.6
1993-94	50.0	26.0	20.6	3.4
1994-95	50.6	27.4	18.6	3.4
1995-96	51.3	27.0	18.4	3.3
1996-97	50.7	27.1	18.8	3.4
1997-98	50.9	27.1	18.3	3.7
1998-99	53.5	26.2	16.6	3.8
1999-2000	56.0	25.6	14.8	3.5
2000-01	60.3	23.9	13.1	2.7
2001-02	60.2	24.8	12.2	2.8
2002-03	57.2	27.3	12.6	3.0
2003-04*	57.8	27.7	11.7	2.9
2004-05**	58.3	27.2	11.8	2.7
2005-06**	59.8	25.6	11.8	2.7
2006-07**	60.1	25.4	11.6	2.8
Historical Average 1972-73 to 2002-03	50.2	29.6	16.6	3.6
Forecast Average 2003-04 to 2006-07	59.0	26.5	11.7	2.8

[1] Personal Income Tax defined as gross receipts less refunds — 2000-01 receipts reflect an adjustment for the timely payment of refunds.
* Estimated.
** Projected.
Note: For law changes affecting amounts flowing into various funds, see individual sections.

Base Growth

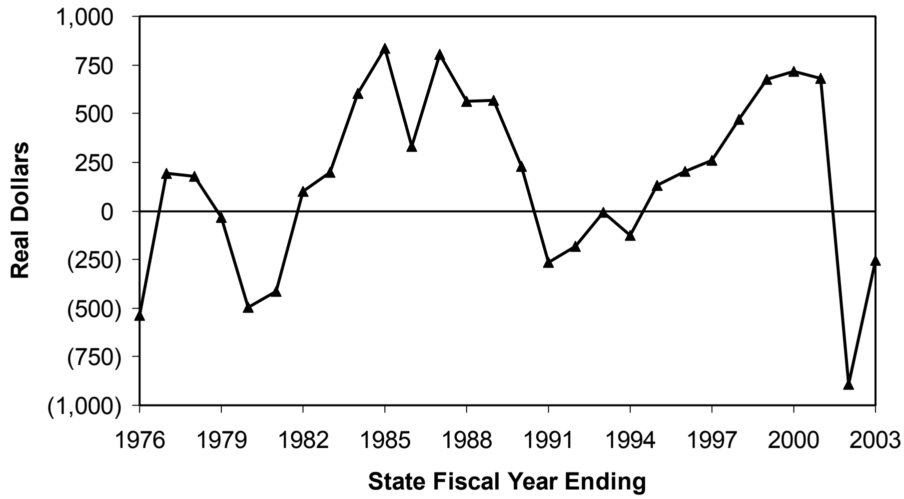
All Funds receipts can be adjusted for the estimated value of tax policy and administrative changes to obtain an approximate base receipts series. The accompanying table reports growth in estimated base receipts compared to growth in actual receipts. Growth in base receipts is higher than for actual receipts in most years, reflecting the impact of tax reductions in lowering actual receipts growth. The impact of the Wall Street Boom on receipts growth in the late 1990s and into 2000-01 is much more evident in base growth. This is as expected, given the fact that tax cuts enacted over the 1995-2000 period have reduced actual revenue growth substantially. However, this trend is estimated to reverse itself in the period between 2003-04 and 2004-05 as a result of temporary tax increases, which will cause actual growth to exceed base growth.

ALL FUNDS
ACTUAL AND BASE GROWTH
(percent change)

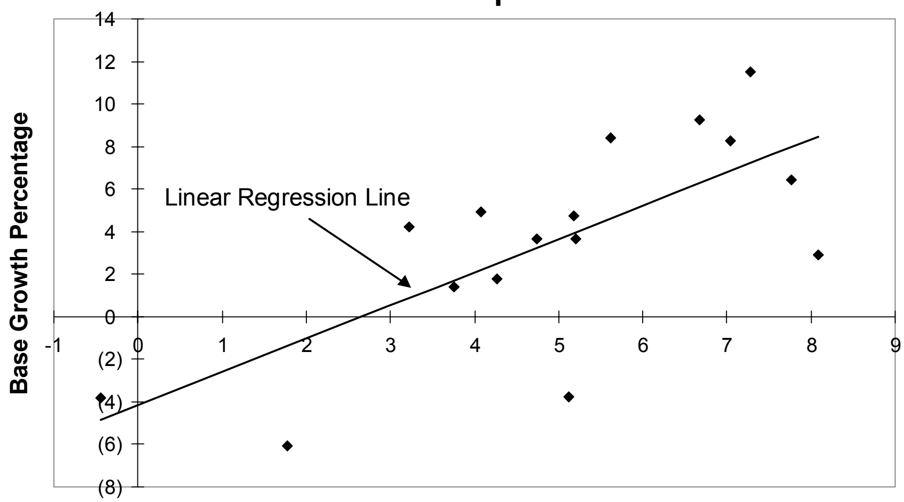
Fiscal Year	Actual Receipts	Base Receipts	Inflation Adjusted Base Receipts
1987-88	6.16	6.44	2.28
1988-89	1.56	2.93	(1.29)
1989-90	6.78	8.29	3.20
1990-91	(0.75)	(3.78)	(8.73)
1991-92	7.25	1.40	(2.15)
1992-93	6.08	4.91	1.75
1993-94	4.31	4.23	1.38
1994-95	0.07	1.76	(0.89)
1995-96	2.65	3.66	0.85
1996-97	2.04	3.66	0.66
1997-98	3.75	4.73	2.71
1998-99	7.17	8.41	6.70
1999-2000	7.52	9.25	6.51
2000-01	7.90	11.50	7.82
2001-02	(4.89)	(3.83)	(6.11)
2002-03	(6.71)	(6.09)	(7.86)
2003-04*	7.74	5.18	3.15
2004-05**	7.54	7.00	5.02
2005-06**	3.21	4.72	2.57
2006-07**	3.51	5.65	3.23
Historical Average 1987-88 to 2002-03	3.18	3.59	0.43
Forecast Average 2003-04 to 2006-07	5.37	5.57	3.49

* Estimated.
** Projected.
Notes:
Taxes only.
PIT is gross receipts less refunds.
Base receipts are actual receipts adjusted for incremental changes in taxes due to tax or administrative actions.

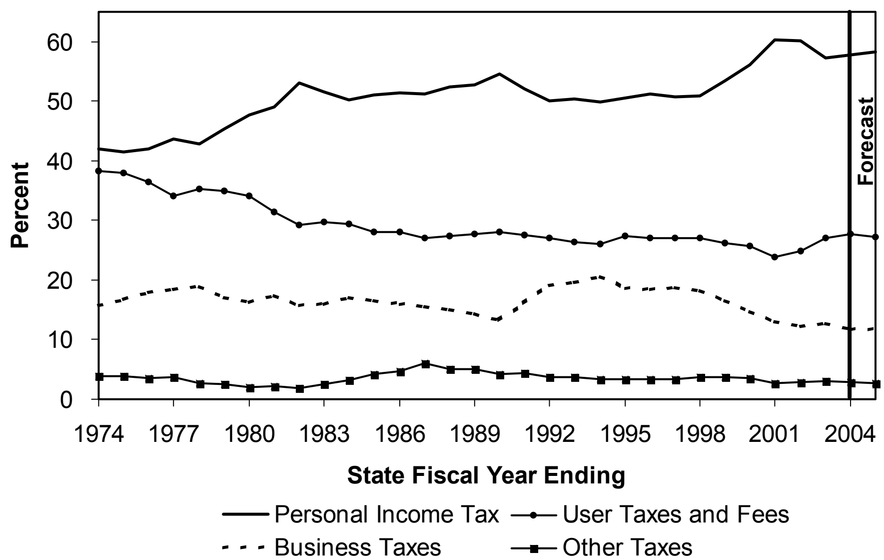
Cost of Business Cycles



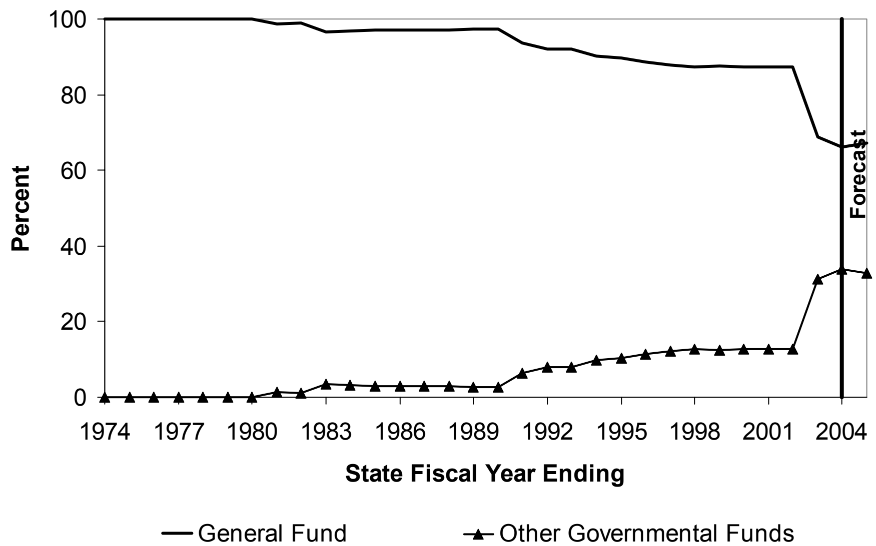
Relationship of Personal Income and Base Tax Receipts Growth

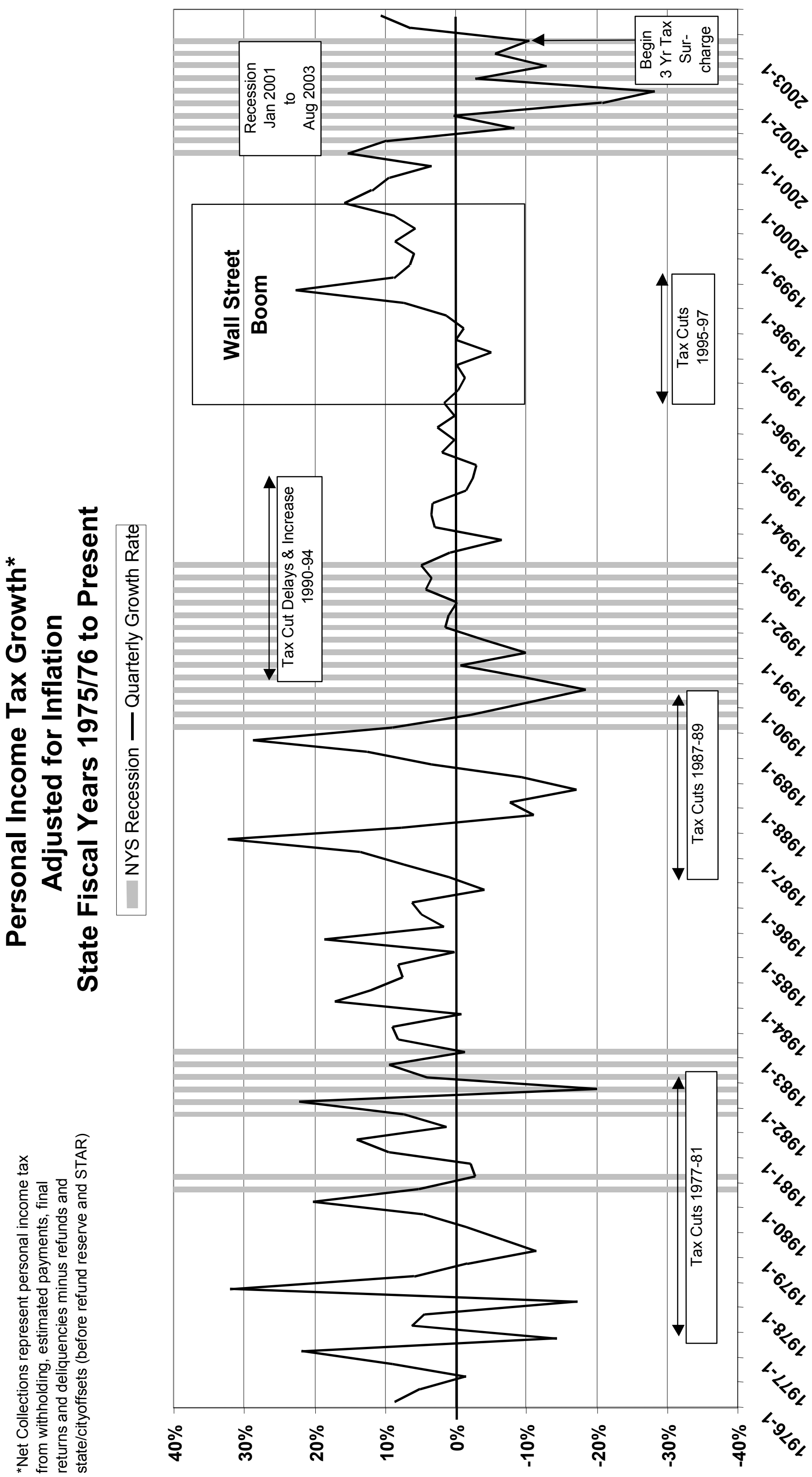


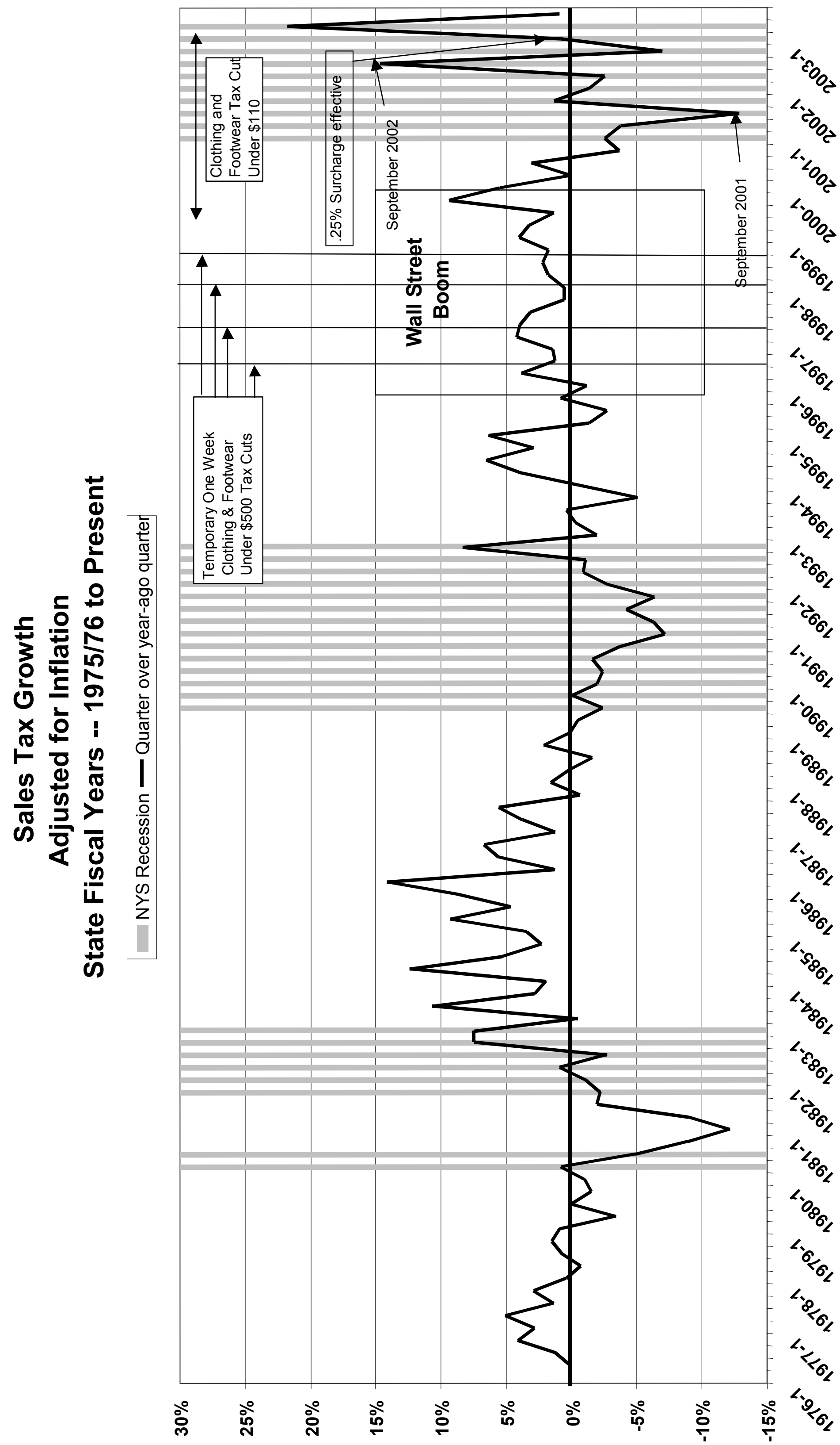
Share of All Funds Tax Receipts by Major Tax Categories



Share of All Funds Tax Receipts by Major Fund Type




Personal Income Tax Growth*
Adjusted for Inflation
State Fiscal Years 1975/76 to Present
NYS Recession
Quarterly Growth Rate
*Net Collections represent personal income tax from withholding, estimated payments, final returns and deliquencies minus refunds and state/cityoffsets (before refund reserve and STAR)
40%
30%
20%
10%
0%
-10%
-20%
-30%
-40%
1976-1
1977-1
1978-1
1979-1
1980-1
1981-1
1982-1
1983-1
1984-1
1985-1
1986-1
1987-1
1988-1
1989-1
1990-1
1991-1
1992-1
1993-1
1994-1
1995-1
1996-1
1997-1
1998-1
1999-1
2000-1
2001-1
2002-1
2003-1
Tax Cuts 1977-81
Tax Cuts 1987-89
Tax Cut Delays & Increase 1990-94
Wall Street Boom
Tax Cuts 1995-97
Recession Jan 2001 to Aug 2003
Begin 3 Yr Tax Sur- charge


Sales Tax Growth
Adjusted for Inflation
State Fiscal Years -- 1975/76 to Present
NYS Recession
Quarter over year-ago quarter
Temporary One Week Clothing & Footwear Under $500 Tax Cuts
Wall Street Boom
Clothing and Footwear Tax Cut Under $110
.25% Surcharge effective
September 2002
September 2001
30%
25%
20%
15%
10%
5%
0%
-5%
-10%
-15%
1976-1
1977-1
1978-1
1979-1
1980-1
1981-1
1982-1
1983-1
1984-1
1985-1
1986-1
1987-1
1988-1
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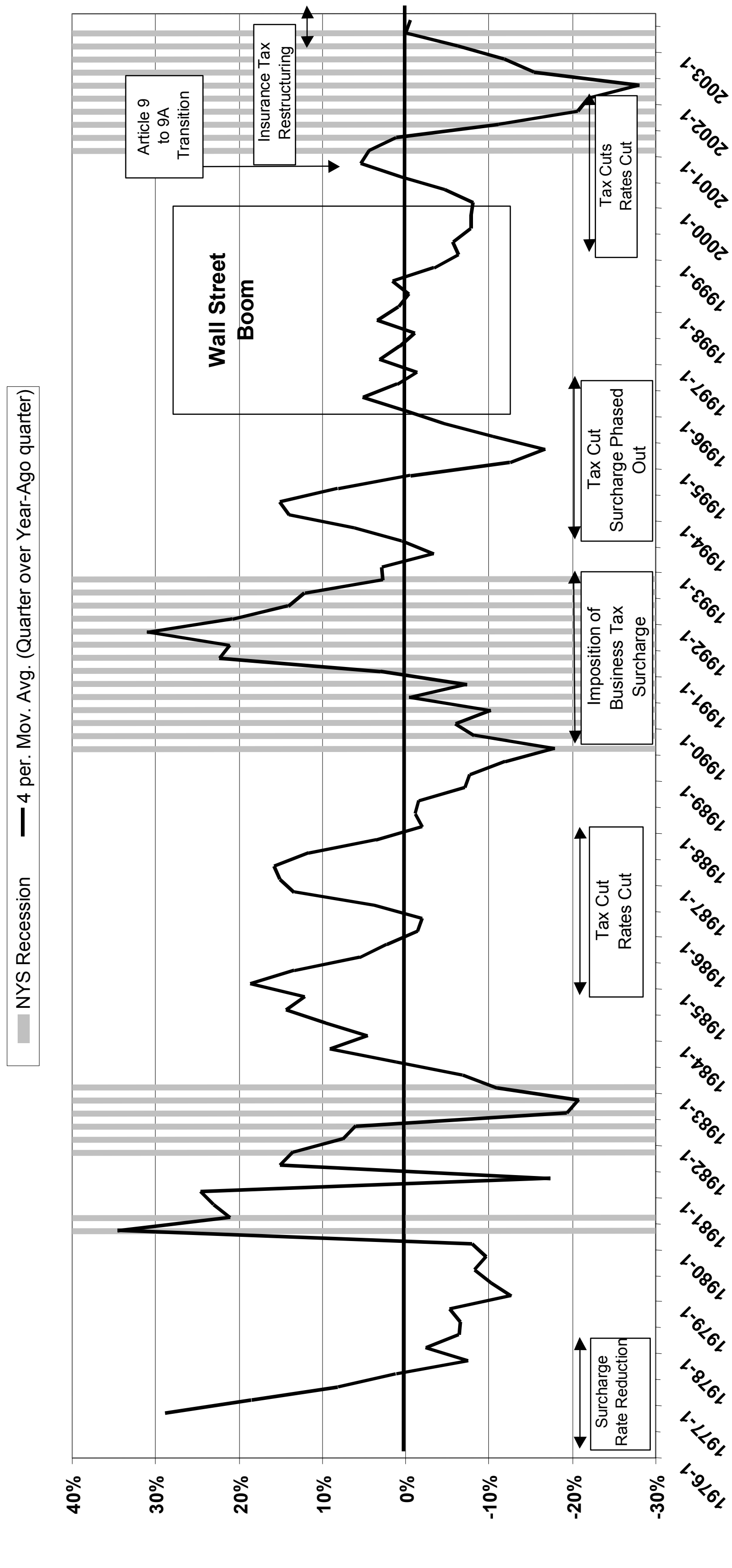
1991-1
1992-1
1993-1
1994-1
1995-1
1996-1
1997-1
1998-1
1999-1
2000-1
2001-1
2002-1
2003-1

Corporate Franchise, Insurance and Bank Tax Growth
Adjusted for Inflation
State Fiscal Years -- 1975/76 to Present



CASH FLOW

The following tables report quarterly cash flow for General Fund tax receipts. Actual results are provided for 2002-03 and the first three quarters of the current State fiscal year, and estimates are reported for the remainder of 2003-04 and 2004-05. The table highlights the impact of STAR, refund reserve, and revenue bond fund transactions on General Fund cash flow. The quarterly estimates for 2003-04 and 2004-05 are consistent with average shares from prior years adjusted for proposed and previously enacted law changes that would impact normal cash flow.

In the personal income tax, withholding tax patterns are derived from quarterly wage forecasts. In addition, personal income tax net receipts reflect several other patterns: large tax settlement payments in the first quarter; high levels of refund payments in the first and fourth quarter of a State fiscal year; high withholding tax collections reflecting bonus payments in the fourth quarter; and STAR deposits primarily in the third quarter of the State fiscal year.

Several significant factors combined to change the 2003-04 personal income tax cash flow pattern from the pattern seen in a typical year. The largest variations were due to the enactment of the three-year temporary surcharge and the pattern of resulting additional withholding and estimated tax payments. Since withholding tables were changed in July 2003 and the Legislature required that the tables be designed to collect the full 2003 increase during 2003-04, there was a doubling-up of withholding increases in the second and third quarters of the fiscal year. In addition, taxpayers required to make quarterly estimated tax payments also increased their payments for the tax increase starting in the second quarter, again raising the share of collections received after the first quarter. Also, before technical corrections were made in estimated tax provisions, partnerships making estimated tax payments for their nonresident partners made extra payments in September, apparently causing the level of estimated tax payments collected in December and January to be depressed. The pattern of underlying growth in the State economy also affected the cash flow pattern. While there was very little wage growth early in the fiscal year, the second, third, and fourth quarters have shown increasingly strong growth.

In general, the personal income cash flow pattern for 2004-05 is expected to return to a more typical quarterly pattern. The 2004-05 year will not experience the doubling-up of withholding or the extra partnership estimated tax payments that occurred in the second half of the 2003 calendar year. This will result in small quarter-over-quarter growth rates for the second and third quarters of the State fiscal year. In addition, the cash flow pattern is expected to be affected by two somewhat-offsetting factors. High settlement payments, resulting from the need to make additional payments on 2003 tax liability, are expected to significantly increase net collections in the first quarter. In contrast, higher wage growth toward the end of the fiscal year is expected to result in a higher share of withholding collections in the January to March quarter than in a typical year.

Double-digit growth rates for user taxes and fees beginning in the second quarter of 2003-04 and ending after the first quarter of 2004-05 are due to the tax law changes contained in the 2003-04 Enacted Budget. Growth after the first quarter returns to more normal rates as the impact of law changes is reflected in the prior year base. On June 1, 2003, all clothing became subject to the sales and use tax except during two tax-free weeks (in August 2003 and January 2004) and the State sales and use tax rate increased from 4 percent to 4.25 percent.

GENERAL FUND 2002-03 QUARTERLY CASH FLOW ACTUALS
(millions of dollars)

	1st Quarter	2nd Quarter	3rd Quarter	4th Quarter	Total
Personal Income Tax	6,754.6	3,762.2	2,147.8	4,126.2	16,790.8
Gross collections	8,019.9	5,522.8	5,836.2	7,565.6	26,944.5
Refunds	(2,254.0)	(326.4)	(676.5)	(1,039.3)	(4,296.2)
Refund reserve	1,677.4	0.0	0.0	(627.5)	1,049.9
STAR Fund deposit	0.0	(180.0)	(2,296.0)	(188.1)	(2,664.1)
DDRF deposit/RBTF	(688.7)	(1,254.2)	(715.9)	(1,584.5)	(4,243.3)
User Taxes and Fees	1,781.2	1,816.1	1,745.2	1,720.0	7,062.5
Sales and use taxes	1,513.1	1,685.7	1,572.4	1,556.4	6,327.6
Cigarette and tobacco taxes	139.4	116.5	102.4	88.2	446.5
Motor vehicle fees	74.1	(44.3)	15.0	21.9	66.7
Alcoholic beverage taxes	46.4	47.9	45.1	40.4	179.8
ABC license fees	8.2	10.3	10.3	13.1	41.9
Business Taxes	702.0	833.3	756.9	1,087.6	3,379.8
Corporation franchise tax	259.6	358.2	319.7	469.7	1,407.2
Corporation and utilities taxes	162.8	202.2	232.8	261.8	859.6
Insurance taxes	156.0	170.0	140.1	237.9	704.0
Bank taxes	123.6	102.9	64.3	118.2	409.0
Other Taxes	209.6	213.5	158.5	161.3	742.9
Estate and gift tax	201.5	202.6	150.2	153.7	708.0
Real property gains tax	1.1	1.3	1.2	1.2	4.8
Pari-mutuel taxes	6.9	9.5	6.8	6.3	29.5
Other taxes	0.1	0.1	0.3	0.1	0.6
TOTAL	9,447.4	6,625.1	4,808.9	7,095.1	27,976.5
TOTAL TAXES (before transfers, STAR and Refund Reserve)	9,070.1	8,730.6	8,453.8	10,123.5	36,378.0

GENERAL FUND 2003-04 QUARTERLY CASH FLOW ACTUALS AND ESTIMATES
(millions of dollars)

	1st Quarter	2nd Quarter	3rd Quarter	4th Quarter	Total
Personal Income Tax	4,600.0	4,130.8	2,550.7	4,509.5	15,791.0
Gross collections	7,758.2	6,003.4	6,471.0	8,852.3	29,085.0
Refunds	(2,461.6)	(315.7)	(595.4)	(1,052.3)	(4,425.0)
Refund reserve	627.5	0.0	0.0	(1,204.5)	(577.0)
STAR Fund deposit	0.0	(180.0)	(2,475.0)	(180.0)	(2,835.0)
DDRF deposit/RBTF	(1,324.1)	(1,376.9)	(850.0)	(1,906.0)	(5,457.0)
User Taxes and Fees	1,820.0	2,107.4	2,056.4	1,912.9	7,896.7
Sales and use taxes	1,602.4	1,917.4	1,892.6	1,765.6	7,178.0
Cigarette and tobacco taxes	111.8	112.4	105.3	90.0	419.5
Motor vehicle fees	43.1	13.0	3.2	8.2	67.5
Alcoholic beverage taxes	48.6	50.4	46.6	38.1	183.7
ABC license fees	14.1	14.2	8.7	11.0	48.0
Business Taxes	650.1	887.1	758.2	1,099.4	3,394.8
Corporation franchise tax	190.1	424.1	294.5	473.2	1,382.0
Corporation and utilities taxes	141.5	173.6	196.6	243.3	755.0
Insurance taxes	204.6	226.4	189.6	251.7	872.3
Bank taxes	113.9	63.0	77.4	131.3	385.6
Other Taxes	175.7	223.0	222.8	162.6	784.0
Estate and gift tax	167.3	212.6	216.6	155.5	751.9
Real property gains tax	1.9	1.3	0.1	0.9	4.2
Pari-mutuel taxes	6.5	9.1	6.1	5.7	27.4
Other taxes	0.0	0.0	0.0	0.5	0.5
TOTAL	7,245.8	7,348.3	5,588.1	7,684.4	27,866.5
TOTAL TAXES (before transfers, STAR and Refund Reserve)	8,581.7	9,623.4	9,632.7	11,592.3	39,430.0

GENERAL FUND QUARTERLY CASH FLOW COMPARISON
SFY 2003-04 vs. SFY 2002-03
(percent)

	1st Quarter	2nd Quarter	3rd Quarter	4th Quarter	Total
Personal Income Tax	(31.9)	9.8	18.8	9.3	(6.0)
Gross collections	(3.3)	8.7	10.9	17.0	7.9
Refunds	9.2	(3.3)	(12.0)	1.3	3.0
Refund reserve	(62.6)	N/A	N/A	92.0	(155.0)
STAR Fund deposit	N/A	0.0	7.8	(4.3)	6.4
DDRF deposit/RBTF	92.3	9.8	18.7	20.3	28.6
User Taxes and Fees	2.2	16.0	17.8	11.2	11.8
Sales and use taxes	5.9	13.7	20.4	13.4	13.4
Cigarette and tobacco taxes	(19.8)	(3.5)	2.8	2.0	(6.0)
Motor vehicle fees	(41.8)	(129.3)	(78.7)	(62.6)	1.2
Alcoholic beverage taxes	4.7	5.2	3.3	(5.7)	2.2
ABC license fees	72.0	37.9	(15.5)	(16.0)	14.6
Business Taxes	(7.4)	6.5	0.2	1.1	0.4
Corporation franchise tax	(26.8)	18.4	(7.9)	0.7	(1.8)
Corporation and utilities taxes	(13.1)	(14.1)	(15.5)	(7.1)	(12.2)
Insurance taxes	31.2	33.2	35.3	5.8	23.9
Bank taxes	(7.8)	(38.8	20.4	11.0	(5.7)
Other Taxes	(16.2)	4.4	40.6	0.8	5.5
Estate and gift tax	(17.0)	4.9	44.2	1.1	6.2
Real property gains tax	72.7	0.0	(91.7)	(25.0)	(12.5)
Pari-mutuel taxes	(5.8)	(4.3)	(10.3)	(9.2)	(7.1)
Other taxes	(100.0)	(100.0)	(100.0)	400.0	(16.7)
TOTAL	(23.3)	10.9	16.2	8.3	(0.4)
TOTAL TAXES (before transfers, STAR and Refund Reserve)	(5.4)	10.2	13.9	14.5	8.4

GENERAL FUND 2004-05 QUARTERLY CASH FLOW ESTIMATES
(millions of dollars)

	1st Quarter	2nd Quarter	3rd Quarter	4th Quarter	Total
Personal Income Tax	6,243.1	4,264.0	2,454.0	5,559.0	18,520.1
Gross collections	9,077.0	6,213.0	6,567.0	9,337.0	31,194.0
Refunds	(2,359.5)	(346.0)	(657.0)	(1,062.5)	(4,425.0)
Refund reserve	1,204.5	0.0	0.0	(511.5)	693.0
STAR Fund deposit	0.0	(180.0)	(2,638.0)	(180.0)	(2,998.0)
DDRF deposit/RBTF	(1,679.0)	(1,423.0)	(818.0)	(2,024.0)	(5,944.0)
User Taxes and Fees	2,053.7	2,162.3	2,122.0	2,002.1	8,340.1
Sales and use taxes	1,870.3	1,979.7	1,956.6	1,859.2	7,665.9
Cigarette and tobacco taxes	117.0	114.4	104.8	87.7	423.8
Motor vehicle fees	6.3	6.4	6.4	6.4	25.6
Alcoholic beverage taxes	47.8	49.4	45.7	40.0	182.9
ABC license fees	12.3	12.4	8.5	8.8	42.0
Business Taxes	903.7	899.1	855.5	1,081.6	3,739.8
Corporation franchise tax	395.9	439.0	387.9	523.8	1,746.6
Corporation and utilities taxes	152.5	162.5	170.8	171.1	656.9
Insurance taxes	222.6	194.4	194.7	300.2	912.0
Bank taxes	117.7	98.2	97.0	111.4	424.3
Other Taxes	199.4	179.5	191.4	190.7	761.1
Estate and gift tax	191.5	170.3	185.0	184.0	730.8
Real property gains tax	0.4	0.4	0.4	0.4	1.7
Pari-mutuel taxes	7.3	8.7	5.8	6.2	28.0
Other taxes	0.2	0.1	0.2	0.1	0.6
TOTAL	9,384.9	7,499.9	5,617.8	8,856.8	31,360.9
TOTAL TAXES (before transfers, STAR and Refund Reserve)	10,538.9	9,846.9	9,798.4	12,249.2	42,433.4

GENERAL FUND QUARTERLY CASH FLOW COMPARISON
SFY 2004-05 vs. SFY 2003-04
(percent)

	1st Quarter	2nd Quarter	3rd Quarter	4th Quarter	Total
Personal Income Tax	35.7	3.2	(3.8)	23.3	17.3
Gross collections	17.0	3.5	1.5	5.5	7.3
Refunds	(4.1)	9.6	10.3	1.0	0.0
Refund reserve	92.0	N/A	N/A	(57.5)	(220.1)
STAR Fund deposit	N/A	0.0	6.6	0.0	5.7
DDRF deposit/RBTF	26.8	3.4	(3.8)	6.2	8.9
User Taxes and Fees	12.8	2.6	3.2	4.7	5.6
Sales and use taxes	16.7	3.2	3.4	5.3	6.8
Cigarette and tobacco taxes	4.6	1.8	(0.5)	(2.6)	1.0
Motor vehicle fees	(85.4)	(50.6)	100.6	(21.5)	(62.1)
Alcoholic beverage taxes	(1.6)	(2.0)	(1.9)	5.0	(0.4)
ABC license fees	(12.8)	(12.7)	(2.3)	(20.0)	(12.5)
Business Taxes	39.4	2.4	13.0	(2.6)	10.2
Corporation franchise tax	109.6	3.4	31.8	10.4	26.4
Corporation and utilities taxes	8.1	(6.4)	(12.9)	(29.9)	(13.0)
Insurance taxes	8.8	(10.4)	2.7	15.0	4.6
Bank taxes	3.3	55.6	25.5	(15.1)	10.1
Other Taxes	13.5	(19.5)	(14.1)	17.3	(2.9)
Estate and gift tax	14.5	(19.9)	(14.6)	18.4	(2.8)
Real property gains tax	(77.6)	(67.3)	325.0	(52.8)	(59.5)
Pari-mutuel taxes	12.6	(4.3)	(5.6)	7.9	2.0
Other taxes	N/A	N/A	N/A	(80.0)	20.0
TOTAL	29.5	2.1	0.5	15.3	12.5
TOTAL TAXES (before transfers, STAR and Refund Reserve)	22.8	2.3	1.7	5.7	7.6

SUMMARY OF STATE TAX REDUCTION PROGRAM

Since 1995-96, a multi-year tax reduction program has significantly reduced tax burdens at the State level. The accompanying table reports the tax reductions by tax type and year. In 2003-04, the annual value of the tax reduction program is estimated to total over $13.6 billion.

STATE TAX REDUCTIONS - ALL FUNDS
Current and Recommended Law
(millions of dollars)

	1996-97	1997-98	1998-99	1999-2000	2000-01	2001-02	2002-03	2003-04	2004-05
Personal Income Taxes	2,796.0	4,484.0	4,780.0	5,333.0	5,570.0	5,126.1	5,319.1	6,030.1	6,530.1
User Taxes and Fees	**210.6**	**268.6**	**388.9**	**560.0**	**1,103.8**	**1,213.1**	**1,232.5**	**825.7**	**823.1**
Sales and use tax	44.9	101.5	154.1	243.6	782.5	871.0	889.1	472.6	464.9
Cigarette and tobacco tax	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Motor fuel tax	13.1	14.1	15.5	17.5	17.8	17.6	17.6	18.6	18.6
Motor vehicle fees	0.0	0.0	49.3	69.7	69.5	75.4	73.6	74.9	73.9
Highway use tax	34.6	33.4	38.7	73.1	75.4	85.2	87.6	90.8	94.3
Alcoholic beverage tax	17.4	17.1	18.0	24.6	25.5	28.3	28.2	30.7	33.3
ABC license fees	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Hotel/Motel tax	75.1	76.5	78.0	79.5	81.1	82.8	84.4	86.1	86.1
Container tax	25.5	26.0	35.3	52.0	52.0	52.0	52.0	52.0	52.0
Auto rental tax	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Business Taxes	**1,026.5**	**1,187.5**	**1,241.8**	**1,565.8**	**2,081.7**	**2,401.9**	**2,713.8**	**3,060.1**	**3,161.8**
Corporation franchise tax	423.9	472.2	496.5	682.0	524.4	836.7	958.7	1,066.0	1,049.0
Corporation and utilities tax	248.8	289.9	306.9	425.8	1,077.8	999.7	1,115.0	1,294.5	1,405.3
Insurance tax	103.7	116.4	119.4	114.7	127.7	160.5	193.0	216.3	216.3
Bank tax	77.3	100.8	90.0	108.1	116.1	160.1	198.7	231.4	239.3
Petroleum business tax	172.8	208.2	229.0	235.2	235.7	244.9	248.4	251.9	251.9
Other Taxes	**182.8**	**178.9**	**322.3**	**317.9**	**582.9**	**785.6**	**823.9**	**851.4**	**898.4**
Estate/Gift tax	78.7	81.7	86.0	133.0	423.0	616.5	648.0	676.0	723.0
Real property gains tax	89.6	81.6	220.6	168.1	142.1	147.0	156.0	156.0	156.0
Real estate transfer tax	0.0	1.6	2.2	2.2	2.2	2.2	1.3	0.8	0.8
Pari-mutuel tax	14.5	14.0	13.5	14.5	15.5	19.8	18.5	18.5	18.5
Other	0.0	0.0	0.0	0.1	0.1	0.1	0.1	0.1	0.1
Subtotal	**4,215.9**	**6,119.0**	**6,733.0**	**7,776.7**	**9,338.4**	**9,525.9**	**10,089.3**	**10,767.3**	**11,413.4**
STAR	0.0	0.0	582.2	1,194.6	1,876.5	2,510.1	2,667.0	2,835.0	2,998.0
Grand Total	**4,215.9**	**6,119.0**	**7,315.2**	**8,971.3**	**11,214.9**	**12,036.0**	**12,753.4**	**13,602.3**	**14,411.4**

REVENUE ACTIONS

The 2004-05 Budget includes a net positive increment of $1.1 billion in All Funds revenue actions necessary for Financial Plan balance. The accompanying table summarizes the revenue proposals by type of action required (legislative or administrative) and provides a short description of the proposal, the Fund type where revenue will be deposited, the last time an action was taken in an area and the incremental revenue gain or loss from the proposed action.

FEE AND REVENUE ACTIONS LIST

Agency*	Fee Description Effective Date	Fund Type and Category	Current Fee	Proposed Fee	Year of Last Change	New Annual Revenue SFY2004-05 (000)	New Full Annual Revenue (000)
I. ADMINISTRATIVE							
DCJS	Increase record review fee -4/1/04	GFMR	$25	$50	1993	$125	$125
DHCR	Increase tax credit application fee - 4/1/04	GFMR/SFMR	Application Fee - $100 Reservation Fee - $250 Allocation Fee - 4.0%	$200 $500 5.0%	1990	$500	$500
DOT	Increase divisible load permits & fines - 4/1/04	GFMR	$50 - $4,700	$150-$3,750	1985	$1,500	$3,000
STATE	Campus fire safety - 4/1/04	GFMR	$50/$500	$50/$500	2003	$1,100	$1,100
CIV SVC	Increase exam fees - 4/1/04	SFMR	Various	Various	1997	$775	$775
DHCR	Increase low income housing credit monitoring fee - 4/1/04	SFMR	0.5%	1.0%	1991	$500	$500
DOCS	Cook Chill Revenue - 9/1/04	SFMR	None	Various	N/A	$1,000	$3,000
DOT	Increase divisible load permits & fines - 4/1/04	CFMR	$50 - $4,700	$150-$3,750	1985	$750	$1,500
				Administrative Actions Subtotals		**$6,250**	**$10,500**
II. STATUTORY							
ABC	Increase filing fees- 4/1/04	GFMR	Various	Various	1976	$200	$400
BANKING	Fee Increase - 4/1/04	GFMR	$10 - $5,000	$20 - $10,000	1992	$2,000	$2,000
DCJS	Expand parking ticket surcharge - Immediately	GFMR	None	$15	NA	$7,500	$7,500
DCJS	Vehicle & Traffic local prosecution program - Immediately	GFMR	None	Various	NA	$17,800	$17,800
DCJS	Work zone automated speed enforcement - Immediately	GFMR	None	$100	NA	$15,000	$33,000

Agency*	Fee Description Effective Date	Fund Type and Category	Current Fee	Proposed Fee	Year of Last Change	New Annual Revenue SFY2004-05	New Full Annual Revenue
						(000)	(000)
DMV	Driver Responsibility Program - Immediately	GFMR	None	$100/$1,000	NA	$17,500	$54,300
DMV	Increase ATV registration fee - Immediately	GFMR	$10	$45	NA	$5,833	$6,125
DOCS	Federal bed capacity contracts - 4/1/04	GFMR	None	$30,000/bed	NA	$15,000	$15,000
ENCON	Extend Waste Tire Fee - 60 days after enactment	GFMR/SFMR	$2.25	$2.25	2003	$300	$575
ENCON	Increase storm water fees - 4/1/04	GFMR/SFMR	$50	$50-$350	1988	$7,000	$7,000
LAW	Increase deceptive trade practices penalty - 4/1/04	GFMR	$500	$5,000	1963	$500	$500
PARKS	Increase Snowmobile Fee - Immediately	GFMR/SFMR	$5	$10	2002	$3,550	$3,550
ST POLIC	Handgun License fee - 90 days after enactment	GFMR/SFMR	None	$20-$100	NA	$32,500	$11,300
AG & MKTS	Retail food stores inspection fee - 10/1/05	SFMR	None	$100	NA	$381	$381
CPB	Increase fine - 9/1/04	SFMR	$5,000	$11,000	2002	$100	$200
CVB	Mandatory fees for youthful offenders - 180 days from passage	SFMR	None	$20 fee + Felony - $250 Misdemeanor - $140 Violation - $75	NA	$540	$1,080
CVB	Crime victim assistance fee & surcharge - 180 days from passage	SFMR	None	$20 fee + Felony - $250 Misdemeanor - $140 Violation - $75	NA	$25	$50
CVB	Sex offender fee - 180 days from passage	SFMR	None	$1,000	NA	$556	$1,112
DCJS	V&T local prosecution program - Immediately	SFMR	None	Various	NA	$5,000	$5,000
DM & NA	Increase REP fee - 4/1/04	SFMR	$550,000	$950,000	1994	$2,400	$2,400
ENCON	Increase air regulation fees - 4/1/04	SFMR	$100 - $11,000	$125 - $1,250	1994	$1,833	$1,833
HLTH OTH	Establish early intervention provider registration fee - 4/1/04	SFMR	None	Individual-$275 Agency-$900	NA	$1,000	$2,300
MED ASST	Home care assessment - 4/1/04	SFMR	None	0.7% of gross revenue	1999	$15,000	$17,000

Agency*	Fee Description Effective Date	Fund Type and Category	Current Fee	Proposed Fee	Year of Last Change	New Annual Revenue SFY2004-05	New Full Annual Revenue
						(000)	(000)
MED ASST	Hospital assessment - 4/1/04	SFMR	None	0.7% of gross revenue	1999	$183,300	$199,900
MED ASST	Nursing home assessment - 4/1/04	SFMR	5.0% of gross revenue	6.0% of gross revenue	2003	$230,400*	$452,800*
ORPS	Real property transfer filing fee - 7/1/04	SFMR	$50	Homes & Farms - $75 Other Properties - $165	2003	$14,175	$18,900
PERB	Impasse/Improper practice filing fee - 4/1/04	SFMR	None	$75/$75	NA	$200	$200
SED GSPS	Eliminate restrictions on Quick Draw - 4/1/04	SFMR	None	None	NA	$43,000	$68,000
SED GSPS	VLT Expansion - Fully effective	SFMR	None	None	NA	$0	$2,000,000**
				Statutory Actions - Subtotal		**$622,593**	**$2,930,206**
		ADMINISTRATIVE AND STATUTORY - GRAND TOTAL				**$628,843**	**$2,940,706**

III. OTHER REVENUE ACTIONS

Agency*	Fee Description Effective Date	Fund Type and Category	Current Fee	Proposed Fee	Year of Last Change	New Annual Revenue SFY2004-05	New Full Annual Revenue
T&F	Add new fixed dollar minimum - 1/1/04	GFTX	None	None	1998	$40,000	$40,000
T&F	Direct Wine Shipments - 6/1/04	GFTX/DFTX	None	None	NA	$2,000	$3,000
T&F	Empire Zones Program - Immediately	GFTX	None	None	2002	$0	$25,000
T&F	Low Income Filings - 1/1/04	GFTX/DFTX	None	None	NA	$1,000	$1,000
T&F	Replace Permanent Clothing Exemption - 6/1/04	GFTX/DFTX	None	None	2003	$400,000	$473,000
T&F	Reverse Meyers' Decision - 1/1/04	GFTX/DFTX	NA	NA	1994	$50,000	$0; acceleration
T&F	Tax Nonresidents gain from sales of Co-op Stock - 1/1/04	GFTX/DFTX	None	Taxpayer's State income tax rate	NA	$5,000	$20,000
T&F	Extend Alternative Fuels Vehicle Credit - 1/1/04	GFTX/DFTX	$2,000 Credit	$2,000 Credit	2002	$(10,000)	$(10,000)
T&F	Biotechnology Investment Credit - 1/1/05	GFTX	None	None	NA	$(5,000)	$(10,000)
T&F	Exempt Federal Military Pay - 1/1/04	GFTX/DFTX	Taxpayer's State income tax rate	0%	NA	$(1,000)	$(1,000)
T&F	Low-Income Housing - Immediately	GFTX	None	None	2002	$(2,000)	$(2,000)

Agency*	Fee Description Effective Date	Fund Type and Category	Current Fee	Proposed Fee	Year of Last Change	New Annual Revenue SFY2004-05	New Full Annual Revenue
						(000)	(000)
T&F	Single Sales Factor for Manufacturers - Immediately	GFTX	None	None	1975	$0	$(40,000)
T&F	STAR Adjustment for Inflation - 1/1/04	GFTX	None	None	NA	$(11,000)	$(57,000)
					Other Revenue Actions - Subtotal		**$469,000**	**$442,000**
					ALL FEE AND REVENUE ACTIONS - GRAND TOTAL		**$1,097,843**	**$3,382,706**

*The General Fund impact is $125 million in 2004-05 and $258 million when fully effective.
**$2.0 billion estimate reflects the full year benefit of both the expansion proposed in this Budget and the estimated value of the existing program authorized at eight racetrack facilities across the state.

Key:

CF = Capital Projects Fund
DF = Debt Service Funds
GF = General Fund
MR = Miscellaneous Receipts
SF = Special Revenue Funds
TX = Tax

DEDICATED FUND TAX RECEIPTS

Several tax sources are dedicated in whole or part to State Funds which are earmarked for specific purposes. The following table reports tax receipts by fund for the dedicated tax sources.

DEDICATED FUND TAX RECEIPTS
(millions of dollars)

	2002-03 Actual	2003-04 Estimate	2004-05 Recommended
SPECIAL REVENUE FUNDS			
School Tax Relief Fund (STAR)			
Personal income tax	2,664.1	2,835.0	2,998.0
Dedicated Mass Transportation Trust Fund	477.9	533.2	587.9
Petroleum business tax	333.6	332.3	347.8
Motor fuel tax	68.6	104.7	106.9
Motor vehicle fees	75.7	96.2	133.2
Mass Trans. Operating Assistance Fund	1,071.5	1,089.4	1,157.5
Corporate Surcharges			
Corporation franchise tax	205.2	188.0	237.5
Corporation and utilities tax	160.1	133.2	120.2
Insurance tax	72.0	104.7	109.4
Bank tax	72.2	65.6	71.9
Other			
Sales and use tax	361.9	399.5	414.3
Petroleum business tax	120.6	126.8	133.0
Corporation and utilities — sections 183 & 184	71.1	71.6	71.2
Fund 339 (State Special Rev. Fund)	0.0	0.0	39.0
Sales Tax Surcharges 339LZ	0.0	0.0	39.0
Total Tax Receipts: - Special Revenue Funds-Other	4,213.5	4,457.6	4,782.4
DEBT SERVICE FUNDS			
Debt Reduction Reserve Fund			
Personal income tax	0.0	0.0	0.0
Revenue Bond Tax Fund			
Personal income tax	4,243.3	5,456.7	5,944.3
Emergency Highway Reconditioning and Preservation Fund			
Motor fuel tax	59.5	0.0	0.0
Emergency Highway Construction and Reconstruction Fund			
Motor fuel tax	59.5	0.0	0.0
Clean Water/Clean Air Fund			
Real estate transfer tax	335.6	338.0	349.0
Local Government Assistance Tax Fund			
Sales and use tax	2,106.5	2,244.5	2,364.0
Total Tax Receipts - Debt Service Funds	6,804.3	8,039.2	8,657.3
CAPITAL PROJECTS FUNDS			
Dedicated Highway and Bridge Trust Funds	1,578.3	1,639.7	1,693.7
Petroleum business taxes	568.1	565.9	592.2
Motor fuel tax	356.2	403.0	411.0
Motor vehicle fees	469.9	485.8	481.2
Highway use tax	146.8	147.0	151.9
Transmission tax	0.0	0.0	17.8
Auto rental tax	37.2	38.0	39.6
Environmental Protection Fund			
Real estate transfer tax	112.0	112.0	112.0
Total Tax Receipts - Capital Projects Funds	1,690.3	1,751.7	1,805.7
Total Tax Receipts - Other Funds	**12,708.1**	**14,428.5**	**15,245.4**

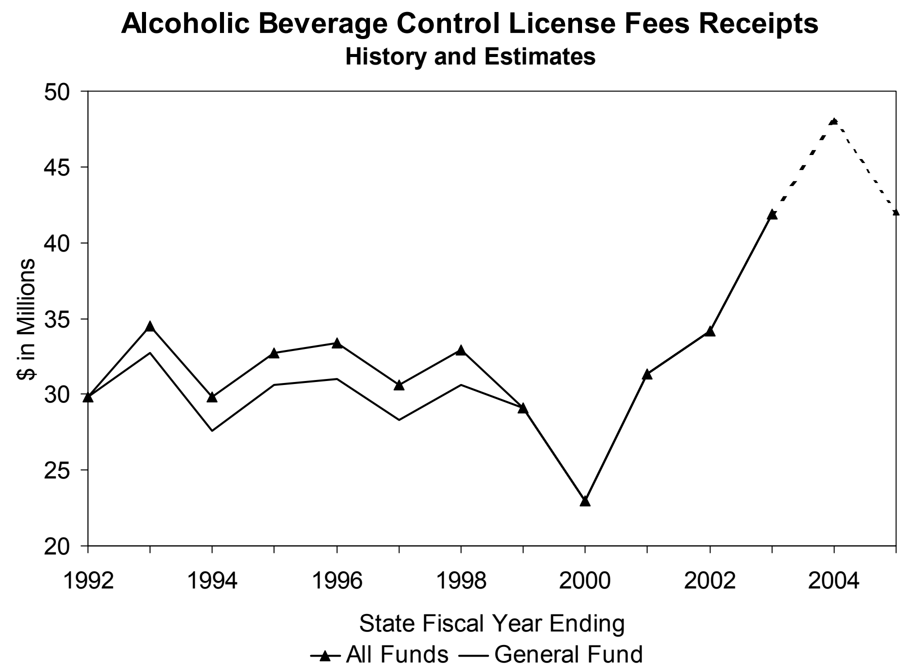
ALCOHOLIC BEVERAGE CONTROL LICENSE FEES

SUMMARY

In 2003-04, All Funds collections from alcoholic beverage control license fees are estimated to be $48 million. This is an increase of $6.1 million, or 14.6 percent, from the prior year.

In 2004-05, All Funds collections alcoholic beverage control license fees are projected to be $42 million. This is a decrease of $6 million, or 12.5 percent, compared with 2003-04.

No new legislation for these fees is proposed with this Budget.



DESCRIPTION

Fee Base and Rate

New York State distillers, brewers, wholesalers, retailers, and others who sell alcoholic beverages are required by law to be licensed by the State Liquor Authority. License fees vary, depending on the type and location of the establishment or premises operated, as well as the class of beverage for which the license is issued.

Administration

Fees are paid directly to the State Liquor Authority on or before the expiration date of the current one-, two-, or three-year license, or with the application for a new license.

NUMBER OF LICENSES BY CATEGORY
(calendar year)

		Bars and Restaurants						
	Liquor Stores	Beer, Wine and Liquor	Beer and Wine	Beer Only	Subtotal	Grocery Stores	Wholesale	Total
1995	2,753	19,831	3,372	1,763	24,966	19,768	1,057	48,544
1996	2,673	19,782	3,497	1,838	25,117	19,743	1,074	48,607
1997	2,621	19,708	3,490	1,843	25,041	19,462	1,125	48,249
1998	2,596	19,853	3,712	1,950	25,515	19,417	1,142	48,670
1999	2,560	20,325	3,640	1,883	25,848	19,202	1,031	48,587
2000	2,491	20,694	3,748	1,877	26,319	19,167	1,201	49,178
2001	2,482	20,545	3,991	1,942	26,478	18,994	1,181	49,135
2002	2,494	21,192	4,256	2,066	27,514	19,051	1,202	50,261

Significant Legislation

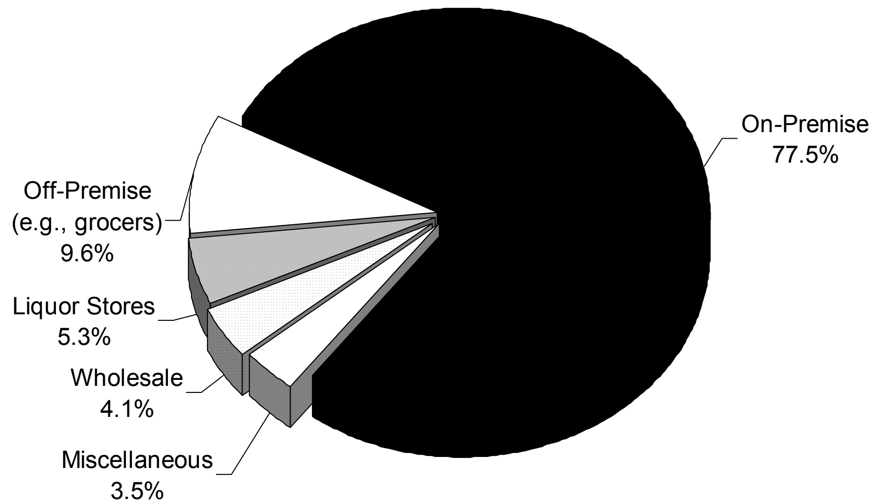
The significant statutory changes for this revenue source since 1994 are summarized below.

Subject	Description	Effective Date
Legislation Enacted in 1997		
License Renewal	The required purchase of a triennial license was changed to allow licensees to continue to purchase a triennial license or optionally purchase an annual or biennial license at a prorated cost.	December 1, 1998
Legislation Enacted in 2002		
Fee Increases	License fees for most licensees increased by 28 percent.	September 1, 2002
Legislation Enacted in 2003		
Open Sundays	Allowed liquor stores to have an option of closing a day other than Sunday.	May 15, 2003

FEE LIABILITY

The most significant source of revenue is the licensing of about 2,500 retail liquor outlets, including package stores engaged in carry-out sales, and about 27,500 bars and restaurants that offer on-premise consumption. The majority of State-licensed bars and restaurants (about 21,200 in 2002) are authorized to sell beer, wine, and liquor. Approximately 4,200 licensees are permitted to sell only beer and wine. The remaining 2,000 licensees in 2002 sold only beer. In addition, there were 19,000 grocery stores licensed to sell beer for off-premise consumption and 1,200 alcoholic beverage wholesalers. Finally, the remaining licenses (not shown above) which account for roughly 6 percent of revenue, are made up of specialty and seasonal licenses (e.g., veterans' clubs, seasonal tour boats, etc.).

Alcoholic Beverage Control License Fees
Share of 2003 Receipts by Licensee Category



PROPOSED LEGISLATION

No new legislation for these fees is proposed with this Budget.

RECEIPTS: ESTIMATES AND PROJECTIONS

All Funds

2003-04 Estimates

Net All Funds collections to date are $38 million, an increase of $9.2 million, or 31.9 percent above the comparable period in the prior fiscal year.

Total net All Funds receipts for 2003-04 are estimated to be $48 million, an increase of $6.1 million, or 14.6 percent above last year.

The increase is attributable to fee increases included in the 2002-03 Enacted Budget, which increased most fees by 28 percent, effective August 1, 2002, as well as a 5 percent growth in new license applications. The increase in new applications represents a rebound from a decline in applications incurred after the World Trade Center attacks. The fee increases are expected to boost collections by more than $10 million in 2003-04.

2004-05 Projections

Total net All Funds receipts are projected to be $42 million, a decrease of $6 million, or 12.5 percent below 2003-04.

The 2002 legislation included a provision to eliminate the two-year installment payment option on one-year licenses. This provision had the effect of boosting 2002-03 and 2003-04 receipts and is expected to depress receipts in 2004-05.

General Fund

Effective April 1, 1998, all proceeds from alcoholic beverage control license fees are deposited in the General Fund.

Other Funds

From 1992-93 through 1997-98, a portion of license fee receipts was deposited in the Alcoholic Beverage Control Enhancement Account. Revenues deposited into the account were used to support efforts to improve compliance with licensing regulations and expedite license processing. Beginning in 1998-99, this special revenue fund was eliminated, and since that time all licensing fees have been deposited in the General Fund.

RECEIPTS BY FUND TYPE

ALCOHOLIC BEVERAGE CONTROL LICENSE FEES RECEIPTS (thousands of dollars)

	Gross General Fund	Refunds	Net General Fund	Special Revenue Funds	Capital Projects Funds	Debt Service Funds	All Funds Net Collections
	Actual						
1995-96	33,956	2,981	30,975	2,400	0	0	33,375
1996-97	31,748	3,417	28,331	2,300	0	0	30,631
1997-98	33,162	2,629	30,533	2,387	0	0	32,920
1998-99	32,282	3,190	29,092	0	0	0	29,092
1999-2000	25,566	2,615	22,951	0	0	0	22,951
2000-01	33,140	1,787	31,353	0	0	0	31,353
2001-02	35,495	1,251	34,244	0	0	0	34,244
2002-03	43,124	1,183	41,941	0	0	0	41,941
	Estimated						
2003-04	49,500	1,500	48,000	0	0	0	48,000
2004-05	43,500	1,500	42,000	0	0	0	42,000

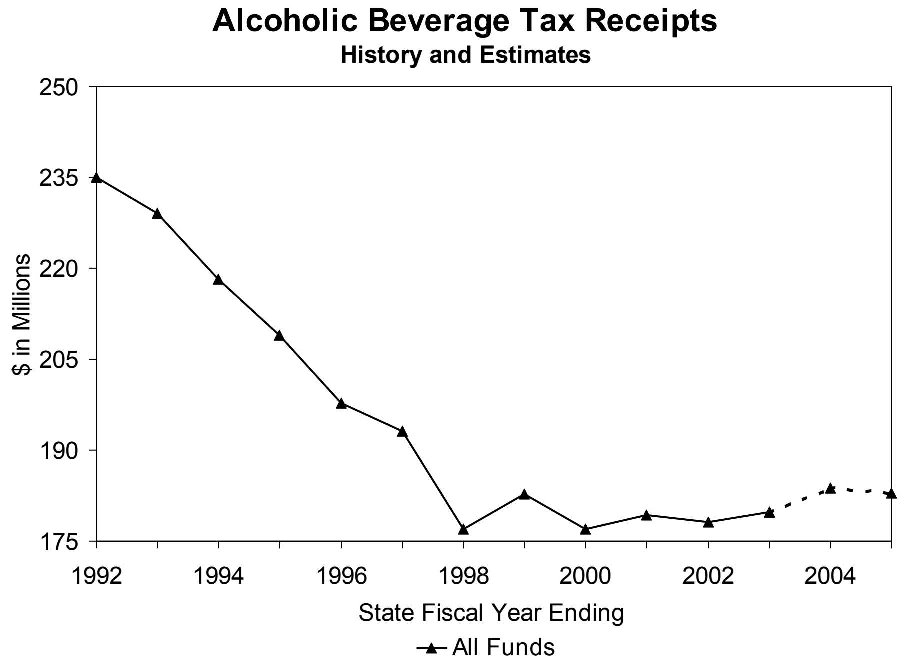
ALCOHOLIC BEVERAGE TAXES

SUMMARY

In 2003-04, All Funds collections from alcoholic beverage taxes are estimated to be $183.7 million. This is an increase of $3.9 million, or 2.2 percent from the prior year.

In 2004-05, All Funds collections from alcoholic beverage taxes are projected to be $182.9 million. This is a decrease of $0.8 million, or 0.4 percent, compared with 2003-04.

Legislation proposed with this Budget would allow for the direct shipment of wine to individual consumers in New York State, effective June 1, 2004.



DESCRIPTION

Tax Base and Rate

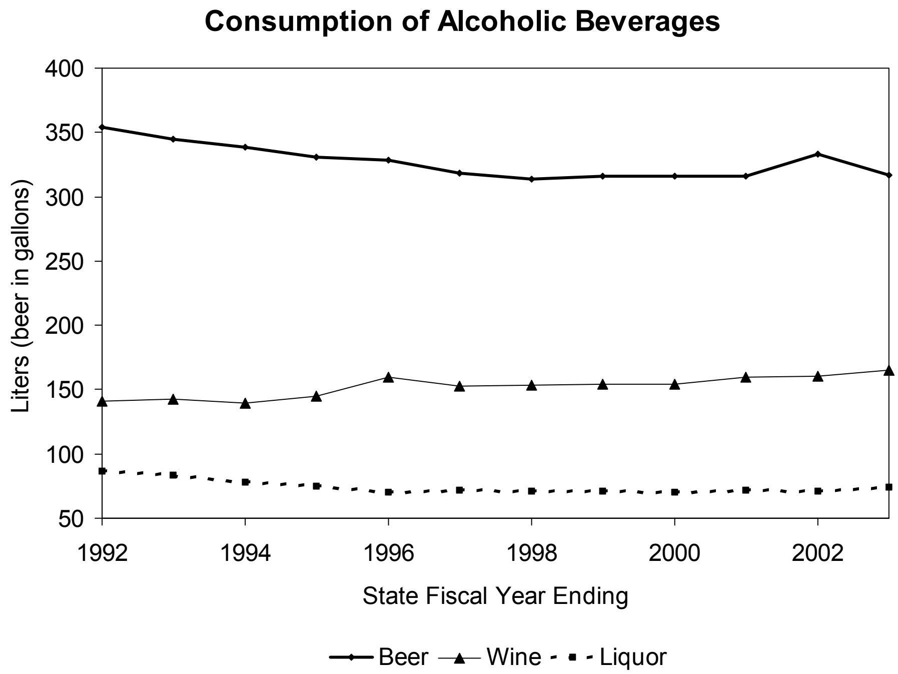
New York State imposes excise taxes at various rates on liquor, beer, wine and specialty beverages.

State tax rates for 2002-03 are as follows (dollars per unit of measure):

Liquor over 24 percent alcohol	1.70	per liter
All other liquor with more than 2 percent alcohol	0.67	per liter
Liquor with not more than 2 percent alcohol	0.01	per liter
Natural sparkling wine	0.05	per liter
Artificially carbonated sparkling wine	0.05	per liter
Still wine	0.05	per liter
Beer with 0.5 percent or more alcohol	0.11	per gallon
Cider with more than 3.2 percent alcohol	0.01	per liter

Administration

The tax is remitted by licensed distributors and noncommercial importers of such beverages in the month following the month of delivery.



Significant Legislation

The significant statutory changes to this tax source since 1994 are summarized below.

Subject	Description	Effective Date
Legislation Enacted in 1995		
Beer Tax Cut	Reduced the State excise tax rate on beer with at least 0.5 percent alcohol from 21 cents to 16 cents per gallon.	January 1, 1996
Legislation Enacted in 1998		
Beer Tax Cut	Reduced the State excise tax rate on beer with at least 0.5 percent alcohol from 16 cents to 13.5 cents per gallon.	January 1, 1999
Legislation Enacted in 1999		
Beer Tax Cut	Reduced the State excise tax rate on beer with at least 0.5 percent alcohol from 13.5 cents to 12.5 cents per gallon.	April 1, 2001
Exemption	Increased the small brewers tax exemption from the first 100,000 barrels of domestically brewed beer to 200,000 barrels.	April 1, 2001
Legislation Enacted in 2000		
Exemption	Accelerated the small brewers exemption increase by moving the effective date from April 1, 2001, to January 1, 2000.	January 1, 2000
Beer Tax Cut	Reduced the State excise tax rate on beer with at least 0.5 percent alcohol from 12.5 cents to 11 cents per gallon.	September 1, 2003

ALCOHOLIC BEVERAGE TAX ENFORCEMENT PROVISIONS

Violations	Volume	Penalties
Import liquor without registration		Class A misdemeanor
Produce, distill, manufacture, compound, mix or ferment liquors without registration or tax payments		Class A misdemeanor
Cause liquor covered by a warehouse receipt to be removed from a warehouse		Class A misdemeanor
Three or more above violations in a five-year period		Class E felony
Import liquor without registration	More than 360 liters within one year	Class E felony
Produce, distill, manufacture, compound, mix or ferment liquors without registration or tax payments	More than 360 liters within one year	Class E felony
Cause liquor covered by a warehouse receipt to be removed from a warehouse	More than 360 liters within one year	Class E felony
Custody, possession or control of liquor without registration or tax payments		Class B misdemeanor
Custody, possession or control of liquor without registration or tax payments	Exceeds 360 liters	Class E felony
Import liquor without registration	More than 90 liters	Seize transportation vehicles and liquor.
Distribute or hold liquor for sale without paying alcoholic beverage taxes	More than 90 liters	Seize transportation vehicles and liquor.
A distributor fails to pay the tax		10 percent of the tax amount due, plus 1 percent each month after the expiration. The penalty shall not be less than $100 but shall not exceed 30 percent in aggregate.
Any other person fails to pay the tax		50 percent of the tax amount due, plus 1 percent each month after the expiration. The penalty shall not be less than $100.

TAX LIABILITY

Overall, per capita consumption of taxed beverages and receipts have remained fairly constant in recent years with declines in one beverage class being offset with increases in others, due to shifts in consumer preferences. For example, wine and liquor consumption have recently increased relative to beer consumption. In addition, the movement of alcoholic beverage demand towards less expensive beverages with lower alcohol content is attributed, in part, to the impact of rising relative prices on beverages with higher alcohol content.

The State continues to suffer tax evasion due to the bootlegging of alcoholic beverages from other states. Enforcement legislation enacted in 1993 added registration, invoice and manifest requirements, as well as seizure and forfeiture provisions. Additionally, the legislation provided higher fines for the bootlegging of varying volumes of liquor. These alcoholic beverage enforcement provisions have provided some protection to the State's liquor industry and the tax base, thereby moderating year-over-year declines in State alcoholic beverage tax receipts. Legislation enacted in 2002 extended these provisions to October 31, 2007.

PROPOSED LEGISLATION

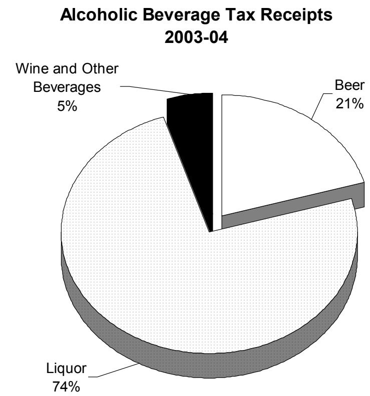
Legislation proposed with this Budget would allow for the direct shipment of wine to individual consumers in New York State, effective June 1, 2004.

RECEIPTS: ESTIMATES AND PROJECTIONS

All Funds

2003-04 Estimates

Net All Funds collections to date are $145.7 million, an increase of $6.3 million, or 4.5 percent above the comparable period in the prior fiscal year.



Total net All Funds receipts for 2003-04 are estimated to be $183.7 million, an increase of $3.9, or 2.2 percent above last year.

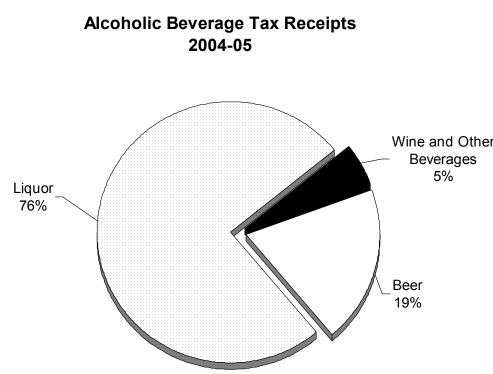
The bulk of estimated receipts, $136.4 million, are derived from the tax on liquor. The 2002 extension of enforcement provisions will protect $3 million in liquor tax receipts in 2003-04 and in subsequent years. The September 1, 2003, excise tax reduction on beer is expected to reduce beer tax collections by $2.4 million. In 2003-04, growth in wine and liquor volume is expected to exceed average growth during the previous three years. This excess growth, which accounts for approximately $0.7 million in 2003-04 receipts, may be attributable to 2003 legislation that allowed liquor stores to open on Sunday.

COMPONENTS OF ALCOHOLIC BEVERAGE TAX RECEIPTS
(millions of dollars)

	1998-99	1999-2000	2000-01	2001-02	2002-03	2003-04	2004-05
	Actual					--Estimated--	--Projected--
Beer	47.8	42.7	42.8	41.8	38.9	38.0	35.6
Liquor	125.7	125.2	128.0	127.9	132.9	136.4	137.9
Wine and Other	8.5	8.3	8.5	8.5	8.7	9.3	9.4
Subtotal	182.0	176.2	179.3	178.2	180.5	183.7	182.9
Reconciliation	0.8	0.8	0.0	0.0	-0.7	0.0	0.0
Net Total	182.8	177.0	179.3	178.2	179.8	183.7	182.9

2004-05 Projections

Total net All Funds receipts are projected to be $182.9 million, a decrease of $0.8 million, or 0.4 percent below 2003-04.



Based on recent trends, the consumption of liquor and wine is expected to grow modestly, while beer consumption is expected to be flat in 2004-05. The September 1, 2003, excise tax reduction on beer is expected to reduce beer tax collections by $4.9 million.

The proposal to allow direct wine shipments noted above would generate minimal revenue in 2004-05.

Of the total projected alcoholic beverage tax receipts, $137.9 million is derived from liquor, $35.6 million from beer, and $9.4 million from wine and other specialty beverages.

General Fund

All receipts from the alcoholic beverage tax are deposited in the General Fund.

RECEIPTS BY FUND TYPE

ALCOHOLIC BEVERAGE TAX RECEIPTS
(thousands of dollars)

	Gross General Fund	Refunds	Net General Fund	Special Revenue Funds	Capital Projects Funds	Debt Service Funds	All Funds Net Collections
				Actual			
1995-96	198,280	492	197,788	0	0	0	197,788
1996-97	192,960	(123)	193,083	0	0	0	193,083
1997-98	177,124	115	177,009	0	0	0	177,009
1998-99	183,087	316	182,771	0	0	0	182,771
1999-2000	177,093	55	177,038	0	0	0	177,038
2000-01	179,407	67	179,340	0	0	0	179,340
2001-02	178,146	1	178,146	0	0	0	178,146
2002-03	180,686	931	179,755	0	0	0	179,755
				Estimated			
2003-04	183,800	100	183,700	0	0	0	183,700
2004-05	183,000	100	182,900	0	0	0	182,900

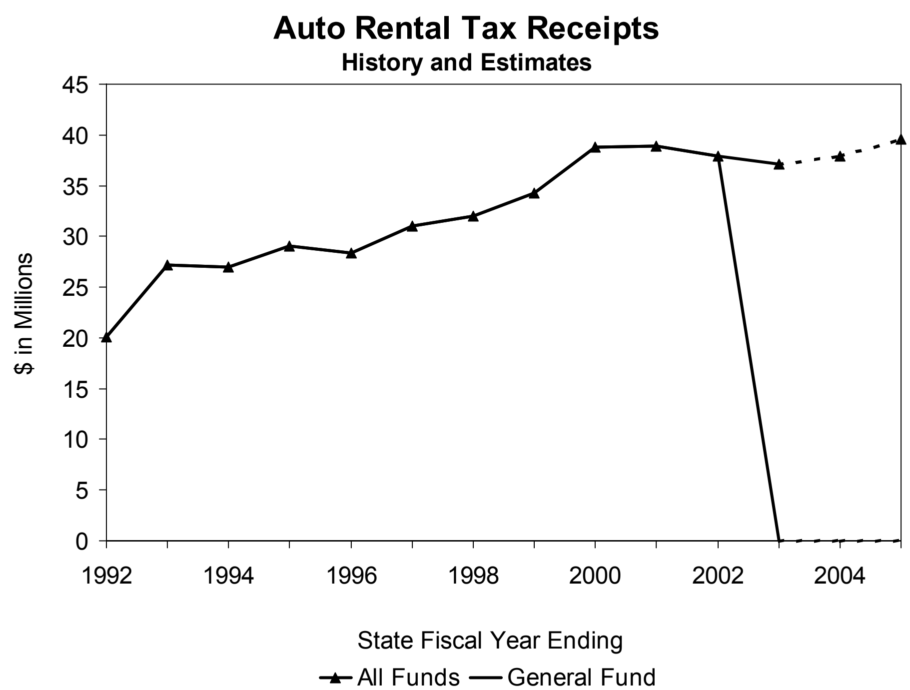
AUTO RENTAL TAXES

SUMMARY

In 2003-04, All Funds collections from auto rental taxes are estimated to be $38 million. This is an increase of $0.8 million, or 2.2 percent, from the prior year.

In 2004-05, All Funds collections from auto rental taxes are projected to be $39.6 million. This is an increase of $1.6 million, or 4.2 percent, compared with 2003-04.

No new legislation for these taxes is proposed with this Budget.



DESCRIPTION

Tax Base and Rate

The auto rental tax applies to a vehicle rented by a resident or a nonresident, regardless of where the vehicle is registered. The tax does not apply to a car lease covering a period of one year or more.

Since June 1, 1990, the State has imposed a 5 percent tax on charges for the rental or use in New York State of a passenger car with a gross vehicle weight of 9,000 pounds or less.

Administration

The auto rental tax is remitted quarterly by the vendor on their sales tax return to the Department of Taxation and Finance.

TAX LIABILITY

Receipts from the auto rental tax are influenced by the overall health of the economy, particularly consumer and business spending on travel. Unusual events that affect travel, such as the WTC attacks, can influence receipts. Due to accounting differences between the Department of Taxation and Finance and the Office of the State Comptroller, the table at the end of this story overstates 2001-02 revenue and understates 2002-03 revenues.

RECEIPTS: ESTIMATES AND PROJECTIONS

All Funds

2003-04 Estimates

Net All Funds collections to date are $32.5 million, an increase of $0.8 million, or 2.5 percent above the comparable period in the prior fiscal year.

Total net All Funds receipts for 2003-04 are estimated to be $38 million, an increase of $0.8 million, or 2.2 percent above last year. The small increase reflects the slow economic recovery from the WTC attacks.

2004-05 Projections

Projected auto rental tax All Funds receipts in 2004-05 are projected to be $39.6 million, an increase of $1.6 million, or 4.2 percent above 2003-04.

General Fund

Since April 1, 2002, no auto rental tax receipts are deposited in the General Fund.

Other Funds

Legislation enacted in 2002 dedicated all receipts from the auto rental tax to the Dedicated Highway and Bridge Trust Fund, effective April 1, 2002.

RECEIPTS BY FUND TYPE

AUTO RENTAL TAX RECEIPTS
(thousands of dollars)

	Gross General Fund	Refunds	Net General Fund	Special Revenue Funds	Gross Capital Projects Funds	Refunds	Net Capital Projects Funds[1]	Debt Service Funds	All Funds Net Collections
	Actual								
1995-96	28,344	0	28,344	0	0	0	0	0	28,344
1996-97	31,056	0	31,056	0	0	0	0	0	31,056
1997-98	32,039	0	32,039	0	0	0	0	0	32,039
1998-99	34,241	0	34,241	0	0	0	0	0	34,241
1999-2000	38,843	0	38,843	0	0	0	0	0	38,843
2000-01	38,916	0	38,916	0	0	0	0	0	38,916
2001-02	37,914	0	37,914	0	0	0	0	0	37,914
2002-03	0	0	0	0	37,191	0	37,191	0	37,191
	Estimated								
2003-04	0	0	0	0	38,000	0	38,000	0	38,000
2004-05	0	0	0	0	39,584	0	39,584	0	39,584

[1] Dedicated Highway and Bridge Trust Fund.

BANK TAX

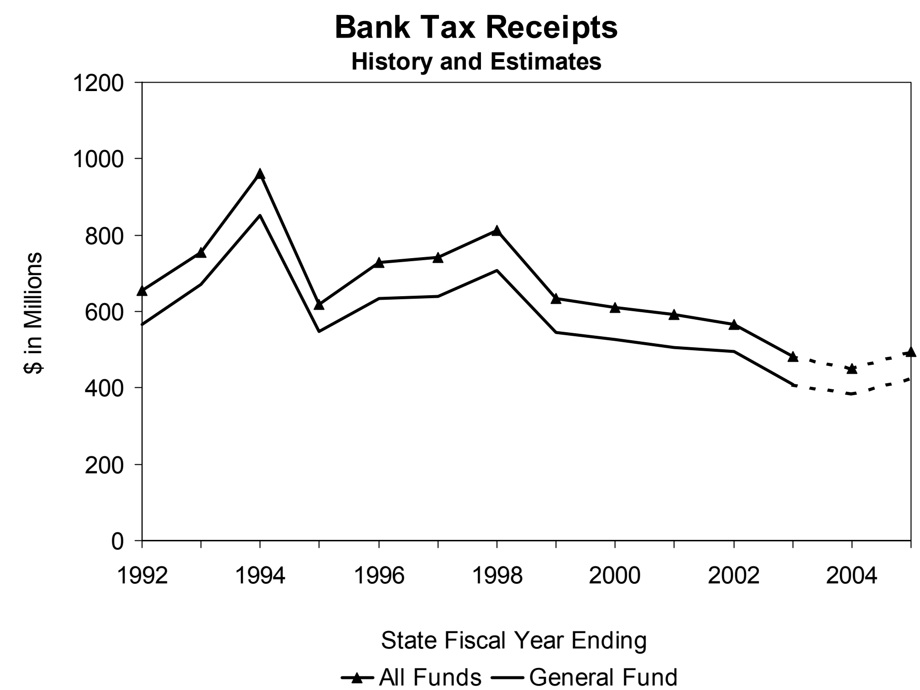
SUMMARY

In 2003-04, All Funds collections from the bank tax are estimated to be $451 million. This is a decrease of $30 million, or 6.2 percent, compared with 2002-03. Collections have been affected by depressed banking sector profitability in recent years that tends to have a lagged impact on current year receipts.

In 2004-05, All Funds collections from the bank tax are projected to be $496 million. This is an increase of $45 million, or 9.8 percent, compared with 2003-04, resulting mainly from expected continued improvement in bank profits.

Legislation proposed with this Budget would:

- extend the bank tax for one year and the Gramm-Leach-Bliley Act transitional provisions for two years; and
- extend the Metropolitan Transportation Authority (MTA) surcharge for four years, until 2009.



DESCRIPTION

Tax Base and Rate

The bank tax is levied by Article 32 of the Tax Law on banking corporations conducting business in New York State. The Article 32 bank tax requires a taxpayer to compute tax liability under four alternative bases and pay under the base that results in the largest tax. The four bases are:

1. An allocated entire net income (ENI) base, which begins with Federal taxable income before net operating loss deductions and special deductions. A rate of 7.5 percent is applied to this base after the exclusion, deduction, or addition of certain items and the base is allocated to New York. Tax credits will further reduce tax otherwise due.

2. An alternative minimum tax (AMT) base, which equals entire net income adjusted to reflect certain Federal tax preference items and adjustments and State-specific net operating loss (NOL) modifications, at a current rate of 3 percent.
3. An assets base at the rate of 1/10, 1/25, or 1/50 of a mill of allocated taxable assets, depending on the size of the bank's assets.
4. A fixed dollar minimum of $250.

The primary source of data on bank tax liability is the Bank Tax Study File, which is compiled by the Department of Taxation and Finance's Office of Tax Policy Analysis (OTPA). The study file includes tax data on all banks filing under Article 32. Banks are classified as commercial banks, savings banks, savings and loan associations, foreign banks and alien banks. Foreign banks are those formed under the laws of another state, whereas alien banks consist of banks formed under the laws of another country. The annual study of bank tax returns indicates that 826 taxpayers filed tax returns as banking corporations in 2000, an 11 percent decrease from the prior year.

Additionally, banks doing business in the Metropolitan Commuter Transportation District (MCTD) are subject to a 17 percent surcharge on the portion of the total tax liability allocated in the MCTD. The collections from the surcharge are deposited into the Mass Transportation Operating Assistance Fund (MTOAF).

Tax Expenditures

Tax expenditures are defined as features of the tax law that reduce the amount of a taxpayer's liability to the State. These provisions include various exclusions, exemptions, tax credits, and other statutory devices designed to reduce State tax liability. The primary objective of these measures is to provide economic incentives to stimulate the New York economy and specifically to strengthen the banking industry in New York. The major tax expenditure items for the bank tax include: the deduction of 60 percent of dividends, gains, and losses from subsidiary capital, the deduction of 22.5 percent of interest income from government obligations, and the international banking facility formula allocation election.

Significant Legislation

The significant statutory changes since 1994 are summarized below.

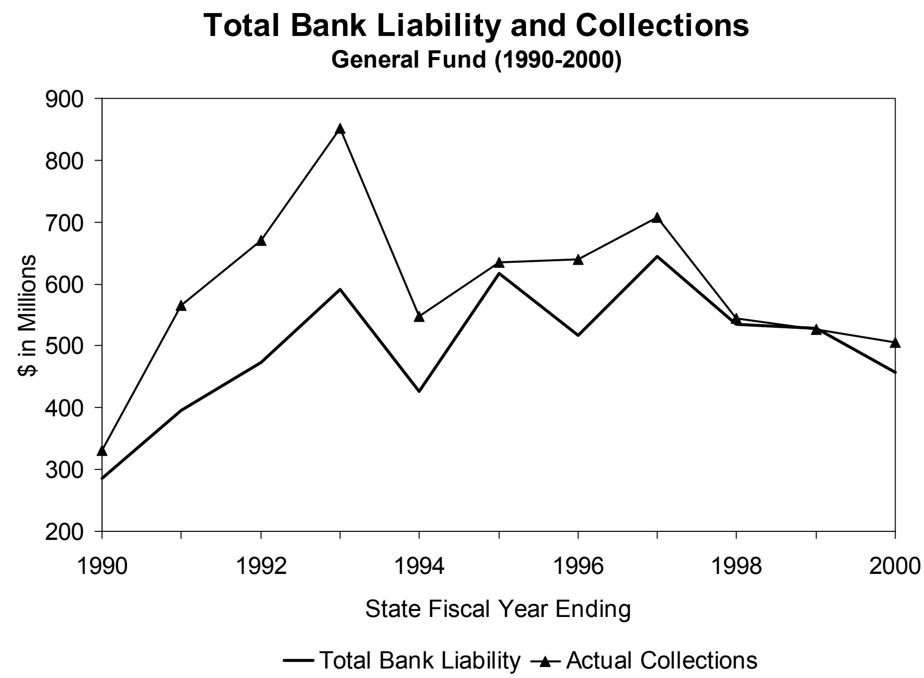
Subject	Description	Effective Date
Legislation Enacted in 1994		
Subsidiary Capital	Specified subsidiary capital taxation rules to allow deduction of 60 percent of the amount by which gains exceed losses from such capital, to the extent such gains and losses were taken into account in determining taxable income.	January 1, 1994
Legislation Enacted in 1997		
Credit for Employing Individuals with Disabilities	Allowed employers who employ individuals with disabilities to claim a credit for a portion of wages paid to such individuals.	January 1, 1998
Net Operating Loss	Allowed banks to claim a net operating loss deduction (NOLD) for losses incurred on or after January 1, 2001.	January 1, 2001
Legislation Enacted in 1998		
Investment Tax Credit	Allowed bank taxpayers that are brokers/dealers in securities to claim a credit for equipment used in broker/dealer activities and in activities connected with broker/dealer operations.	October 1, 1998
Legislation Enacted in 1999		
Rate Reduction — ENI	Reduced the ENI tax rate from 9 percent to 7.5 percent in phases over three years.	June 30, 2000

Subject	Description	Effective Date
Legislation Enacted in 2000		
Empire Zones (EZ)	Transformed Economic Development Zones (EDZ) to Empire Zones, effectively providing for virtual "tax free" zones for certain businesses. The enhanced benefits include a tax credit for real property taxes, a tax reduction credit, and sales and use tax exemption. The tax reduction credit may be applied against the fixed dollar minimum tax, which may reduce the taxpayer's liability to zero.	January 1, 2001
Legislation Enacted in 2001		
Bank Tax Extension	Provided an extension of the bank tax that had expired for commercial banks. The tax did not apply to tax years beginning on or after January 1, 2001. Sunsets for tax years beginning on or after January 1, 2003.	January 1, 2001
Legislation Enacted in 2002		
Estimated Payment Requirement	Increased the first quarterly payment of estimated tax from 25 percent to 30 percent of the prior year's liability for those corporate taxpayers whose prior year's liability exceeds $100,000.	January 1, 2003
Empire Zones Program	Amended to clarify certain provisions and implement new components for several credit calculations.	Various
Legislation Enacted in 2003		
Bank Tax Extension	Provided an extension of the Bank Tax that had expired for commercial banks. The tax did not apply to tax years beginning on or after January 1, 2003. Sunsets for tax years beginning on or after January 1, 2005.	January 1, 2003
Modification for Decoupling from Federal Bonus Depreciation	Required taxpayers to make modifications to Federal taxable income for property placed in service on or after June 1, 2003, that qualified for the special bonus depreciation allowance allowed by the Federal Job Creation and Worker Assistance Act of 2002 and the Jobs and Growth Tax Relief Reconciliation Act of 2003. The modifications do not apply to qualified resurgence zone property or qualified New York Liberty Zone property.	2003
Intangible Holding Companies	Required taxpayers to modify Federal taxable income relating to certain royalty and interest payments made with respect to the use of intangible property by related members or royalty and interest payments received from related members.	January 1, 2003
Superfund-Brownfield Tax Credits	Created tax incentives for the redevelopment of brownfields through three tax credits: a redevelopment tax credit, a real property tax credit, and an environmental remediation insurance credit. There are three components in the redevelopment tax credit: a site preparation component; a tangible property component; and an onsite groundwater remediation component.	April 1, 2005

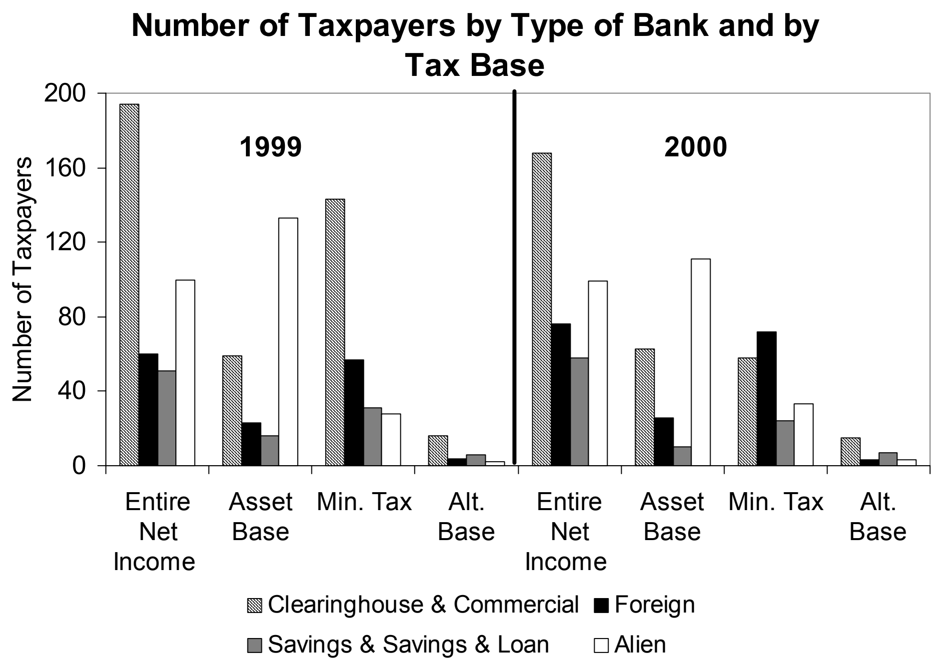
TAX LIABILITY

Tax liability and tax collections, while clearly related, can follow different patterns over time. Tax collections are payments made by taxpayers on returns and extensions for a certain filing period. These include a mandatory first installment payment based on 30 percent of the prior year's liability. Throughout the tax year, banks must also make estimated payments based on their expectation of tax liability at the end of their tax year. Taxpayers may make adjustments to these payments to better reflect their financial status. In contrast, tax liability is determined based on actual performance for a given year. It is generally calculated by tax bases, tax rates, special deductions and additions, losses and tax credits. Taxpayers have generous extensions under current law that allow the filing of returns many months after the end of their tax year.

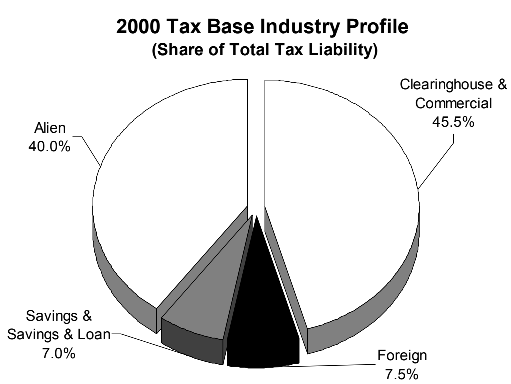
The following graph compares total bank tax liability and collections over a ten-year period. The point illustrated is that, while liability and collections generally followed the same pattern from 1990 to 1997, there is significant volatility in the underlying relationship between each payment and liability. As discussed above, because taxpayers must pay estimated taxes months in advance of knowing actual liability, it is difficult for taxpayers to determine the proper level of payments to make over the course of a year. This is especially true if business or economic conditions change.

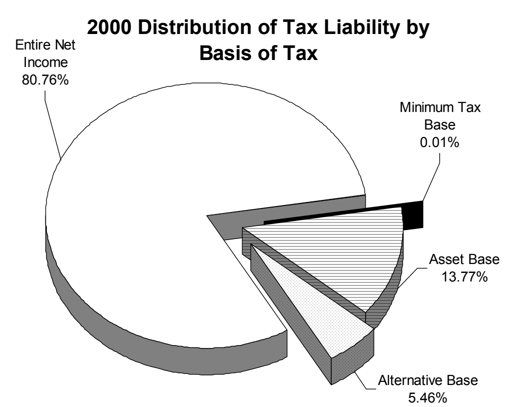


Between 1999 and 2000 (2000 representing the latest year for which tax data are available), total General Fund tax liability decreased by roughly 14 percent, from $529 million, to $457 million. The number of taxpayers decreased by 11 percent, with the majority of the decrease in clearinghouse and commercial banking institutions. This may be partially explained by the large number of consolidations and mergers resulting in subsidiaries filing as a single taxpayer with the parent corporation. The following graph illustrates that, between 1999 and 2000, the number of clearinghouse and commercial taxpayers paying under the fixed dollar minimum tax base decreased by roughly 59 percent. It is likely that these small taxpayers were merged with larger banks or possibly ceased operations in New York State because of the significant changes in the structure of the banking industry.



The following pie charts show that clearinghouse and commercial banking institutions accounted for 45.5 percent of total tax liability in 2000, and alien banking institutions accounted for 40 percent of total liability, while foreign banking institutions and savings and savings and loan institutions together accounted for the remaining 14.5 percent of total liability. Additionally, payments under the ENI base compromised about 80.8 percent of total tax liability.





PROPOSED LEGISLATION

The bank tax for commercial banks is scheduled to expire January 1, 2005. This proposal would extend the bank tax for one year and the Gramm-Leach-Bliley Act provisions for two years to preserve current revenues. Both provisions would expire in 2006. The Executive Budget also proposes to extend the MTA surcharge from tax years ending before December 31, 2005, to December 31, 2009.

RECEIPTS: ESTIMATES AND PROJECTIONS

All Funds

2003-04 Estimates

Net All Funds collections to date are $304 million, a decrease of $44 million, or 13 percent, below the comparable period in the prior fiscal year. Total net All Funds receipts for 2003-04 are estimated to be $451 million, a decrease of $30 million, or 6.2 percent below last year.

The weakness in current year net collections is the result of several factors. The slow growth of the national and State economies has contributed to the poor performance of the banking sector, which is sensitive to overall economic conditions. Additionally, there has been an increase in the bad debt and credit risks carried by banks in both the personal and commercial areas. Although lower interest rates have had a positive effect on the housing and durable goods markets, the effect on commercial bank earnings has worked in the opposite direction. This is primarily due to the reduced spread between the lending and borrowing rates.

Another major factor contributing to the weak growth in banking receipts is the continued restructuring of the banking sector in New York. There have been an increasing number of mergers and acquisitions as well as downsizing of banking facilities. The rapid entry and exit of banking institutions has also added to volatility. To attract customers, banks have been cutting fees, lowering lending rates, and offering other incentives. These activities are expected to drive down earnings.

In addition, net collections have been affected by the recent financial sector accounting scandals. Firms involved in illegal or unethical activities are paying large amounts to settle lawsuits, in addition to legal fees and penalties. The scandals may force regulators to adopt stricter measures to prevent unlawful activities, thereby setting limitations on the creation of new products. These factors have affected bank tax profitability and have had a negative impact on receipts.

The Executive Budget proposal to extend the bank tax for one year and the Gramm-Leach-Bliley provisions for two years will protect current revenues. The Budget proposal to extend the MTA surcharge for four years, until 2009, will maintain the existing annual revenue stream available to support transportation services in the Metropolitan Commuter Transportation District.

2004-05 Projections

Total net All Funds receipts are projected to be $496 million, an increase of $45 million, or 9.8 percent, above 2003-04.

The bank tax gains for State fiscal year 2004-05 are mainly due to the expected improvement in banking industry profitability. The increase is based in part on the underlying relationship between tax liability and expected bank profitability. Overall, bank earnings, which have improved over the course of the 2003-04 State fiscal year, are expected to improve further during 2004-05.

General Fund

Based on collections to date, General Fund net collections for State fiscal year 2003-04 are projected to reach $386 million, a decrease of $23 million, or 5.6 percent from State fiscal year 2002-2003 levels, primarily due to the economic and industry influences already discussed.

Bank tax receipts for State fiscal year 2004-05 are expected to increase by 9.8 percent, primarily driven by improved profitability and a more optimistic economic outlook.

GENERAL FUND RECEIPTS BY TYPE OF BANK
(millions of dollars)

	State Banks, Trust Companies and National Banks	Savings Banks	Savings and Loan Associations	Total
	Actual			
1995-96	612	24	(1)	635
1996-97	637	(3)	5	640
1997-98	700	1	6	707
1998-99	527	12	5	544
1999-2000	516	5	5	526
2000-01	496	5	4	505
2001-02	487	5	5	496
2002-03	398	5	6	409
	Estimated			
2003-04	376	5	5	386
2004-05	412	6	6	424

Other Funds

Under current law, a business tax surcharge is imposed at a rate of 17 percent of the portion of the statewide tax liability allocated to the MCTD. It is the principal revenue source of the Mass Transportation Operating Assistance Fund (MTOAF). MTOAF bank tax receipts are affected by the same factors impacting overall bank tax receipts. Based on collections to date, the bank tax contribution to MTOAF for 2003-04 is projected to reach approximately $66 million. These receipts are expected to increase to $72 million in 2004-05.

RECEIPTS BY FUND TYPE

BANK TAX RECEIPTS
(millions of dollars)

	Gross General Fund	Refunds	Net General Fund	Special Revenue Funds	Refunds	Net Special Revenue Funds[1]	All Funds Net Collections
	Actual						
1995-96	702	68	635	99	5	94	729
1996-97	724	84	640	110	9	101	741
1997-98	766	58	707	114	8	105	812
1998-99	624	80	544	102	11	91	635
1999-2000	598	72	526	94	9	85	611
2000-01	598	92	505	97	11	86	591
2001-02	565	69	496	80	10	70	566
2002-03	525	114	409	84	12	72	481
	Estimated						
2003-04	511	125	386	78	12	66	451
2004-05	524	100	424	82	10	72	496

[1]MCTD 17 percent surcharge deposited in Mass Transportation Operating Assistance Fund.
Note: Components may not add to net collections due to rounding.

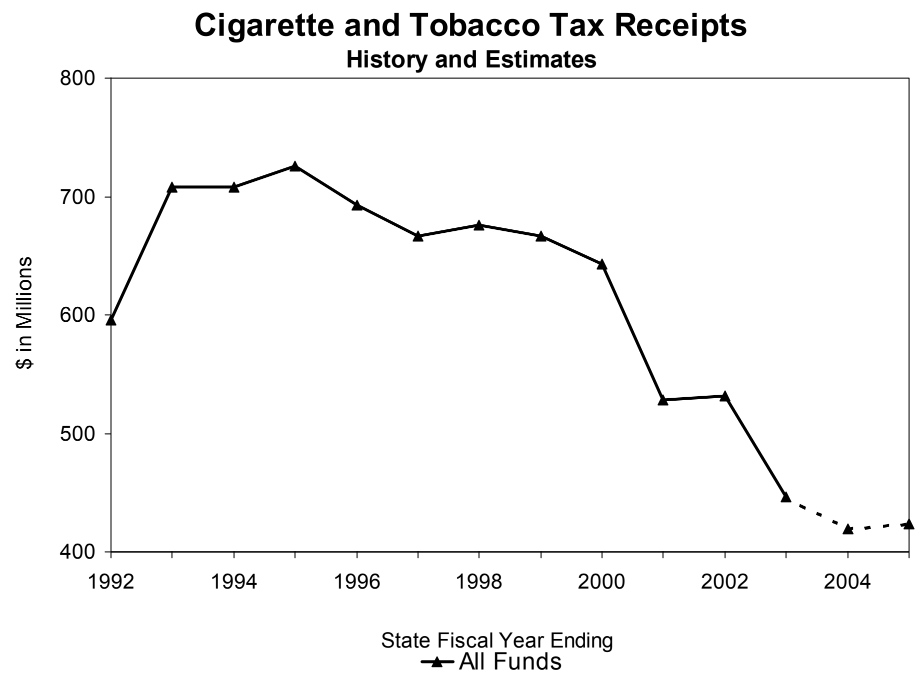
CIGARETTE AND TOBACCO TAXES

SUMMARY

In 2003-04, total collections from cigarette and tobacco taxes are estimated to be $1,013.2 million. This is a decrease of $108.1 million, or 9.6 percent from the prior year.

In 2004-05, total collections from cigarette and tobacco taxes are projected to be $1,021.1 million. This is an increase of $7.9 million, or 0.8 percent, compared with 2003-04.

Legislation proposed with this Budget would postpone implementation of regulations related to taxation of sales on Native American lands and authorizes the State to execute agreements with Native American nations regarding product prices and taxes.



DESCRIPTION

Tax Base and Rate

The New York State cigarette excise tax is imposed by Article 20 of the Tax Law on the sale or use of cigarettes within the State. The current tax rate is $1.50 per package of 20 cigarettes.

The Federal government imposes a cigarette excise tax on manufacturers and first importers of cigarettes. The Federal tax rate was increased from 24 cents to 34 cents per pack on January 1, 2000, and again to 39 cents per pack on January 1, 2002. Effective March 1, 2000, New York raised its tax by 55 cents to $1.11 per pack and effective April 3, 2002, by 39 cents to $1.50 per pack. New York City also levies a separate cigarette excise tax of $1.50 per pack. Historical changes in State, Federal and City tax rates are shown in the following table.

STATE, FEDERAL AND NEW YORK CITY CIGARETTE EXCISE TAX RATES PER PACK OF 20 CIGARETTES (since 1950)

State	Rate (cents)	Federal	Rate (cents)	New York City	Rate (cents)
Before April 1, 1959	2	Before November 1, 1951	7	Before May 1, 1959	1
April 1, 1959	5	November 1, 1951	8	May 1, 1959	2
April 1, 1965	10	January 1, 1983	16	June 1, 1963	4
June 1, 1968	12	January 1, 1991	20	January 1, 1976	8
February 1, 1972	15	January 1, 1993	24	July 2, 2002	150
April 1, 1983	21	January 1, 2000	34		
May 1, 1989	33	January 1, 2002	39		
June 1, 1990	39				
June 1, 1993	56				
March 1, 2000	111				
April 3, 2002	150				

The State also imposes a tax on other tobacco products, such as chewing tobacco, snuff, cigars, pipe tobacco and roll-your-own cigarette tobacco, at a rate of 37 percent of their wholesale price. The Federal government also imposes an excise tax on manufacturers and importers of tobacco products at various rates, depending on the type of product.

Retail establishments that sell cigarettes are required to purchase licenses, and vending machine owners are required to purchase stickers from the Department of Taxation and Finance.

Administration

State registered stamping agents, most of whom are wholesalers, purchase tax stamps from the State and affix the stamps to cigarette packages to be sold by New York State registered retailers. Purchasers of non-State stamped cigarettes, such as cigarettes sold out-of-State or on Native American lands, must remit the cigarette excise tax directly to the Department of Taxation and Finance when they purchase more than two cartons.

Tax Evasion

Cigarette tax evasion is a serious problem in New York and throughout the Northeast. Widespread evasion not only reduces State and local revenues, but also reduces the income of legitimate wholesalers and retailers. The Department of Taxation and Finance has acted vigorously to curb cigarette bootlegging through investigatory and enforcement efforts. Legislation, enacted in 1996, substantially increased penalties for retailers and wholesalers who sell unstamped or illegally stamped packages of cigarettes. Further legislation enacted in 2002 increased the number of enforcement agents.

The positive effects of the 1996 enforcement legislation were realized later that year, with an increase in the number of new retailer license applications. This increase, as well as an enhanced State enforcement presence, may have led to less severe declines in taxable cigarette consumption than would otherwise have occured.

CIGARETTE TAX RATES IN NEW YORK AND BORDERING STATES*
(cents per pack)

	2003	2002	2001	2000	1999	1998
Connecticut	151	111	50	50	50	50
Massachusetts	151	76	76	76	76	76
New Jersey	205	150	80	80	80	80
New York	150	150	111	111	56	56
Pennsylvania	100	31	31	31	31	31
Vermont	119	93	44	44	44	44
NYS and NYC	300	300	119	119	64	64

* Highest rate in effect during calendar year.

In 2000, the Governor signed comprehensive legislation targeted at combating cigarette bootlegging and reducing youth and adult smoking by banning Internet sales and the delivery by common carrier of cigarettes to individual consumers in New York. This law does not apply to the U.S. Postal Service. After a lawsuit by Brown and Williamson Tobacco, this legislation was ruled unconstitutional by the U.S. District Court of the Southern District of New York and enjoined from going into effect. The State's appeal was heard in June 2002 and the law became effective in March 2003 when the U.S. Circuit Court of Appeals ruled for the State. Appeals in this case have been exhausted. Currently, the statute is the subject of other litigation. In April 2003, trucking associations from New York, New Jersey and Connecticut filed suit to have the statute declared unconstitutional. Currently, the case is pending a decision by the U.S. District Court of the Southern District of New York. Four other cases filed by Native American tribes in New York seek to allow the tribes to ship cigarettes directly to New York consumers via common carriers and are pending decisions by various courts.

Significant Legislation

The significant statutory changes since 1994 are summarized below.

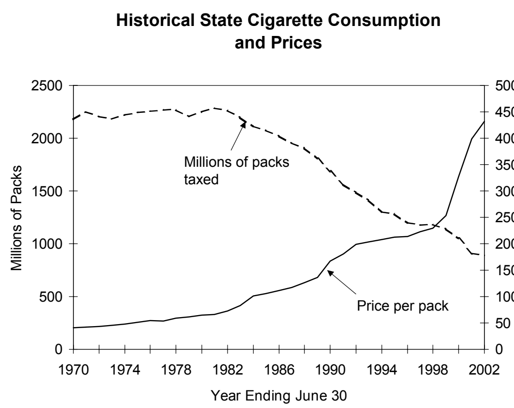
Subject	Description	Effective Date
Legislation Enacted in 1996		
Enforcement Provisions	Increased penalties and fines for selling unstamped cigarettes, violation of retail dealer and vending machine registration provisions, and providing inaccurate registration information.	December 3, 1996
Legislation Enacted in 1999		
Cigarette Tax Increase	Increased the cigarette excise tax from 56 cents to $1.11 per pack, as part of the Health Care Reform Act (HCRA) of 2000.	March 1, 2000
Legislation Enacted in 2000		
Underage Smoking	Increased penalties for illegal sales of tobacco products to minors.	September 1, 2000
Enforcement Provisions	Created civil and criminal penalties for persons who sell and ship cigarettes to persons who are not licensed or registered cigarette dealers or agents.	November 16, 2000
Enforcement Provisions	Created civil and criminal penalties for carriers who transport cigarettes to persons who are not licensed or registered cigarette dealers or agents.	January 1, 2001
Safe Cigarettes	Required the promulgation and imposition of fire-safety standards for cigarettes and rolled tobacco products sold in New York.	July 1, 2004
Legislation Enacted In 2002		
Cigarette Tax Increase	Increased the cigarette excise tax from $1.11 per pack to $1.50 per pack.	April 3, 2002
Tobacco Tax Increase	Increased the other tobacco products tax from 20 percent of the wholesale price to 37 percent.	July 3, 2002
Enforcement Provisions	Increased the number of enforcement agents.	May 29, 2002

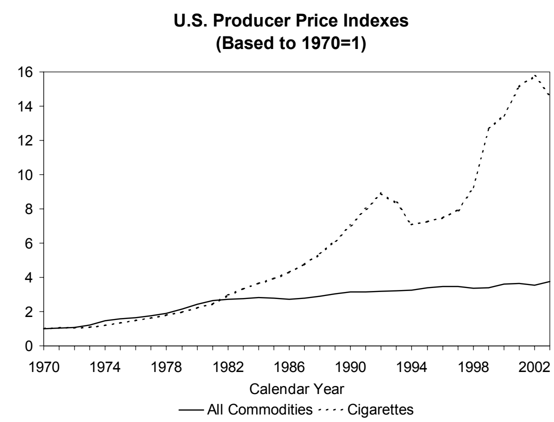
Subject	Description	Effective Date
Legislation Enacted in 2003		
Native American Regulations	Required the Commissioner of Taxation and Finance to promulgate regulations requiring the taxation of cigarettes sold to non-Native Americans.	March 1, 2004

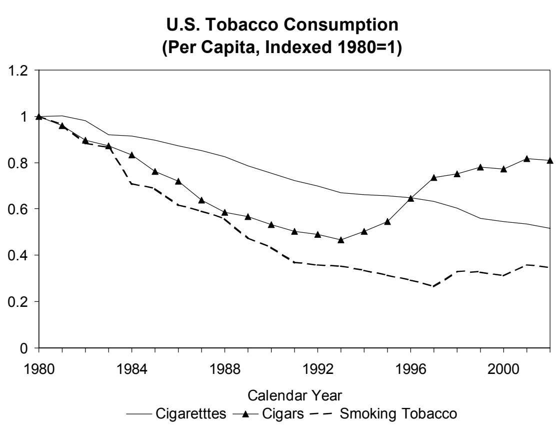
TAX LIABILITY

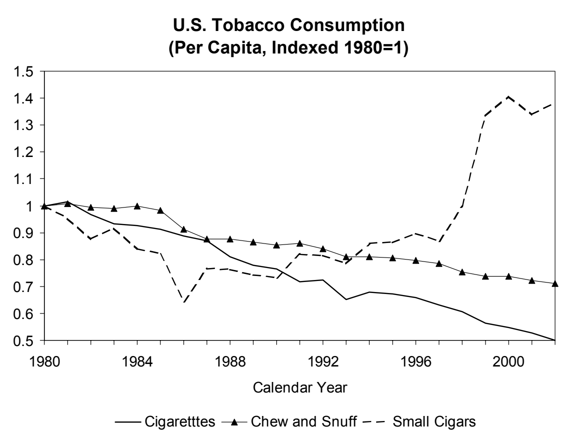
Taxable cigarette consumption is a function of retail cigarette prices and a long-term downward trend in consumption reflecting the negative impact of public awareness of the adverse health effects of smoking, smoking restrictions imposed by governments, anti-smoking education programs, and changes in consumer preferences toward other types of tobacco. Recently, declines in taxable consumption have been exacerbated by evasion.

Taxable cigarette consumption in New York has declined by more than 66 percent since 1970, due to the factors noted in the previous paragraph. The following graphs summarize the most important trends, which are the inverse relationship between cigarette prices and consumption, the large magnitude of wholesale cigarette price increases relative to other goods, and consumer substitution of other tobacco products for cigarettes.









TOBACCO MSA PAYMENTS

Under the Tobacco Master Settlement Agreement (MSA) reached between states and manufacturers in 1998, manufacturers are required to make payments to New York. The amounts of these payments are subject to various adjustments. The volume adjustment is based on national consumption, not consumption in New York.

PROPOSED LEGISLATION

Legislation proposed with this Budget would postpone implementation of regulations related to taxation of sales on Native American lands and authorizes the State to execute agreements with Native American nations regarding product prices and taxes.

RECEIPTS: ESTIMATES AND PROJECTIONS

All Funds

2003-04 Estimates

Total net collections to date are $796.5 million, a decrease of $92.9 million, or 10.4 percent below the comparable period in the prior fiscal year.

Total net collections for 2003-04 (including HCRA) are estimated to be $1,013.2 million, a decrease of $108.1 billion, or 9.6 percent below last year.

The Division of the Budget estimates that producer prices will fall 3.1 percent, and that retail prices will increase 3.1 percent in 2003-04. This increase is due to the New York City tax increase that took effect July 3, 2002. If the one-quarter impact of the City tax increase on 2003-04 retail prices is excluded, retail prices during the remainder of 2003-04 are estimated to decline. Despite this estimated price decline, underlying taxable cigarette consumption is estimated to continue its secular decline during the remaining three quarters of 2003-04. It appears from the historical data that national cigarette price declines do not cause those who have stopped smoking to start again, nor do they affect the price gap that exists between New York City and neighboring states. Hence, New York smokers, particularly those in the City, have continued to find alternatives to purchasing taxable cigarettes. Also, restrictions on cigarette advertising contained in the MSA and a general increase in the awareness of the health consequences of smoking have contributed to the long-term declining trend in cigarette consumption.

2004-05 Projections

Total net collections are projected to be $1,021.1 million, $7.9 million or 0.8 percent above 2003-04.

Prospective agreements between Native American governments and the State based on legislation submitted with this Budget are projected to add $40 million in revenue in 2004-05.

The long-term factors reducing cigarette consumption will continue to exert negative pressure on receipts. Price increases are expected to resume and have a significant effect on underlying taxable cigarette consumption in 2004-05. Wholesale prices are expected to rise 9 percent, and retail prices are expected to rise 4 percent. Since cigarette prices are high in New York relative to the surrounding states, there remains an added incentive for smokers to avoid paying the tax by purchasing retail cigarettes in surrounding states, bootlegged cigarettes, or cigarettes sold through mail order or on the Internet.

Health Care Reform Act (HCRA)

More than 60 percent of the proceeds from the State cigarette tax of $1.50 is deposited in the Tobacco Control and Insurance Initiatives Pool established in the Health Care Reform Act of 2000. Based on the percentage distribution of cigarette tax receipts in effect between April 1, 2003, and March 31, 2005 (see table below), the pool will receive an estimated $593.6 million in 2003-04 and a projected $597.4 million in 2004-05. This fund is maintained outside the State's fund structure and, therefore, is not included in All Funds net collections.

Legislation passed in 2002 established the percentage distribution of cigarette tax revenue shown in the following table.

Cigarette Tax Distribution (percent)
Current Law

April 1, 2002, to April 30, 2002	
General Fund	56.30
HCRA	43.70
May 1, 2002, to March 31, 2003	
General Fund	35.45
HCRA	64.55
Beginning April 1, 2003	
General Fund	38.78
HCRA	61.22

CIGARETTE AND TOBACCO TAX REVENUE
(millions of dollars)

	General Fund				HCRA
Fiscal Year	Cigarette Tax	Tobacco Tax	Other	Total	Cigarette Tax
2000-01	504.4	20.5	3.5	528.4	495.4
2001-02	507.6	21.9	2.2	531.7	481.4
2002-03	404.4	37.6	4.6	446.5	674.6
2003-04*	376.0	40.1	3.3	419.5	593.6
2004-05*	378.4	41.9	3.4	423.8	597.4

Note: Components may not add to total due to rounding.
*Estimated

General Fund

General Fund cigarette and tobacco tax receipts for 2003-04 are estimated at $419.5 million, a decline of $27 million, or 6 percent, from 2002-03. To date, General Fund cigarette and tobacco tax receipts are an estimated $329.5 million, a decline of $28.8 million, or 8 percent below the comparable period in the prior fiscal year.

For 2004-05, General Fund cigarette tax receipts are projected to be $423.8 million. The tax on tobacco products is expected to total $41.9 million, an increase of $1.8 million from 2003-04. This increase is due to continuation of consumption trends, and an expected shift of cigarette smokers to tobacco products, including roll-your-own tobacco, as a result of continued price increases for cigarettes. Sales of retail licenses and vending machine stickers are projected to yield $3.4 million.

RECEIPTS BY FUND TYPE

CIGARETTE AND TOBACCO TAX RECEIPTS
(millions of dollars)

	Gross General Fund	Refunds	Net General Fund	Special Revenue Funds	Capital Projects Funds	Debt Service Funds	All Funds Net Collections
	Actual						
1995-96	701	7	693	0	0	0	693
1996-97	676	9	667	0	0	0	667
1997-98	681	5	676	0	0	0	676
1998-99	672	5	667	0	0	0	667
1999-2000	649	5	643	0	0	0	643
2000-01	533	4	528	0	0	0	528
2001-02	539	7	532	0	0	0	532
2002-03	454	8	446	0	0	0	446
	Estimated						
2003-04*	429	9	420	0	0	0	420
2004-05*	432	8	424	0	0	0	424

* In 2003-04, an estimated $594 million will be deposited in the Tobacco Control and Insurance Initiatives Pool, and, in 2004-05, a projected $597 million will be deposited therein.

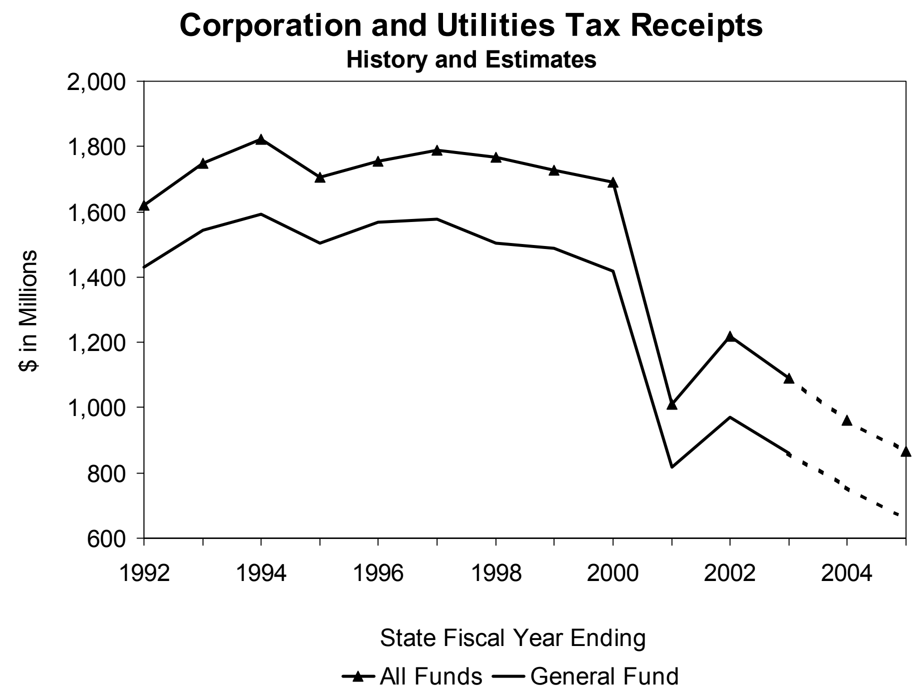
CORPORATION AND UTILITIES TAXES

SUMMARY

In 2003-04, All Funds collections from corporation and utilities taxes are estimated to be $960 million. This is a decrease of $131 million, or 12.0 percent, from the prior year resulting from the phase in of previously enacted tax law changes for utility taxpayers and increased competition and price pressure in the telecommunications industry.

In 2004-05, All Funds collections from corporation and utilities taxes are projected to be $866 million. This is a decrease of $94 million, or 9.8 percent, compared with 2003-04. Collections will continue to be affected primarily by legislation enacted in 2000 to reform the utility tax and the competitive environment facing the telecommunications industry.

Legislation proposed with this Budget would extend the Metropolitan Transportation Authority (MTA) surcharge for four years, until 2009. This would preserve current revenues.



DESCRIPTION

Tax Base and Rate

Article 9 of the Tax Law imposes taxes and fees on a number of specialized industries, including public utilities, newly organized or reorganized corporations, out-of-State corporations doing business in New York State, transportation and transmission companies, and agricultural cooperatives. Article 9 receipts come primarily from the public utility, telecommunications, and transportation industries. Recent statutory and regulatory changes have significantly diminished the role of traditional energy utilities as the primary source of Article 9 receipts. In recent years, the telecommunications industry has become the primary source of these receipts.

Section 180 assesses an organization tax upon newly incorporated or reincorporated domestic (in-State) corporations. The tax is imposed at a rate of 1/20 of 1 percent of the total amount of the par value (the nominal or face value of a security) of the stock that the corporation is authorized to issue; for shares of "no-par" value, the rate is five cents per share. The tax also applies to any subsequent change in the capital structure on stocks (adjustment to the par value, a change in the number of "no-par" value stocks, etc.), or newly authorized stock.

Section 181 imposes a license fee on out-of-State corporations for the privilege of exercising a corporation franchise or conducting business in a corporate or organized capacity in New York State. The fee is assessed at a rate equivalent to the organization tax imposed by section 180. An annual maintenance fee of $300 is also imposed.

Section 183 provides for a franchise tax on transportation and transmission companies, including telecommunications, trucking, railroad, and other transportation companies. The tax is imposed at the highest of the following three alternatives: a rate of 1.5 mills on each dollar of the net value of capital stock allocated to New York State; a tax rate of 3/8 of a mill per dollar of par value for each 1 percent of dividends paid on capital stock if dividends amount to 6 percent or more; or a minimum tax of $75.

Section 184 stipulates an additional franchise tax on the transportation and telecommunication corporations in the State. The tax rate on telephone companies subject to this section is 0.375 percent of gross earnings, as of July 1, 2000. All toll revenues from international, interstate, and inter-Local Access Transport Areas (LATAs) services and 30 percent of intra-LATA toll revenues are excluded from the tax. Railroad and trucking companies that elect to remain subject to Article 9 taxes pay the tax at a rate of 0.375 percent of gross earning, including an allocated portion of receipts from interstate transportation-related transactions.

Section 185 imposes a franchise tax on agricultural cooperatives at the rate of 1 mill per dollar of the net value of the corporation's issued capital stock allocated to New York State.

Legislation enacted with the 2000-01 Budget repealed section 186 retroactive to January 1, 2000. This section had imposed a franchise tax on public utilities, including waterworks, gas, electric, steam heating, lighting and power companies. These companies are now taxed under Article 9-A of the Tax Law (corporate franchise tax).

Section 186-a imposes a tax on the furnishing of utility services (including both energy and lighting public utilities). This includes the commodity tax imposed on the gross operating income of utilities, corporations, and other entities not subject to the supervision of the Department of Public Service. It also includes the transmission and distribution tax imposed on the gross income of utilities and other entities that sell or furnish fuel, such as gas or electricity, through pipes or mains under the supervision of the Department of Public Service. Legislation enacted in 2000 established a separate tax rate on commodity sales and on the sale of transmission/distribution services used to transport and deliver utility services to homes and businesses. The commodity portion of the section 186-a tax will be eliminated January 1, 2005. The tax rate schedule for the commodity and transmission/distribution portions of the current tax is reported in the table below.

TAX RATES CONTAINED IN SECTION 186-A

Effective Date	Type	Rate (percentage)
Prior to January 1, 2000	Commodity	3.25
	Transmission/Distribution	3.25
January 1, 2000	Commodity	2.10
	Transmission/Distribution	2.50
January 1, 2001	Commodity	2.00
	Transmission/Distribution	2.45
January 1, 2002	Commodity	1.90
	Transmission/Distribution	2.40
January 1, 2003	Commodity	0.85
	Transmission/Distribution	2.25
January 1, 2004	Commodity	0.40
	Transmission/Distribution	2.125
January 1, 2005	Commodity	0.00
	Transmission/Distribution	2.00

The portion of the section 186-a tax imposed on the transmission/distribution of electric and gas utility services for nonresidential customers will be eliminated through a phased-in exclusion of gross receipts according to the following schedule. When fully phased in on January 1, 2005, only the residential portion of transmission/distribution services will remain taxable under section 186-a, at a rate of 2.0 percent.

PHASE-IN SCHEDULE FOR EXCLUSION OF T&D NONRESIDENTIAL CUSTOMERS

Effective Date	Rate (percentage)
Calendar Year 2000	0
Calendar Year 2001	0
Calendar Year 2002	25
Calendar Year 2003	50
Calendar Year 2004	75
Calendar Year 2005	100

Section 186-e imposes a tax on the gross receipts generated from telecommunications services. The tax rate was reduced to 2.5 percent on January 1, 2000.

Section 189, effective August 1, 1991, imposes a tax on the importation of natural gas for consumption. The amount of tax is determined by multiplying the number of thousand cubic feet of gas services delivered during the taxable period, the national average wellhead annual gas price published by the United State Department of Energy and the tax rate described in the table below. Recent legislative acts phase down the rate over a five-year period and eliminate the tax effective January 1, 2005. Gas services sold to a co-generation facility and gas services used to generate electricity for sale are exempt from the tax.

On May 1, 2001, the New York State Court of Appeals ruled that section 189 violated the Commerce Clause insofar as it failed to avoid theoretical double taxation by failing to provide a valid credit against this section for certain taxes that may have been paid to other states. In October 2001, legislation was enacted that provides a credit for taxes paid to another state, thus eliminating the double taxation issue and the Commerce Clause violation. The phase out of the tax will continue, as scheduled.

TAX RATES CONTAINED IN SECTION 189

Effective Date	Rate (percentage)
Prior to January 1, 2000	4.25
January 1, 2000	2.10
January 1, 2001	2.00
January 1, 2002	1.90
January 1, 2003	0.85
January 1, 2004	0.40
January 1, 2005	0.00

In addition, Article 9 taxpayers that conduct business in the Metropolitan Commuter Transportation District (MCTD) are subject to a 17 percent surcharge on their liability attributable to the MCTD.

Administration

Taxpayers subject to sections 184, 186, 186-a and 186-e make tax payments on an estimated basis in March, June, September and December. A final payment is made in March. These payment schedules are comparable to those required for corporations taxable under other articles of the Tax Law. Legislation enacted in 2002 requires companies to pay 30 percent as a first installment in March, rather than 25 percent. For taxable years beginning in 1994, large businesses must pay 100 percent of their tax liability by the twelfth month of their fiscal year.

Special Revenue Funds (SRFs) are dedicated funds used to support activities that are outside the scope of the General Fund. For Article 9, there are three such revenue streams.

Section 205 of the Tax Law requires that portions of the taxes imposed under sections 183 and 184 to be deposited in the Metropolitan Mass Transportation Operating Assistance Fund (MTOAF). Legislation enacted in 2003 allocated the remaining 20 percent of section 183 and 184 collections to the Dedicated Highway and Bridge Trust Fund (DHBTF), beginning on April 1, 2004. The table below reports the statutory allocation of tax receipts by fund.

SECTIONS 183 AND 184 DISTRIBUTION TO FUNDS
SINCE 1982
(percentage)

Effective Date	General Fund	MTOAF	DHBTF
July 1, 1982	60.0	40.0	0.0
April 1, 1996	52.0	48.0	0.0
January 1, 1997	50.5	49.5	0.0
January 1, 1998	46.0	54.0	0.0
January 1, 2000	36.0	64.0	0.0
January 1, 2001	20.0	80.0	0.0
April 1, 2004	0.0	80.0	20.0

As stated earlier, the MCTD business tax surcharge applies to Article 9. Taxpayers that do business within the MCTD (which includes the counties of New York, Bronx, Kings, Queens, Richmond, Dutchess, Nassau, Orange, Putnam, Rockland, Suffolk and Westchester) are subject to a 17 percent surcharge on their liability. These funds are deposited in the MTOAF.

Significant Legislation

The significant statutory changes to this tax source since 1994 are summarized below.

Subject	Description	Effective Date
Legislation Enacted in 1994		
Temporary Business Tax Surcharge	Eliminated the 15 percent surcharge for sections 183, 184, 186, and 186-a over three years.	January 1, 1994
Legislation Enacted in 1995		
Telecommunications Act of 1995	Restructured the transmission portion of section 184 to apply to only local telecommunication services. Also, all toll revenues from interstate, and inter-LATAs services were exempted.	January 1, 1995
	Enacted section 186-e, which imposed a 3.5 percent excise tax on receipts from telecommunications services.	
	Replaced the property factor with a new allocation mechanism. Under the "Goldberg" allocation method, receipts are allocated to New York if the call originates or terminates in this State and is charged to a service address in this State, regardless of where the charges for such services are billed or ultimately paid.	
	Shifted the access deduction from inter-exchange carriers and local carriers who are ultimate sellers to initial sellers.	
Section 184	Exempted 30 percent of intra-LATA toll receipts.	January 1, 1996
Legislation Enacted in 1996		
Trucking and Railroad Companies	Allowed these companies the option of being taxed under the general corporate franchise tax (Article 9-A).	January 1, 1997
	Reduced the tax rate on section 184 for these companies from 0.75 percent to 0.6 percent.	
Legislation Enacted in 1997		
Power for Jobs Program	Created a tax credit against section 186-a to compensate utilities for revenue losses associated with participation in the program. The program makes low-cost power available to businesses, small businesses and not-for-profit corporations for job retention and creation. The credit is allowed to the utility providing low cost power to retail customers selected by the Power Allocation Board.	1997
Alternative Fuels Vehicle Credit	Created a tax credit equaling 50 percent of the incremental costs (capped at $5,000 per vehicle); 60 percent of the cost of clean-fuel components (capped at $5,000 or $10,000 per vehicle depending on weight); and 50 percent of the cost of new clean-fuel refueling property.	January 1, 1998
Rate Reductions	Reduced the section 184 tax rate from 0.75 percent to 0.375 percent.	January 1, 1998
	Reduced section 186-a and section 186-e tax rates from 3.5 percent to 3.25 percent as of October 1, 1998, and to 2.5 percent on January 1, 2000.	
Credit for Employers Who Hire Persons With Disabilities	Created a tax credit equaling 35 percent of the first $6,000 of qualified wages (maximum of $2,100 per employee).	January 1, 1998
Legislation Enacted in 1999		
MTOA Fund	Increased the percent of collections from section 183 and section 184 to be distributed to the MTOA Fund from 54 percent to 64 percent on January 1, 2000, and to 80 percent on January 1, 2001.	January 1, 2000 January 1, 2001
Section 189	Exempted generation plants that import natural gas for the production of electricity.	January 1, 2001
Section 183	Eliminated the excess dividends base for those local telecommunications companies with fewer than one million access lines.	January 1, 2002

Subject	Description	Effective Date
Legislation Enacted in 2000		
Utility Tax Reform	Repealed the section 186 tax. Section 186-a and section 189 tax are phased-out over a five-year period. Elimination of the gross receipts tax for manufacturers and industrial energy customers retroactive to January 1, 2000; elimination of the tax for all other business customers over a five-year period. For residential consumers, the commodity tax is eliminated and the transmission/distribution rate of the 186-a tax is reduced from 2.5 percent to 2.0 percent.	January 1, 2000
Power for Jobs	Provided an additional 300 megawatts of low-cost power to businesses across New York through the Power for Jobs program.	January 1, 2001
Legislation Enacted in 2001		
Section 189	Created a prospective and retroactive credit for taxes paid to other states where natural gas was purchased.	Retroactive to August 1, 1991
Legislation Enacted in 2002		
Power for Jobs	Provided low cost power for economic development through phase five of the Power for Jobs Program and provided an energy service company option for recipients under the program	July 30, 2002
Estimated Payments	Increased the first quarterly payment of estimated tax, for taxpayers paying under sections 182, 182-a, 184, 186-a, and 186-e, from 25 percent to 30 percent of the prior year's liability. Taxpayers whose prior year's liability exceeds $100,000 are affected. Taxpayers whose prior year's liability is between $1,000 and $100,000 will continue to make a first quarterly payment of 25 percent of the prior year's liability. Within Article 9, only taxpayers under sections 182, 182-a, 184, 186-a, and 186-e are affected. Sunsets for tax years beginning on or after January 1, 2006, and expires January 1, 2007.	January 1, 2003
Empire Zones Program	Amended to clarify certain provisions and implement new components for several credit calculations.	Various
Legislation Enacted in 2003		
Superfund-Brownfield Credits	Created tax incentives for the redevelopment of brownfields through three tax credits: a redevelopment tax credit, a real property tax credit, and an environmental remediation insurance credit. There are three components in the redevelopment tax credit: a site preparation component, a tangible property component, and an onsite groundwater remediation component.	April 1, 2005
Sections 183 & 184	Allocated the remaining 20 percent of section 183 and 184 collections to the Dedicated Highway and Bridge Trust Fund (DHBTF).	April 1, 2004

TAX LIABILITY

For State fiscal years 1991-92 through 2002-03, Article 9 receipts growth has been highly variable. To a large extent, this volatility is due to the numerous statutory changes reported in the prior section. Additionally, historical fluctuations in energy prices and telecommunications demand have led to uneven growth over this period. In recent years, the emergence of the evolving wireless telecommunications sector has also contributed to the unstable nature of collections.

All of section 186-e receipts and more than half of section 184 receipts in recent years have come from telecommunications companies. These companies are dealing with intense competition and pricing pressures. Wireless communication services continue to take a larger role in the industry, creating an increased call and message volume. On November 24, 2003, telecommunications companies, by order of the Federal Communications Commission (FCC), implemented wireless phone number portability. Larger telecommunications companies are expected to benefit the most from number portability as a result of their action to secure long-term contracts with customers before the action was implemented. In addition, third generation (3G) services have been brought to the marketplace and are realizing more stable, and even higher, monthly average revenue-per-user numbers. In the outyears, we expect the industry to produce higher revenues as a result of these efforts and their push for making text messaging, picture transfers, web access and video games a “must have” feature.

However, certain actions taken by the U.S. Congress with respect to extending provisions of the Federal Internet Tax Freedom Act, if enacted, could remove a portion of these earnings from the base of taxable telecommunications services. The issue is expected to be addressed during the 2004 session of Congress, after 2003 negotiations failed to reach a compromise on a permanent moratorium on the taxation of Internet services by States and local governments.

The primary factors affecting the estimate of the remainder of Article 9 collections include the quantity consumed of electricity and natural gas, and the associated price of each commodity. Quantity is affected by:

- Expansion and contraction phases of the New York economy;
- Colder than normal weather during wintertime and springtime which increases gas volume;
- Summer heat waves which increase electricity demand; and
- Changes in oil and natural gas prices that affect electricity prices.

The tables below report annual consumption and price data for electricity and natural gas. The information shown for the years 1992 to 2001 is based on published reports of the Public Service Commission. The 2001 report reflects the most recent data available. The quantities in the table report sales to ultimate consumers and include sales for resale.

CALENDAR YEAR HISTORY OF ELECTRICITY AND NATURAL GAS SALES
1992 TO 2001
(quantity in millions)

	Electricity Sales (kilowatt hours)	Percent Change	Gas Sales (M cubic feet)	Percent Change
1992	124,926	(6.9)	497.6	15.7
1993	136,236	9.0	506.0	1.7
1994	133,531	(2.0)	530.0	4.7
1995	134,609	0.8	622.9	17.5
1996	135,256	0.5	603.6	(3.1)
1997	135,605	0.3	638.2	5.7
1998	116,305	(14.2)	482.5	(24.4)
1999	115,059	(1.1)	531.4	10.1
2000	105,637	(8.2)	636.1	19.7
2001	103,390	(2.1)	551.6	(13.3)

CALENDAR YEAR HISTORY OF ELECTRICITY AND NATURAL GAS PRICES
1992 TO 2001

	Electricity Price (kilowatt hours)	Percent Change	Gas Price (M cubic feet)	Percent Change
1992	11.39	3.7	6.51	1.0
1993	12.00	5.4	7.14	9.7
1994	12.23	1.9	7.55	5.7
1995	10.95	(10.5)	7.21	(4.5)
1996	11.09	1.3	8.03	11.4
1997	11.08	(0.0)	7.22	(10.1)
1998	10.50	(5.2)	8.25	14.3
1999	10.26	(2.3)	7.73	(6.3)
2000	11.21	9.3	8.40	8.7
2001	11.22	0.0	9.18	9.3

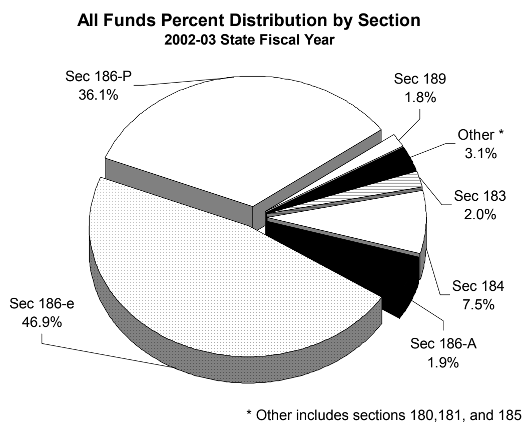
Factors such as the substitution of cheaper fuel types, the severity of the weather, and the availability of oil or natural gas all influence energy consumption and energy prices. The rate of growth of economic activity and inflation impact the price and quantity of utility services consumed. In addition, collections will continue to be affected by scheduled tax rate reductions.

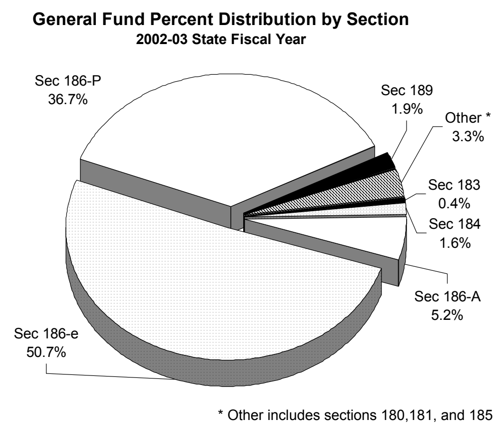
PROPOSED LEGISLATION

Legislation proposed with this Budget would extend the MTA surcharge, until 2009.

RECEIPTS: ESTIMATES AND PROJECTIONS

The pie charts below depict the share of total 2002-03 Article 9 All Funds and General Fund collections accounted for by each section of the Article. For State fiscal years 1991-92 through 2002-03, the General Fund received more than 80 percent of All Funds. The distribution between General Fund and Other Funds will remain relatively constant in 2003-04. In 2004-05, the distribution is expected to shift as a result of a legislation enacted with the 2003-04 Budget to transfer the remaining 20 percent of section 183 and 184 collections to the DHBTF. Small reductions in the estimated fund shares over the forecast can be attributed to statutory changes enacted in recent years.





All Funds

2003-04 Estimates

Net All Funds collections to date are $540.9 million, a decrease of $107 million, or approximately 16.5 percent, below the comparable period in the prior fiscal year.

Total net All Funds receipts for 2003-04 are estimated to be $960 million, a decrease of $131 million, or 12.0 percent below last year. This decrease is due mainly to increased competitive pressure in the wireless industry and the scheduled tax rate reductions that continue to phase in. The Executive Budget proposal to extend the MTA surcharge for four years, until 2009, would maintain the existing annual revenue stream available to support transportation services in the Metropolitan Commuter Transportation District.

In 2003, telecommunications companies' receipts are expected to show a slight decline of 0.1 percent. The consumption of electricity is projected to remain relatively flat, while natural gas consumption is expected to increase by more than 10 percent. Severe weather in the Northeast and other factors caused a drop in supply and an increase in the prices of natural gas. Prices were expected to be moderate this year, but colder than normal weather and winter storms have caused this price increase. However, some industry insiders believe this price increase results from possible price gouging and market manipulation and have called for a congressional investigation into this issue.

In recent months, the economy has shown signs of recovery and the labor market has improved. Business investment rose, profits increased and stock prices all improved in the third quarter of 2003. However, some companies are still struggling to meet earnings expectations without raising prices and, since the jobless rate is still elevated, most employers are omitting or paying out modest year-end bonuses for employees.

2004-05 Projections

Total net All Funds receipts are projected to be $866 million, a decrease of $94 million, or 9.8 percent below 2003-04. All Funds collections are affected by the continuing price competition in the telecommunications industry and the fluctuations in the price and quantity of utility services.

General Fund

General Fund collections for 2003-04 are estimated to be $755 million, a decrease of more than $104 million, or 12 percent from last year. These receipts include an estimated $26 million in audit collections, offset by $35 million in refunds.

For 2004-05, General Fund collections are projected to be $657 million, a decrease of $98 million or, approximately, 13 percent from 2003-04. This includes an estimated $26 million in audit receipts, offset by $35 million in refunds.

CORPORATION AND UTILITIES TAX RECEIPTS BY SECTION
(millions of dollars)

Section of Law	Type of Companies	Collections[1] 2002-03 Actual	2003-04 Estimated	2004-05 Projected
180	Organizations and reorganizations	2.7	3.9	3.9
181	Foreign corporations and maintenance fees	26.0	25.6	25.6
183	Transportation and transmission companies	18.6	23.2	23.5
184	Additional tax on transportation and transmission companies	70.2	66.2	65.5
185	Agricultural cooperatives	0.0	0.0	0.0
186	Water, steam, gas, electric, light and power companies	0.6	0.6	0.6
186a & e	Public utilities/telecommunication	795.9	701.4	624.1
189	Natural gas importers	16.6	5.7	2.8
	Subtotal	930.6	826.6	746.0
		Special Revenue Funds		
	Less Other Funds			
	MTOAF[2]	71.1	71.6	71.2
	DHBTF[3]	0.0	0.0	17.8
	Net General Fund	859.5	755.0	657.0

[1] Receipts from the regional business tax surcharge are excluded.
[2] Per statute, 80 percent of sections 183 and 184 receipts in 2001 and thereafter, are dedicated to the MTOAF.
[3] Per statute, 20 percent of sections 183 and 184 receipts after April 1, 2004 are dedicated to the DHBTF.

Other Funds

As mentioned previously, a portion of Article 9 receipts are deposited into three special revenue funds. The section 183 and 184 collections deposited in the MTOAF will total an estimated $71.6 million for 2003-04 and $71.2 million for 2004-05. The remaining portion of sections 183 and 184, estimated at $17.8 million, is earmarked for the Dedicated Highway and Bridge Trust Fund beginning in State fiscal year 2004-05.

The MCTD business tax surcharge will result in deposits of an estimated $133.4 million for 2003-04 and $120 million for 2004-05 into the MTOAF.

RECEIPTS BY FUND TYPE

CORPORATION AND UTILITIES TAX RECEIPTS
(millions of dollars)

	Gross General Fund	Refunds	Net General Fund	Gross Special Revenue Funds	Refunds	Net Special Revenue Funds[1]	All Funds Net Collections
	Actual						
1995-96	1,581	14	1,567	190	1	189	1,756
1996-97	1,616	39	1,577	214	2	212	1,789
1997-98	1,517	13	1,504	243	2	241	1,745
1998-99	1,509	20	1,489	242	2	240	1,729
1999-2000	1,450	32	1,418	276	2	274	1,692
2000-01	847	30	817	193	1	192	1,009
2001-02	999	27	972	247	1	246	1,218
2002-03	909	49	860	232	1	231	1,091
	Estimated						
2003-04	790	35	755	206	1	205	960
2004-05	692	35	657	210	1	209	866

[1] Receipts from the MTA business tax surcharge and funds dedicated to MTOAF and DHBTF from sections 183 and 184.

CORPORATION FRANCHISE TAX

SUMMARY

In 2003-04, All Funds collections from the corporation franchise tax are estimated to be $1,570 million, a decrease of $43 million, or 2.6 percent, compared with 2002-03. Collections have been adversely impacted by depressed corporate profits in recent years that tend to have a lagged impact on current year receipts.

In 2004-05, All Funds collections from the corporation franchise tax are projected to be $1,984 million. This is an increase of $414 million, or 26 percent, compared with 2003-04, resulting mainly from expected improvement in the profitability of corporations and the impact of recently enacted tax policy changes.

Legislation proposed with this Budget would:

- modify the fixed dollar minimum tax base;
- phase in a single sales factor for income allocation for manufacturers;
- create a new targeted incentive for biotech companies;
- reform and extend the Empire Zones Program;
- enhance the Low Income Housing Tax Credit; and
- extend the Metropolitan Transportation Authority (MTA) surcharge for four years, until 2009.

DESCRIPTION

Tax Base and Rate

The corporation franchise tax is levied by Article 9-A of the Tax Law on domestic and foreign corporations for the privilege of exercising their corporate franchise or doing business, employing capital, owning or leasing property, or maintaining an office in New York.

The corporation franchise tax is made up of business entities classified as either C corporations or S corporations. The New York State Department of Taxation and Finance's Office of Tax Policy Analysis (OTPA) compiles corporate tax return data relating to the total number of C and S corporations and tax liability for these entities. The *1999 New York State Corporation Tax Statistical Report* indicates that 259,961 taxpayers filed as C corporations, while 286,122 taxpayers filed as S corporations. This report contains the most recent data available on C and S corporations. The number of C corporations increased by roughly 0.3 percent from the prior year, while the number of S corporations increased by nearly 2.2 percent.

For C corporations, the Article 9-A corporation franchise tax requires a taxpayer to compute tax liability under four alternative bases and pay under the base that results in the largest tax. The four bases are:

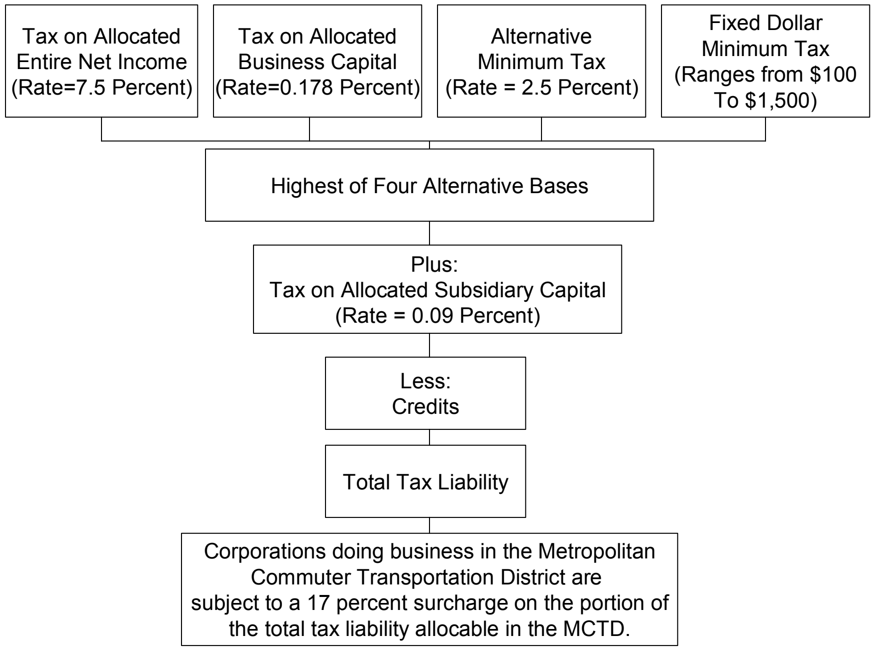
1. An allocated entire net income (ENI) base, which begins with Federal taxable income before net operating loss deductions and special deductions. A rate of 7.5 percent applies to this base after the exclusion, deduction, or addition of certain items and the base is allocated to New York. Tax credits will further reduce tax otherwise due.
2. An alternative minimum tax (AMT) base, which equals entire net income adjusted to reflect certain Federal tax preference items and adjustments and State-specific net operating loss (NOL) modifications, taxed at a rate of 2.5 percent.
3. A capital base, taxed at a rate of 0.178 percent. Allocated business and investment capital form the capital base, with a maximum annual tax of $350,000.
4. A fixed dollar minimum, which ranges from $100 to $1,500, depending on the size of the corporation's gross payroll, including general executive officers, during the applicable tax period.

For S corporations, the Article 9-A corporation franchise tax requires a taxpayer to pay a fixed dollar minimum, ranging from $100 to $1,500, depending on the size of the corporation's gross payroll during the applicable tax period. S corporations are subject to the fixed dollar minimum for tax years 2003, 2004 and 2005, after which they will revert back to the prior tax structure of an entity level tax.

Additionally, corporations doing business in the Metropolitan Commuter Transportation District (MCTD) are subject to a 17 percent surcharge on the portion of the total tax liability allocable in the MCTD. The collections from the surcharge are deposited into the Mass Transportation Operating Assistance Fund (MTOAF).

The following flow chart shows how alternative tax bases are used to compute Article 9-A tax liability.

Article 9-A Flowchart



Tax Expenditures

Tax expenditures are defined as features of the tax law that reduce the amount of a taxpayer's liability to the State by providing either economic incentives or tax relief to particular classes of persons or entities to achieve a public purpose. The corporate franchise tax structure includes various exclusions, exemptions, tax credits, and other statutory devices designed to reduce State tax liability. The distribution of these benefits varies widely among firms. Among the major tax expenditure items for the corporate franchise tax are the exclusion of interest, dividends and capital gains from subsidiary capital, the investment tax credit, the Empire Zone credits, and the preferential tax rates for qualifying small business corporations.

Significant Legislation

The significant statutory changes since 1994 are summarized below.

Subject	Description	Effective Date
Legislation Enacted in 1994		
Exclusion of Income for Foreign Airlines	Allowed foreign airlines to exclude the following items from entire net income: all income from international operations of aircraft effectively connected to the United States; foreign passive income, and income earned overseas.	Retroactive to January 1, 1989
Temporary Business Tax Surcharge	Eliminated the temporary 15 percent surcharge over a three year period.	January 1, 1994
Special Additional Mortgage Recording Tax (SAMRT)	Provided for refundability of the unused portion of the SAMRT credit to both regular and S corporation nonbank mortgage lenders.	January 1, 1994
Depreciation	Changed the Modified Accelerated Cost Recovery System (MACRS) depreciation rule for non-New York property to conform to provisions of the Federal Tax Reform Act of 1986.	January 1, 1994
Limited Liability Companies (LLC) and Limited Liability Partnerships (LLP)	Provided New York State authority for formation of LLCs and LLPs, which are business organizations that provide many of the tax benefits associated with partnerships and the liability protection afforded to corporations.	October 24, 1994

Subject	Description	Effective Date
Investment Tax Credit/ Employment Incentive Credit (EIC)	Extended carryover period for this credit from seven to ten years.	January 1, 1994
Rate Reduction – Alternative Minimum Tax (AMT)	Reduced rate from 5.0 percent to 3.5 percent.	January 1, 1995
Legislation Enacted in 1996		
Rehabilitation Credit for Historic Barns	Allowed taxpayers to claim corporate franchise tax credit for the rehabilitation of historic barns in New York State.	January 1, 1997
Agricultural Property Tax Credit	Allowed eligible farmers to claim a real property tax credit against the corporate franchise tax.	January 1, 1997
Legislation Enacted in 1997		
Investment Tax Credit Carryforward	Allowed any unused pre-1987 investment tax credit to remain available until 2002. Post-1986 investment tax credit extended to 15-year carry forward.	January 1, 1998
Alternative Fuel Vehicle Credit	Provided corporations and individuals with a tax credit for a portion of the cost of purchasing or converting vehicles to operate on alternative fuels.	January 1, 1998
Credit for Employing Individuals with Disabilities	Allowed employers who employ individuals with disabilities to claim a credit for a portion of wages paid to such individuals.	January 1, 1998
Legislation Enacted in 1998		
Rate Reduction – AMT	Reduced rate from 3.5 percent to 3.0 percent phased in over two years.	June 30, 1998
Investment Tax Credit	Allowed brokers/dealers in securities to claim a credit for equipment or buildings used in broker/dealer activity and in activities connected with broker/dealer operations.	October 1, 1998
Emerging Technology Companies Credit	Provided, under the New York State Emerging Industry Jobs Act, corporate franchise tax credits for qualified emerging technology companies that create new jobs or for certain corporate taxpayers that invest in emerging technology companies located in New York State.	January 1, 1999
Rate Reduction – ENI	Reduced the tax rate from 9 percent to 7.5 percent over a three-year period beginning after June 30, 1999.	June 30, 1999
Legislation Enacted in 1999		
Rate Reduction – AMT	Reduced rate from 3.0 percent to 2.5 percent.	June 30, 2000
Mergers and Acquisitions	Repealed the provisions relating to mergers, acquisitions and consolidations.	January 1, 2000
Alternative Fuel Vehicle Credit	Expanded the alternative fuel credits to electric and clean fuel vehicles sold or leased to governmental entities, provided that the companies manufacture the vehicles in New York and create at least 25 full-time jobs.	January 1, 2000
Airline Apportionment	Reduced the percentage of income apportioned to New York by 40 percent by changing the allocation formula to multiply the New York Factor in the numerator of each component in the formula.	January 1, 2001
EDZ/ZEA Wage Tax Credit	Doubled the existing Economic Development Zone (EDZ) and Zone Equivalent Area (ZEA) wage tax credits.	January 1, 2001
Defibrillator Credit	Granted a new credit of $500 per automated external defibrillator.	January 1, 2001
Legislation Enacted in 2000		
Energy Reform and Reduction	Reformed energy taxation for energy companies, previously taxed under section 186 of Article 9, to pay tax under the Article 9-A corporate franchise tax.	January 1, 2000
Industrial or Manufacturing Business Credit (IMB)	Provided a refundable credit provided for any of the gross receipts taxes and the section 189 gas import tax on manufacturing uses of energy.	January 1, 2000
Low Income Housing Tax Credit	The credit is based on the structure of the Federal low-income housing tax credit. The State program provides tax credits for housing constructed for moderate income households. The amount of the credit depends on whether a building is new, existing, or federally subsidized.	January 1, 2000

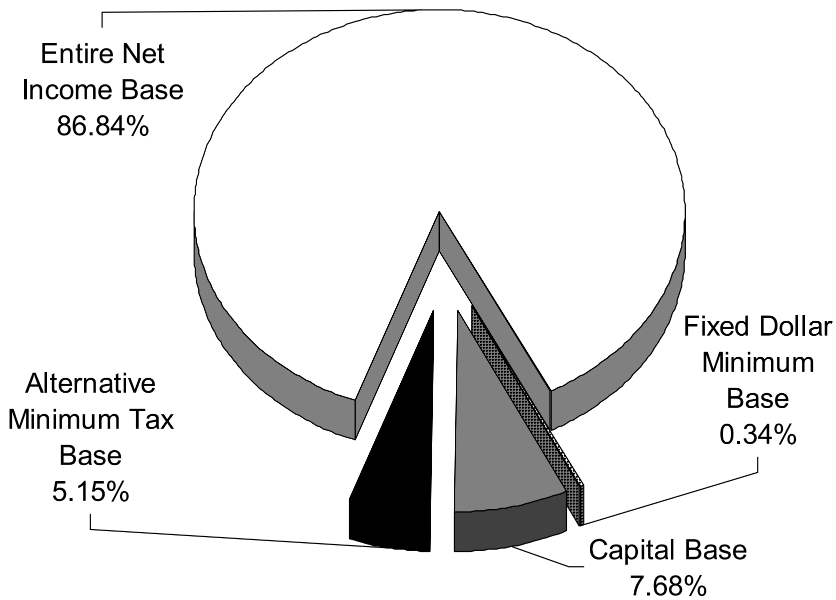
Subject	Description	Effective Date
Securities and Commodities Brokers or Dealers Customer Sourcing	Allowed securities broker/dealers to allocate receipts, which constitute commissions, margin interest or account maintenance fees, as a service performed at the customer's mailing address.	January 1, 2001
Empire Zones (EZ)	Transformed the Economic Development Zones (EDZ) to Empire Zones, effectively providing for virtual "tax free" zones for certain businesses. The enhanced benefits include a tax credit for real property taxes, a tax reduction credit, and a sales and use tax exemption. The tax reduction credit may be applied against the fixed dollar minimum tax, which may reduce the taxpayer's liability to zero.	January 1, 2001
Rate Reduction – S Corporations	Reduced the differential tax rate imposed on S corporations by 45 percent.	June 20, 2003
Rate Reduction – Small Businesses	Reduced tax rate for small businesses with entire net income of $200,000 or less to 6.85 percent.	June 30, 2003
Legislation Enacted in 2002		
Low-Income Housing Tax Credit	Doubled the statewide aggregate credit limit for the low-income housing tax credit from $2 million to $4 million.	May 29, 2002
Estimated Payment Requirement	Increased the first quarterly payment of estimated tax from 25 percent to 30 percent of the prior year's liability for those corporate taxpayers whose prior year's liability exceeds $100,000.	January 1, 2003
Empire Zones Program	Amended to clarify certain provisions and implement new components for several credit calculations.	Various
Legislation Enacted in 2003		
Modification for Decoupling from Federal Bonus Depreciation	Decoupled from Federal depreciation allowances for property placed in service on or after June 1, 2003, that qualified for the special bonus depreciation allowance allowed by the Federal Job Creation and Worker Assistance Act of 2002 and the Jobs and Growth Tax Relief Reconciliation Act of 2003. The modifications do not apply to qualified resurgence zone property or qualified New York Liberty Zone property.	June 1, 2003
Intangible Holding Companies	Required taxpayers to modify Federal taxable income relating to certain royalty and interest payments made with respect to the use of intangible property by related members or royalty and interest payments received from related members.	January 1, 2003
S Corporation Tax Change	Taxed S corporations on a fixed dollar minimum amount for tax years 2003, 2004 and 2005 only. The fixed dollar minimum amounts are those imposed under Article 9-A, ranging from $100 to $1,500.	January 1, 2003
Superfund-Brownfield Tax Credits	Created tax incentives for the redevelopment of brownfields through three tax credits: a redevelopment tax credit, a real property tax credit, and an environmental remediation insurance credit. There are three components in the redevelopment tax credit: a site preparation component, a tangible property component, and an onsite groundwater remediation component.	April 1, 2005

TAX LIABILITY

The OTPA's Corporate Franchise Tax Study File contains the most recent data available on Article 9-A liability. The study file includes all corporations filing under Article 9-A, except fixed dollar minimum tax filers and S corporations. The most current liability information is for the 2000 tax year.

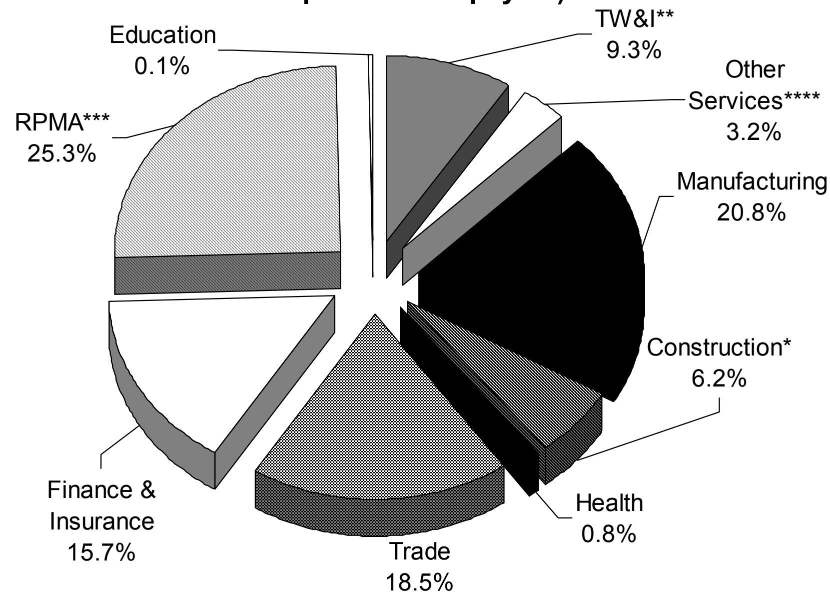
As noted above, C corporations pay under the highest of four bases. In 2000, nearly 87 percent of liability was paid under the entire net income base. The capital base was the second largest base, at 7.7 percent of liability. These percentages are fairly constant over time. The AMT base, however, has begun to diminish due to tax law changes, including a drop in the tax rate from 3.5 percent in 1995 to the current rate of 2.5 percent. (See following chart.)

2000 Distribution of Tax Liability by Basis of Tax



The next chart shows the distribution of tax liability by major industry sector. Liability paid by the finance and insurance sector made up 15.7 percent of total tax liability paid by C corporation taxpayers in 2000, with the manufacturing sector accounting for 20.8 percent of liability. The service industries (consisting of RPMA and Other Services) share has grown quite significantly throughout the 1990s and, in 2000, represented over 28.5 percent of total liability.

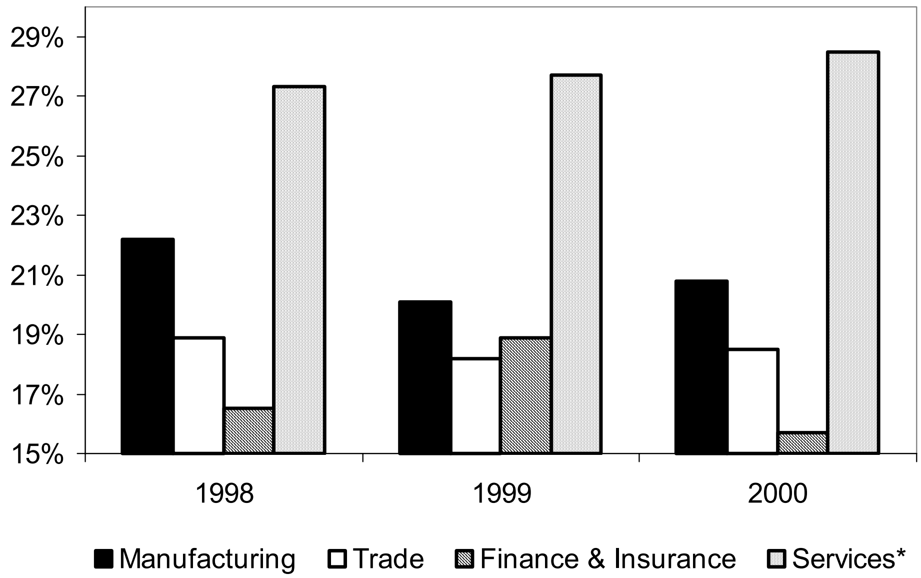
2000 Tax Base Industry Profile:
(Share of Total Tax Liability of C Corporation Taxpayers)



* Construction, agriculture, mining, and utilities. (NAICS Sectors 11, 21, 22, and 23)
** Transportation and warehousing and information. (NAICS Sectors 48, 49, and 51)
*** Real estate and rental and leasing; professional, scientific, and technical services; management of companies and enterprises; and administrative and support and waste management and remediation services. (NAICS Sectors 53, 54, 55, and 56)
**** Art, entertainment, and recreation services; accommodation and food services; and other services. (NAICS Sectors 71, 72, and 81)

The following chart illustrates the fluctuation in the percentage of liability paid by the four industry groups that typically make up the vast majority of total tax liability for the period of 1998 to 2000: finance and insurance, trade, manufacturing, and services (consisting of RPMA and Other Services). Liability for the finance and insurance sector tends to fluctuate significantly over time. Liability shares for this industry rose from 16.5 percent in 1998 to 18.9 percent in 1999, and then dropped to 15.7 percent in 2000. In comparison, the service industry's share of total liability had increased steadily for this same three-year period. The manufacturing industry's share of total liability is also quite volatile and depends on both economic conditions and the ability of the companies in this sector to take advantage of tax credit programs designed to stimulate the industry. For manufacturers, liability decreased in 1999 and then increased in 2000, a mirror image of the finance and insurance industry.

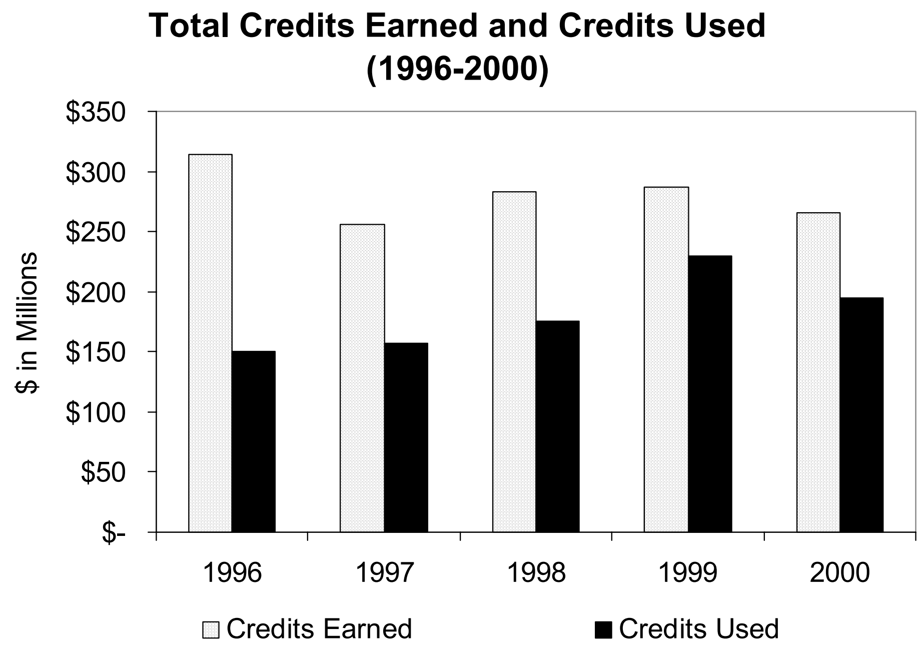
Industry Profile: Percent of Total Liability
(1998-2000)



* Services consist of real estate and rental and leasing; professional, scientific, and technical services; management of companies and enterprises; administrative and support and waste management and remediation services; art, entertainment, and recreation services; accommodation and food services; and other services. (NAICS Sectors 53, 54, 55,, 56, 71, 72, and 81)

Credits

The following graph shows major credits earned and used by Article 9-A taxpayers, and illustrates that the amount of credits earned greatly exceeds the amount of credits used. These credits include the investment tax credit (ITC), the Empire Zone credits, the alternative minimum tax (AMT) credit, the agricultural property tax credit, and the special additional mortgage recording credit. Credit earned is the amount of credit earned by a taxpayer in the current tax year. This is prior to any credit recapture, and does not include credits earned in or carried over from any prior years. In 2000, the ITC, a benefit to manufacturing companies, accounted for about 74 percent of all tax credits earned and about 57 percent of all tax credits used.



For the most part, Tax Law provisions prevent taxpayers from using tax credits to reduce final tax liability below the fixed dollar minimum tax or the AMT. This has resulted in taxpayers carrying forward a significant amount of tax credits into subsequent tax years. Legislation enacted in 2000, however, made it possible to apply the employment incentive credit and the tax reduction credit against the AMT if taxpayers are within an Empire Zone. The tax reduction credit for qualified Empire Zone enterprises may be applied against the fixed dollar minimum tax, which may reduce the taxpayer's corporate franchise tax liability to zero. In addition, the Empire Zone property tax credit is refundable, whereby taxpayers use the credit against liability, but receive a refund of any remaining credit. It is expected that the Empire Zone tax relief measures will result in somewhat fewer tax credits being carried forward to future years.

PROPOSED LEGISLATION

Legislation proposed with this Budget would:

- modify the fixed dollar minimum tax base to add three new categories to the fixed dollar minimum amounts. Firms with a gross payroll amount of $25 million or higher would pay $10,000, those with a gross payroll amount between $6.25 million and $25 million would pay $5,000 and those with a gross payroll amount of $0.5 million or less would pay $100.
- phase in a single sales factor for manufacturers to replace the current three-factor allocation method for allocating out-of-State income for manufacturers. This measure would cut the tax on manufacturers and encourage them to stay and expand in New York.
- create a new targeted incentive program for biotech firms which would allow the transfer of losses to qualified corporations.
- reform the Empire Zones Program to extend the program beyond the current sunset date of 2004 and reduce the benefits period currently at 15 years, to 10 years.
- enhance the Low Income Housing Tax Credit Program by providing an additional $2 million in tax credits annually, or $20 million over the 10-year period of the

program, which would spur a new round of affordable housing construction. Total funding allocated over the life of the program, including this new proposal, would be $60 million.

- extend the MTA surcharge for four years, until 2009.

RECEIPTS: ESTIMATES AND PROJECTIONS

All Funds

2003-04 Estimates

Net All Funds collections through December are $1,042 million, a decrease of $33 million, or 3.1 percent, compared with the comparable period in the prior fiscal year. The decline is due to several factors, including tax cuts enacted in prior years, the slow growth of the national and State economies in the past two years, and the depressed corporate profitability of recent years. Total net All Funds receipts for 2003-04 are estimated to be $1,570 million, a decrease of $43 million, or 2.6 percent, compared with last year.

Significant tax law changes at both the State and Federal levels have driven down collections in the current fiscal year. At the State level, the incremental value of tax reductions over last year is nearly $100 million. The most significant tax benefits are those available under the Empire Zones program. Additionally, the change in the sales allocation for financial services has eroded receipts in the current year. Partially offsetting these tax reductions is a legislative action which has affected receipts beginning in the second quarter of the State fiscal year. This change, made with the 2003-04 Enacted Budget, involves decoupling from the Federal bonus depreciation rules. Starting in June 2003, taxpayers must add back to State income the special bonus depreciation allowance allowed by the Federal law. Extending the MTA surcharge for four years to 2009 will maintain the existing revenue stream available to support transportation services in the Metropolitan Commuter Transportation District.

Taxpayer behavior continues to influence collections. Adjustments in 2003-04 to prior year payments are expected to be somewhat lower than the large adjustments made over the past 2 years. These adjustments reduce cash collections during the State fiscal year. Last year, calendar year filers made adjustments to prior years' liability, reducing current year cash results by over $535 million. This year, adjustments are expected to reach $471 million.

2004-05 Projections

Total net All Funds receipts are projected to be $1,984 million, an increase of $414 million, or 26 percent above 2003-04.

The strong growth in tax receipts is driven mainly by the expected improvement in the economy, consistent with the recent surge in corporate profitability that is expected to continue at a more modest pace in 2004. Receipts are expected to increase as a result of a tax law change enacted with the 2003-04 Enacted Budget, which requires taxpayers to modify taxable income by adding back certain royalty and interest payments made with respect to the use of intangible property by related members or royalty and interest payments received from related members. In addition, tax receipts will increase as a result of the incremental value of the tax effects of decoupling from the Federal bonus depreciation rules. Executive Budget proposals for the targeted tax incentive for biotech companies and the enhancement to the Low Income Housing Tax Credit are projected to reduce tax revenues by $7 million while the modification to the fixed dollar minimum tax base is expected to increase tax revenues by $40 million. Executive Budget proposals to reform the Empire Zones Program and to phase in a single sales factor for manufacturers will not affect receipts until State fiscal year 2005-06.

Taxpayers are expected to continue to make adjustments to prior year payments that will tend to depress 2004-05 receipts, although current information suggests the adjustments in 2004-05 will be consistent with adjustments in 2003-04.

General Fund

Based on collections to date, General Fund net collections for State fiscal year 2003-04 are projected to be $1,382 million, a decrease of $25 million, or 1.8 percent, compared with State fiscal year 2002-03.

General Fund receipts for State fiscal year 2004-05 are expected to increase by 26 percent over 2003-04 levels to $1,746 million. This increase is the result of improved corporate profitability and an overall upswing in economic conditions.

Other Funds

Under current law, corporations doing business in the MCTD are subject to a 17 percent surcharge on the portion of the total tax liability allocable to the region. The MTOAF was held harmless from the ENI rate reduction, which began in 1999. As a result, MTOAF collections will not be diminished by the corresponding reduction in General Fund receipts. Based on collections to date, the Article 9-A MTOAF contribution for 2003-04 is projected to reach approximately $188 million, an 8.4 percent decrease from 2002-03. As with General Fund receipts, surcharge collections are affected by the volatility of the financial services sector and general growth in business activity for the current tax year. Consistent with overall estimates, and the fact that the MTOAF is protected from the corporate franchise tax reduction, 2004-05 State fiscal year collections are expected to increase by roughly 26 percent.

RECEIPTS BY FUND TYPE

CORPORATION FRANCHISE TAX RECEIPTS
(millions of dollars)

	Gross General Fund	Refunds	Net General Fund	Special Revenue Funds	Refunds	Net Special Revenue Funds[1]	All Funds Net Collections
	Actual						
1995-96	2,217	396	1,821	217	36	182	2,002
1996-97	2,414	348	2,067	274	36	239	2,306
1997-98	2,381	300	2,081	289	27	262	2,343
1998-99	2,479	429	2,050	243	30	213	2,262
1999-2000	2,422	483	1,939	272	43	229	2,168
2000-01	2,817	482	2,335	316	21	295	2,630
2001-02	2,012	497	1,515	236	48	188	1,703
2002-03	1,940	533	1,407	247	42	205	1,612
	Estimated						
2003-04	1,882	500	1,382	233	45	188	1,570
2004-05							
(current law)	2,214	500	1,714	283	45	238	1,952
(proposed law)	2,246	500	1,746	283	45	238	1,984

[1]MCTD 17 percent surcharge deposited in Mass Transportation Operating Assistance Fund.
Note: Components may not add to net collections due to rounding.

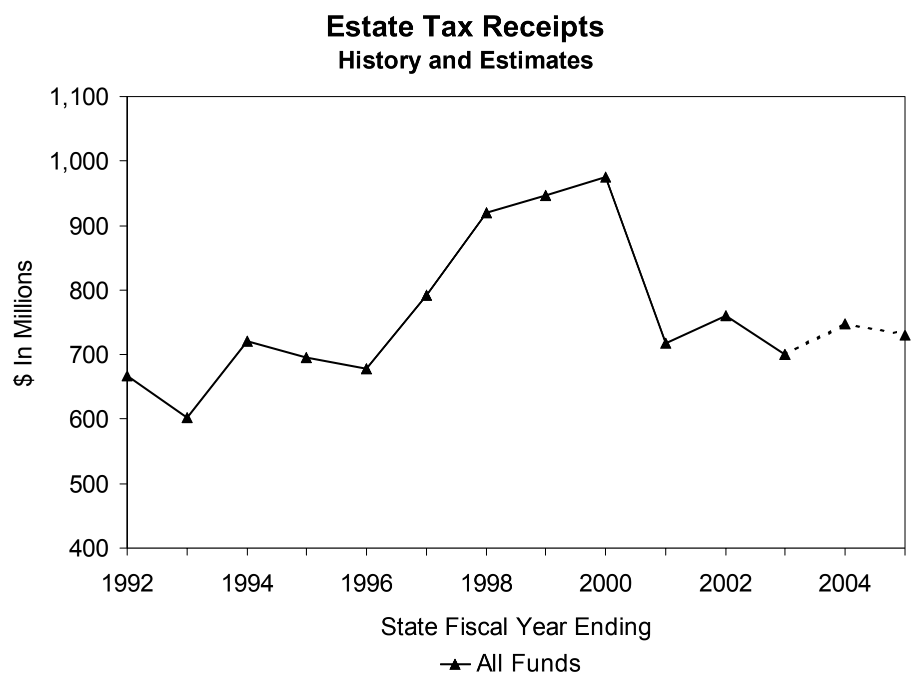
ESTATE TAXES

SUMMARY

In 2003-04, All Funds collections from estate taxes are estimated to be $747.4 million. This is an increase of $46.5 million, or 6.6 percent, from the prior year, reflecting the estimated rise in the market value of large estates.

In 2004-05, All Funds collections from estate taxes are projected to be $730.8 million. This is a decrease of $16.6 million, or 2.2 percent, compared with 2003-04.

No new legislation for this tax is proposed with this Budget.



DESCRIPTION

Tax Base and Rate

New York imposes a tax on the estates of deceased State residents and on that part of a nonresident's estate made up of real and tangible personal property located within New York State.

The tax base is calculated by first determining the Federal gross estate as of July 22, 1998. The Federal gross estate is comprised of the total amount of real estate, stocks and bonds, mortgages, notes, and cash, insurance on decedent's life, jointly owned property, other miscellaneous property, transfers during decedent's life, powers of appointment, and annuities that the decedent owned.

The Federal gross estate is reduced by the Qualified Conservation Easement Exclusion and the following deductions: funeral expenses and expenses incurred in administering property subject to claims; debts of the decedent; mortgages and liens; net losses during administration, and expenses incurred in administration of the estate not subject to claims;

bequests to a surviving spouse (marriage deduction), certain property interests; charitable, public, and similar gifts; and a qualified family-owned business interest deduction. This yields the Federal taxable estate for New York and becomes the basis for calculating New York's estate tax.

The total value of all items of real and tangible personal property of the taxpayer located outside of New York State is divided by the taxpayer's Federal gross estate to arrive at the proportion of the estate outside New York State. This proportion is then used to allocate the Federal credit for state death taxes.

Legislation enacted in 1997 significantly reduced State estate tax collections and changed the way the New York State estate tax was imposed. The State's estate tax rate structure, credits and exemptions were eliminated in two phases.

The first phase of the estate tax legislation, for those dying on or after October 1, 1998, and before February 1, 2000, increased the unified credit (the credit that can be used to reduce liability of either the estate or gift tax under the unified imposition of these taxes) from $2,950 to $10,000, thereby increasing the value of transfers exempt from taxation to $300,000. In addition, the requirement for 90 percent of the estate tax to be paid within six months of death to avoid underpayment interest was changed to seven months.

The second phase, for decedents dying on or after February 1, 2000, eliminated New York's estate tax rate schedule and provided that New York State's estate tax would be equal to the maximum Federal credit for state death taxes paid, commonly called the pick-up tax. New York also automatically conformed State law to the unified credit provisions specified in Federal law, but capped the maximum credit to exempt the first $1 million in the taxable value of an estate. In February 2000, Federal law set the unified credit at $675,000 and contained a schedule that increased the credit to $1 million by 2006. (See table below.) In addition, consistent with Federal law, 100 percent of tax liability is due within nine months of the decedent's death.

Estates of decedents dying after 2004 will be subject to a graduated rate structure with tax rates that range from 0.8 percent on adjusted taxable estates in excess of $40,000 but less than $90,000, and up to 16 percent on adjusted taxable estates of $10,040,000 or more.

Federal Legislation

Current Federal law converted the old unified credit to an exemption and will continue to increase the value of the exemption until it reaches $3.5 million in 2009. As reported, State law capped the exemption at $1 million, effective in 2002. (See table below.)

STATE UNIFIED CREDIT/EXEMPTION AMOUNTS

Year	Prior to 2001 Federal Tax Reduction Program	After 2001 Federal Tax Reduction Program
2000, 2001	$675,000	$675,000
2002, 2003	700,000	1,000,000
2004	850,000	1,000,000*
2005	950,000	1,000,000*
2006 and thereafter	1,000,000	1,000,000*

* New York State law caps the unified exemption set in Federal law at $1 million. The Federal law increases the amount to $1.5 million in 2004 and 2005, $2 million in 2006, 2007, and 2008, and $3.5 million in 2009.

In addition, the Federal law phases out the Federal credit for state death taxes over four years, by 25 percent per year. The credit will be repealed for the estates of decedents dying after 2004. In 2005, it will become a deduction until the phase-out of the Federal estate tax in 2010. The provisions of New York's law setting the estate tax liability equal to the Federal credit for state death taxes conforms to the Federal law as it existed on July 22, 1998. As a result, New York estate tax liability will be unaffected by the phase-out of the Federal credit for state death taxes.

Administration

The Surrogate Court has jurisdiction of the probate of the estate and the authority to finalize the amount of the tax. The tax due is required to be paid on or before the date fixed for filing the return, nine months after the decedent's date of death. A twelve-month extension may be granted by the Commissioner of Taxation and Finance for paying the tax.

If the payment of the tax would cause undue hardship, the Commissioner may authorize a payment extension for up to four years from the decedent's date of death. It may be necessary for the taxpayer to provide a bond in an amount of no more than twice the amount due if an extension is approved for payment of the tax.

If the payment of the tax due is not made within nine months of the decedent's date of death, additional interest is charged to the remaining payments of the tax. The interest for extended payments is computed and compounded daily on the portion remaining from the first day of the 10th month following the decedent's date of death to the date of the payment. There is no discount for early payment of the estate tax.

The executor and the spouse are personally liable for the payment of the estate tax. If there is no will, the Federal, New York and foreign death taxes paid or payable by estate representative are apportioned among the beneficiaries.

There is reciprocity with other states with the collection of inheritance and estate taxes in nonresident estates. Refund claims of an overpayment of the tax must be filed by the executor within three years from the time the return was filed or two years from the time the tax was paid, whichever is later.

Tax Expenditures

Since the tax is equal to the Federal credit for state death taxes, as it existed on July 22,1998, there are no New York specific tax expenditures.

Significant Legislation

The significant statutory changes since 1994 are summarized below.

Subject	Description	Effective Date
Legislation Enacted in 1994		
Unified Credit for Estate and Gift Taxes	Increased credit from $2,750 to $2,950, thereby eliminating the tax on taxable gifts/estates of $115,000 or below, up from $108,600.	June 9, 1994
Legislation Enacted in 1995		
Deduction	Authorized a principal residence deduction of $250,000 (maximum).	June 7, 1995
Legislation Enacted in 1997		
Unified Credit for Estate and Gift Taxes	Increased credit from $2,950 to $10,000, thereby eliminating the tax on taxable estates of $300,000 or below.	October 1, 1998
	Increased credit from $2,950 to $10,000, thereby eliminating the tax on taxable gifts of $300,000 or below.	January 1, 1999
	Set the States' unified credit to equal the Federal credit, but capped the maximum credit to exempt the first $1,000,000 of the estate.	February 1, 2000
Estate Tax Rate	Set the New York estate tax rates equal to the Federal credit for State estate taxes paid.	February 1, 2000

Subject	Description	Effective Date
Gift Tax	Repealed.	January 1, 2000
Tax Liability Due Date	Increased from six to seven months.	October 1, 1998
	Increased from seven to nine months (same as Federal).	February 1, 2000
Legislation Enacted in 1998		
Closely-Held Business	Interest on deferred payments of estate tax, where estate consists largely of a closely-held business, reduced from 4 percent to 2 percent.	January 1, 1998
Legislation Enacted in 1999		
Federal Conformity	Conformed New York State law to Federal law as of July 22, 1998, except for the unified credit provisions.	August 9, 1999
Family-Owned Business Deduction	Family-owned business exclusion repealed and replaced with family-owned business deduction, conforming to Federal law changes.	December 31, 1997
Penalty and Interest	Penalty and interest waived on estate tax associated with a cause of action that was pending on the date of death, or which was associated with the decedent's death. The waiver is applicable from the date of the return disclosing the cause of action if filed.	July 13, 1999

TAX LIABILITY

The recent yield of this tax has been heavily influenced by three factors: tax law changes, annual variations in the relatively small number of large estates, and the value of the equity market, given the large component of corporate stock in large taxable estates. Recent tax law changes have reduced estate tax collections across the board and thousands of the smallest estates have been eliminated from potential tax. As a result, the volatility in receipts from this source is expected to increase, due to the more random nature of collections from large estates.

In developing projections for estate tax receipts, the value of household net worth is used to forecast receipts from estates that make payments of less than $4 million. In addition to the value of equities, a distributional analysis is utilized to estimate receipts and the number of estates where payments exceed $4 million.

PROPOSED LEGISLATION

No new legislation for this tax is proposed with this Budget.

RECEIPTS: ESTIMATES AND PROJECTIONS

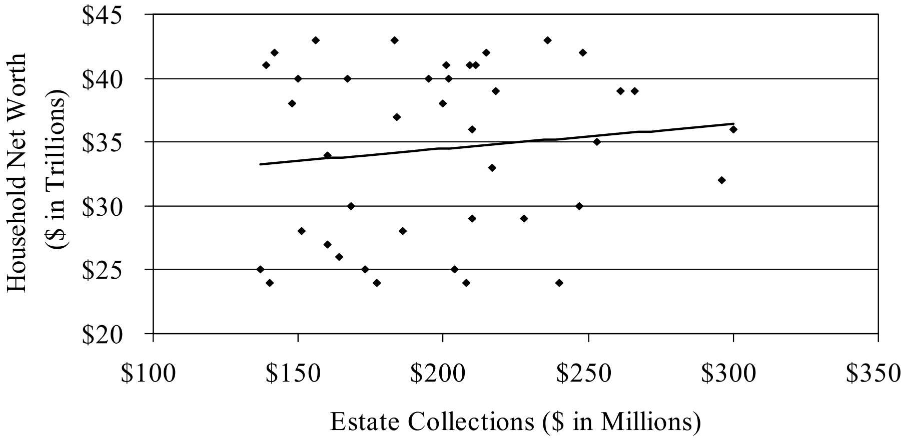
All Funds

2003-04 Estimates

Net All Funds collections to date are $593.4 million, an increase of $42.5 million, or 7.7 percent above the comparable period in the prior fiscal year.

Total net All Funds receipts for 2003-04 are estimated to be $747.4 million, an increase of $46.5 million, or 6.6 percent above last year. Receipts are expected to increase modestly over the rest of the fiscal year, reflecting estimated increases in the value of household net worth of 5 percent over the past year. (See table below.)

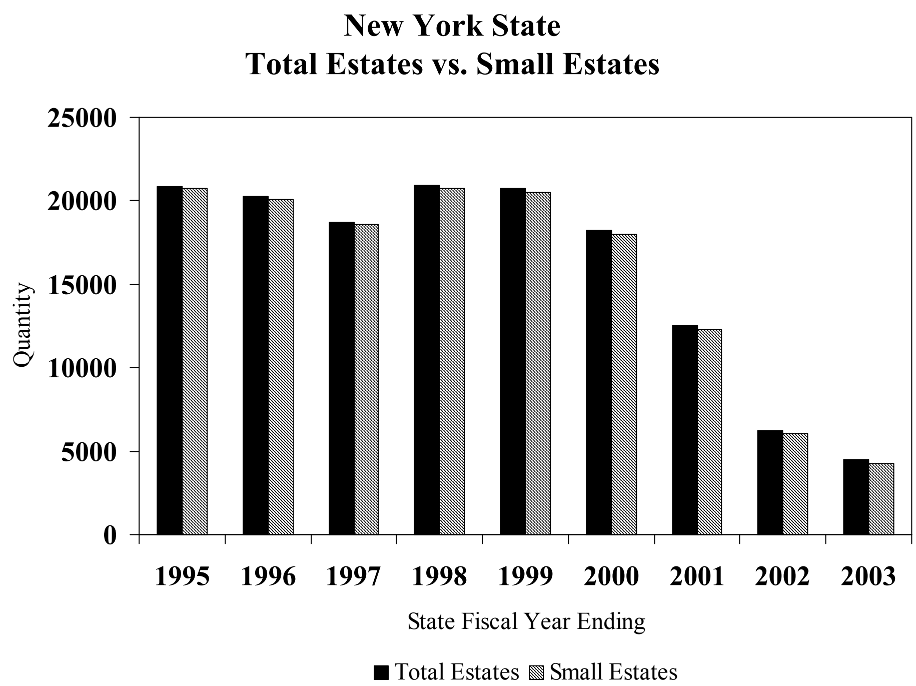
Estate Tax Collections vs. Household Net Worth

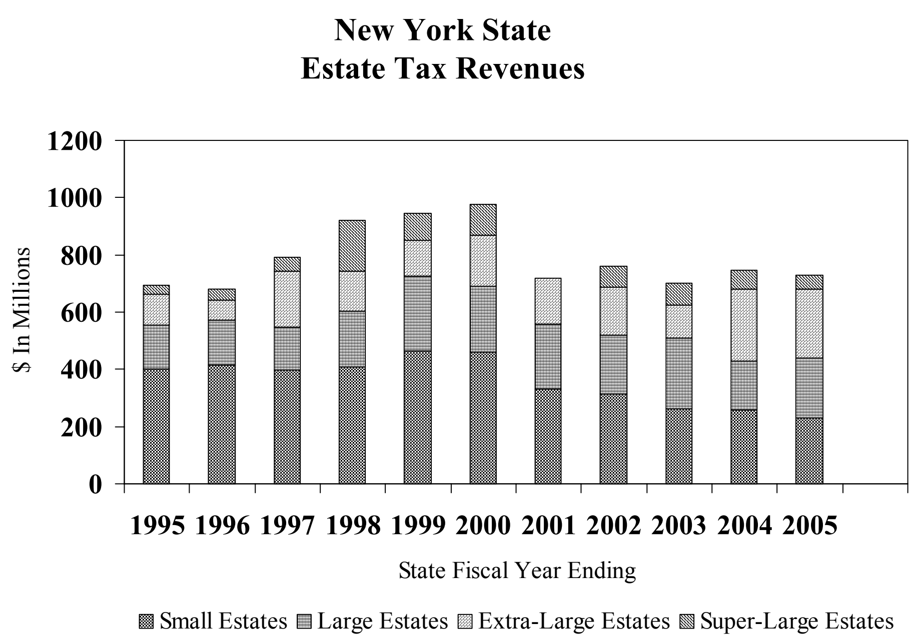


Quarterly Data: 1993 - 2003
The trend line represents the average increase in collections versus
A trillion dollar increase in Household Net Worth.

Extra-large estates year-to-date collections are $198 million, a significant increase of $124 million, or 16.8 percent from the comparable period in 2002-03, reflecting in part the $1 million unified exemption that reduces payments that otherwise would have been in the Super-large estate category to the Extra-large category and actual growth in the equity markets. Collections from small estate payments have experienced a decrease of $17 million, down 7.6 percent to $206 million from the similar period of 2002-03. This trend reflects a substantial impact from the $1 million unified exemption. It is estimated that the full year effects of the tax reductions enacted in 1997 have reduced total receipts by $483.3 million or 33 percent, from the 1993-94 base.

CARTS collections through nine months of 2003-04 were $19.6 million, a decrease of 24 percent from the same period of 2002-03. Year-to-date refunds for 2003-04 are $23.8 million, 9.4 percent above the same period of 2002-03.


New York State
Total Estates vs. Small Estates
25000
20000
15000
10000
5000
0
Quantity
1995 1996 1997 1998 1999 2000 2001 2002 2003
State Fiscal Year Ending
Total Estates
Small Estates


New York State
Estate Tax Revenues
1200
1000
800
600
400
200
0
$ In Millions
1995 1996 1997 1998 1999 2000 2001 2002 2003 2004 2005
State Fiscal Year Ending
Small Estates
Large Estates
Extra-Large Estates
Super-Large Estates

2004-05 Projections

All Funds receipts are projected to be $730.8 million, a decrease of $16.2 million or 2.2 percent below 2003-04. The estimate includes CARTS collections of $32 million and refunds of $42 million.

The estate collections will continue to be affected by the Federal unified credit amount of $1 million and the recent move to a pick-up tax, which will partially offset an estimated 1 percent increase in the base liability of the tax.

Super-large estate payments are projected to decrease by $15.8 million, or 24 percent, to $50.2 million. The payments from extra-large estates are expected to decrease to $240 million. The projections for the super-large and extra-large estates are based upon the distributional analysis that suggests the number of estates in this category will shrink in 2004-05. Large estate payments are estimated to increase by 21.7 percent to $209.5 million and small estates are expected to decline by 8 percent to $273.1 million. The results for the large and small estate payments are based on the projected value of household net worth, which is expected to increase by 3 percent in 2004-05.

ESTATE TAX RECEIPTS BY SIZE OF ESTATE
(millions of dollars)

	Super Large Estates[1]		Extra Large Estates[2]		Large Estates[3]		Small Estates[4]	Grand Total
	Number	Taxes	Number	Taxes	Number	Taxes	Taxes	Taxes
1995-96	1	37.5	8	67.5	132	158.2	415.4	678.6
1996-97	1	48.1	23	194.9	123	151.3	397.2	791.5
1997-98	5	176.7	18	140.7	160	195.5	406.4	919.3
1998-99	2	93.7	17	128.1	215	259.5	465.1	946.4
1999-2000	2	108.0	22	177.0	192	229.6	460.6	975.2
2000-01	0	0	22	160.0	179	224.7	332.4	717.1
2001-02	2	75.4	19	164.7	167	208.8	312.5	761.4
2002-03	3	77.8	13	112.7	200	247.6	262.8	700.9
---------- Estimated ----------								
2003-04	2	66.0	20	252.5	185	172.2	256.7	747.4
2004-05	2	50.2	19	240.0	195	209.5	231.1	730.8

[1] Liability of at least $25.0 million.
[2] Liability of at least $4.0 million, but less than $25.0 million.
[3] Liability of at least $0.5 million but less than $4.0 million.
[4] Liability less than $0.5 million. (Small estates include CARTS, but all refunds are subtracted.)

RECEIPTS BY FUND TYPE

ESTATE TAX RECEIPTS
(millions of dollars)

	Gross General Fund	Refunds	Net General Fund	Special Revenue Funds	Capital Projects Funds	Debt Service Funds	All Funds Net Collections
---------- Actual ----------							
1995-96	723	44	679	0	0	0	679
1996-97	842	50	792	0	0	0	792
1997-98	968	48	919	0	0	0	919
1998-1999	993	47	946	0	0	0	946
1999-2000	1,029	54	975	0	0	0	975
2000-01	777	60	717	0	0	0	717
2001-02	791	30	761	0	0	0	761
2002-03	741	40	701	0	0	0	701
---------- Estimated ----------							
2003-04	787	40	747	0	0	0	747
2004-05	773	42	731	0	0	0	731

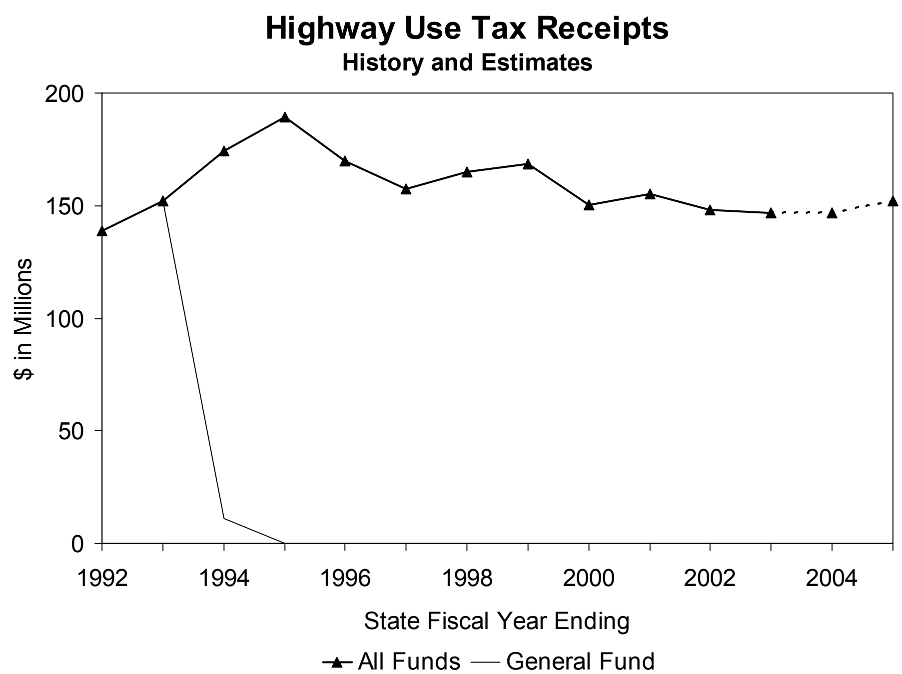
HIGHWAY USE TAX

SUMMARY

In 2003-04, All Funds collections from the highway use tax are estimated to be $147 million. This is an increase of $0.2 million, or 0.1 percent, from the prior year.

In 2004-05, All Funds collections from the highway use tax are projected to be $151.9 million. This is an increase of $4.9 million, or 3.3 percent, compared with 2003-04.

No new legislation for these taxes is proposed with this Budget.



DESCRIPTION

Highway use tax revenues are derived from three sources: the truck mileage tax, highway use permit fees, and the fuel use tax.

Truck Mileage Tax

The truck mileage tax is levied on commercial vehicles having a loaded gross weight of more than 18,000 pounds, or an unloaded weight in excess of 8,000 pounds for trucks and 4,000 pounds for tractors. The tax is imposed at rates graduated according to the gross vehicle weight. Under the gross weight method, the tax is calculated by multiplying the number of "laden" or "unladen" miles traveled on public highways of the State by the appropriate tax rate.

In addition, a supplemental tax equal to the base truck mileage tax was imposed prior to January 1, 1999. Effective January 1, 1999, the supplemental tax was reduced by 50 percent, and effective April 1, 2001, the supplemental tax was reduced by an additional 20 percent of the remaining tax.

BASE TRUCK MILEAGE TAX RATES

Gross Weight Method

Laden Miles Gross Weight of Vehicle	Mills Per Mile
18,001 to 20,000	6.0
20,001 to 22,000	7.0
(increased gradually to)	
74,001 to 76,000	35.0
76,001 and over	add 2 mills per ton and fraction thereof
Unladen Miles Unloaded Weight of Truck	
18,001 to 20,000	6.0
20,001 to 22,000	7.0
(increased gradually to)	
28,001 to 30,000	10.0
30,001 and over	add 5/10 of a mill per ton and fraction thereof
Unloaded Weight of Tractor	
7,001 to 8,500	6.0
8,501 to 10,000	7.0
(increased gradually to)	
16,001 to 18,000	10.0
18,001 and over	add 5/10 of a mill per ton and fraction thereof

Unloaded Weight Method

Unloaded Weight of Truck	Mills Per Mile
8,001 to 9,000	4.0
9,001 to 10,000	5.0
(increased gradually to)	
22,501 to 25,000	22.0
25,001 and over	27.0
Unloaded Weight of Tractor	
4,001 to 5,500	6.0
5,501 to 7,000	10.0
(increased gradually to)	
10,001 to 12,000	25.0
12,001 and over	33.0

Highway Use Permits

Highway use permits are used to denote those vehicles subject to the highway use tax. The permits are issued triennially at a cost of $15 for an initial permit and $4 for a permit renewal. Additionally, special permits are issued for the transportation of motor vehicles, for automotive fuel carriers, and for trips into New York State not to exceed 72 hours.

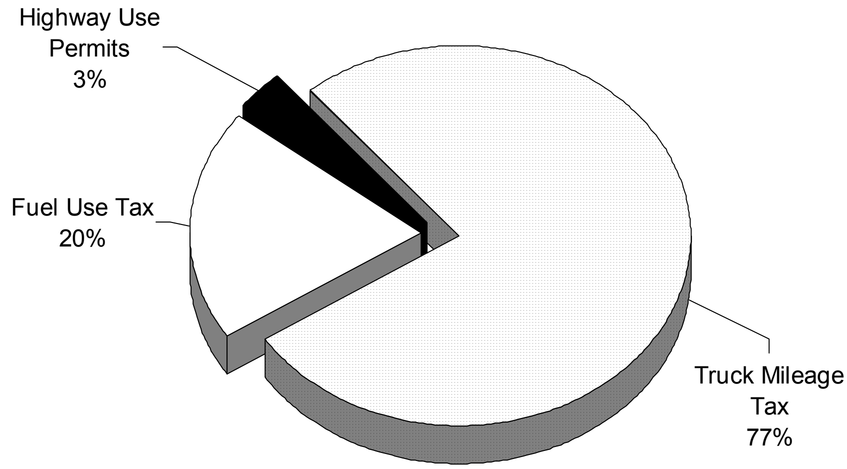
Fuel Use Tax

The fuel use tax is a complement to the motor fuel tax and the sales tax, and is levied on commercial vehicles: (1) having two axles and a gross vehicle weight of more than 26,000 pounds; (2) with three or more axles, regardless of weight; or (3) used in combination when the gross vehicle weight exceeds 26,000 pounds. In contrast to the motor fuel tax, which is imposed upon the amount of fuel purchased within the State, the fuel use tax is imposed on fuel purchased outside but used within New York. This tax is levied on the basis of the number of miles traveled on the public highways of the State. The aggregate fuel use tax rate is the sum of the appropriate motor fuel tax rate and the sales tax rate. The statewide rate for the sales tax component is 7 percent of the average price of fuel — a cents-per-gallon equivalent is set quarterly. A credit or refund is allowed for motor fuel tax or sales tax paid on fuels purchased but not used within the State.

Administration

Most taxpayers remit the truck mileage tax on a monthly basis. The tax is remitted on or before the last day of each month for the preceding month. Fuel use taxpayers file quarterly with their home state under the rules of the International Fuel Tax Agreement (IFTA). The home state subsequently distributes the funds to the state where the liability occurred.

Components of Highway Use Tax Receipts
Estimated State Fiscal Year 2003-04



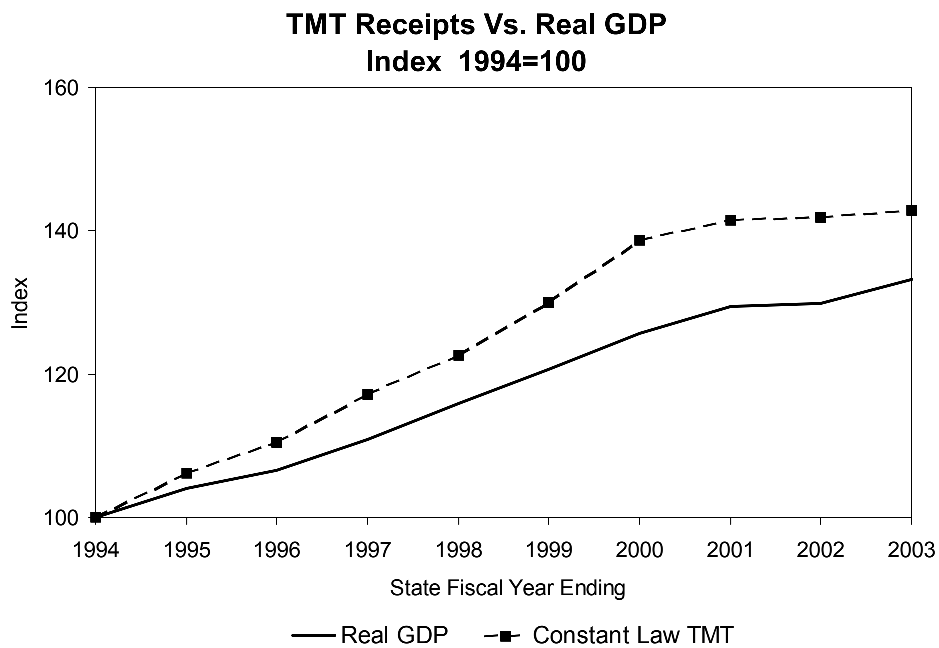
Significant Legislation

The significant statutory changes to this tax source since 1994 are summarized below.

Subject	Description	Effective Date
Legislation Enacted in 1994		
Thruway Mileage	Reduced the truck mileage tax rates imposed on New York State Thruway mileage by one-half and eliminated such rates on and after January 1, 1996	January 1, 1995
Refunds	Permitted taxpayers who purchase more fuel in New York State than they consume in the State to claim refunds or credits for all excess payments of State fuel use taxes (prior to January 1, 1995, taxpayers could only obtain a refund or credit for the motor fuel tax portion of the fuel use tax).	January 1, 1995
International Fuel Tax Agreement	Authorized the State to join the federally mandated International Fuel Tax Agreement (IFTA) on January 1, 1996. This agreement provides for the uniform reporting and collection of fuel-use-related taxes among IFTA jurisdictions. Under IFTA, jurisdictions may only impose a fuel use tax on vehicles with loaded gross weights of more than 26,000 pounds or with three or more axles. Therefore, since January 1, 1996, vehicles with loaded gross weights between 18,000 pounds and 26,000 pounds and with fewer than three axles that had been taxed in New York were excluded from the fuel use tax.	January 1, 1996
Legislation Enacted in 1995		
Fuel Use Tax Rate Cut	Reduced the diesel fuel excise tax rate from ten cents per gallon to eight cents per gallon. As a result, the diesel fuel tax component of the fuel use tax was also reduced to eight cents per gallon.	January 1,1996
Legislation Enacted in 1998		
Supplemental Tax	Reduced the truck mileage supplemental tax by 50 percent.	January 1, 1999
Legislation Enacted in 2000		
Supplemental Tax	Reduced the truck mileage supplemental tax by 20 percent.	April 1, 2001

TAX LIABILITY

Highway use tax receipts are a function of the demand for trucking, which fluctuates with national economic conditions. Liability declined in 1999-2000, reflecting tax cuts, and grew in 2000-01 although the increase was tempered by further tax cuts.



PROPOSED LEGISLATION

No new legislation for these taxes is proposed with this Budget.

RECEIPTS: ESTIMATES AND PROJECTIONS

All Funds

2003-04 Estimates

Net All Funds collections to date are $113.7 million, an increase of $0.9 million, or 0.8 percent above the comparable period in the prior fiscal year.

Total net All Funds receipts for 2003-04 are estimated to be $147 million, an increase of $0.2 million, or 0.1 percent above last year.

In the current fiscal year, the slow economic recovery and less audit collections contributed to a moderate decline in trucking receipts. Truck mileage tax receipts to date in 2003-04 are 0.8 percent below the comparable 2002-03 period. Fuel use tax receipts to date in 2003-04 are 14.1 percent above the comparable 2002-03 period due to higher fuel prices.

Based on collection experience to date, and the improved economic outlook (see Economic Backdrop section), highway use taxes will continue to grow in line with real growth in the economy for the rest of the State fiscal year. Net truck mileage tax receipts are projected at $113.2 million and fuel use tax receipts at $29.1 million. Permit fees of $4.7 million reflect a non-peak triennial renewal year.

2004-05 Projections

Total net All Funds receipts are projected to be $151.9 million, an increase of $4.9 million, or 3.3 percent above 2003-04.

The base of the truck mileage tax (demand for trucking) is expected to increase by 3.7 percent as a result of the improving economy. Net truck mileage tax receipts are estimated at $117.4 million. Due to the effect of increased fuel prices, the sales tax component of the fuel use tax is estimated to increase by 2.1 percent. As a result, fuel use tax receipts are expected to grow to $30.3 million. Permit fees of $4.2 million reflect a non-peak triennial renewal year.

General Fund

Since 1994-95, no highway use tax receipts have been deposited in the General Fund.

Other Funds

The Dedicated Highway and Bridge Trust Fund receives all highway use tax receipts.

RECEIPTS BY FUND TYPE

HIGHWAY USE TAX RECEIPTS
(millions of dollars)

	Gross General Fund	Refunds	Net General Fund	Special Revenue Funds	Gross Capital Projects Funds[1]	Refunds	Net Capital Projects Funds[1]	Debt Service Funds	All Funds Net Collections
	Actual								
1995-96	0	0	0	0	174	4	170	0	170
1996-97	0	0	0	0	164	7	157	0	157
1997-98	0	0	0	0	168	3	165	0	165
1998-99	0	0	0	0	172	3	169	0	167
1999-2000	0	0	0	0	152	2	150	0	150
2000-01	0	0	0	0	157	2	155	0	155
2001-02	0	0	0	0	150	2	148	0	148
2002-03	0	0	0	0	149	2	147	0	147
	Estimated								
2003-04	0	0	0	0	149	2	147	0	147
2004-05	0	0	0	0	154	2	152	0	152

[1] Dedicated Highway and Bridge Trust Fund

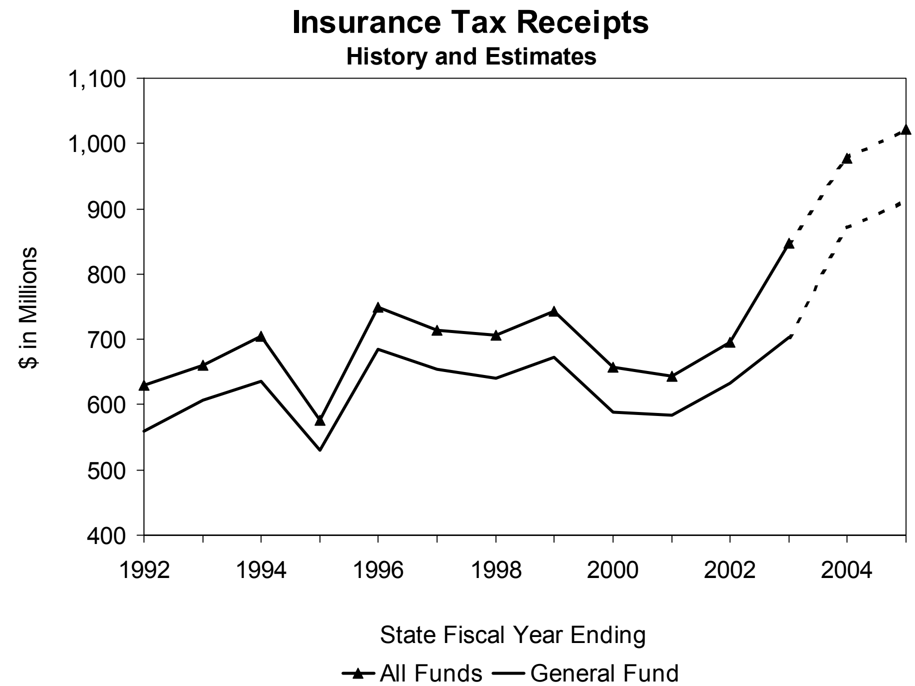
INSURANCE TAXES

SUMMARY

In 2003-04, All Funds collections from insurance taxes are estimated to be $977.0 million. This is an increase of $201 million, or 26.0 percent from the prior year, resulting mainly from the re-structuring of the insurance tax in 2003.

In 2004-05, All Funds collections from insurance taxes are projected to be $1,021 million. This is an increase of $44 million, or 4.5 percent, compared to 2003-04. Collections will continue to be affected by the tax law changes enacted with the 2003-04 Budget as well as overall industry trends.

Legislation proposed with this Budget would extend the Metropolitan Transportation Authority (MTA) surcharge for four years, until 2009. This would preserve current revenues.



DESCRIPTION

Tax Base and Rate

Under Article 33 of the Tax Law and the Insurance Law, the State collects taxes from insurance corporations, insurance brokers and certain insureds for the privilege of doing business or otherwise exercising a corporate franchise in New York. The Tax Department's Insurance Franchise Tax Study File contains the most recent data available on the tax liability of these taxpayers under Article 33 of the Tax Law. The most current liability information is for the 2000 tax year.

Tax Rate on Non-Life Insurers

Tax law changes enacted in 2003 now require non-life insurance companies to pay a premiums-based tax. For tax years beginning on or after January 1, 2003, non-life insurance corporations are subject to a franchise tax based solely on gross direct premiums, less return premiums. These premiums are taxed at the rate of 2.0 percent, except non-life accident and health premiums, which are taxed at the rate of 1.75 percent. The $250 minimum tax imposed is still applicable to non-life insurers.

Tax Rate on Life Insurers

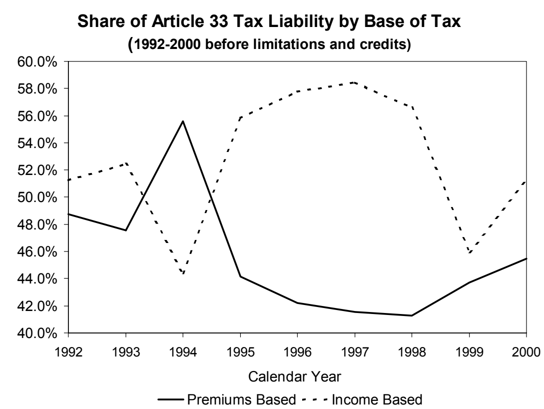
The recent law changes also impose a different tax structure on life insurers. The franchise tax on life insurers has two components. The first component is a franchise tax that is computed under four alternative bases, with tax due based on the maximum of the four alternative bases and rates described in the table below. In addition, there is a 0.08 percent tax rate applied to subsidiary capital allocated to New York.

RATES FOR THE NET INCOME COMPONENT OF THE FRANCHISE TAX ON LIFE INSURERS BY TYPE OF BASE

Base	Rate
Allocated entire net income	7.5 percent
Allocated business and investment capital	1.6 mills for each dollar
Allocated income and officers' salaries	9.0 percent
Minimum tax	$250

Tax is allocated to New York under the entire net income base (ENI) by a formula, which apportions ENI based on weighted ratios of premiums (with a weight of nine) and wages (with a weight of one), earned or paid in New York, to total premiums and total wages for the tax year for all employees.

The second component is an additional franchise tax on gross premiums, less refunded premiums, written on risks located or resident in New York. This tax is added to the highest of the alternatives from the net income base. The tax rate on net income is 0.7 percent.



A maximum and a minimum tax limitation are computed based on net premiums. Life insurers determine their maximum limitation by multiplying net premiums by 2.0 percent. As of January 1, 2003, life insurers also determine a minimum limitation of 1.5 percent of net premiums.

Generally, taxpayers with tax liability that exceeds the limitation may not reduce their liability with tax credits to a level below the limitation. However, taxpayers may use Empire Zone and Zone Equivalent Area tax credits to reduce their tax liability below the limitation.

Other Tax Rates Imposed on Insurers

In addition, Chapter 190 of the Laws of 1990 established a tax of 3.6 percent of premiums on independently procured insurance under Article 33-A of the Tax Law. This tax is imposed on any individual, corporation or other entity purchasing or renewing an insurance contract covering certain property and casualty risks located in New York from an insurer not authorized to transact business in New York under a certificate of authority from the Superintendent of the Insurance Department.

The Insurance Law also imposes a premiums tax on a licensed excess lines insurance broker when a policy covering a New York risk is procured through such broker from an unauthorized insurer (an unauthorized insurer is an insurer not authorized to do business in New York). Transactions involving a licensed excess lines broker and an insurer not authorized to do business in New York are permissible under limited circumstances delineated in Article 21 of the Insurance Law. The tax is imposed at a rate of 3.6 percent of premiums covering risks located in New York.

Furthermore, those Article 33 taxpayers doing business in the Metropolitan Commuter Transportation District (MCTD), which includes the counties of New York, Bronx, Kings, Queens, Richmond, Dutchess, Nassau, Orange, Putnam, Rockland, Suffolk and Westchester, are subject to a temporary 17 percent surcharge on their tax liability attributable to the MCTD area.

Administration

The Insurance Law authorizes the Superintendent of Insurance to assess and collect retaliatory taxes from a foreign insurance corporation when the overall tax rate imposed by its home jurisdiction on New York companies exceeds the comparable tax rate imposed by New York on such foreign insurance companies.

Retaliatory taxes have been utilized by the states since the nineteenth century to ensure a measure of fairness in the interstate taxation of insurance corporations. Retaliatory taxes deter other states from discriminating against foreign corporations and effectively require states with a domestic insurance industry to maintain an overall tax rate on insurance corporations that is generally consistent with other states.

Nevertheless, there are a variety of mechanisms for taxing insurance corporations throughout the states, and differences in overall tax rates among the states are inevitable. New York provides an additional measure of protection for its domestic insurance industry by allowing domestic corporations to claim a credit under Article 33 of the Tax Law for 90 percent of the retaliatory taxes legally required to be paid to other states.

Additionally, receipts from the 17 percent temporary business tax surcharge on tax liability within the MCTD region are deposited in a special revenue fund, the Mass Transportation Operating Assistance Fund (MTOAF), dedicated to mass transit assistance in the New York metropolitan region.

Tax Expenditures

Article 33 taxpayers are eligible for several targeted tax credits, including the certified capital companies (CAPCOs) credit, the investment tax credit (ITC), the long-term care insurance credit, and the Empire Zones credits. The table below lists the major tax credits available under Article 33.

Subject	Description
Retaliatory Tax Credit	Allows a credit up to 90 percent of retaliatory taxes paid to other states by New York domiciled or organized insurers.
Fire Insurance Tax Credit	Allows a credit for taxes paid on certain fire insurance premiums.
Investment in Certified Capital Companies Tax Credit	Equals 100 percent of the amount invested in CAPCOs for taxable years beginning after 1998. The credit is claimed at 10 percent per year for ten years. There is a dollar cap on the investment proceeds eligible for the credit. The original statewide cap was $100 million set in 1998. It was increased to $130 million in 1999 and to $280 million in 2000.
Special Additional Mortgage Recording Tax (SAMRT)	Provides up to 100 percent of SAMRT paid. A carry forward is allowed.

Investment Tax Credit	Allows insurance taxpayers that are brokers/dealers in securities to claim a credit for equipment or buildings used in broker/dealer activity and in activities connected with broker/dealer operations.
Long-Term Care Insurance Credit	Creates a 10 percent credit for the cost of purchasing long-term care insurance as defined in the Insurance Law.
Empire Zones Program	Provides various tax incentives for insurers certified in Empire Zones. The enhanced benefits of this program include a tax credit on real property taxes paid, a tax reduction credit, and a sales and use tax exemption.

Furthermore, there are also several types of insurance contracts that are exempt from the franchise tax. These include, but are not limited to, annuity contracts and certain health insurance contracts for insureds aged 65 years and older as provided under section 4236 of the Insurance Law.

Certain corporations and other entities that provide insurance are exempt from State franchise taxes and the regional business surcharge. Non-profit medical expense indemnity corporations and other health service corporations, organized under Article 43 of the Insurance Law, are exempt from these State taxes. Health maintenance organizations (HMOs) are examples of such exempt entities.

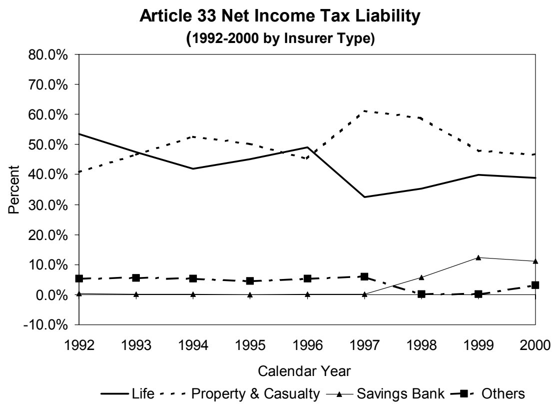
Significant Legislation

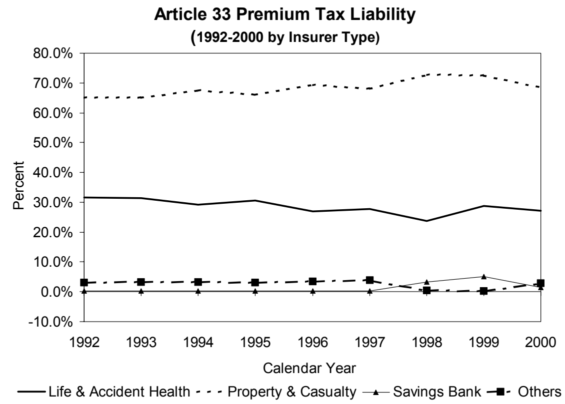
The significant statutory changes to this tax source since 1994 are summarized below.

Subject	Description	Effective Date
Legislation Enacted in 1994		
Temporary Business Tax Surcharge	Eliminated the surcharge over a three-year period.	January 1, 1994
Legislation Enacted in 1997		
Premium Tax Rate for Life Insurers	Reduced the premium tax rate from 0.8 percent to 0.7 percent.	January 1, 1998
Cap on Tax Liability	Reduced the limitation on tax liability for life insurers from 2.6 percent to 2.0 percent.	January 1, 1998
Credit for Investment in Certified Capital Companies (CAPCOs)	Credit changed to equal 100 percent of amount invested in CAPCO's for taxable years beginning after 1998. The rate was changed to equal 10 percent per year for ten years. The statewide cap was set at $100 million.	January 1, 1999
Captive Insurance Companies	Allowed the formation of captive insurance companies. Subject to a special premiums tax with a top rate of 0.4 percent or $5,000. This is in lieu of the premiums and income-based tax.	January 1, 1998
Legislation Enacted in 1999		
CAPCOs	The statewide cap was increased from $100 million to $130 million.	January 1, 2001
State Insurance Fund	Conformed the State Insurance Fund tax treatment to the regular insurance tax.	January 1, 2001
Entire Net Income (ENI) Tax Rate	Reduced ENI tax rate over a three-year period: • 8.5 percent for taxable years beginning after June 30, 2000 and before July 1, 2001. • 8.0 percent for taxable years beginning after June 30, 2001 and before July 1, 2002. • 7.5 percent for taxable years beginning on or after July 1, 2002.	June 30, 2000
Cap on Tax Liability	Reduced the limitation on tax liability for non-life insurers over a three-year period: • 2.4 percent for taxable years beginning after June 30, 2000 and before July 1, 2001. • 2.2 percent for taxable years beginning after June 30, 2001 and before July 1, 2002. • 2.0 percent for taxable years beginning on or after July 1, 2002.	June 30, 2000

Subject	Description	Effective Date
Legislation Enacted in 2000		
CAPCOs	The statewide cap was increased from $130 million to $280 million.	January 1, 2002
Investment Tax Credit	Insurance taxpayers that are brokers/dealers in securities may claim a credit for equipment or buildings used in broker/dealer activity and in activities connected with broker/dealer operations.	Available for property placed in service between January 1, 2002 and October 1, 2003.
Long-Term Care Insurance Credit	Created a 10 percent credit for cost of purchasing long-term care insurance as defined in the Insurance Law.	January 1, 2002
Empire Zones Program	Provided Qualified Empire Zone Enterprises (QEZE) tax incentives in Empire Zones. Transformed the current Economic Development Zones into virtual "tax-free" zones for certain businesses. The enhanced benefits of this program include a tax credit on real property taxes paid, tax reduction credit, and sales and use tax exemption.	January 1, 2001
Legislation Enacted in 2002		
Estimated Payments	Increased the first quarterly payment of estimated tax from 25 percent to 30 percent of the prior year's liability for non-life insurance companies under Article 33. Life insurance companies, which currently pay a first quarterly payment of 40 percent, are not affected. Taxpayers whose prior year's liability exceeds $100,000 are affected. Taxpayers whose prior year's liability is between $1,000 and $100,000 will continue to make a first quarterly payment of 25 percent of the prior year's liability. Sunsets for tax years beginning on or after January 1, 2006, and expires January 1, 2007.	January 1, 2003
Empire Zones Program	Amended to clarify certain provisions and implement new components for several credit calculations.	Various
Legislation Enacted in 2003		
Insurance Tax Structure	Changed the tax base for insurance taxpayers as follows: • Life and Health insurance taxpayers covering life and accident/health premiums are taxed on the four tax bases and are now subject to a minimum tax of 1.5 percent of premiums. • Non-life insurers covering accident & health premiums are subject to tax on 1.75 percent of premiums. • All other non-life insurers are subject to tax on 2.0 percent of premiums.	January 1, 2003
Modification for Decoupling from Federal Bonus Depreciation	Taxpayers must make modifications to Federal taxable income for property placed in service on or after June 1, 2003 that qualified for the special bonus depreciation allowance allowed by the Federal Job Creation and Worker Assistance Act of 2002 and the Jobs and Growth Tax Relief Reconciliation Act of 2003. The modifications do not apply to qualified resurgence zone property or qualified New York Liberty Zone property.	2003
Intangible Holding Companies	Taxpayers are required to modify Federal taxable income relating to certain royalty and interest payments made with respect to the use of intangible property by related members or royalty and interest payments received from related members.	January 1, 2003
Superfund-Brownfield Credits	Created tax incentives for the redevelopment of brownfields through three tax credits: a redevelopment tax credit, a real property tax credit, and an environmental remediation insurance credit. There are three components in the redevelopment tax credit: a site preparation component, a tangible property component, and an onsite groundwater remediation component.	April 1, 2005

TAX LIABILITY





Property and Casualty Companies

The property and casualty sector is the largest sector of the industry and typically accounts for over half of the State's insurance tax collections. In 2003, property and casualty companies experienced an upturn in premium rates reflecting strong demand for industry products. The five largest lines of business under property and casualty sector are automobile, workers' compensation, commercial multi-peril, general liability, and homeowners' multi-peril. In 2002, these lines accounted for more than 80 percent of premiums. The table below reports actual property and casualty premiums and growth from 1996 through 2002 for New York State. The large premiums growth in 2002 reflects the tight demand conditions, particularly in the automobile and general liability lines of insurance.

PROPERTY AND CASUALTY INSURANCE PREMIUMS
NEW YORK CALENDAR YEAR
(millions of dollars/percent)

Lines of Insurance	1996	1997	1998	1999	2000	2001	2002
Automobile	9,466	9,490	9,631	9,594	9,664	10,773	11,910
percent change	*6.20*	*0.26*	*1.49*	*(0.38)*	*0.73*	*11.48*	*10.55*
Workers' Compensation	3,121	2,725	2,686	2,725	3,154	3,282	3,412
percent change	*(14.49)*	*(12.70)*	*(1.41)*	*1.44*	*15.74*	*4.06*	*3.96*
Commercial Multi-Peril	2,097	2,031	2,071	2,002	2,085	2,178	2,680
percent change	*(1.96)*	*(3.15)*	*1.99*	*(3.33)*	*4.15*	*4.46*	*23.05*
General Liability	1,851	2,091	2,734	1,825	2,148	2,455	3,319
percent change	*(0.11)*	*12.99*	*30.90*	*(33.25)*	*17.70*	*14.29*	*35.19*
Homeowners' Multi-Peril	2,053	2,133	2,181	2,230	2,326	2,469	2,661
percent change	*4.43*	*3.91*	*2.33*	*2.25*	*4.30*	*6.15*	*7.78*
Other	3,574	3,620	3,641	3,635	3,720	4,476	5,164
percent change	*0.20*	*1.29*	*0.61*	*(1.53)*	*2.34*	*20.32*	*15.37*
TOTAL P/C PREMIUMS	22,162	22,090	22,945	22,011	23,098	25,808	29,146
Annual Increase/Decrease							
percent change	*0.34*	*(0.32)*	*3.87*	*(4.07)*	*4.94*	*11.73*	*12.93*

Net premiums for property and casualty companies overall grew by 12.9 percent in 2002. This upward trend is expected to continue through 2003. However, as more companies are attracted to the market, we expect an easing of price increases in 2004 and after.

The industry is facing a threat of costly asbestos claims for which it may be under-reserved. The ultimate liability for asbestos-related losses could approach $200 billion, with the U.S. insurance industry estimating their responsibility at $55 billion to $65 billion of that total.

Life and Health Companies

Life and health insurance is the second largest sector of the industry and represents approximately a third of the State's insurance tax collections. Tax collections on premiums for life and health companies, a mature and relatively slow growth industry, are expected to grow modestly throughout the forecast period.

Changes in the demographic and competitive landscape have forced insurers to contend simultaneously with an aging population's need to save for retirement and the ongoing competitive threat from banks and securities brokers. The struggling economy and weak equity market that persisted during early 2003 have intensified many of these challenges. However, uncertain economic times have led some consumers to the safety of these large, well-capitalized life insurers.

The Federal tax law changes, such as the Gramm-Leach-Bliley Act of 1999, which permits insurance companies, banks and brokerages to form consolidated companies offering a full range of financial services, have broken down the barriers that once separated the various sectors of the financial services industry. Banks and brokerage houses now sell more annuities than do life insurance agents. Life insurance agents, in turn, now sell investment-oriented products, including mutual funds.

PROPOSED LEGISLATION

Legislation proposed with this Budget would extend the MTA surcharge, until 2009.

RECEIPTS: ESTIMATES AND PROJECTIONS

All Funds

2003-04 Estimates

Net All Funds collections to date are $611 million, an increase of more than $145 million, or 31 percent above the comparable period in the prior fiscal year.

Total net All Funds receipts for 2003-04 are estimated to be $977 million, an increase of $201 million or 26.0 percent above last year. This increase is due mainly to the restructuring of the tax enacted in 2003 as well as industry demand and competitive pressures that have driven up premium volume. The Executive Budget proposal to extend the MTA surcharge for four years, until 2009, would maintain the existing annual revenue stream available to support transportation services in the Metropolitan Commuter Transportation District.

2004-05 Projections

Total net All Funds receipts are projected to be $1,021 million, an increase of $44 million, or 4.5 percent above 2003-04. The State fiscal year 2004-05 receipt gains are primarily due to modest growth in the life insurance and property and casualty lines of insurance.

The forecast of receipts from property and casualty insurers is based on an increase in premium liability of 6.4 percent in 2004, primarily resulting from continued growth in the automobile and general liability sectors.

A continuing significant risk to the forecast would be changes in the factors that impact overall premium growth and the economic performance of industry members. Given industry and economic conditions over the past few years, some companies have withdrawn from certain lines of business, such as homeowners and private passenger automobile.

Consolidations in this industry have continued, which reduced some competition and price pressure, allowing companies to increase premium rates. However, in recent months, economic factors have suggested that the economy is recovering from the economic slowdown that began shortly after the September 11, 2001 attacks (see Economic Backdrop section). As a result, renewed competition in the industry should reduce premium growth in 2004 and after.

The forecast assumes that the life and health sector will grow modestly through the 2004 tax year. Premium liability for this sector is projected to grow by approximately 1.0 percent. Sales of variable annuities are affected by the changes in the stock market. Major risks would be weather-related catastrophes, continuing asbestos claims, as well as a decline in investment income affecting investment portfolios and annuity sales.

General Fund

Based on collections to date, net collections for 2003-04 are estimated to be $872.3 million. This represents an increase of approximately $160 million from the prior year, mainly due to the premiums tax restructuring. The receipts estimate for 2003-04 includes an estimated $40 million in audit collections, $35 million in refunds and $40 million in insurance premiums tax collections.

For 2004-05, collections are estimated at $912 million. The majority of the increase for 2004-05 can be attributed to economic factors and growth in the number of premiums written. This estimate includes an estimated $40 million in audits, offset by $35 million in refunds. It also includes 40 million in insurance premiums tax collections. The table below provides the receipts estimate for 2003-04 and the forecast for 2004-05, as well as a history of receipts for 1995-96 through 2002-03.

Other Funds

A surcharge of 17 percent of tax liability attributed to the MCTD region is deposited in the Mass Transportation Operating Assistance Fund. The MTOAF is estimated at $105 million for 2003-04 and $109 million for 2004-05.

RECEIPTS BY FUND TYPE

INSURANCE TAX RECEIPTS
(millions of dollars)

	Gross General Fund	Refunds	Net General Fund	Gross Special Revenue Funds	Refunds	Net Special Revenue Funds[1]	All Funds Net Collections
				Actual			
1995-96	714	29	685	68	4	64	749
1996-97	682	29	653	68	8	60	713
1997-98	673	32	641	69	3	66	707
1998-99	718	45	673	76	6	70	743
1999-2000	634	45	589	79	10	69	658
2000-01	626	42	584	66	6	60	644
2001-02	667	34	633	81	18	63	696
2002-03	724	20	704	82	10	72	776
				Estimated			
2003-04	907	35	872	115	10	105	977
2004-05	947	35	912	119	10	109	1,021

[1] Mass Transportation Operating Assistance Fund

MOTOR FUEL TAX

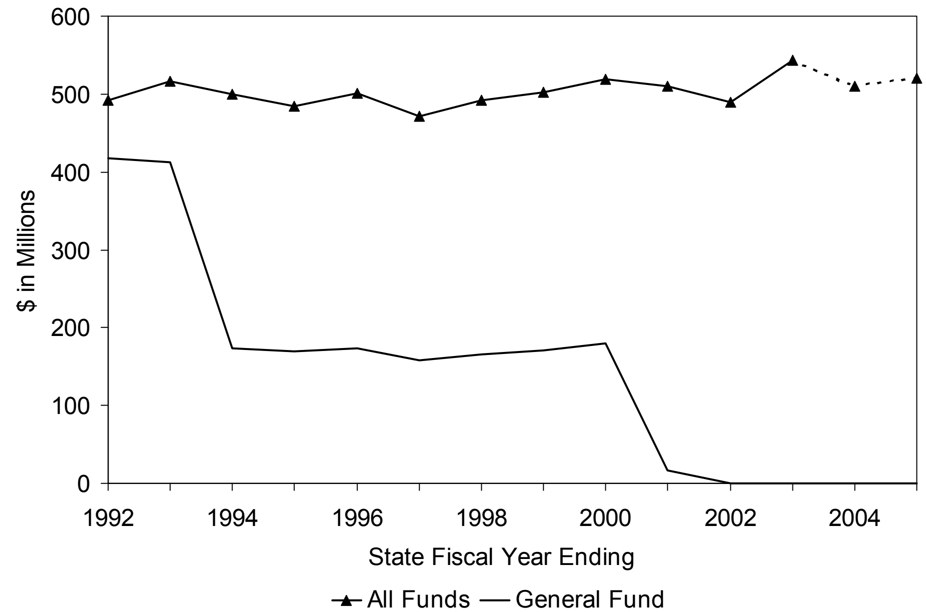
SUMMARY

In 2003-04, All Funds collections from the motor fuel tax are estimated to be $507.7 million. This is a decrease of $36.1 million, or 6.6 percent, from the prior year.

In 2004-05, All Funds collections from the motor fuel tax are projected to be $517.9 million. This is an increase of $10.2 million, or 2 percent, compared with 2003-04.

Legislation proposed with this Budget would postpone implementation of regulations related to taxation of sales on Native American lands and authorizes the State to execute agreements with Native American nations regarding product prices and taxes.

Motor Fuel Tax Receipts
History and Estimates



DESCRIPTION

Tax Base and Rate

Motor fuel and diesel motor fuel taxes are imposed by Article 12-A of the Tax Law upon the sale, generally for highway use, of gasoline and diesel fuel, respectively. The rate of tax imposed on each gallon of gasoline and diesel fuel is eight cents. The motor fuel tax is levied primarily on fuel used in motor vehicles operating on the public highways of the State or in recreational motorboats operating on the State's waterways. Exemptions, credits and refunds are allowed for certain other uses of gasoline and diesel motor fuel.

Administration

Although the motor fuel tax is imposed on the ultimate consumer of the fuel, the tax is remitted upon importation into New York. This tax-on-first-import system is designed to reduce gasoline tax evasion, which has involved bootlegging from other states and successions of tax-free sales among "dummy" corporations masked by erroneous record keeping and reporting.

Since 1988, taxes on diesel motor fuel have been collected upon the first non-exempt sale in the State. Prior to that time, the diesel motor fuel tax was collected at the time of retail sale or use by a bulk user.

Chapter 55 of the Laws of 1992 requires accelerated remittance of the tax by taxpayers with annual liability of more than $5 million for motor fuel and petroleum business taxes (PBT) combined. These taxpayers should remit taxes electronically or by certified check by the third business day following the first 22 days of each month. Taxpayers can choose to make either a minimum payment of three-fourths of the comparable month's tax liability for the preceding year, or 90 percent of actual liability for the first 22 days. Taxes for the balance of the month are remitted on the twentieth of the following month.

Tax Expenditures

Exemptions from the motor fuel tax include:
- kerosene and crude oil;
- fuel not used in motor vehicles. "Motor vehicle" is defined as any vehicle propelled by power, except muscular power. However, vehicles such as boats (other than pleasure craft), road building machinery and tractors used exclusively for agricultural purposes are excluded from the definition of motor vehicles;
- fuel used in tanks of vehicles entering New York State;
- sales to state, local and Federal governments, the United Nations and qualifying Indian nations; and
- certain hospitals that qualify as exempt organizations under section 1116(a)(4) of the Tax Law.

Other exemptions apply only to the diesel motor fuel tax, including certain sales for heating purposes and sales of kero-jet fuel for use in airplanes.

Full and partial refunds and credits for tax paid are available for fuel used by:
- omnibus carriers or taxicabs;
- nonpublic school vehicle operators, exclusively for education-related purposes; and
- volunteer ambulance services.

Significant Legislation

The significant statutory changes for this tax source since 1994 are summarized below.

Subject	Description	Effective Date
Legislation Enacted in 1995		
Tax Liability	Reduced the diesel motor fuel tax from 10 cents to 8 cents per gallon.	January 1, 1996
Exemption	Provided an up-front exemption from the motor fuel excise tax for retail sales of aviation gasoline.	September 1, 1995
Legislation Enacted in 2003		
Native American Regulations	Required the Commissioner of Taxation and Finance to promulgate regulations requiring the taxation of motor fuel sold to non-Native Americans on Native American lands.	March 1, 2004

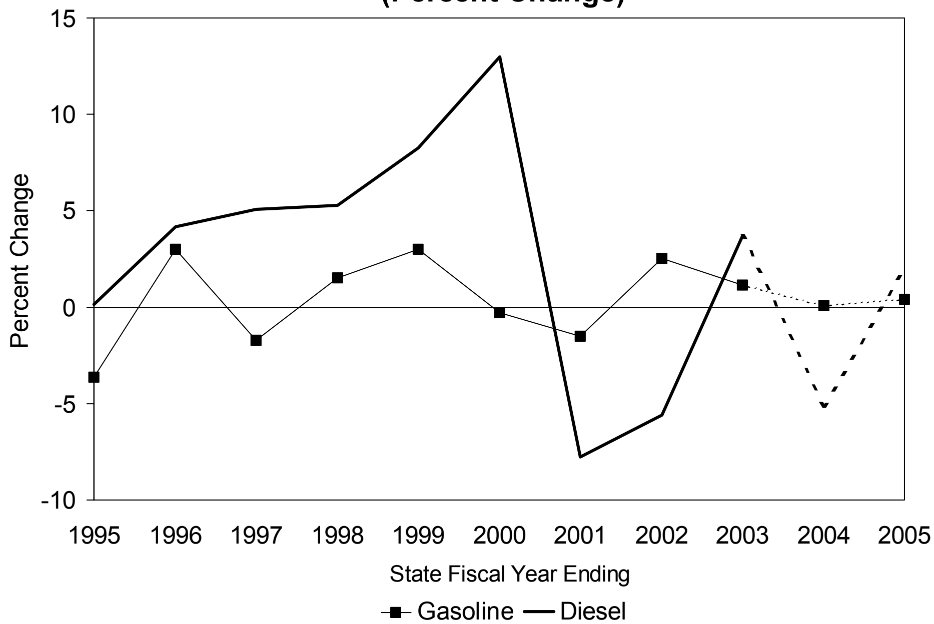
TAX LIABILITY

Motor Fuel tax collections are a function of the number of gallons of fuel imported into the State by distributors. Gallonage is determined in large part by: fuel prices, the amount of fuel held in inventories, the fuel efficiency of motor vehicles, and overall state economic performance.

Taxable Gallonage History

As the following graph illustrates, taxable diesel gallonage increased rapidly between 1995-96 and 1999-2000, reflecting robust demand for diesel fuel resulting from strong economic growth. The sharp decline in 2000-01 and the decline in 2001-02 diesel gallonage reflects, in part, higher prices for diesel fuel and the economic slowdown. Taxable diesel gallonage increased sharply in 2002-03 due to improved national economic growth. Taxable gasoline gallonage has grown more slowly, but increased sharply in 1998-99, partially due to low gasoline prices during that period. Taxable gasoline gallonage declined slightly in 1999-2000 and 2000-01 due in part to price increases, and increased in 2001-02 due to price declines. Gasoline gallonage declined slightly in 2002-03 due in part to price increases.

Gasoline and Diesel Reported Gallons
(Percent Change)



PROPOSED LEGISLATION

Legislation proposed with this Budget would postpone implementation of regulations related to taxation of sales on Native American lands and authorizes the State to execute agreements with Native American nations regarding product prices and taxes.

RECEIPTS: ESTIMATES AND PROJECTIONS

All Funds

2003-04 Estimates

Net All Funds collections to date are $384.7 million, a decrease of $33.6 million, or 8 percent below the comparable period in the prior fiscal year.

Total net All Funds receipts for 2003-04 are estimated to be $507.7 million, a decrease of $36.1 million, or 6.6 percent below last year. This large decline is due to a carry-in of $2.6 million of 2001-02 receipts into 2002-03 and a reallocation of petroleum business tax

(PBT) receipts to motor fuel. In 2001-02, motor fuel tax receipts were misallocated to PBT and in 2002-03 this misallocation was corrected by reversing the 2001-02 misallocation. These factors combined to overstate 2002-03 motor fuel tax receipts by $18.4 million.

In 2003-04, further corrections have been made to motor fuel tax receipts for allocation errors made within the tax in prior fiscal years by reclassifying diesel receipts as motor fuel receipts in May and July of 2003. As a result, diesel receipts to date appear artificially low and gasoline receipts to date appear artificially high. These adjustments limit the value of a discussion of year-over-year receipts changes by fuel type.

2004-05 Projections

Total net All Funds receipts are projected to be $517.9 million, an increase of $10.2 million, or 2 percent above 2003-04.

Increases in taxable gasoline and diesel gallonage are projected to be modest, consistent with improved economic conditions, but tempered by estimated increases in fuel prices.

Prospective agreements between Native American governments and the State based on legislation submitted with this Budget are expected to add $7 million to 2004-05 revenue.

General Fund

Motor fuel tax revenues are no longer deposited in the General Fund.

Other Funds

Since 2000, motor fuel tax revenues have been distributed by law to four funds: the Dedicated Highway and Bridge Trust Fund (DHBTF), the Dedicated Mass Transportation Trust Fund (DMTTF), the Emergency Highway Reconditioning and Preservation Fund, and the Emergency Highway Construction and Reconstruction Fund. Currently, all motor fuel receipts are deposited into the DHBTF and DMTTF. The fund distribution since 1993 is shown in the following table.

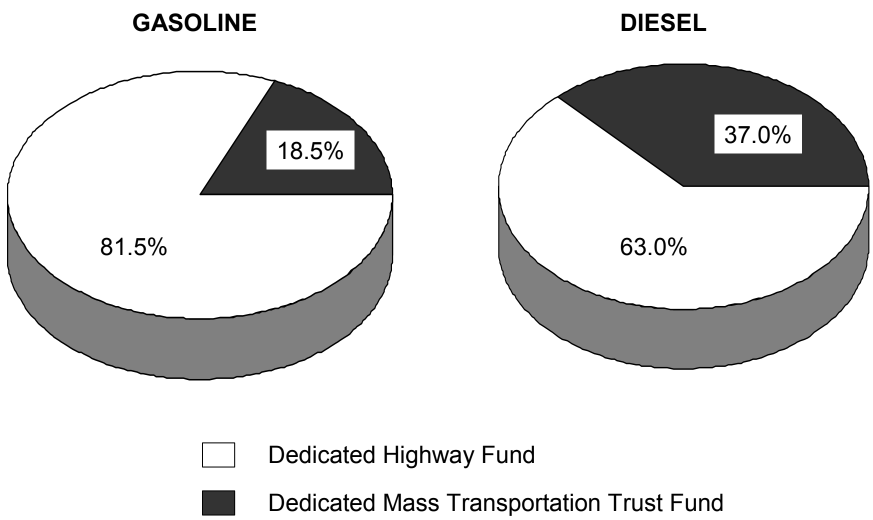
MOTOR FUEL TAX FUND DISTRIBUTION
(percent)

Effective Date	General Fund	DHBTF[1]	EHF[2]	DMTTF[3]
Prior to April 1, 1993				
Gasoline	78.1	0.0	21.9	0.0
Diesel	78.1	0.0	21.9	0.0
Prior to April 1, 2000				
Gasoline	28.1	50.0	21.9	0.0
Diesel	78.1	0.0	21.9	0.0
Prior to April 1, 2001				
Gasoline	0.0	67.7	21.9	10.4
Diesel	28.1	31.5	21.9	18.5
Prior to April 1, 2003				
Gasoline	0.0	67.7	21.9	10.4
Diesel	0.0	49.2	21.9	28.9
After April 1, 2003				
Gasoline	0.0	81.5	0.0	18.5
Diesel	0.0	63.0	0.0	37.0

[1] Dedicated Highway and Bridge Trust Fund.
[2] Emergency Highway Reconditioning and Preservation Fund and the Emergency Highway Construction and Reconstruction Fund.
[3] Dedicated Mass Transportation Trust Fund.

The percentage distributions of motor fuel tax revenue by fund and fuel type for State fiscal years 2003-04 and 2004-05 are displayed in the following pie charts.

Motor Fuel Tax Distributions by Fund
State Fiscal Years 2003-04 and 2004-05



RECEIPTS BY FUND TYPE

MOTOR FUEL TAX RECEIPTS
(millions of dollars)

	All Funds Gross Collections	Net General Fund	Net Special Revenue Funds[1]	Net Capital Projects Funds[2]	Net Debt Service Funds[3]	All Funds Refunds	All Funds Net Collections
	Actual						
1995-96	516	174	0	220	107	14	501
1996-97	484	158	0	211	103	13	472
1997-98	504	165	0	219	108	12	492
1998-99	512	171	0	221	110	10	502
1999-2000	534	180	0	225	113	15	519
2000-01	524	17	58	323	112	14	510
2001-02	503	0	62	321	107	13	489
2002-03	560	0	69	356	119	16	544
	Estimated						
2003-04	521	0	105	403	0	13	508
2004-05	531	0	107	411	0	13	518

[1] Dedicated Mass Transportation Trust Fund.
[2] Dedicated Highway and Bridge Trust Fund.
[3] Emergency Highway Reconditioning and Preservation Fund and Emergency Highway Construction and Reconstruction Fund.

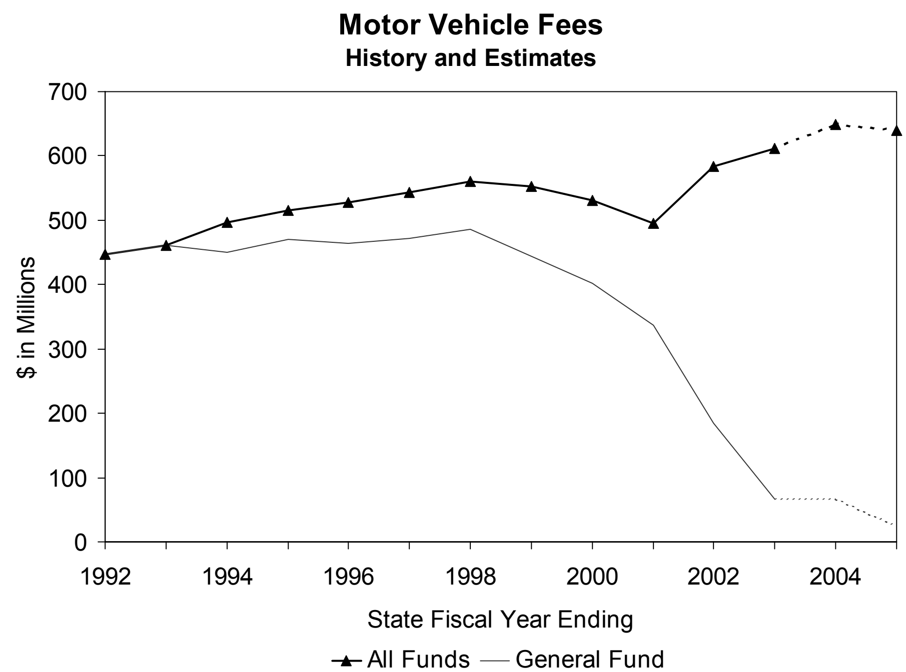
MOTOR VEHICLE FEES

SUMMARY

In 2003-04, All Funds collections from motor vehicle fees are estimated to be $649.5 million. This is an increase of $37.2 million, or 6.1 percent, from the prior year.

In 2004-05, All Funds collections from motor vehicle fees are projected to be $640 million. This is a decrease of $9.5 million, or 1.4 percent, compared with 2003-04.

No new legislation for these fees is proposed with this Budget.



DESCRIPTION

Fee Base

In general, motor vehicles, motorcycles, trailers, semitrailers, buses, and other types of vehicles operating in New York are required to be registered with the Department of Motor Vehicles. Vehicles owned by nonresidents and registered with a political jurisdiction outside the State are not usually required to be registered in New York.

Fee Schedules

Most vehicle registration fees in New York are based on weight. Two important exceptions are buses, which are charged according to seating capacity, and semitrailers, which are charged a flat fee. The main registration fees are as follows:

MAIN REGISTRATION FEES

Type of Vehicle	Weight of Vehicle	Annual Fee (dollars)
Passenger vehicle	Each 100 lbs. or major fraction thereof up to 3,500 lbs.	0.645
	Plus: for each 100 lbs or major fraction thereof above 3,500 lbs.	0.97
Passenger vehicle – minimum fee		10.35
Passenger vehicle – maximum fee		56.06
Passenger vehicle propelled by electricity		12.94
Auto truck and light delivery vehicle	Each 500 lbs. maximum gross weight or fraction thereof	2.88
Tractors (registered separately from semitrailers)	Each 100 lbs. maximum gross weight or fraction thereof	1.21
Trailers	Each 500 lbs. maximum gross weight or fraction thereof	4.31
Semitrailers – pre-1989 model year		23.00 per year
Semitrailers – model year 1989 or later		69.00 for period of 5.5 years to 6.5 years
Bus – seating capacity 15 to 20 passengers		59.80

The main categories of licensing fees are listed below.

MAIN LICENSING FEES

Type of License	Fee (dollars)
Initial application	10.00
Learner’s permit	2.50 – for each six months
Learner’s permit – commercial driver’s license	7.50 – for each six months
License renewal	2.50 – for each six months
License renewal – commercial driver’s license	7.50 – for each six months

Administration

Registration and licensing occur in person or by mail at the central and district offices of the Department of Motor Vehicles, and county clerks’ offices in most counties. The county clerks were historically compensated with a fixed portion of each fee, but, more recently, they receive a percentage of gross receipts.

COUNTY CLERKS’ RETENTION SCHEDULE

Type of Retention	Period
Fixed portion of each fee.	Until December 31, 1996
8.1 percent of gross receipts.	From January 1, 1997
9.3 percent of gross receipts.	From July 1, 1998
12.7 percent of gross receipts.	From April 1, 1999

Fee Exemptions

Certain vehicles registered in New York are exempt from registration fees. The exemptions include: vehicles owned by the State or municipalities; passenger vehicles owned by consular offices, provided reciprocity is granted; and vehicles owned and used for the transportation of animals by societies for the prevention of cruelty to animals. The amount of these exemptions is minimal.

Significant Legislation

The significant statutory changes to motor vehicle fees since 1994 are summarized below.

Subject	Description	Effective Date
Administrative Changes 1996		
Licenses	License renewal period extended to five years.	April 1, 1996
Legislation Enacted in 1997		
Licenses	Original license period extended to five years.	September 1, 1997
Motorcycles	Add $2.50 to annual fee for registration and $0.50 for each six months to license or permit and earmark both to Motorcycle Safety Fund.	January 1, 1998
Administrative Changes 1997		
Photo image fee	Photo image fee raised to $3.00.	April 1, 1997
Legislation Enacted in 1998		
Registration fees	Fees on passenger vehicle registration reduced 25 percent.	July 1, 1998
Administrative Changes in 2000		
License plates	Reissuance (January 2001-January 2003)	January 1, 2001
Licenses	License renewal period extended to eight years.	April 1, 2000
Administrative Changes in 2003		
Photo Image Fee	Photo image fee raised to $5.00.	February 1, 2003

PROPOSED LEGISLATION

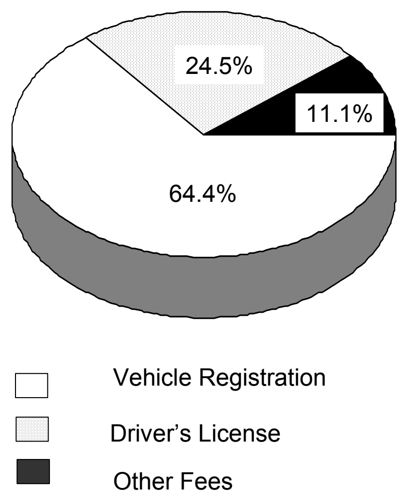
No new legislation for these fees is proposed with this Budget.

Fee Liability

The two main sources of motor vehicle fees are motor vehicle registrations and driver licensing.

Other fees, relating to the operation of motor vehicles in the State, yield relatively minor amounts of revenue. The pie chart below shows the shares of revenue from vehicle registrations, licenses, and other fees.

Motor Vehicle Fees Receipts by Sources
State Fiscal Year 2002-03



Vehicle registration and driver licensing fees are a function of the fee schedules, the number of licensed drivers and registered vehicles, and the number of years between license and vehicle registration renewals. Historically, these motor vehicle fees fluctuate little as a result of economic conditions. In general, collections change when fee and or renewal schedules change.

RECEIPTS: ESTIMATES AND PROJECTIONS

All Funds

2003-04 Estimates

Net All Funds collections to date are $496 million, an increase of $35.3 million, or 7.7 percent above the comparable period in the prior fiscal year.

Total net All Funds receipts for 2003-04 are estimated to be $649.5 million, an increase of $37.2 million, or 6.1 percent above last year. The estimate for net receipts from registrations is $417 million, and the estimate for receipts from licenses and other fees is $232.5 million. An estimated $22 million in refunds will result in estimated gross All Funds receipts from motor vehicle fees of $671.5 million.

The estimate reflects registration fee increases due to higher vehicle weights in the passenger car category and the extension of a driver's license renewal to eight years.

2004-05 Projections

Total net All Funds receipts are projected to be $640 million, a decrease of $9.5 million, or 1.4 percent below 2003-04.

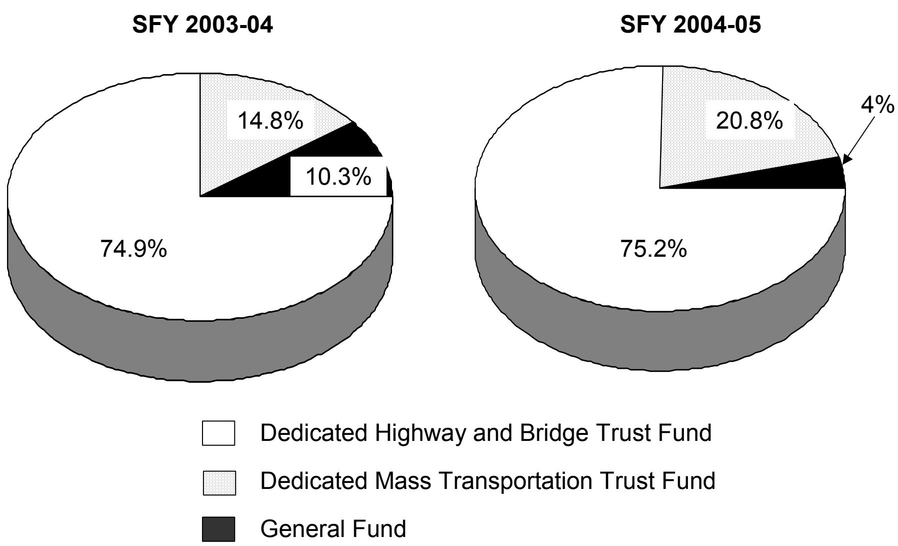
The projection for net receipts from registrations is $444 million and $196 million for receipts from licenses and other fees. A projected $21 million in refunds will result in estimated gross All Funds receipts from motor vehicle fees of $661 million.

The projection reflects continuing registration fee increases resulting from higher vehicle weights and a decline in receipts due to the declining impact of the eight-year renewal cycle for driver's licenses.

General Fund

As a result of shifting a portion of motor vehicle receipts to dedicated transportation related funds, there has been a reduction in General Fund receipts from this source. The pie chart below shows the estimated fund distribution from all sources of motor vehicle fees in State fiscal year 2003-04 and 2004-05.

Motor Vehicle Fees Distributions by Fund
State Fiscal Years 2003-04 and 2004-05



In State fiscal year 2003-04, the General Fund will receive an estimated $67.5 million in motor vehicle fees. In State fiscal year 2004-05, the General Fund will receive a projected $25.6 million.

Other Funds

A portion of motor vehicle fee receipts is distributed to the Dedicated Highway and Bridge Trust Fund. Since April 1, 1993, a percentage of registration fees has been earmarked to this fund. The percentage dedicated to the fund has been adjusted several times.

Pursuant to Chapter 63, Laws of 2000, in 2001-02 an additional 23.5 percent of registration fees was earmarked to (1) the Dedicated Highway and Bridge Trust Fund and (2) the Dedicated Mass Transportation Trust Fund. Of this additional dedication, 63 percent is allocated to highways and 37 percent to mass transportation.

Also pursuant to Chapter 63, Laws of 2000, beginning in 2002-03, an additional 31 percent of registration fees is earmarked to the same funds and in the same proportion as stated above. Thus, the total percentage of additional registration fees dedicated pursuant to Chapter 63, Laws of 2000, amounts to 54.5 percent. Since previous legislation had already earmarked 45.5 percent, all registration fees are earmarked to the two Trust Funds.

Pursuant to Chapter 63, Laws of 2000, in State Fiscal Year 2003-04, $152.7 million from non-registration fees is dedicated to the Dedicated Highway and Bridge Trust Fund. An additional $67.9 million from the same source is dedicated to the Trust Fund pool, of which 63 percent is dedicated to the Dedicated Highway and Bridge Trust Fund and 37 percent is dedicated to the Mass Transportation Trust Fund.

In State fiscal year 2003-04, the Dedicated Highway and Bridge Trust Fund will receive an estimated $485.8 million and the Dedicated Mass Transportation Trust Fund will receive an estimated $96.2 million.

In State fiscal year 2004-05, the Dedicated Highway and Bridge Trust Fund will receive a projected $481.2 million and the Dedicated Mass Transportation Trust Fund will receive a projected $133.2 million.

RECEIPTS BY FUND TYPE

MOTOR VEHICLE FEES
(millions of dollars)

	Gross General Fund	Refunds	Net General Fund	Special Revenue Funds[1]	Capital Projects Funds[2]	Debt Service Funds	All Funds Net Collections
	Actual						
1995-96	484	19	465	0	62	0	527
1996-97	494	22	472	0	71	0	543
1997-98	497	11	486	0	73	0	560
1998-99	438	14	444	0	108	0	552
1999-2000	419	18	401	0	130	0	531
2000-01	356	19	337	0	157	0	495
2001-02	208	23	185	28	371	0	583
2002-03	92	25	67	76	470	0	612
	Estimated						
2003-04	90	22	68	96	486	0	650
2004-05	47	21	26	133	481	0	640

[1] Dedicated Mass Transportation Transit Fund
[2] Dedicated Highway and Bridge Trust Fund

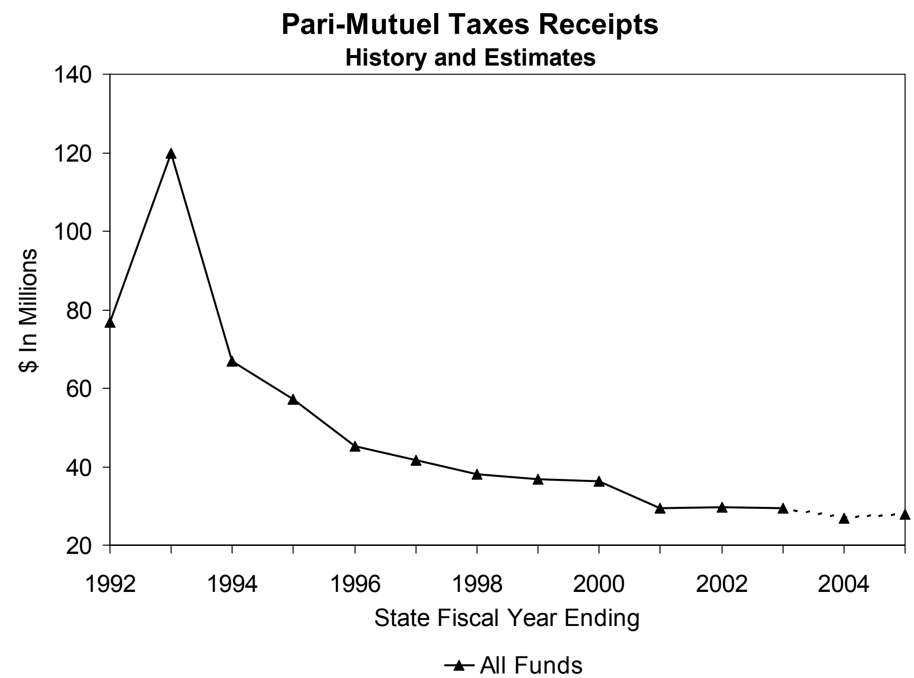
PARI-MUTUEL TAXES

SUMMARY

In 2003-04, All Funds collections from pari-mutuel taxes are estimated to be $27.4 million, a decrease of $2.1 million, or 7.1 percent, from the prior year.

In 2004-05 All Funds collections from pari-mutuel taxes are projected to be $28 million. This is an increase of $0.6 million, or 2.2 percent, compared with 2003-04. Collections will continue to be affected by the expected increase in simulcasts and declines in handle and attendance at racetracks.

No new legislation for these taxes is proposed with this Budget.



DESCRIPTION

Tax Base and Rate

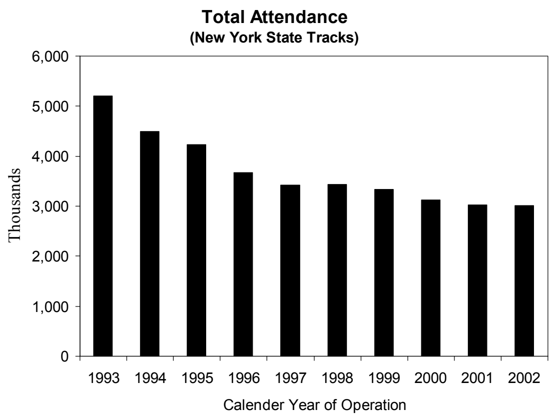
The State has levied taxes on pari-mutuel wagering activity conducted at horse racetracks, since 1940. Off-track betting (OTB) parlors were first authorized in 1970 and simulcasting was first authorized in 1984. Each racing association or corporation and Off Track Betting Corporation pays the State a portion of the commission (the "takeout") withheld from wagering pools (the "handle") as a tax for the privilege of conducting pari-mutuel wagering on horse races. There are numerous tax rates imposed on wagering on horse races. The rates vary depending upon the type of bet, whether the wager is on live racing, simulcasting or placed at an Off Track Betting Corporation. The average effective pari-mutuel tax rate is currently 1.05 percent of the handle.

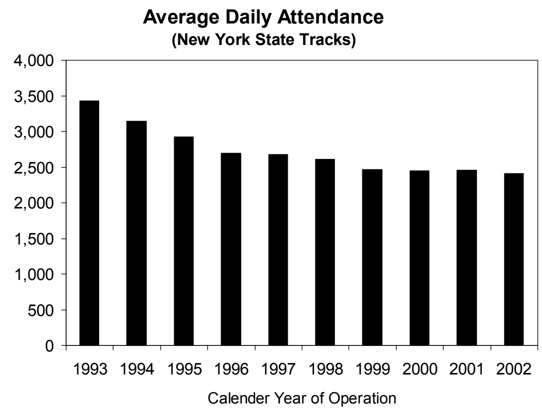
In an effort to support the New York agricultural and breeding industries, a portion of the takeout is allocated to the State's thoroughbred and standard bred (harness) horse breeding and development funds. During the calendar year 2002, $13.6 million and $7 million were allocated to the thoroughbred and harness funds, respectively.

With the increase in OTB activity and simulcasting over the last 20 years, off-track bets now account for 80 percent of the statewide handle. The expansion of OTBs has contributed, in part, to the corresponding decline in handle and attendance at racetracks.

The State has authorized higher takeouts to support capital improvements at non-New York Racing Association (NYRA) tracks and, more importantly, reduced its on-track tax rates by as much as 90 percent at thoroughbred and harness tracks.

To promote growth of the industry, the State has authorized the expansion of simulcasting at racetracks and OTB facilities, in-home simulcasting experiments, and telephone betting. In addition, the State lowered the tax rates on simulcast wagering, eliminated the State franchise fee on nonprofit racing associations, and reduced tax rates on NYRA bets.





Administration

The New York State Racing and Wagering Board has general jurisdiction over all horse racing activities and all pari-mutuel betting activities, both on-track and off-track, in the State and over the corporations, associations, and persons engaged in gaming activities. The racetracks and OTBs calculate the Pari-Mutuel tax owed to the State based upon the handle and the odds of the races ran, then remit the taxes as prescribed by law.

Significant Legislation

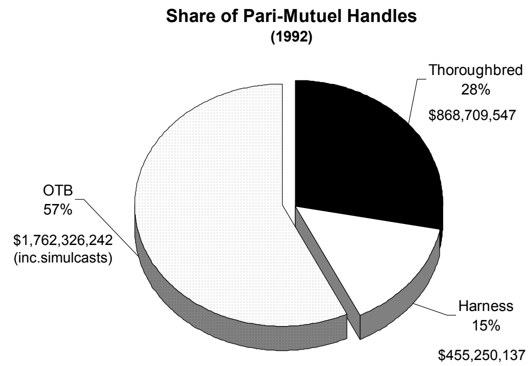
The significant statutory changes to this tax source since 1994 are summarized below.

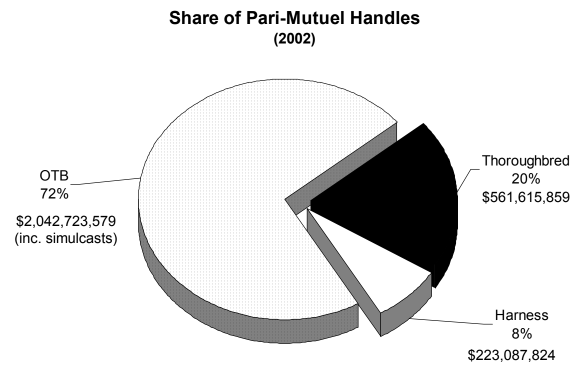
Subject	Description	Effective Date
Legislation Enacted in 1994		
Tax Rates	Lowered rates on all wagers at harness tracks and at the Finger Lakes Race Association to 0.5 percent and provided credits up to 0.4 percent based on OTB simulcast handle of respective track.	September 1, 1994
Expanded Betting	Authorized widespread in-home simulcasting experiments, simulcasts of flat racing bridging the time gap between the end of New York flat racing and the beginning of harness racing, and tripled the number of out-of-State harness track simulcasts.	July 6, 1994
Breakage	Allotted the State's share of all OTB breakage to horse breeding funds.	July 6, 1994

Subject	Description	Effective Date
Legislation Enacted in 1995		
Tax Rates	Lowered rate on regular bets (involving one horse) at NYRA from 5 percent to 4 percent and reduced the tax on NYRA wagers at OTBs: from 1.1 percent to 0.5 percent on regular and multiple (involving two horses) bets, and from 3.1 percent to 1.5 percent on exotic (involving three or more) bets.	June 1, 1995
Takeout	Increased the takeout on NYRA wagers involving two horses (multiple bet) from 17 percent to 20 percent, while lowering the takeout on NYRA wagers involving one horse (regular bet) from 17 percent to 15 percent.	June 1, 1995
Legislation Enacted in 1998		
Tax Rates	Established the tax rate on all simulcast races at 1.5 percent for the initial race of the day and at 1.0 percent for later races, if NYRA is running. If NYRA is not racing, the tax rate on these races are 1.0 percent and 0.5 percent, respectively. Extended authorizations for lower tax rates for on-track and off-track bets on NYRA through June 30, 2002.	January 1, 1998
Franchise Fee	Eliminated NYRA franchise fee.	January 1, 1998
Legislation Enacted in 1999		
Tax Rates	Cut the tax rate on all NYRA bets to 2.6 percent.	September 10, 1999
	Cut the tax rate on all NYRA bets to 1.6 percent.	April 1, 2001
Legislation Enacted in 2001		
Expanded Simulcasting	Lowered the takeout on NYRA races, decreased the percentage of takeout going to purses, allowed a "pick six" wager, provided two contemporaneous out-of-State simulcast signals during the Saratoga meeting, and provided a third out-of-State contemporaneous simulcast signal during the winter months and provided lower State tax rates for the additional simulcast racing.	June 12, 2001
Legislation Enacted in 2002		
Extended Expiring Laws	Extended to July 1, 2007, simulcasts for thoroughbred and harness racing, in-home simulcasts, telephone accounts and telephone wagering, simulcasts of out-of-State races, and current tax rates for off-track betting corporations.	June 17, 2002
	Extended the NYRA franchise to December 31, 2012, provided that Aqueduct racetrack commences video lottery gaming on April 1, 2003.	January 28, 2002
Legislation Enacted in 2003		
NYRA Franchise	Franchise extended to December 31, 2013, provided that VLTs are in operation at the Aqueduct raceway on or before March 1, 2004. If NYRA is not able to initiate VLT operation by that date, then the NYRA franchise will expire on December 31,2007.	January 29,2003
Regulatory fee	Instituted a regulatory fee to directly fund the State's regulation of racing, authorized tracks to set their own takeout rates within a narrow range, allowed unlimited simulcasts, and eliminated mandatory fund balances for telephone betting accounts.	May 16, 2003

TAX LIABILITY

The primary factors that affect pari-mutuel tax liability are: the handle and attendance at racetracks and OTB parlors, the number of simulcasts, and competition from other forms of gambling.





PROPOSED LEGISLATION

No new legislation for these taxes is proposed with this Budget.

RECEIPTS: ESTIMATES AND PROJECTIONS

All Funds

2003-04 Estimates

Net All Funds collections to date are $21.7 million, a decrease of $1.5 million, or 6.4 percent below the comparable period in the prior fiscal year.

Total net All Funds receipts for 2003-04 are estimated to be $27.4 million, a decrease of $2.1 million, or 7.1 percent below last year. Legislation, enacted on May 16, 2003, established a regulatory fee of 0.39 percent of all handle at Off Track Betting or racetrack facilities. This legislation also gave tracks the ability to change their takeout rate within a specified range, authorized unlimited simulcasts, and eliminated mandatory fund balances for telephone betting accounts. Despite the enactment of the new legislation, the anticipated increase in handle has yet to materialize. Recent concerns over the no-smoking laws that were passed in New York State in 2003, negative press from legal entanglements of NYRA, and terrorism fears may have contributed to the decline in the handle. The estimated total pari-mutuel handle for 2003-04 is expected to decline to approximately $2.5 billion.

The total thoroughbred on-track handle, including simulcasts, is estimated at $605 million, down 2.4 percent from last year. Total harness on track handle is estimated at $193 million. The handle at off-track betting corporations is estimated to decline to $1.7 billion, down 10 percent from the 2002-03 level.

Thoroughbred revenues, including simulcast receipts, are expected to decline by 2 percent from 2002-03 to $10.4 million. OTB receipts are estimated to decline by 10.5 percent to $16.2 million. Receipts from harness tracks are expected remain at $0.8 million. Total pari-mutuel tax receipts are estimated to be $27.4 million.

2004-05 Projections

Total net All Funds receipts are projected to be $28 million, an increase of $0.6 million, or 2.2 percent above 2003-04 estimates.

Total on-track thoroughbred receipts are projected to decline by 2 percent; a continuation of the downward trend in handle and attendance. An estimated thoroughbred handle of $600 million, including betting on out-of-State races, will produce $10.3 million in tax receipts.

The receipts for harness racing are expected to stay constant at $0.8 million; collections include $0.3 million in revenue from on-track wagers and $0.5 million from simulcasting.

The OTB handle is projected at $1.8 billion, generating tax receipts of $16.9 million, reflecting an estimated minor increase in handle due to recent legislation that authorized unlimited simulcasts and eliminated mandatory fund balances for telephone betting accounts.

RECEIPTS BY FUND TYPE

PARI-MUTUEL TAXES RECEIPTS
(thousands of dollars)

	General Fund			Special Revenue Funds	Capital Projects Funds	Debt Service Funds	All Funds Collections
	Flat	Harness	OTB				
	Actual						
1995-96	23,985	1,220	19,906	0	0	0	45,111
1996-97	20,417	1,075	20,124	0	0	0	41,616
1997-98	19,329	1,013	18,022	0	0	0	38,364
1998-99	18,643	923	17,355	0	0	0	36,921
1999-2000	17,218	795	18,356	0	0	0	36,369
2000-01	14,152	750	14,444	0	0	0	29,346
2001-02	10,500	800	18,300	0	0	0	29,600
2002-03	10,600	800	18,100	0	0	0	29,500
	Estimated						
2003-04	10,400	800	16,200	0	0	0	27,400
2004-05	10,300	800	16,900				28,000

PERSONAL INCOME TAX

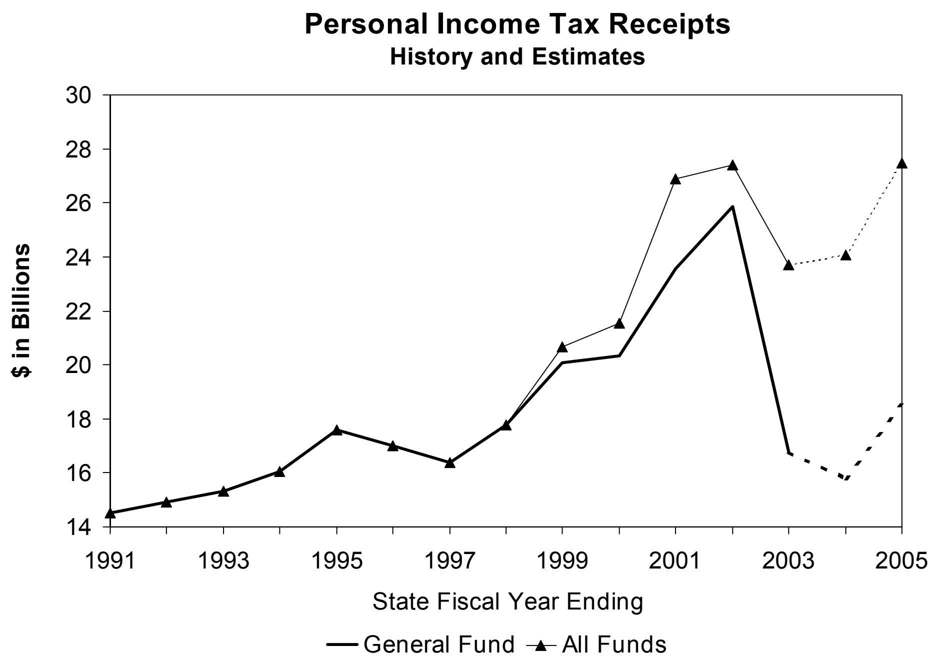
SUMMARY

In 2003-04, All Funds collections from the personal income tax are estimated to be $24,660 million. This is an increase of $2,012 million, or 8.9 percent, from the prior year, resulting from the emerging recovery from the economic weakness of the previous two years and the large temporary tax increase enacted in 2003.

In 2004-05, All Funds collections from the personal income tax are projected to be $26,769 million. This is an increase of $2,109 million, or 8.6 percent, compared with 2003-04. Collections will continue to be affected by the strengthening of the economy and the temporary tax increase.

Legislation proposed with this Budget will:

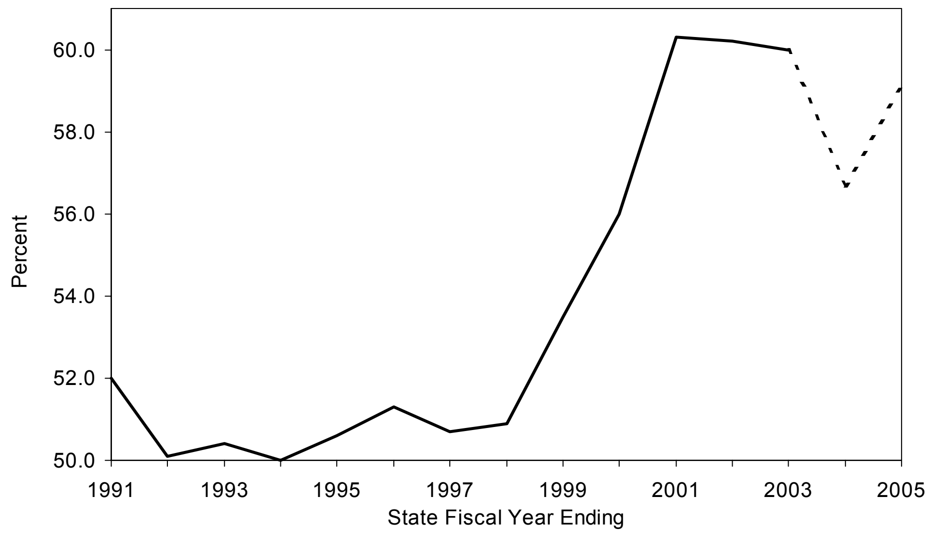
- create a State STAR credit;
- clarify prepayment hearing availability;
- include in New York source income, gains from sales of cooperative apartment stock for non-residents;
- extend the alternative fuels vehicle program;
- ease filing requirements for low-income taxpayers; and
- exempt Federal military pay from the personal income tax for New York State Guard members activated and deployed full-time in the New York War on Terror.



DESCRIPTION

The personal income tax is New York State's largest source of tax revenue. It is estimated that, during State fiscal years 2003-04 and 2004-05, the personal income tax will account for more than one-half of All Funds receipts.

PIT Receipts as Share of All Funds Tax Receipts



Note: Personal Income Tax (PIT) is defined as gross receipts less refunds

Tax Base

Over the last decade, New York has greatly simplified its tax structure by reducing the rates applied to income and increasing standard deductions. Since 1995, the overall income tax burden had been reduced by about 20 percent. The three-year temporary tax increase imposed last year is offsetting a portion of this reduction for the 2003 through 2005 tax years.

The State's tax structure adheres closely to the definitions of adjusted gross income and itemized deductions used for Federal personal income tax purposes, with certain modifications, such as: (1) the inclusion of investment income from debt instruments issued by other states and municipalities and the exclusion of income on certain Federal obligations; and (2) the exclusion of pension income received by Federal, New York State and local government employees, private pension and annuity income up to $20,000 ($40,000 for married couples filing jointly), and any Social Security income and refunds otherwise included in Federal adjusted gross income.

Beginning in 1991, the Federal limit on itemized deductions for taxpayers with Federal adjusted gross income (AGI) above a certain threshold is applied for State personal income tax purposes. This threshold amount, set at $100,000 ($50,000 for married couples filing separately) in 1991, was indexed for inflation. For 2003, the threshold is $139,500 ($69,750 for married couples filing separately). Allowable itemized deductions, except for medical expenses, casualty and theft losses, and interest payments, are reduced by the lower of either 3 percent of Federal adjusted gross income in excess of the threshold amount or 80 percent of allowable itemized deductions.

The Federal Economic Growth and Tax Relief Reconciliation Act of 2001 stipulates that the limitation on itemized deductions will be phased out over four years beginning in 2006. The limitation will be eliminated for 2010 and after.

Basic Tax Structure

For the 1989 through 1994 tax years, the tax was imposed at rates ranging from 4 percent to 7.875 percent on the taxable income of individuals, estates and trusts. For taxpayers with $100,000 or more of AGI, the benefit of the marginal tax rates in the lower brackets was recaptured through a supplementary mechanism in effect since 1991. In 1995, the State embarked on a major personal income tax cut program that was phased in over the three years 1995 through 1997. The table below includes the temporary tax changes for the 2003 through 2005 tax years. For liability years 2006 and after, the tax reverts back to the rates in effect between 1997 and 2002.

TABLE 1
PERSONAL INCOME TAX
TOP RATE, STANDARD DEDUCTIONS AND DEPENDENT EXEMPTIONS
1995 - 2005
(dollars)

	1995	1996	1997-2000	2001	2002	2003-2005
Top Rate	7.59375%	7.125%	6.85%	6.85%	6.85%	7.70%
Thresholds						
Married Filing Jointly	25,000	26,000	40,000	40,000	40,000	500,000
Single	12,500	13,000	20,000	20,000	20,000	500,000
Head of Household	19,000	17,000	30,000	30,000	30,000	500,000
Standard Deduction						
Married Filing Jointly	10,800	12,350	13,000	13,400	14,200	14,600
Single	6,600	7,400	7,500	7,500	7,500	7,500
Head of Household	8,150	10,000	10,500	10,500	10,500	10,500
Dependent Exemption	1,000	1,000	1,000	1,000	1,000	1,000

TABLE 2
CURRENT TAX SCHEDULES FOR 2004 LIABILITY YEAR
(dollars)

Married - Filing Jointly			Single			Head of Household		
Taxable Income	Tax	of Amt. Over	Taxable Income	Tax	of Amt. Over	Taxable Income	Tax	of Amt. Over
0 to 16,000	0 +4.00%	0	0 to 8,000	0 +4.00%	0	0 to 11,000	0 +4.00%	0
16,000 to 22,000	640 +4.50%	16,000	8,000 to 11,000	320 +4.50%	8,000	11,000 to 15,000	440 +4.50%	11,000
22,000 to 26,000	910 +5.25%	22,000	11,000 to 13,000	455 +5.25%	11,000	15,000 to 17,000	620 +5.25%	15,000
26,000 to 40,000	1,120 +5.90%	26,000	13,000 to 20,000	560 +5.90%	13,000	17,000 to 30,000	725 +5.90%	17,000
40,000 to 150,000	1,946 +6.85%	40,000	20,000 to 100,000	973 +6.85%	20,000	30,000 to 125,000	1,492 +6.85%	30,000
150,000 to 500,000	9,481 7.375%*	150,000	100,000 to 500,000	6.453 7.375%*	100,000	125,000 to 500,000	8,000 7.375%*	125,000
500,000 and over	35,294 7.70%	500,000	500,000 and over	35,953 7.70%	500,000	500,000 and over	35,656 7.70%	500,000

* In 2005, the percentage drops to 7.25 percent.
* In 2006, the schedule reverts to the pre-2003 rates.

Tax Expenditures

Tax expenditures are defined as features of the tax law that reduce the amount of a taxpayer's liability to the State by providing either economic incentives or tax relief to particular classes of persons or entities to achieve a public purpose. The personal income tax structure includes various exclusions, exemptions, tax credits, and other statutory devices designed to adjust State tax liability.

Credits

Current law authorizes a wide variety of credits against personal income tax liability. The major credits are:

Credit	Description
Earned Income Tax Credit (EITC)	Allowed at a rate of 7.5 percent of the Federal credit in 1994, 10 percent in 1995, and 20 percent in 1996 and later. Starting in 1996, the EITC is offset by the amount of the household credit. The EITC was raised to 22.5 percent of the Federal credit in 2000, 25 percent in 2001, 27.5 percent in 2002, and 30 percent in 2003 and after. The credit is fully refundable for New York residents whose credit amount exceeds tax liability. The 2001 Federal Economic Growth and Tax Relief Reconciliation Act provided marriage penalty relief for married taxpayers filing jointly by increasing the phase-out range for the credit beginning in 2002.
Household Credit	Permitted for single taxpayers in amounts declining from $75 to $20, as their household income rises to $28,000 and for married couples and heads of households, in amounts declining from $90 to $20, as their household income rises to $32,000. This latter category is also eligible for additional amounts based on the number of eligible exemptions and income level. Legislation in 1995 continued the credit permanently.
Child and Dependent Care Credit	Allowed at a rate of 20 percent or more of the comparable Federal credit. In 1997, the credit became refundable and equal to 60 percent of the Federal credit for those with incomes under $10,000, with a phase-down until it was 20 percent for incomes of $14,000 and above. In 1998, the percentage of the Federal credit increased to 100 percent for those with incomes less than $17,000, with this percentage gradually phasing down to 20 percent for those with incomes of $30,000 or more. For 1999, the phase-down from 100 percent to 20 percent began at incomes of $35,000 and ended at incomes of $50,000. For 2000 and later years, the credit as a share of the Federal credit equals 110 percent for incomes up to $25,000, phases down from 110 percent to 100 percent for incomes between $25,000 and $40,000, equals 100 percent for incomes between $40,000 and $50,000, phases down from 100 percent to 20 percent for incomes between $50,000 and $65,000, and equals 20 percent for incomes over $65,000. The credit is fully refundable for New York residents whose credit amount exceeds tax liability. Federal legislation passed in 2001 enriches the child and dependent care credit starting in 2003. This new legislation increases the maximum allowable expenses from $2,400 to $3,000 for one dependent ($4,800 to $6,000 for two or more dependents); the maximum credit rate from 30 percent to 35 percent; and the income at which the credit begins to phase down from $10,000 to $15,000.
College Tuition Tax Credit	Available as an alternative to the college tuition deduction, this refundable credit equals the applicable percentage of allowed tuition expenses multiplied by 4 percent. The credit will be at least the lesser of tuition paid or $200. It is being phased in over a four-year period with applicable percentages of allowed tuition expenses beginning at 25 percent in tax year 2001, 50 percent in 2002, 75 percent in tax year 2003, and 100 percent in 2004 and thereafter.
Real Property Tax Circuit Breaker Credit	Based on a more inclusive definition of income than that used generally in the income tax. For eligible taxpayers over the age of 65, the credit ranges downward from $375 as income rises to $18,000; for other taxpayers, the credit can be as high as $75.
Agricultural Property Tax Credit	Permitted for allowable school district property taxes paid by an eligible farmer on qualified agricultural property. Initially, a farmer had to derive at least two-thirds of his or her Federal gross income from farming to be eligible. If a farmer's qualified acreage exceeds the base acreage stipulated for that tax year, the credit is reduced to less than the full amount of school property taxes paid. Base acreage is 100 acres for 1997, and 250 acres in 1998 and later tax years. Legislation in 1997, applying to 1998 and later years, extended the credit to additional farmers by: (1) altering the eligibility test to require that farm income be at least two-thirds of gross income less $30,000; (2) reducing adjusted gross income by farm debt principal payments when determining the credit phase-out; and (3) making the credit available based on sales from maple syrup, cider, and farm wineries. In 1998, the rise in the base acreage level to 250 acres was accelerated into the 1998 tax year; prior to this legislation, the 1998 base acreage level had been set at 175 acres. In 1999, legislation expanded the farmer's credit to include agricultural land set aside or retired under a Federal supply management or soil conservation program.
Rehabilitation Credit for Historic Barns	Effective for tax years starting in 1997 and after. This credit equals 25 percent of a taxpayer's qualified rehabilitation expenses incurred in restoring a pre-1936 agricultural barn.

In addition, credits are allowed for investment in certain productive facilities, for investment in economic development zones, and for personal income taxes paid to other states. The Economic Development Zone Program for Qualified Empire Zone Enterprise (QEZEs) is discussed in more detail in the corporate franchise tax section. However, these credits have become an increasingly valuable benefit for partnerships, LLCs and S corporations. Finally, the excess deduction credit was allowed in 1995 only to ease the transition to the new tax structure for taxpayers who itemized their deductions and whose taxable income was less than $24,500 ($49,000 for married couples).

Significant Legislation

The significant statutory changes since 1994 are summarized below.

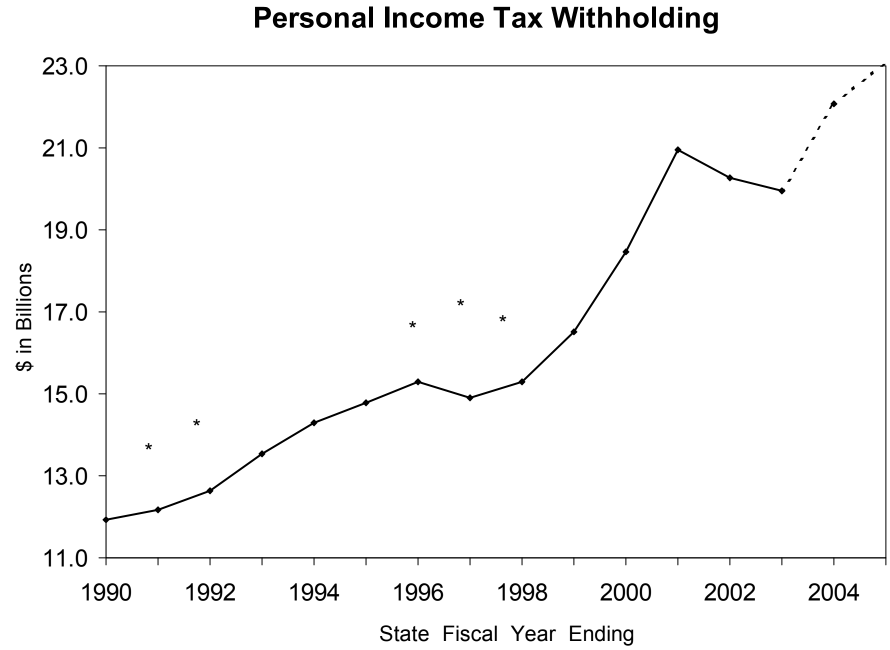
Subject	Description	Effective Date
Legislation Enacted in 1994		
Tax Reform Deferral	Continued deferral of the remainder of the tax cut enacted in the Tax Reform and Reduction Act of 1987.	1994 tax year
Earned Income Tax Credit	Created a State credit as a percentage of the Federal amount. The rates were set at 7.5 percent of the Federal credit in 1994, 10 percent in 1995, 15 percent in 1996, and 20 percent for 1997 and after.	1994 and after
Legislation Enacted in 1995		
Standard Deduction	Increased the standard deduction over three years.	1995 and after
Tax Rate Schedule	Reduced the top tax rate from 7.875 percent to 6.85 percent and raised bracket thresholds over three years.	1995 and after
Earned Income Tax Credit	Accelerated into 1996 from 1997 the credit of 20 percent of the Federal amount, but offset it by the household credit.	1996
Legislation Enacted in 1996		
Child and Dependent Care Credit	Increased the credit for taxpayers with adjusted gross incomes of less than $14,000 and made the credit refundable for residents beginning in 1996.	1996 and after
Agricultural Property Tax Credit	Created the credit.	1997 and after
Legislation Enacted in 1997		
Child and Dependent Care Credit	Increased credit to 100 percent of the Federal credit for incomes up to $17,000, phasing down to 20 percent for incomes of $30,000 or more.	1998 and after
Agricultural Property Tax Credit	Allowed $30,000 to be subtracted from income before calculating the percent of income from farming to qualify for the credit; subtracted principal payments on farm debt in calculation of the income to which the credit phase-out applies.	1998 and after
Solar Energy Credit	Created a credit for residential investment in solar electric generating equipment.	1998 and after
College Choice Tuition Savings Program	Created the New York State College Choice Tuition Savings Program.	1998 and after
Legislation Enacted in 1998		
Child and Dependent Care Credit	Increased the credit to 100 percent of the Federal credit for incomes up to $35,000, phasing down to 20 percent for incomes of $50,000 or more.	1999 and after
School Tax Relief Program (STAR)	Accelerated the fully effective senior citizens' school property tax exemption and began the deposit of a portion of personal income tax receipts into the STAR fund.	1998-99 school year
Legislation Enacted in 1999		
Earned Income Tax Credit	Increased the EITC to 22.5 percent of the Federal credit in 2000 and 25 percent of the Federal credit for subsequent tax years.	2000 and after
Agricultural Property Tax Credit	Expanded the credit to include land set aside or retired under a Federal supply management or soil conservation program. Also increased "base acreage" by acreage enrolled or participating in a Federal environmental conservation acreage reserve program.	2001 and after
Legislation Enacted in 2000		
Earned Income Tax Credit	Increased the EITC to 30 percent of the Federal credit over a two-year period, beginning in 2002. The expansion will first increase the EITC to 27.5 percent of the Federal credit in 2002 and then to 30 percent of the Federal credit in 2003 and after.	2002 and after

Subject	Description	Effective Date
Child and Dependent Care Credit	Increased the credit to 110 percent of the Federal credit for those with incomes up to $25,000, phased down from 110 percent to 100 percent for incomes between $25,000 and $40,000, equal to 100 percent for incomes between $40,000 and $50,000, phased down from 100 percent to 20 percent for incomes between $50,000 and $65,000, and equal to 20 percent for incomes greater than $65,000.	2000 and after
Long-Term Care Insurance Credit	Created a long-term care insurance credit equal to 10 percent of a taxpayer's long-term care insurance premium.	2002 and after
Marriage Penalty	Reduced the marriage penalty by increasing the standard deduction for taxpayers who are married filing jointly from $13,000 to $14,600 in three stages.	2001 and after
College Tuition Deduction/Credit	Created a deduction for the amount of tuition paid, up to $10,000, for attendance at a qualified institution of higher education. Also, the legislation provides the alternative of a refundable tax credit equal to 4 percent of such tuition. The credit will be at least the lesser of tuition paid or $200. The college tuition deduction will be implemented in four stages.	2001 and after
Petroleum Tank Credit	Created a two-year personal income tax credit of up to $500 for homeowners who remove and/or replace a residential fuel oil storage tank.	2001 and 2002
Alternative Energy Fuel Cell Credit	Created an alternative energy fuel cell credit equal to 20 percent of the cost of purchasing and installing a fuel cell to supply power to the taxpayer's home.	2003 and after
Legislation Enacted in 2003		
Three-Year Tax Increase	Created two new tax brackets intended to temporarily boost collections for 2003, 2004, and 2005. See Table 2 — Current Tax Schedules for details.	2003 to 2005

Withholding Changes

Various changes in tax rates, deductions and exemptions have been reflected in withholding tables as follows:

Effective Date	Feature	Changes
10/1/91	Rate Schedule	Changed for taxpayers with taxable wages in excess of $90,000 annually to account for the Federal limitation on itemized deductions and for the State tax table benefit recapture.
7/1/92	Rate Schedule	Changed for taxpayers with taxable wages in excess of $150,000 annually to account for the State tax table benefit recapture.
7/1/95	Deduction Allowance Rate Schedule	Increased to $5,650 for single individuals, $6,150 for married couples. Lowered maximum rate to 7.59 percent and reduced the number of tax brackets.
4/1/96	Deduction Allowance Rate Schedule	Increased to $6,300 for single individuals, $6,800 for married couples. Lowered maximum rate to 7 percent and broadened the wage brackets to which the rates apply.
1/1/97	Deduction Allowance Rate Schedule	Increased to $6,975 for single individuals, $7,475 for married couples. Lowered maximum rate to 6.85 percent and broadened the wage brackets to which the rates apply.
7/1/03	Rate Schedule	Raised maximum rate to 7.7 percent and added two new wage brackets.
1/1/04	Rate Schedule	Lowered rate for second highest bracket to 7.375 percent.



The above graph shows the history of withholding collections beginning 1989-90. The symbol "*" indicates the date of withholding table changes.

Refund Reserve Account Transactions

The personal income tax refund reserve account has been used to adjust fiscal-year collections for: (1) changes in withholding tables; (2) delays in implementation of withholding changes; and (3) accomplishing other State fiscal goals. The schedule shown in Table 3 traces the changes in the year-end balance of this account and the effect of those changes on reported fiscal-year collections. (Also, see Table 6 below for the effects of refund reserve transactions on the current and subsequent fiscal years.)

TABLE 3
MARCH 31 PERSONAL INCOME TAX REFUND RESERVE ACCOUNT BALANCES AND EFFECTS OF CHANGES ON REPORTED COLLECTIONS
(millions of dollars)

Year Ending March 31	Year End Balance	Change from Prior Year	Effect of Change in Year-End Balance on Reported General Fund Receipts
2003	627.4	(1,050.0)	Increased receipts by 1,050.0
2002	1,677.4	(1,840.0)	Increased receipts by 1,840.0
2001	3,517.4	(449.5)	Increased receipts by 449.5
2000	3,966.9	1,661.0	Decreased receipts by 1,661.0
1999	2,305.9	(86.3)	Increased receipts by 86.3
1998	2,392.2	530.4	Decreased receipts by 530.4
1997	1,861.8	1,183.5	Decreased receipts by 1,183.5
1996	678.4	400.4	Decreased receipts by 400.4
1995	278.0	(861.6)	Increased receipts by 861.6
1994	1,139.6	468.5	Decreased receipts by 468.5
1993	671.1	641.9	Decreased receipts by 641.9
1992	29.2	29.2	Decreased receipts by 29.2
1991	0.0	(48.6)	Increased receipts by 48.6

As part of the State's multi-year effort to end the Spring Borrowing through the Local Government Assistance Corporation (LGAC), State funds were deposited annually from 1993-94 through 1995-96 in the refund reserve account. The amounts deposited were $114 million in 1993-94, $136 million in 1994-95, and $271 million in 1995-96. Thereafter, no additional LGAC funds were deposited in the refund reserve account. At the end of each fiscal year, these funds are available to finance refunds issued at the start of the new fiscal year, but will be restored to the reserve by the end of that year.

Since 1994-95, when the EITC was created, additional funds have been deposited in the refund reserve account at the end of each fiscal year to pay for a portion of the cost of new tax reductions. Typically, an amount equal to one-quarter of a tax reduction's cost for a specific tax year has been deposited in the account on the following March 31. This practice reflects the sound fiscal policy of paying for a tax reduction in a timely fashion and provided extra reserves to pay additional refunds during April and May. As part of a multi-year strategy, these reserves were used to address the fiscal deficiencies caused by the September 11th attack and the national recession.

Table 4 shows the amount of reserves at the end of each fiscal year and the purposes for which the funds were reserved.

TABLE 4
PURPOSES OF MARCH 31 PERSONAL INCOME TAX REFUND RESERVE ACCOUNT BALANCES
(millions of dollars)

Date March 31 of	LGAC	Reserves for Tax Reductions [1]	Reserves for Other Purposes	Total
1996	521	32	125	678
1997	521	73	1,268	1,862
1998	521	90	1,781	2,392
1999	521	107	1,678	2,306
2000	521	125	3,321	3,967
2001	521	141	2,855	3,517
2002	521	195	961	1,677
2003	521	6[2]	100	627
2004 est.	521	47	636	1,204

[1] For EITC starting in 1995 (and subsequent increments), agricultural property tax credit starting in 1998, college choice tuition savings program starting in 1998, child care credit enhancements starting in 1999, petroleum tank credits, marriage penalty relief and college tuition deduction/credit starting in 2002, and the long-term care insurance and starting in 2003, and the State STAR credit starting in 2004.
[2] The 2002-03 Budget Agreement reduced the end of the year reserves by $250 million.

Timing of the Payment of Refunds

For many years, the payment of refunds during the final quarter of the State's fiscal year (i.e., the January-March period) had been explicitly modified to minimize potential year-end imbalances in the State's General Fund. This practice was possible because the statute only required that all refunds on timely filed claims (due no later than April 15, absent an approved request for an extension) be made by July 15 (i.e., within three months of the statutory due date) to avoid State liability for interest on late refunds. Effective since 1995, refunds must be paid within 45 days of the statutory due date to avoid State liability for interest. As has been administrative practice since 2001, refunds of $960 million will be paid during the period January through March 2004.

PROPOSED LEGISLATION

Legislation submitted with this Budget will:

- create a State STAR credit designed to protect the STAR benefit from the effects of inflation;

- clarify prepayment hearing availability for a taxpayer issued an original notice and demand;
- include in New York source income, gains from sales of cooperative apartment stock;
- extend the alternative fuels vehicle program;
- ease filing requirements for low-income taxpayers; and
- exempt Federal military pay from the personal income tax for New York State Guard members activated and deployed full-time in the New York War on Terror.

Components of Adjusted Gross Income and Estimated Tax Liability

Adjusted gross income (AGI), the income base used to determine personal income tax liability, includes the major components listed in Table 5.

TABLE 5
DISTRIBUTION OF THE MAJOR COMPONENTS
OF NEW YORK ADJUSTED GROSS INCOME (AGI)
(millions of dollars)

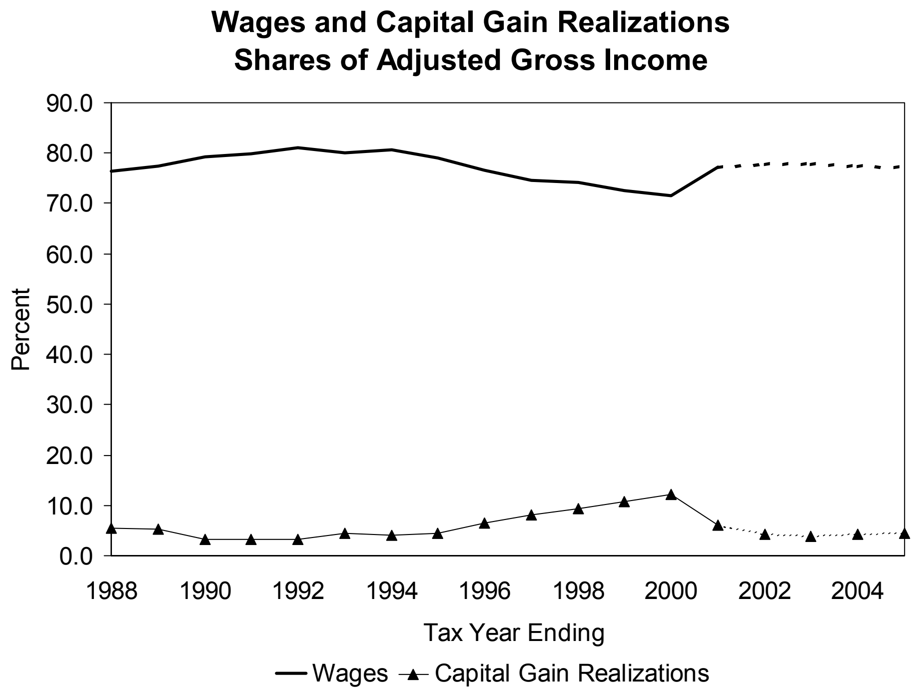
Component of Income	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004
	Actual							Estimated		
NYSAGI										
Amount	321,124	347,981	383,179	417,996	453,130	514,501	487,532	467,119	475,598	502,290
% Change	6.6	8.4	10.1	9.1	8.4	13.5	(5.2)	(4.2)	1.8	5.6
Wages										
Amount	253,551	266,334	285,919	309,614	328,851	368,177	376,158	363,933	370,432	389,169
% Change	4.4	5.0	7.4	8.3	6.2	12.0	2.2	(3.2)	1.8	5.1
Share of NYSAGI	79.0	76.5	74.6	74.1	72.6	71.6	77.2	77.9	77.9	77.5
Net Capital Gains										
Amount	14,086	22,441	31,563	38,929	48,330	62,302	29,451	19,582	18,312	20.974
% Change	17.1	59.3	40.7	23.3	24.1	28.9	(52.7)	(33.5)	(6.5)	14.5
Share of NYSAGI	4.4	6.4	8.2	9.3	10.7	12.1	6.0	4.2	3.9	4.2
Interest and Dividends										
Amount	22,680	23,534	24,652	24,807	25,299	30,290	26,507	24,016	23,386	24,003
% Change	15.5	3.8	4.8	0.6	2.0	19.7	(12.5)	(9.4)	(2.6)	2.6
Share of NYSAGI	7.1	6.8	6.4	5.9	5.6	5.9	5.4	5.1	4.9	4.8
Taxable Pension										
Amount	16,620	17,391	18,953	18,891	20,854	22,121	23,165	24,889	26,151	27,508
% Change	5.9	4.6	9.0	(0.3)	10.4	6.1	4.7	7.4	5.1	5.2
Share of NYSAGI	5.2	5.0	4.9	4.5	4.6	4.3	4.8	5.3	5.5	5.5
Net Business and Partnership Income										
Amount	25,868	31,425	35,288	37,142	42,035	44,004	45,191	46,357	49,569	53,015
% Change	31.5	21.5	12.3	5.3	13.2	4.7	2.7	2.6	6.9	7.0
Share of NYSAGI	8.1	9.0	9.2	8.9	9.3	8.6	9.3	9.9	10.4	10.6
All Other Incomes/ Adjustments [1]										
Amount	(11,680)	(13,142)	(13,195)	(11,387)	(12,239)	(12,392)	(12,940)	(11,658)	(12,252)	(12,379)
% Change	38.6	12.5	0.4	(13.7)	7.5	1.2	4.4	(9.9)	5.1	1.0

[1] Include alimony received, unemployment income, IRA income, and other incomes. This number is negative due to the Federal and New York adjustments to income, which together reduce final NYSAGI.

Strong performances in the financial sector in recent years caused a significant shift in the capital gains share of AGI. From 1994 to 2000, the share of capital gains in AGI tripled, from 4.0 percent to 12.1 percent. Over the same period, the share of wages in AGI decreased from 80.6 percent to 71.6 percent. Business and partnership income also posted strong growth between 1994 and 2000 and accounted for 8.6 percent of AGI in 2000. During the same period, the number of domestic limited partnerships (LPs), Limited Liability Companies

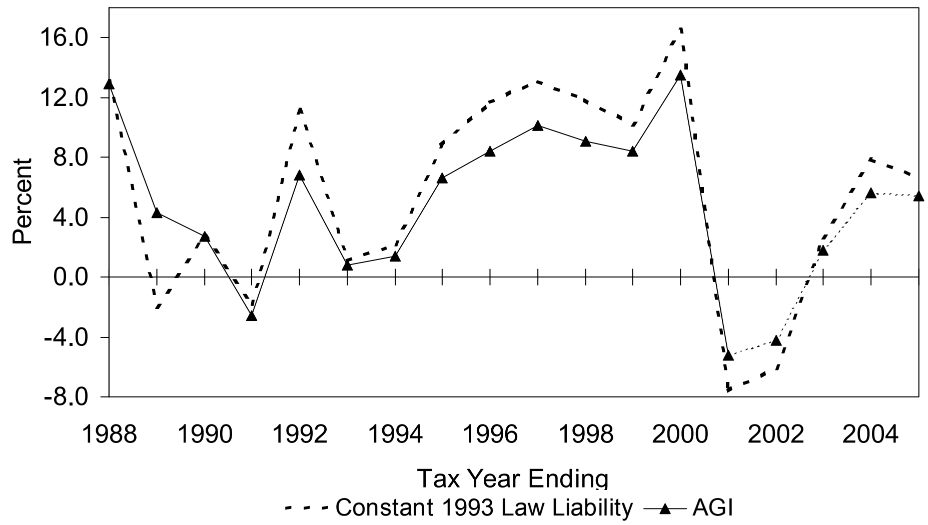
(LLCs) and Limited Liability Partnerships (LLPs) grew from approximately 4,000 to over 90,000. The AGI data demonstrate that much of the rapid growth in liability in the years before 2001 can be attributed to the large increases in realized capital gains and business income (see Economic Backdrop - AGI components).

With the bursting of the stock market bubble and the national recession, there has been a precipitous decline in investment related incomes (Table 5). Interest and dividends declined 12.5 percent in 2001 compared to a 19.7 percent increase in 2000. Net capital gain decreased close to 53 percent after growing 29 percent in 2000. As the accompanying chart illustrates, realized capital gains have also declined as a share of adjusted gross income.



The following graph illustrates the relationship between the growth rates of liability, measured over time on a constant law basis, and AGI. A change in AGI typically results in a larger relative change in liability (see Economic Backdrop section titled Sources of Volatility in the Income Base). This discrepancy is due, in part, to the volatility of net capital gains and partnership income (which tends to be concentrated among high-income taxpayers) and the interaction of income changes with a progressive rate schedule.

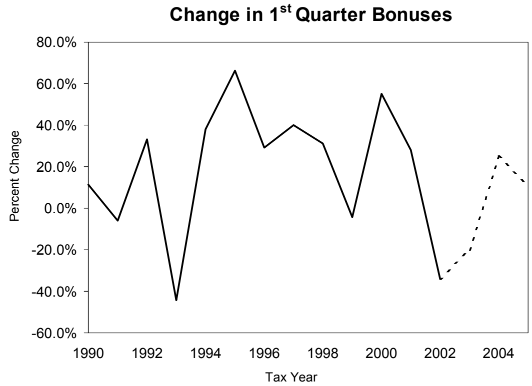
Constant 1993 Law Liability and AGI
Annual Growth Rates



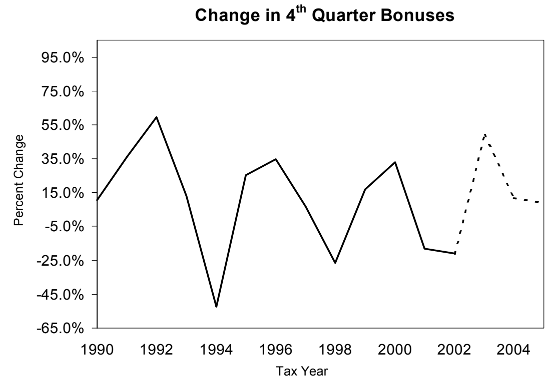
Changes in timing of year-end bonus payments also affect the AGI growth rate. It is estimated that bonuses in the financial and insurance sector represent more than half of the total bonuses paid out each year. The pattern of these bonus payments has shifted over the years from approximately 40 percent paid at the end of the calendar year, and 60 percent paid early in the following year to 30 percent and 70 percent respectively.

In May 2003, the State Legislature passed a personal income tax increase for the 2003, 2004 and 2005 tax years. Since withholding on 2003 wages could not be increased until July 2003, the Legislature required the withholding rate increase for that latter part of the year to be twice that required by the increase in rates. As a result, it is expected that a significant share of bonus payments for 2003 will be postponed until the beginning of 2004.

Change in 1st Quarter Bonuses



Change in 4th Quarter Bonuses



Prior to the World Trade Center disaster of September 11, 2001, an economic slowdown was already underway. The terrorist attacks shocked the struggling economy and pushed the nation into recession. New York State was more severely affected than the nation as a whole. (See Economic Backdrop section.) After an impressive growth rate of 13.5 percent in 2000, AGI declined 5.2 percent in 2001 and is estimated to have declined another 4.2 percent in 2002, due in large part to the recession. Such back-to-back AGI decreases are unprecedented in the history of the present State personal income tax system, which was established in 1960. The last time the State experienced a drop in AGI was in 1991, with a 2.6 percent decline. This decline was followed by a 6.8 percent increase in 1992.

The State economy has begun to emerge from recession and there has been resurgence in equity market growth and a return to financial sector profitability. As a result, a 1.8 percent AGI increase is projected for 2003 and 5.6 percent is estimated for 2004. (See Economic Backdrop section.)

2001 and 2002 Liability

Based on tax collections, total liability for 2001 was approximately $23.2 billion. Of this amount, $22.4 billion was accounted for by the nine million returns covered in the annual study of personal income tax returns prepared by the New York State Department of Taxation and Finance. The balance reflects liability received from fiduciary returns, late filed returns and other transactions not included in the annual study. The AGI amount in the tax study for 2001 was $488 billion, yielding an average effective tax rate of 4.6 percent. By contrast, AGI for 2000 was $514.5 billion and liability for that year was $24.5 billion, an effective rate of 4.76 percent. The 2001 decline in AGI and liability represents a reversal after several years of tremendous expansion in the State.

Reflecting continued poor economic conditions and the decline in stock market activity, AGI in 2002 is estimated to have declined to $467 billion, a 4.2 percent additional loss in the personal income tax revenue base. Wages and salaries are estimated to have decreased 3.2 percent, after a modest growth of 2.2 percent in 2001. The drop in wages reflect the drastic cuts in financial sector bonuses as a result of the weak investment banking performance in 2001 and 2002, as well as slow growth in non-bonus average wages and a decline in employment. (See the Economic Backdrop section for a detailed account of the recent declines in the taxable income base.)

Following considerable gains in the latter part of the 1990s, capital realizations dropped close to 53 percent in 2001, as a result of the collapse of the equity market bubble. It is estimated that taxable gains declined another 33.5 percent in 2002.

Interest and dividend income is estimated to have dropped 9.4 percent in 2002, following a 12.5 percent decrease the previous year. These declines reflect the several cuts in the federal fund rates by the Federal Reserve, and poor corporate dividend earnings. Business net income and income derived from partnerships and S corporations are expected to have experienced a 2.6 percent increase in 2002 after growing 4.7 percent in 2000 and 2.7 percent in 2001.

In total, estimated liability is projected to have declined 7.4 percent to $20.7 billion in 2002, an estimated loss of $1.7 billion in the base compared to 2001 and $3.8 billion compared to 2000, yielding an affective tax rate of 4.44 percent.

2003 AGI and Liability

In 2003, the State economy is expected to have begun improving and AGI is estimated to have increased by 1.8 percent. This increase translates into a total AGI of $475.6 billion, still considerably below the 2000 peak of $514.5 billion.

Wages and salaries are projected to have grown 1.8 percent. Capital gains realizations are expected to have decreased 6.5 percent, reflecting the fact that individuals are allowed to carry indefinitely into future tax years unclaimed capital losses from previous years.

Business net income and income derived from partnerships and S corporations are expected to have grown 6.9 percent.

Under current law, estimated liability is projected to have grown 8.2 percent to $22.4 billion, $1.7 billion more than 2002, signaling the turnaround in the State economy, as well as the temporary tax measures passed by the Legislature in May 2003, which are estimated to have increased liability by nearly $1.3 billion.

2004 AGI and Liability

In 2004, with the State economic recovery accelerating, AGI is projected to increase by 5.6 percent. This increase, however, still leaves the AGI level below its 2000 peak.

Wages and salaries are projected to grow 5.1 percent, reflecting in large part the bonuses paid early in 2004.

Interest and dividend income is estimated to grow 2.6 percent. Capital gains are expected to grow 14.5 percent, while incomes from businesses, partnerships and S corporations are projected to increase 7 percent.

Overall, under current law, estimated liability is expected to grow 8.6 percent to $24.4 billion, including a $1.4 billion increase due to the temporary tax measure passed by the Legislature for the 2004 tax year.

Tax Changes and Liability

The 1997 tax year was the final phase of the three-year personal income tax cut enacted in June 1995. This legislation raised the standard deduction and reduced the tax rate imposed on taxable income. Further legislation enacted since 1995 has increased the child and dependent care credit and the earned income tax credit. Other new credits and the New York State College Choice Tuition Savings Program were also created. These tax reductions have resulted in considerable savings for New York State taxpayers. The downturn in the economy has further eroded the personal income tax liability. The 2002 liability, as extrapolated from the 2001 study file, is estimated to be $20.7 billion, representing an 7.4 percent decline compared to 2001. The effective tax rate is estimated to have been 4.44 percent. Without the tax cuts enacted since 1995, it is estimated that liability would have been approximately $25.8 billion, about $5.1 billion higher than under current law.

Under current law, liability is estimated at $22.4 billion and $24.4 billion in 2003 and 2004, respectively. These numbers reflect the tax increase passed by the Legislature in 2003. This tax increase is estimated to raise personal income tax liability by $1.3 billion in 2003 and $1.4 billion in 2004. Without the tax changes enacted since 1995, liability would be estimated at $26.5 billion in 2003 and $28.6 billion in 2004.

Under both current law and constant law, effective tax rates are estimated to be significantly lower in 2002 than in 2001. They are expected to be higher in 2003 and 2004 due to the economic recovery and the tax increase. (See Table 6.)

TABLE 6
LIABILITY AND EFFECTIVE TAX RATES*
Current Law and Constant Law
1995 - 2004
(millions of dollars)

	Current Law			Constant (1994) Law		
	Liability		Effective	Liability		Effective
	Amount	Growth Rate	Tax Rate	Amount	Growth Rate	Tax Rate
			(percent)			(percent)
1995	16,011	5.1	4.99	16,541	8.5	5.15
1996	16,319	1.9	4.69	18,390	11.2	5.28
1997	16,950	3.9	4.42	20,711	12.6	5.40
1998	18,986	12.0	4.54	23,201	12.0	5.55
1999	20,977	10.5	4.63	25,595	10.3	5.65
2000	24,494	16.8	4.76	29,853	16.6	5.80
2001	22,406	(8.5)	4.6	27,523	(7.8)	5.65
2002**	20,738	(7.4)	4.44	25,812	(6.2)	5.53
2003**	22,448	8.2	4.72	26,510	2.7	5.57
2004**	24,387	8.6	4.86	28,629	8.0	5.70

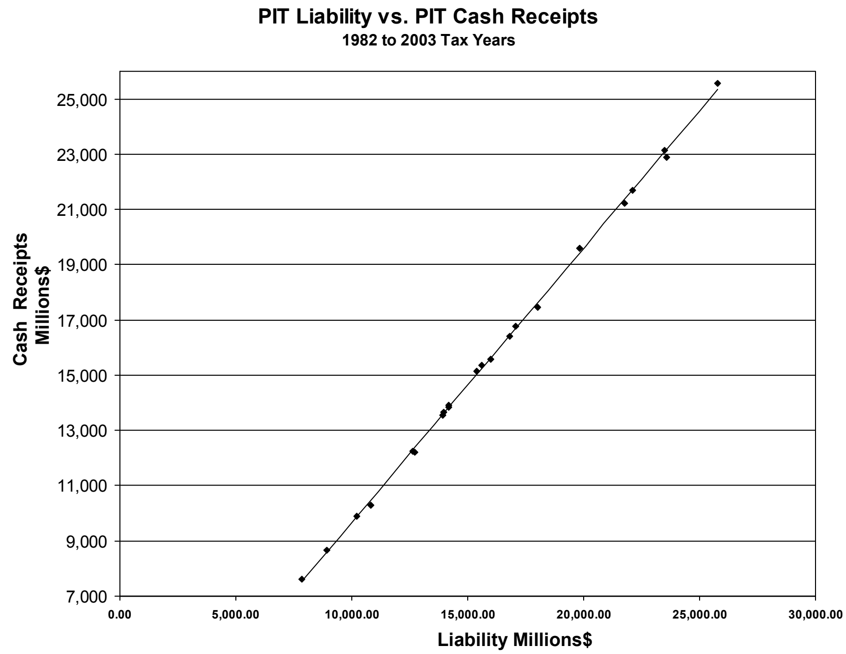
* Liability divided by AGI
** Estimated

Risks in Liability Estimates

The estimates are subject to significant risks. The national economy is still emerging from recession and thereby vulnerable to any significant shock. In addition, a slow rate of growth in employment may weaken economic growth. The stock market and financial services industry may do much better or worse than envisioned. Capital gains, as always, exhibit a high degree of volatility. (See Economic Backdrop section titled Sources of Volatility in the Income Base.)

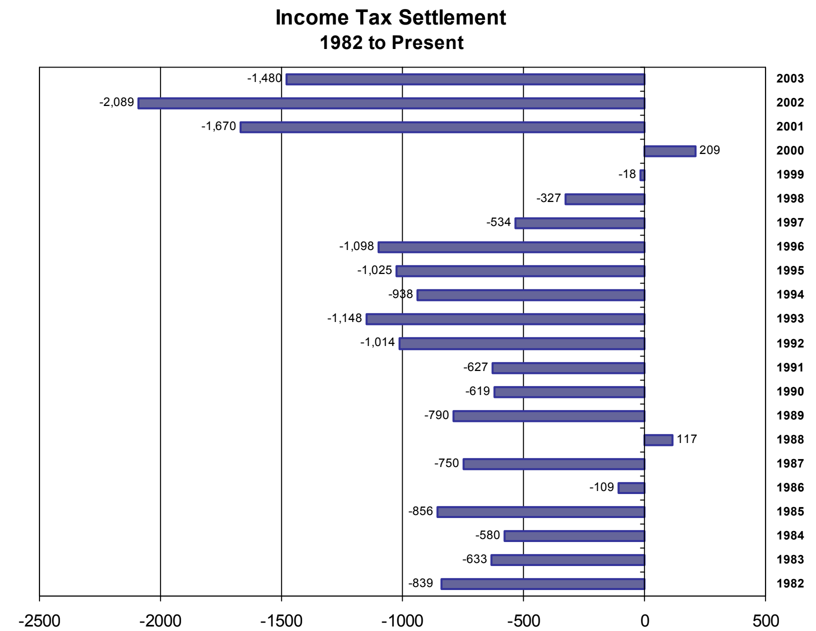
Tax Liability and Cash Payments

Although significant risks necessarily remain in any estimates of income tax liability, estimation of the level of tax liability for a particular tax year leads, with a high degree of confidence, to the approximate level of cash receipts that can be expected for the particular tax year. The consistency in this relationship is shown in the graph below.



Despite the strong relationship between tax-year liability and cash receipts, estimation of cash payments is subject to an important complication that pervades forecasts for the Executive Budget and other State Financial Plan updates. This complication is determining the portions of tax-year liability that will occur in particular State fiscal years. Income tax prepayments — withholding tax and quarterly estimated tax payments — tend to be received not long after income is earned. For example, most withholding tax payments and quarterly estimated tax payments for the 2003 tax year will be received before the end of the 2003-04 State fiscal year. Settlement payments — those payments received when taxpayers file final returns for a tax year — tend to be received in the next State fiscal year after the end of a tax year. Thus, settlement payments for the 2003 tax year will be received largely in the 2004-05 fiscal year. Some settlement payments (known as prior-year payments) are received later and can occur in a subsequent fiscal year. Such payments for the 2003 tax year can be received in 2005-06 or a later fiscal year.

As is evident in the graph below showing net settlement payments for the1982 through 2004 tax years, the amount of liability received in the settlement can vary widely from year to year. In most years, the net settlement has been very negative, with State settlement outlays (such as refunds and offsets) far exceeding taxpayer settlement payments (such as those sent with returns and extension requests). There have been some important exceptions to this pattern — most notably during times of tax reform (in 1986 and 1988) and in times of rapid economic growth (in the late1990s and in 2000).



Note: The settlement is comprised of extension payments plus final return payments minus refunds and the state-city offset

Several different settlement patterns are reflected in recent years. With the rapid growth of the New York economy in the late1990s, the settlement became much less negative than it traditionally had been. This pattern, accompanying the strongly growing economy, resulted generally from prepayment growth rates that fell short of liability growth rates, leading to the need for increased settlement payments with filed returns. With the weak economy of 2001 and 2002, taxpayers, in aggregate, dramatically reduced their settlement payments and the total settlement became very negative again, with the net amount paid out by the State exceeding $2 billion for the 2002 tax year. Due to the temporary tax increases enacted by the Legislature in 2003, the net settlement payout by the State is estimated to remain negative but below $1.5 billion for the 2003 tax year. This expected net settlement increase will reflect the need of high-income taxpayers to add to their settlement payments to cover liability increases that were not collected through added prepayments.

RECEIPTS: ESTIMATES AND PROJECTIONS

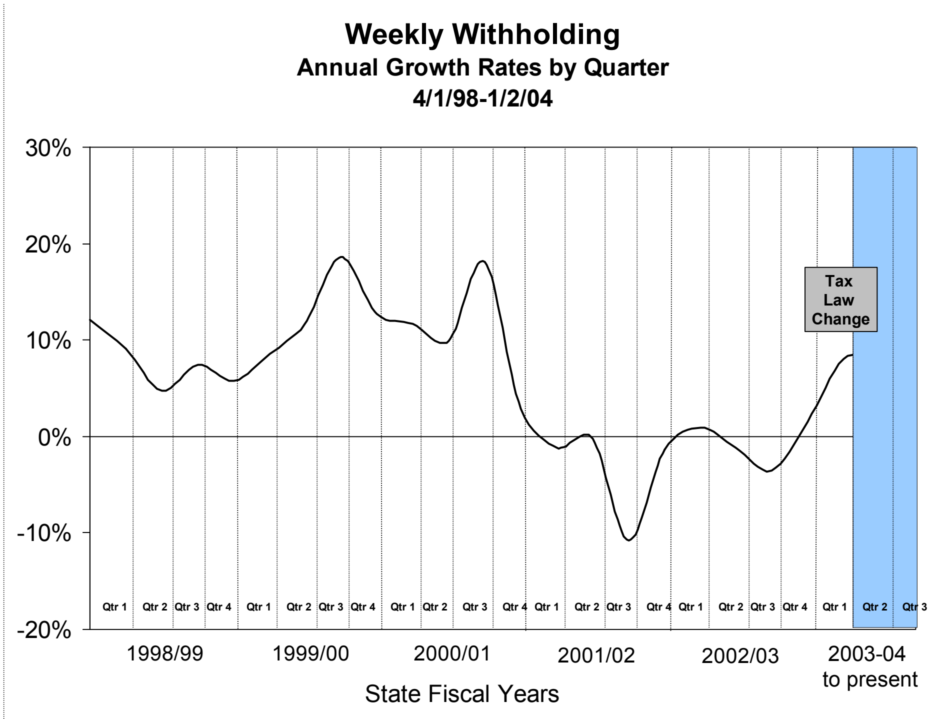
All Funds

2003-04 Estimates

Net All Funds collections to date are $16.9 billion, an increase of $0.7 billion, or 4.6 percent above the comparable period in the prior fiscal year.

Total net All Funds receipts for 2003-04 are estimated to be $24,083 million, an increase of $385 million, or 1.6 percent, above last year.

Key risks for the remainder of the fiscal year include the amount of withholding tax collections to be received in the first quarter of 2004, the balance of estimated payments to be received on 2003 liability, and the remaining uncertainty of the effects of the legislative tax increases.



The current forecast assumes that estimated payments on 2003 liability will be 12.1 percent higher than comparable payments on 2002 liability.

Compared with the same period a year ago, withholding collections increased 6.3 percent through the first nine months of the fiscal year. The bulk of this growth is attributed to the legislative tax increases, while, in comparison, base growth was relatively weak. It is expected that withholding collections will pick up and increase 20.6 percent for the remainder of 2003-04, largely reflecting the continued economic recovery and renewed strength in bonus payments during the December to March period.

Without refund reserve transactions, net All Funds receipts are estimated at $24,660 million, an increase of 8.9 percent from comparable 2002-03 receipts. The components of the estimate are detailed in Table 7 and are based on actual collections of $16.9 billion through December.

TABLE 7
PROJECTED FISCAL-YEAR COLLECTION COMPONENTS
ALL FUNDS
(millions of dollars)

	2001-02 (Actual)	2002-03 (Actual)	2003-04 (Estimated)	2004-05 (Projected)
Receipts				
Withholdings	20,261	19,959	22,085	23,104
Estimated Payments	6353	4,855	5,130	5,785
Current Year	4,685	3,831	4,295	4,695
Prior Year*	1,668	1,024	835	1,090
Final Returns	1,874	1,333	1,275	1,645
Current Year	101	101	125	145
Prior Year*	1,773	1,232	1,150	1,500
Delinquent Collections	601	797	595	660
Gross Receipts	29,089	26,944	29,085	31,194
Refunds				
Prior Year*	2,165	2,780	2,945	2,985
Previous Years	165	268	250	230
Current Year	960	960	960	960
State-City Offset*	225	288	270	250
Total Refunds	3,515	4,296	4,425	4,425
Net Receipts	25,574	22,648	24,660	26,769
Reserve Transactions	1,840	1,050	(577)	693
Net Reported	27,414	23,698	24,083	27,462

* These components, collectively, are known as the “settlement” on the prior year’s tax liability.

At the beginning of 2003-04, the balance in the refund reserve account was $627 million. The planned account balance on March 31, 2004, is $1,204 million. As a result, the net contribution of the refund reserve to 2003-04 receipts is expected to be a reduction of $577 million.

An added risk to the estimate of 2003-04 receipts results from the timing of bonus payments paid by financial services companies. A large portion of these bonuses is paid in the first quarter of the calendar year. Consequently, information about such payments was not available when the 2003-04 estimates were constructed.

2004-05 Projections

Total net All Funds receipts are projected to be $27,462 million, an increase of $3,379 million, or 14.0 percent above 2003-04.

Under current law, withholding receipts would be projected to rise by 4.7 percent.

The other major component of collections, estimated payments on 2004 income, would be projected to increase by 9.2 percent. This is consistent with the improved health of Wall Street, an increase in capital gains realizations, and additional collections resulting from the 2003 law changes.

Final payments related to 2003 returns are expected to increase by $350 million from 2002 returns, reflecting a liability increase and settlement payments for the 2003 tax increase.

In 2004-05, largely as a result of the temporary three-year tax increase passed in 2003, there is expected to be a reversal of the recent trend of the income settlement becoming more negative each year than in the preceding year (see income tax settlement chart). Although some uncertainty remains about the level of additional prepayments being made due to the temporary tax increase and other 2003 enacted legislation, it appears that high-income taxpayers affected by the tax increase will need to add to their settlement payments to cover the full amount of the extra liability resulting from the temporary tax increase.

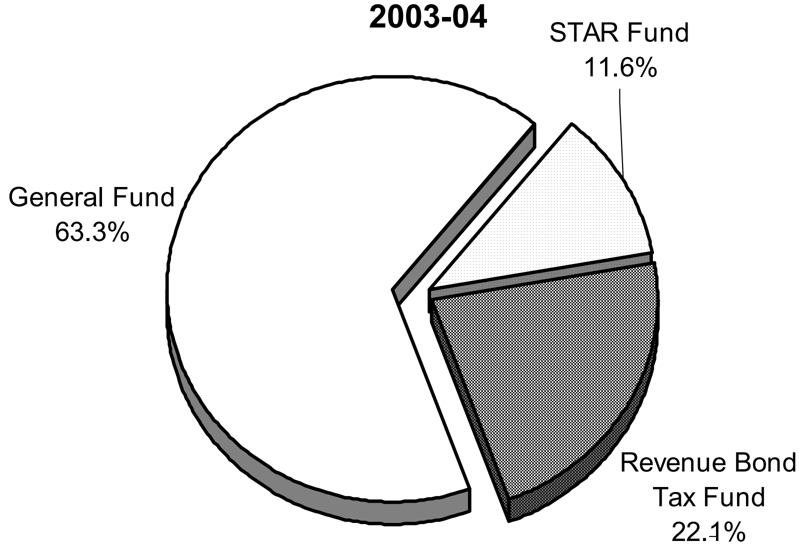
Based on proposed law, withholding receipts are projected to rise 4.6 percent, total estimated tax payments are projected to increase 12.8 percent, and final payments are projected to increase by $370 million from 2003-04 collections. As a result, net personal income tax receipts are expected to increase by 14.0 percent, to $27,462 million, in 2004-05.

General Fund

Under current law, General Fund net personal income tax receipts are estimated at $15,791 million in 2003-04 and would be estimated at $18,499 million in 2004-05, a 17.1 percent increase from the 2003-04 total. Under proposed law, General Fund net personal income tax receipts are projected at $18,520 million in 2004-05.

Other Funds

Fund Shares of Net Receipts
2003-04



Legislation enacted in 1998 created the School Tax Relief (STAR) Fund to help provide school tax reductions under the STAR program. The same legislation accelerated the fully effective level of the enhanced senior citizens' school property tax exemption into 1998-99, and accelerated the final level of the New York City personal income tax credit into the 1998 tax year for taxpayers age 65 or more. In 2003-04 and 2004-05, respectively, dedicated personal income tax receipts of $2,835 million and $2,998 million will be deposited into the School Tax Relief Fund.

Chapter 383, Laws of 2001, provides for the issuance of, and a source of payment for State Personal Income Tax Revenue Bonds. Since May 2002, a portion of personal income tax receipts has been deposited in the Revenue Bond Trust Fund (RBTF), a State debt service fund under the joint custody of the Commissioner of Taxation and Finance and the State Comptroller. Chapter 383 requires the State Comptroller to deposit an amount equal to 25 percent of estimated monthly State personal income tax receipts (after payment of refunds and STAR deposits, but before any contribution from the refund reserve account) into the RBTF each month. These large deposits into the RBTF significantly reduce the amount reported as General Fund personal income tax receipts. Each month, RBTF moneys in excess of the amount needed for debt service payments are transferred back to the General Fund. Personal income tax receipts of $5,457 million and $5,944 million will be deposited in the RBTF in 2003-04 and 2004-05, respectively.

RECEIPTS BY FUND TYPE

TABLE 8
PERSONAL INCOME TAX RECEIPTS
(millions of dollars)

	Gross General Fund	Refunds	Net General Fund Receipts	Refund Reserve Transactions	Net General Fund	Special Revenue Funds[1]	Capital Projects Funds	Debt Service Funds[2]	All Funds Net Collections
	Actual								
1995-96	19,857	2,459	17,398	400	16,998	0	0	0	16,998
1996-97	20,238	2,684	17,554	1,183	16,371	0	0	0	16,371
1997-98	21,088	2,799	18,289	530	17,759	0	0	0	17,759
1998-99	23,371	2,795	19,994	(86)	20,080	582	0	0	20,662
1999-2000	25,041	3,041	22,000	1,661	20,339	1,195	0	0	21,534
2000-01	26,744	3,629	23,115	(450)	23,565	3,077	0	250	26,892
2001-02	27,529	3,515	24,014	(1,840)	25,854	1,310	0	250	27,414
2002-03	20,037	4,296	15,741	(1,050)	16,791	2,664	0	4,243	23,698
	Estimated								
2003-04	20,793	4,425	16,368	577	15,791	2,835	0	5,457	24,083
2004-05									
current law	22,220	4,425	17,795	(704)	18,499	2,998	0	5,932	27,429
proposed law	22,252	4,425	17,827	(693)	18,520	2,998	0	5,944	27,462

[1] STAR Fund.
[2] Debt Reduction Reserve Fund and Revenue Bond Trust Fund.

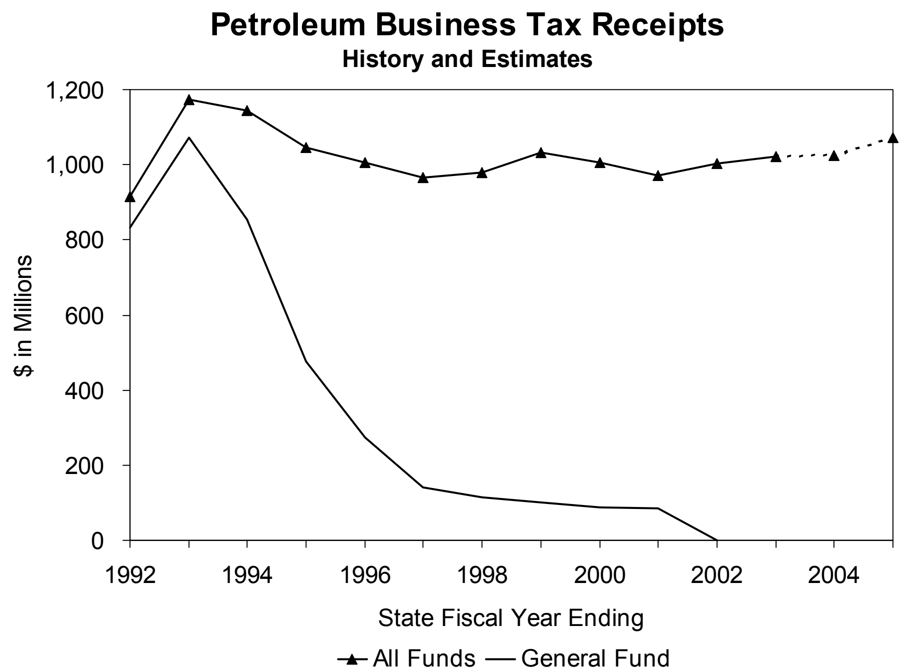
PETROLEUM BUSINESS TAXES

SUMMARY

In 2003-04, All Funds collections from petroleum business taxes are estimated to be $1,025 million. This is an increase of $2.2 million, or 0.2 percent, from the prior year.

In 2004-05, All Funds collections from petroleum business taxes are projected to be $1,073 million. This is an increase of $48 million, or 4.7 percent, compared with 2003-04.

Legislation proposed with this Budget would postpone implementation of regulations related to taxation of sales on Native American lands and authorizes the State to execute agreements with Native American nations regarding product prices and taxes.



DESCRIPTION

Tax Base and Rate

Article 13-A of the Tax Law imposes a tax on petroleum businesses for the privilege of operating in the State, based upon the quantity of various petroleum products imported for sale or use in the State. Petroleum business tax (PBT) rates have two components: the base tax, whose rates vary by product type; and the supplemental tax, which is imposed, in general, at a uniform rate.

Legislation in 1994 provided the current methodology for tax rate indexing, which began on January 1, 1996, and applies to both the base and supplemental tax rates. Tax rates cannot increase or decrease by more than 5 percent per year. In addition to the 5 percent cap on tax rate changes, the statute requires that the base and supplemental tax rates each be rounded to the nearest tenth of one cent. As a result, the percent change in tax rates usually does not exactly match the percent change in the index. The annual adjustments reflect the change in the producer price index for refined petroleum products for the 12 months ending August 31 of the immediately preceding year.

Based on changes in the index, PBT rates for 2003 decreased by 5 percent, and then will increase by 5 percent beginning in 2004. The index for January 1, 2005, is projected to decrease by 2.67 percent, triggering a tax rate decrease of 2.67 percent for 2005. (See Tables 1 and 2.)

TABLE 1
PETROLEUM BUSINESS TAX RATES FOR 2003 - 2005
(cents per gallon)

	2003			2004			2005*		
Petroleum Products	**Base**	**Supp**	**Total**	**Base**	**Supp**	**Total**	**Base**	**Supp**	**Total**
Automotive fuel									
Gasoline and other non-diesel	8.40	5.60	**14.00**	8.80	5.80	**14.60**	8.60	5.60	**14.20**
Diesel	8.40	3.85	**12.25**	8.80	4.05	**12.85**	8.60	3.85	**12.45**
Aviation gasoline	8.40	5.60	**14.00**	8.80	5.80	**14.60**	8.60	5.60	**14.20**
Net rate after credit	5.60	0.0	**5.60**	5.80	0.0	**5.80**	5.60	0.0	**5.60**
Kero-jet fuel	5.60	0.0	**5.60**	5.80	0.0	**5.80**	5.60	0.0	**5.60**
Non-automotive diesel fuels	7.60	5.60	**13.20**	7.90	5.80	**13.70**	7.70	5.60	**13.30**
Commercial gallonage after credit	7.60	0.0	**7.60**	7.90	0.0	**7.90**	7.70	0.0	**7.70**
Nonresidential heating after credit	4.10	0.0	**4.10**	4.30	0.0	**4.30**	4.20	0.0	**4.20**
Residual petroleum products	5.80	5.60	**11.40**	6.10	5.80	**11.90**	5.80	5.60	**11.40**
Commercial gallonage after credit	5.80	0.0	**5.80**	6.00	0.0	**6.00**	5.80	0.0	**5.80**
Nonresidential heating after credit	3.10	0.0	**3.10**	3.20	0.0	**3.20**	3.10	0.0	**3.10**
Railroad diesel fuel	8.40	3.85	**12.25**	8.80	4.05	**12.85**	8.60	3.85	**12.45**
Net rate after exemption/refund	7.10	0.0	**7.10**	7.50	0.0	**7.50**	7.30	0.0	**7.30**

* Projected — A fuel price decrease of 2.7 percent through August 2004 will result in a decrease of 2.7 percent in the PBT tax rates on January 1, 2005.

Administration

The tax is collected monthly in conjunction with the State motor fuel taxes (Article 12-A). Article 13-A also imposes the petroleum business carrier tax on fuel purchased outside New York and consumed within the State. The carrier tax is collected quarterly along with the fuel use tax portion of the highway use tax. (See section titled Highway Use Tax.)

Under 1992 legislation, businesses with yearly motor fuel and petroleum business tax liability of more than $5 million are required to remit, using electronic funds transfer, their total tax liability for the first 22 days of the month, within three business days after that date. Taxpayers can choose to make either a minimum payment of three-fourths of the comparable month's tax liability for the preceding year, or 90 percent of actual liability for the 22 days. The tax for the balance of the month is paid with the monthly returns filed by the twentieth of the following month.

Tax Expenditures

Specifically exempted from Article 13-A taxes are fuel used for manufacturing, residential or not-for-profit organization heating purposes, fuel sold to governments, kerosene other than kero-jet fuel, crude oil, liquefied petroleum gas (LPG), and certain bunker fuel. For further expenditure items related to the PBT, please see the New York State Tax Expenditure Report.

TABLE 2
FUEL PRICE AND PETROLEUM BUSINESS TAX INDEX
(percent change)

Year	Fuel Price	PBT Index
1992	16.47	16.47
1993	(14.40)	0.00
1994	(0.46)	0.00
1995	(8.72)	0.00
1996	4.41	4.41
1997	6.57	5.00
1998	7.96	5.00
1999	(18.60)	(5.00)
2000	(7.85)	(5.00)
2001	55.84	5.00
2002	13.08	5.00
2003	(19.51)	(5.00)
2004	26.98	5.00
2005*	(2.67)	(2.67)

* Estimated

Significant Legislation

The significant statutory changes to this tax source since 1994 are summarized below.

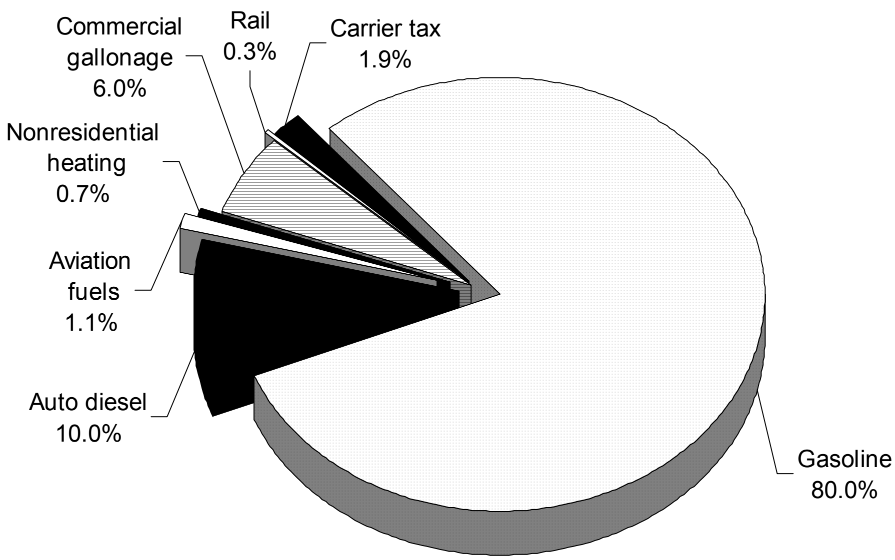
Subject	Description	Effective Date
Legislation Enacted in 1995		
Aviation Fuels	Effectively eliminated the supplemental tax imposed on aviation gasoline and kero-jet fuel and reduced the base tax rate for those products to a rate that is equivalent to the statutory supplemental tax rate. To maintain the first import system, which imposes the petroleum business tax on aviation gasoline upon importation, and still allow retail sellers of aviation gasoline to sell such product at a reduced rate, distributors of aviation gasoline must remit the full tax imposed on that product and may subsequently take a credit for the difference between the full rate and the reduced rate.	September 1, 1995
Not-for-profit Organizations	Provided full exemption for heating fuel that is for the exclusive use and consumption of certain not-for-profit organizations.	January 1, 1996
Legislation Enacted in 1996		
Railroads	Exempted diesel motor fuel used for railroads from the supplemental portion of the tax and reduced the base rate by 1.33 cents per gallon.	January 1, 1997
Commercial Heating	Provided full exemption from the supplemental tax imposed on distillate and residual fuels used by the commercial sector for heating.	March 1, 1997
Manufacturing	Expanded to a full exemption, the partial exemption provided for residual and distillate fuels used in manufacturing.	January 1, 1998
Diesel Supplemental Tax	Reduced by three-quarters of one cent per gallon the supplemental tax imposed on diesel motor fuel.	January 1, 1998
	Reduced by an additional one cent per gallon the supplemental tax imposed on diesel motor fuel.	April 1, 1999
Utilities	Increased by one-half cent per gallon the base tax credit for residual and distillate fuels used by utilities to generate electricity.	April 1, 1999
Legislation Enacted in 1997		
Vessels	Created a credit or refund for fuel used in vessels that was purchased in the State and consumed outside the State; clarified that the export credit/refund applies to export for use, as well as sale; stated that the legal incidence of the tax is on consumers; and limited the judicial remedies available to taxpayers.	April 1, 1984
Legislation Enacted in 1999		
Commercial Heating	Reduced by 20 percent the petroleum business tax rates on commercial gallons for space heating.	April 1, 2001
Mining and Extraction	Provided for reimbursement of petroleum business tax imposed on fuels used for mining and extraction.	April 1, 2001

Subject	Description	Effective Date
Legislation Enacted in 2000		
Minimum Tax	Eliminated the minimum taxes on petroleum businesses and aviation fuel businesses under the PBT.	March 1, 2001
Commercial Heating	Reduced by 33 percent the petroleum business tax rates on commercial gallons for space heating.	September 1, 2002
Legislation Enacted in 2003		
Native American Regulations	Required the Commissioner of Taxation and Finance to promulgate regulations requiring the taxation of petroleum productions sold to non-Native Americans on Native American lands.	March 1, 2004

TAX LIABILITY

Petroleum business tax collections are primarily a function of the number of gallons of fuel imported into the State by distributors. Gallonage is largely determined by overall fuel prices, the amount of gallons held in inventories, the fuel efficiency of motor vehicles, and State economic performance. The following pie chart displays the composition of PBT receipts by fuel type.

PBT Components
Share of 2002-03 Receipts



PROPOSED LEGISLATION

Legislation proposed with this Budget would postpone implementation of regulations related to taxation of sales on Native American lands and authorizes the State to execute agreements with Native American nations regarding product prices and taxes.

RECEIPTS: ESTIMATES AND PROJECTIONS

All Funds

2003-04 Estimates

Net All Funds collections to date are $781.7 million, an increase of $0.5 million, or 0.1 percent above the comparable period in the prior fiscal year.

Total net All Funds receipts for 2003-04 are estimated to be $1,025 million, an increase of $2.2 million, or 0.2 percent above last year.

Petroleum business tax receipts derived from motor fuel and diesel motor fuel are estimated to follow the same consumption trends as fuel subject to the motor fuel excise tax. (See section titled Motor Fuel Tax.) In 2001-02 motor fuel tax receipts were misallocated to PBT and in 2002-03 this misallocation was corrected by reversing the 2001-02 misallocation. These factors combined to understate 2002-03 PBT receipts by $15.8 million. Residual fuels used by utilities are estimated to increase due to the decrease in the relative price of residual fuel oil compared to natural gas.

The estimate for 2003-04 reflects the 5 percent decrease in PBT rates that took effect on January 1, 2003, and the scheduled 5 percent increase effective January 1, 2004. The estimate also reflects 2000 legislation that reduced taxes on commercial heating by 33 percent and eliminated PBT minimum taxes.

2004-05 Projections

Total net All Funds receipts are projected to be $1,073 million, an increase of $48 million, or 4.7 percent above 2003-04.

Without counting projected tax receipts from Native American lands, gasoline and diesel receipts are projected to increase by $24.4 million and $5 million respectively. Increases in taxable gasoline and diesel gallonage are projected to be marginal. The increase is mainly generated by the 5 percent increase in PBT rates effective January 1, 2004.

In addition, receipts for 2004-05 are based on an anticipated decrease in January 2005 of 2.67 percent in the index used to set PBT tax rates.

Prospective agreements between Native American governments and the State based on legislation submitted with this Budget are expected to add a projected $13 million in revenue in 2004-05.

General Fund

Legislation enacted in 2000 provided that all remaining PBT receipts deposited in the General Fund be deposited in the Dedicated Funds Pool, effective April 1, 2001. As a result, no PBT receipts will be deposited in the General Fund in 2003-04 and 2004-05.

Other Funds

In past years, revenues from the petroleum business tax have been shared by the General Fund and the Mass Transportation Operating Assistance Fund (MTOAF). Prior to the 1990 revisions, the General Fund received 72.7 percent and MTOAF received 27.3 percent or a guaranteed amount. The 1990 statute converted the tax from a gross receipts tax to a cents-per-gallon tax, expanded the tax yield, and limited the MTOAF share to slightly more than 17.7 percent of the nonsurcharge revenues — the dollar equivalent of its share prior to the expansion. Carrier tax receipts were deposited in the General Fund until April 1, 2001.

Separate 1991 transportation legislation provided that effective April 1, 1993, 100 percent of the supplemental tax and a portion of the base tax (see Table 3) would be split between the Dedicated Mass Transportation Trust Fund and the Dedicated Highway and Bridge Trust Fund. Numerous pieces of legislation were enacted in subsequent years that reduced the amount of deposits in the General Fund and increased the amount deposited in the Dedicated Transportation funds.

Legislation enacted in 2000 redistributed PBT receipts. Effective April 1, 2001, all remaining PBT General Fund receipts, including carrier tax receipts, were redistributed to the Dedicated Highway and Bridge Trust Fund and the Dedicated Mass Transportation Trust Fund.

Statutory changes to the allocation of the PBT by fund type are reported in Table 3.

TABLE 3
PBT BASE TAX FUND DISTRIBUTION
(percent)

Effective Date	General Fund	MTOAF[1]	Dedicated Funds Pool[2]
Prior to April 1, 1993	82.3	17.7	0.0
April 1, 1993	28.3	17.7	54.0
September 1, 1994	22.4	18.6	59.0
September 1, 1995	18.0	19.2	62.8
April 1, 1996	17.4	19.3	63.3
January 1, 1997	14.5	19.3	66.2
January 1, 1998	12.4	19.5	68.1
April 1, 1999	10.7	19.5	69.8
April 1, 2001	0.0	19.7	80.3

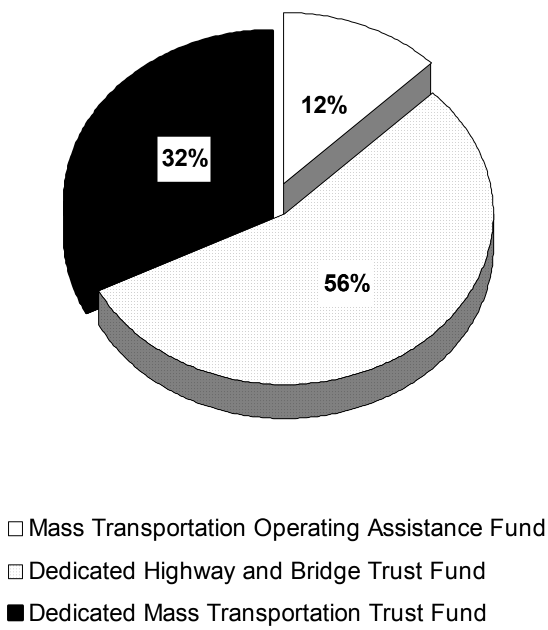
[1] This fund is split between the Public Transportation System Operating Assistance Account and the Metropolitan Mass Transportation Operating Assistance Account.
[2] This pool is split between the Dedicated Mass Transportation Trust Fund (37 percent) and the Dedicated Highway and Bridge Trust Fund (63 percent).

Legislation enacted in 2000 significantly increased the flow of PBT funds to the Dedicated Funds Pool. Effective April 1, 2001, all PBT receipts previously deposited in the General Fund, including the balance of the basic tax and the carrier tax, are now deposited in the Dedicated Funds Pool.

Petroleum business tax receipts in 2003-04 are estimated to be $126.8 million for MTOAF, $565.9 million for the Dedicated Highway and Bridge Trust Fund, and $332.3 million for the Dedicated Mass Transportation Trust Fund.

Petroleum business taxes in 2004-05 are projected to provide MTOAF receipts of $133 million, Dedicated Highway and Bridge Trust Fund receipts of $592.2 million, and Dedicated Mass Transportation Trust Fund receipts of $347.8 million.

PBT Receipts 2003-04



RECEIPTS BY FUND TYPE

PETROLEUM BUSINESS TAX RECEIPTS
(millions of dollars)

	Gross General Fund	Refunds	Net General Fund	Gross Special Revenue Funds[1]	Refunds	Net Special Revenue Funds[1]	Gross Capital Projects Funds[2]	Refunds	Net Capital Projects Funds[2]	All Funds Net Collections
Actual										
1995-96	276	3	273	303	4	299	438	5	433	1,005
1996-97	144	3	141	379	7	372	462	8	454	967
1997-98	116	2	114	396	8	388	487	10	477	979
1998-99	103	1	102	423	5	418	519	6	513	1,033
1999-2000	90	1	89	415	5	410	512	6	506	1,005
2000-01	88	2	86	405	9	396	501	12	489	971
2001-02	0	0	0	459	10	449	566	12	554	1,003
2002-03	0	0	1	462	8	454	578	10	568	1,023
Estimated										
2003-04	0	0	0	467	8	459	576	10	566	1,025
2004-05	0	0	0	489	8	481	602	10	592	1,073

[1] Dedicated Mass Transportation Trust Fund and Mass Transportation Operating Assistance Fund.
[2] Dedicated Highway and Bridge Trust Fund.

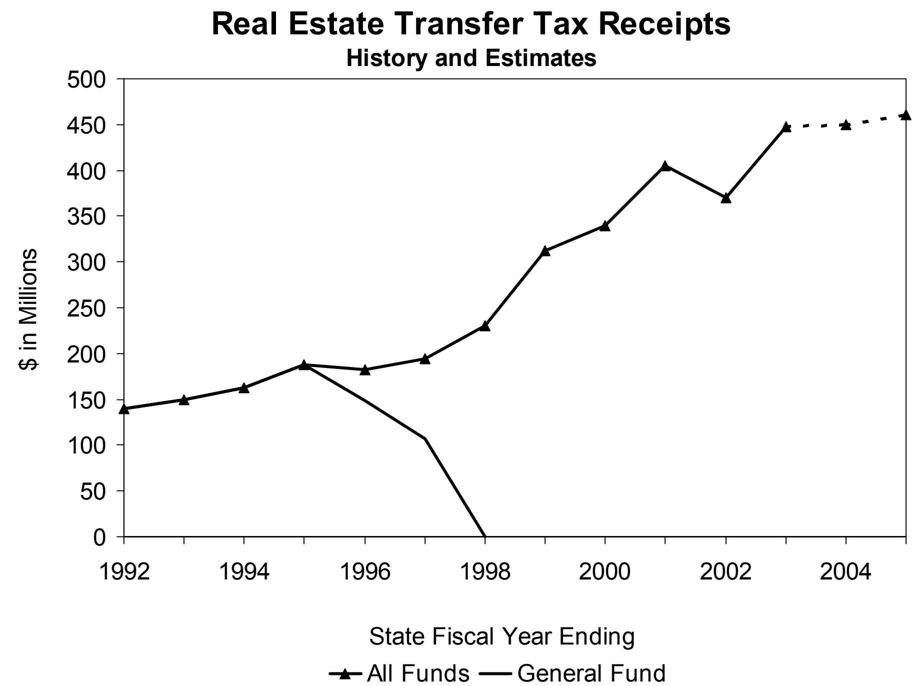
REAL ESTATE TRANSFER TAX

SUMMARY

In 2003-04, All Funds collections from the real estate transfer tax are estimated to be $450 million. This is an increase of $2.4 million, or 0.5 percent, from the prior year.

In 2004-05, All Funds collections from the real estate transfer tax are projected to be $461 million. This is an increase of $11 million, or 2.4 percent, compared with 2003-04.

No new legislation for these taxes is proposed with this Budget.



DESCRIPTION

Tax Base and Rate

The New York State real estate transfer tax is imposed by Article 31 of the Tax Law on each conveyance of real property or interest therein, when the consideration exceeds $500, at a rate of $4 per $1,000 of consideration. The tax became effective August 1, 1968. Prior to May 1983, the rate was $1.10 per $1,000 of consideration. Effective July 1, 1989, an additional 1 percent tax was imposed on conveyances for which the consideration is $1 million or more.

Administration

Typically, the party conveying the property (grantor) is responsible for payment of the tax, either through the purchase of adhesive documentary stamps, by the use of a metering machine, or through other approaches provided by the Commissioner of Taxation and Finance.

For deeded transfers, the tax is paid to a recording agent (generally the county clerk). For non-deeded transactions, payments are made directly to the Commissioner of Taxation and Finance ("central office" collections). All payments are due to the recording agent within 15 days of the transfer. For counties with more than $1.2 million in liability during the previous calendar year, payments received between the first and fifteenth day of the month are due to the Commissioner by the twenty-fifth day of the same month. Payments received in such counties between the sixteenth and the final day of the month are due to the Commissioner by the tenth day of the following month. Payments from all other counties are due to the Commissioner by the tenth day of the month following their receipt. Although the county payment schedule is statutory, it is not useful for predicting monthly cash flows, due to the unpredictable payment behavior of some large counties.

Tax Expenditures

The tax rate imposed on conveyances into new or existing real estate investment trusts is $2 per $1,000 of consideration. New York State (including agencies, instrumentalities, subdivisions, and public corporations), the United States (including agencies and instrumentalities), and the United Nations are exempt. If an exempt entity is the grantor in a transfer, the tax burden falls upon the grantee. Other significant exemptions from the tax are: conveyances pursuant to the Federal bankruptcy act and mere change of identity conveyances. A deduction from taxable consideration is allowed for any lien or encumbrance remaining at the time of sale involving a one-, two-, or three-family house or individual residential condominium unit.

TAX LIABILITY

Real estate transfer tax receipts are a function of the number of conveyances and the consideration (price) per conveyance. Conveyances and prices are largely determined by mortgage rates, vacancy rates and inflation. The Manhattan commercial real estate market, which has historically been subject to large swings in demand and capacity, can have a significant impact on receipts.

PROPOSED LEGISLATION

No new legislation for these taxes is proposed with this Budget.

RECEIPTS: ESTIMATES AND PROJECTIONS

All Funds

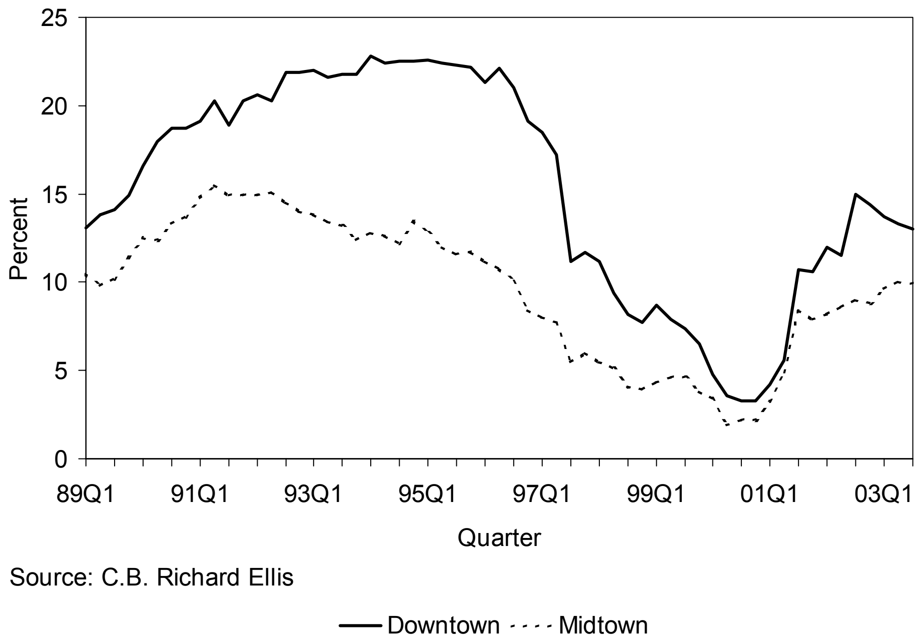
2003-04 Estimates

Net All Funds collections to date are $378 million, an increase of $18.8 million, or 5.2 percent above the comparable period in the prior fiscal year.

Total net All Funds receipts for 2003-04 are estimated to be $450 million, an increase of $2.4 million, or 0.5 percent above last year.

The booming housing market, spurred by record-low mortgage rates that began in 2002-03, continued into the current fiscal year. The 2003-04 estimate reflects liability data for the first seven months of the fiscal year, which indicate a decline in the overall number of conveyances (including non-residential) of 2.5 percent, combined with an average price increase of 1.7 percent across all conveyances when compared with the first seven months of 2002-03. The weak Manhattan commercial market may have reached its nadir in 2003-04. The vacancy rate downtown fell to 13 percent during the third quarter of 2003, down from its recent peak of 15 percent during the same period last year. The midtown vacancy rate fell to 9.9 percent during the third quarter of 2003, which is the first quarterly decline (excluding the quarter following the WTC attacks) since the second quarter of 2000. As the graph below indicates, the rise in Manhattan vacancy rates since 2001 has not been as severe as during the early 1990s, due to far less excess capacity during the current downturn. The negative impact of the current Manhattan commercial downturn on receipts has been masked by the torrid statewide residential market.

Vacancy Rates in Manhattan



Source: C.B. Richard Ellis

FISCAL YEAR LIABILITY THROUGH OCTOBER
(millions of dollars)

Region	2002-03 Liability	2003-04 Liability	Percent Change
Manhattan	56.1	52.6	(6.3)
Other Four Boroughs	39.8	43.2	8.4
Long Island	61.4	65.5	6.7
Rest of State	76.4	72.1	(5.6)
Central Office*	57.6	49.9	(13.4)

* Through November

2004-05 Projections

Total net All Funds receipts are projected to be $461 million, an increase of $11 million, or 2.4 percent above 2003-04.

Collections are expected to rise despite a projected rise in the mortgage rate from 5.76 percent to 6.11 percent. Projected increases in prices for both residential housing and commercial real estate should more than compensate for the increase in mortgage rates.

General Fund

The General Fund will receive no direct deposit of real estate transfer tax receipts in 2003-04 or 2004-05. However, the balance of the Clean Water/Clean Air Fund, not needed for debt service, is transferred to the General Fund.

Other Funds

During 2003-04 and 2004-05, the statutory amount of real estate transfer tax receipts diverted to the Environmental Protection Fund is $112 million. The remainder of real estate transfer tax receipts, estimated at $338 million in 2003-04 and $349 million in 2004-05, are to be deposited in the Clean Water/Clean Air Bond Debt Service Fund.

RECEIPTS BY FUND TYPE

REAL ESTATE TRANSFER TAX RECEIPTS
(thousands of dollars)

	Gross General Fund	Refunds	Net General Fund	Special Revenue Funds	Capital Projects Funds[1]	Gross Debt Service Funds[2]	Refunds	Debt Service Funds[2]	All Funds Net Collections
	Actual								
1995-96	148,505	307	148,198	0	33,500	0	0	0	181,698
1996-97	107,859	371	107,488	0	87,000	0	0	0	194,488
1997-98	0	0	0	0	87,000	142,747	115	142,632	229,632
1998-99	0	0	0	0	112,000	200,383	14	200,369	312,369
1999-2000	0	0	0	0	112,000	229,269	1,039	228,230	340,230
2000-01	0	0	0	0	112,000	293,181	436	292,745	404,745
2001-02	0	0	0	0	112,000	258,677	55	258,622	370,622
2002-03	0	0	0	0	112,000	335,761	202	335,559	447,559
	Estimated								
2003-04	0	0	0	0	112,000	338,720	720	338,000	450,000
2004-05	0	0	0	0	112,000	349,060	60	349,000	461,000

[1] Environmental Protection Fund.
[2] Clean Water/Clean Air Bond Debt Service Fund.

REPEALED TAXES

GIFT TAX

Until the gift tax repeal on January 1, 2000, New York was one of five states that imposed a gift tax as a complement to the transfer tax on estates to equalize the tax burden on lifetime transfers. Like the estate tax, the base of this levy was derived from the Federal tax base, with exclusions for transfers of property located outside the State. The tax was imposed on a lifetime basis — taxable gifts made during a taxpayer's lifetime, after allowable exclusions, were taxed in aggregate as one gift.

2003-04 Receipts and 2004-05 Projections

All Funds net gift tax collections to date are $3.5 million. Net collections for 2003-04 are expected to be $4.5 million, consisting of $4.9 million in gross receipts and $0.4 million in refunds. No receipts are expected for 2004-05 or for any subsequent fiscal year.

REAL PROPERTY GAINS TAX

The real property gains tax, enacted in 1983, was repealed on July 13, 1996. All property transferred after June 15, 1996, is exempt from the provisions of the real property gains tax. This tax was levied at a rate of 10 percent of the gain from sales of New York commercial property of $1 million or greater, including anything of value arising from land ownership, such as air rights or zoning credits. This tax was unique to New York State, and its elimination has made real property located in New York more appealing to investors.

2003-04 Receipts and 2004-05 Projections

Remaining collections stem primarily from assessments on prior year tax liability and from deferred installment payments for tax liability arising from sales of condominium and cooperative housing for projects that were still being sold at the time of the gains tax repeal. To date, All Funds collections are $3.4 million, with an additional $0.8 million expected by the end of the State fiscal year. Total refunds for the year are estimated to be negligible. As a result, net real property gains tax collections for 2003-04 are estimated to be $4.2 million.

All Funds collections from outstanding installments and recovered assessments will produce a projected $3 million in 2004-05. Refunds will be negligible.

REPEALED TAXES RECEIPTS
(thousands of dollars)

	Gross General Fund	Refunds	Net General Fund	Special Revenue Funds	Capital Projects Funds	Debt Service Funds	All Funds Net Collections
				Actual			
1995-96	320,930	47,010	228,319	0	0	0	228,319
1996-97	198,442	31,963	140,982	0	0	0	140,982
1997-98	201,143	38,572	135,532	0	0	0	135,532
1998-99	184,301	11,309	154,033	0	0	0	154,033
1999-2000	109,442	15,107	94,327	0	0	0	94,327
2000-01	53,183	5,548	47,628	0	0	0	47,628
2001-02	11,120	1,120	10,000	0	0	0	10,000
2002-03	12,623	732	11,891	0	0	0	11,891
				Estimated			
2003-04	9,100	400	8,700	0	0	0	8,700
2004-05	3,000	0	3,000	0	0	0	3,000

SALES AND USE TAX

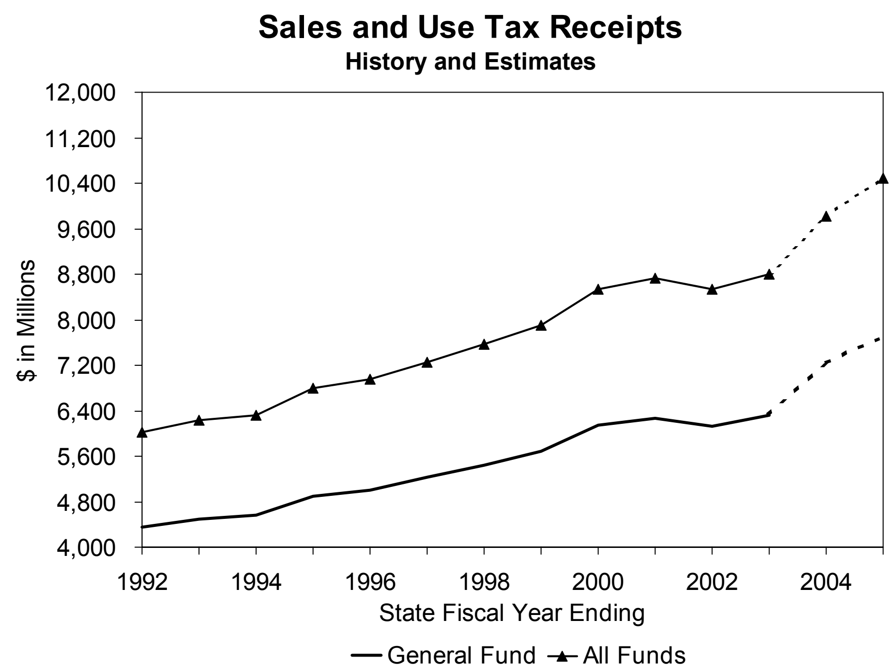
SUMMARY

In 2003-04, All Funds collections from the sales and use tax are estimated to be $9,822 million. This is an increase of $1,026 million, or 11.7 percent from the prior year.

In 2004-05, All Funds collections from the sales and use tax are projected to be $10,483.2 million. This is an increase of $661.2 million, or 6.7 percent, compared with 2003-04.

Legislation proposed with this Budget includes:

- replacing the exemption on clothing and footwear priced under $110 with a $500 per item threshold during three to four exemption weeks;
- extending the exemption for alternative fuel vehicles by one year; and
- surcharges of 3 percent on the sale of protective and detective services and 4 percent on certain admission charges to fund public safety and security.



DESCRIPTION

Tax Base

In general, all retail sales of tangible personal property are taxed under Article 28 of the Tax Law unless specifically exempt, but services are taxable only if they are enumerated in the Tax Law.

Specifically, the sales tax is applied to receipts from the retail sale of:

- tangible personal property (unless specifically exempt);
- certain gas, electricity, refrigeration and steam, and telephone service;
- selected services;

- food and beverages sold by restaurants, taverns and caterers;
- hotel occupancy; and
- certain admission charges and dues.

Examples of taxable services include installing or maintaining tangible personal property, and protective and detective services. An additional 5 percent sales tax is imposed on the receipts from the sale of telephone entertainment services that are exclusively delivered aurally.

Tax Rate

The sales and compensating use tax, was enacted in 1965 at the rate of 2 percent. The tax rate was increased to 3 percent in 1969, to 4 percent rate in 1971, and to the current 4.25 percent rate in 2003. The rate is scheduled to revert to 4 percent on June 1, 2005.

Counties and cities are authorized to impose the tax at up to a combined 3 percent rate. However, 28 counties and 15 cities (including New York City) have sought and received legislative authority to temporarily impose a higher rate. Thus, the combined State-local sales and use tax rate exceeds 7 percent in many instances. More than 70 percent of the State's population resides in areas where the tax rate is 8 percent or higher. An additional 0.25 percent sales and use tax is imposed in the 12-county Metropolitan Commuter Transportation District (MCTD). The entire proceeds from the MCTD tax are earmarked for the Mass Transportation Operating Assistance Fund (MTOAF).

Administration

Persons selling taxable property or services are required to register with the Department of Taxation and Finance as sales tax vendors. Vendors generally are required to remit the tax quarterly. However, vendors who collect more than $300,000 of tax in one of the immediately preceding four quarters must remit the tax monthly, by the twentieth of the month following the month of collection. Vendors collecting less than $3,000 yearly may elect to file annually, in June. Prior to June 1998, the threshold for opting to file annually was $250 in tax collected.

Vendors collecting more than $500,000 annually in State and local tax are required to remit the tax by electronic funds transfer (EFT). Collections for the first 22 days of the month must be remitted electronically or by certified check within three business days thereafter. Legislation enacted in 1992 started the EFT program, originally with the threshold for mandatory participation at $5 million in annual tax liability. Legislation in 1994, 1995, and 2002 reduced the threshold to $4 million, $1 million and to the current $500,000 threshold, respectively. Approximately 54 percent of the tax is remitted via EFT.

To reduce tax evasion, special provisions for remitting the sales tax on gasoline motor fuel and cigarettes have been enacted. Since 1985, the sales tax on gasoline has been remitted by the first importer of the fuel into New York. The tax is prepaid at a per gallon rate based on regional prices. Legislation, enacted in 1995, required prepayment of the sales tax on cigarettes. The tax is prepaid by cigarette agents at the same time that they pay for cigarette excise tax stamps.

Sales tax vendors are allowed to retain a portion of the sales tax that they have collected, both as partial compensation for the administrative costs of collecting and remitting the tax and as an incentive for timely payment of the tax to the State. The vendor allowance, enacted in 1994, is currently 3.5 percent of tax liability, up to a maximum of $150 per quarter for returns filed on time.

Effective with the 2003 personal income tax filing year, the New York State personal income tax return will contain a line on which taxpayers may enter the amount of use tax they owe for the preceding calendar year.

Tax Expenditures

A myriad of exemptions from the sales tax have been enacted over the life of the tax. Broad exemptions have been provided for sales for resale and for machinery and equipment used in production or in research and development. These exemptions prevent multiple taxation of the same property, a situation known as tax pyramiding. Additionally, items including food, medicines, medical supplies, residential energy, and clothing and shoes costing less than $110 have been excluded from the sales tax to reduce the regressivity of the tax and promote economic competiveness.[1]

Other exemptions, such as sales to exempt organizations, certain vending machine sales and certain other coin-operated sales, are also provided. Legal, medical and other professional services, sales of real property, and rental payments are also beyond the current scope of the sales tax.

Significant Legislation

The significant statutory changes to this tax source since 1994 are summarized below.

Subject	Description	Effective Date
Legislation Enacted in 1994		
Racehorses	Exempted certain registered racehorses used in authorized pari-mutuel events.	June 1, 1994
Vendor Allowance	Enacted the vendor allowance credit for timely filed quarterly or annual returns at the rate of 1.5 percent of State sales tax collected up to a maximum of $100 per return.	September 1, 1994
Legislation Enacted in 1995		
Homeowners' Associations	Exempted dues paid to homeowners' associations operating social or athletic facilities for their members.	September 1, 1995
Meteorological Services	Exempted the sale of meteorological information services.	September 1, 1995
Legislation Enacted in 1996		
Clothing and Footwear	Exempted clothing and footwear priced under $500 for the one-week period of January 18-24, 1997.	January 18-24, 1997
Promotional Materials	Expanded the exemption for certain printed promotional materials distributed by mail to customers in New York State.	March 1, 1997
Legislation Enacted in 1997		
Buses	Provided an exemption for buses used to transport persons for hire, and related parts and services.	December 1, 1997
Clothing and Footwear	Exempted clothing priced under $100 for the one-week periods of September 1-7, 1997, and September 1-7, 1998.	September 1-7, 1997 September 1-7, 1998
	Permanently exempted clothing priced under $100.	December 1, 1999
Homeowner Association Parking	Exempted parking services sold by a homeowners' association to its members.	December 1, 1997
Various Coin-Operated Devices	Raised the exemption threshold for bulk vending machine sales to 50 cents from 25 cents, exempted coin-operated car washes, exempted coin-operated photocopying costing under 50 cents, and exempted certain hot food and beverages sold through vending machines.	December 1, 1997
Vendor Allowance	Increased the sales tax vendor allowance from 1.5 percent to 3.5 percent of State tax collected, capped at $150 per quarter.	March 1, 1999

[1] A tax on goods or services is regressive if lower-income persons pay a relatively greater share of their income on the taxed good or service than higher-income persons.

Subject	Description	Effective Date
Legislation Enacted in 1998		
Clothing and Footwear	Included footwear in the September 1-7, 1998, temporary clothing exemption and raised exemption threshold to $500 from $100.	September 1-7, 1998
	Exempted clothing and footwear priced under $500 during the January 17-24, 1999, period.	January 17-24, 1999
	Included footwear in the permanent clothing exemption beginning on December 1, 1999, and raised exemption threshold from $100 to $110.	December 1, 1999
Coin Telephones	Increased the exemption threshold for coin-operated telephone calls to 25 cents from 10 cents.	September 1, 1998
College Textbooks	Exempted textbooks purchased by college students that are required for their courses.	June 1, 1998
Computer Hardware	Exempted computer system hardware used to design and develop computer software for sale.	June 1, 1998
Internet Access Service	Codified State policy of exempting charges for Internet access services.	February 1, 1997
Materialmen	Allowed certain materialmen (i.e., building materials suppliers) to remit sales tax returns on either a cash or an accrual basis.	June 1, 1999
Telephone Central Office Equipment	Expanded existing exemption for telephone central office equipment to include such equipment or apparatus used in amplifying, receiving, processing, transmitting, and re-transmitting telephone signals.	September 1, 1998
Legislation Enacted in 1999		
Clothing and Footwear	Changed the effective date of the permanent exemption for clothing and footwear priced under $110 from December 1, 1999, to March 1, 2000.	March 1, 2000
	Temporarily exempted clothing and footwear priced under $500 for the periods of September 1-7, 1999, and January 15-21, 2000.	September 1-7, 1999; January 15-21, 2000
Computer Hardware	Provided an exemption for computer system hardware used to design and develop Internet web sites for sale.	March 1, 2001
Farm Production	Expanded the farm production exemption to include fencing and certain building materials. Converted the refund for tax paid on motor vehicles to an exemption.	March 1, 2001
Telecommunications Equipment	Exempted machinery and equipment used to upgrade cable television systems to provide telecommunications services for sale and to provide Internet access service for sale.	March 1, 2001
Theater	Exempted certain tangible personal property and services used in the production of live dramatic or musical arts performances.	March 1, 2001
Legislation Enacted in 2000		
Farm Production	Exempted property, building materials and utility services used in farm production. Expanded definition of farms to include commercial horse boarding operations.	September 1, 2000
Internet Data Centers	Exempted computer hardware and software purchased by Internet Data Centers (web site hosting facilities) operating in New York. Included required equipment such as air conditioning systems, power systems, raised flooring, cabling, and the services related to the exempted property.	September 1, 2000
Vending Machines	Exempted food and drink sold through a vending machine that costs 75 cents or less.	September 1, 2000
Telecommunications Equipment and Communications Services	Exempted property used to provide telecommunications services, Internet access services, or a combination thereof. Also, exempted certain services to the exempted property, such as installation and maintenance. Provided a three-year exemption for machinery and equipment used to upgrade cable television systems to a digital-based technology.	September 1, 2000
Radio and Television Broadcasting	Exempted machinery and equipment (including parts, tools and supplies) and certain services used for production and transmission of live or recorded programs. A broadcaster includes Federal communications licensed radio and television stations, television networks, and cable television networks.	September 1, 2000
Pollution Abatement	Exempted manufacturing and industrial pollution control equipment and machinery.	March 1, 2001

Subject	Description	Effective Date
Transmission and Distribution of Electricity and Gas	Phased out over three years the sales tax on the separately purchased transmission of electricity and gas.	September 1, 2000
Empire Zones	Exempted property and services used or consumed by qualified businesses within Empire Zones.	March 1, 2001
Purchase of Gas or Electricity from Outside of New York	Imposed a compensating use tax on purchases of gas or electricity from vendors located outside of New York	June 1, 2000
Legislation Enacted in 2001		
Empire Zones	Added eight new Empire Zones, for a total of 66 zones throughout the State. Four of the eight new Empire Zones became effective immediately.	October 29, 2001
Legislation Enacted in 2002		
Temporary Exemption in Liberty Zone	Temporarily exempted most tangible personal property priced under $500 sold in the Liberty and Resurgence Zones in New York City for the periods of June 9-11, July 9-11 and August 20-22, 2002.	June 1, 2002
EFT Threshold Change	Lowered the Electronic Fund Transfer threshold from $1 million to $500,000.	September 1, 2002
Legislation Enacted in 2003		
Surcharge	Raised the State sales tax rate from 4 to 4.25 percent through May 31, 2005.	June 1, 2003
Temporary repeal of clothing exemption	Temporarily repealed the exemption on items of clothing and footwear priced under $110 and created two clothing exemption weeks at the same $110 threshold.	June 1, 2003
Use tax line on PIT return	Required a line on PIT returns for taxpayers to report use tax owed.	May 24, 2003

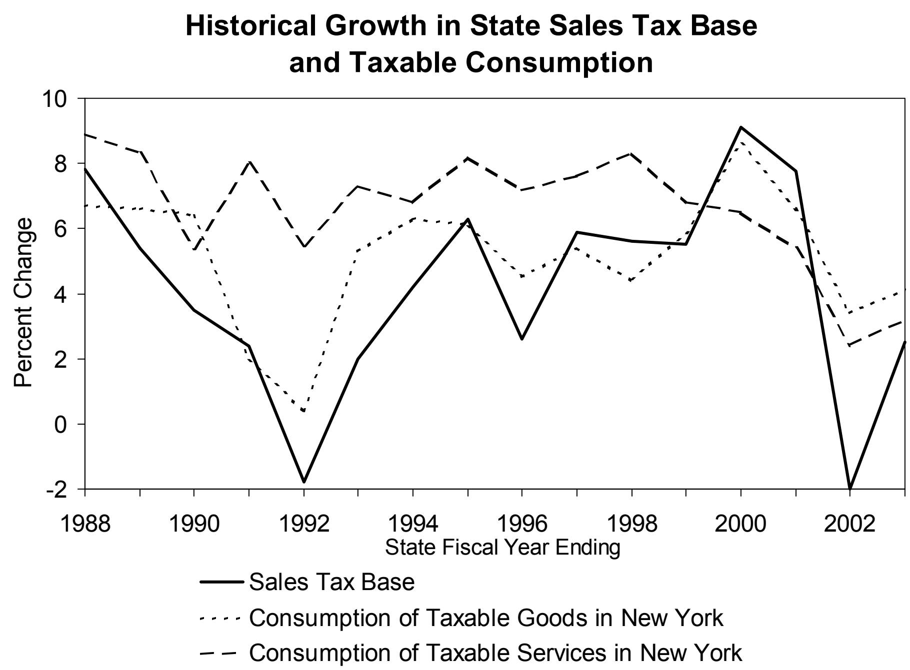
TAX LIABILITY

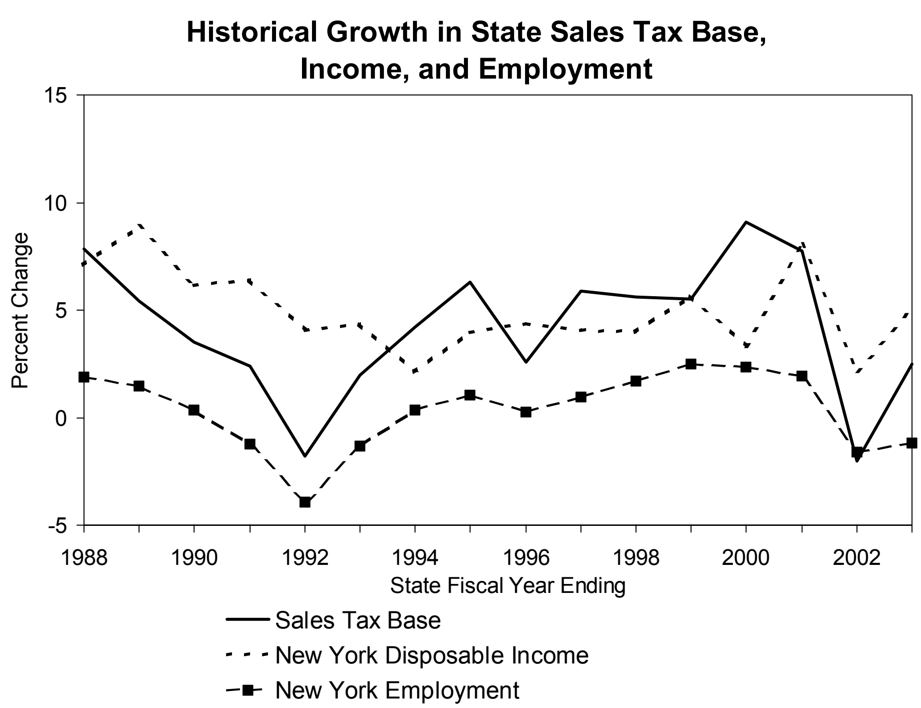
The sales and compensating use tax, which accounted for over 16.9 percent of 2002-03 General Fund tax revenues, not including transfers from other funds, is the second largest State tax revenue source (the personal income tax is the largest).

In the long run, sales tax receipts are a function of changes in the tax rate and the State's economic performance as measured by such factors as disposable income and employment. Short-run fluctuations can result from rapid changes in fuel prices, auto sales, and home sales. The following table and graphs shows the growth rate of major economic factors affecting the sales tax.

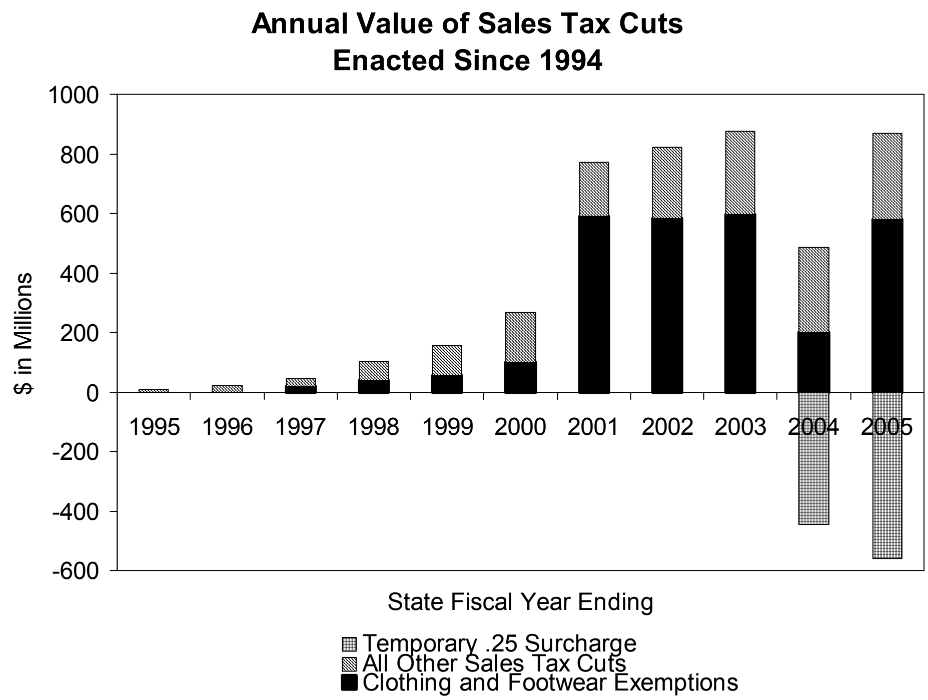
MAJOR ECONOMIC FACTORS AFFECTING SALES TAX RECEIPTS
STATE FISCAL YEARS 1995-96 TO 2004-05
Percent Change

	95-96	96-97	97-98	98-99	99-2000	2000-01	01-02	02-03	Estimated 03-04	Projected 04-05
Consumption of Taxable Goods in NY	4.5	5.4	4.4	5.9	8.6	6.6	3.4	4.1	6.0	6.7
Consumption of Taxable Services in NY	7.2	7.6	8.3	6.8	6.5	5.4	2.4	3.2	3.0	5.6
NY Employment	0.2	1.0	1.7	2.5	2.3	1.9	(1.6)	(1.2)	(0.2)	0.9
NY Disposable Income	4.4	4.1	4.0	5.7	3.3	8.1	2.1	5.0	5.1	5.3
NY Nominal Value of New Auto and Light Truck Registrations	(0.6)	12.1	3.5	14.2	12.6	(5.2)	8.2	5.0	10.5	7.2
Sales Tax Base	2.6	5.9	5.6	5.5	9.1	7.8	(2.0)	2.5	2.3	5.1

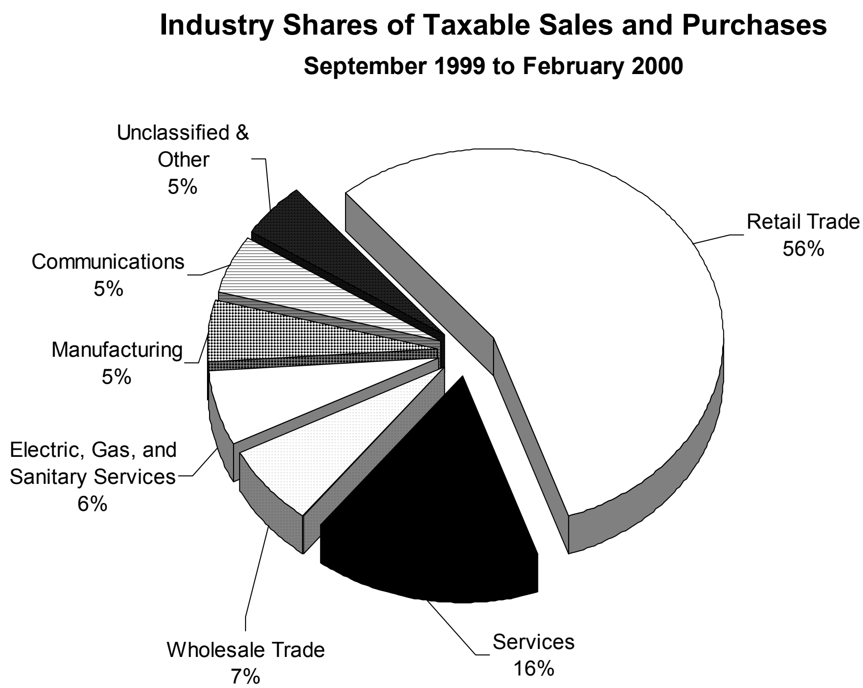




The tax cuts enacted since 1994-95 have had a substantial impact on sales tax receipts. The graph below depicts the estimated annual value of sales tax cuts enacted since 1994. The 0.25 percent temporary surcharge enacted in 2003 is shown as a negative bar.



Although numerous exemptions from tax on the sales of tangible personal property have been enacted (see “Tax Expenditures”), 56 percent of total taxable sales and purchases subject to the sales and use tax are accounted for by the retail trade industry. This includes, for example, automobile dealers and general merchandise stores. The service industry, including accommodations and food services, information, and administrative services, at 16 percent of the statewide total, accounts for the next largest share of taxable sales and purchases.



States are currently constrained by United States Supreme Court decisions limiting which out-of-state vendors can be required to collect the sales tax on a state's behalf. In general, a vendor must have some physical presence or nexus in a state to be required to collect that particular state's sales tax. Thus, a compensating use tax complements the sales tax, and is imposed on the use of taxable property or services in-state, if the transaction has not already been subject to tax. This would include, for example, taxable items purchased via mail order or over the Internet if the vendor has no taxable nexus with New York. The use tax also applies to certain uses of self-produced property or services. With some exceptions, the base of the use tax mirrors the base of the sales tax. The use tax is remitted by the purchaser directly to the New York State Department of Taxation and Finance, but low compliance for certain transactions is a continuing issue.

PROPOSED LEGISLATION

Legislation submitted with this budget includes:

- replacing the exemption on clothing and footwear priced under $110 with a $500 per item threshold during three to four exemption weeks;
- extending the exemption for alternative fuel vehicles by one year; and
- surcharges of 3 percent on the sale of protective and detective services and 4 percent on certain admission charges to fund public safety and security.

RECEIPTS: ESTIMATES AND PROJECTIONS

All Funds

2003-04 Estimates

Net All Funds collections to date are $7,477 million, an increase of $816.4 million, or 12.2 percent above the comparable period in the prior fiscal year.

Total net All Funds receipts for 2003-04 are estimated to be $9,822 million, an increase of $1,026 million, or 11.7 percent above last year.

The underlying sales tax base is estimated to increase 2.3 percent. Taxable sales were bolstered by several factors. Continued strength in mortgage refinancing allowed consumers to tap increased home equity. Brisk home sales buoyed spending on furniture and other household items, and Federal tax cuts in the form of direct payments to taxpayers allowed consumers to increase spending. In terms of real receipts growth, this recovery is somewhat similar to the early 1990s when absolute declines were followed by an initial year of slow growth (see following graph). However, the recent recession was not as severe or as prolonged as the previous recession. This may be due to buoyant consumer spending during this recession, which in turn could result in more moderate, post-recession consumption growth than, for example, the early 1980s.

Legislation enacted in 2003 imposed a 0.25 percent sales and use tax surcharge on all taxable sales. The surcharge is expected to generate $445 million in additional receipts in 2003-04. Additional legislation that suspended the clothing and footwear exemption and replaced it with two separate exemption weeks during the 2003-04 fiscal year is expected to add $441 million to 2003-04 receipts.

2004-05 Projections

Total net All Funds receipts are projected to be $10,483.2 million, an increase of $661.2 million, or 6.7 percent above 2003-04.

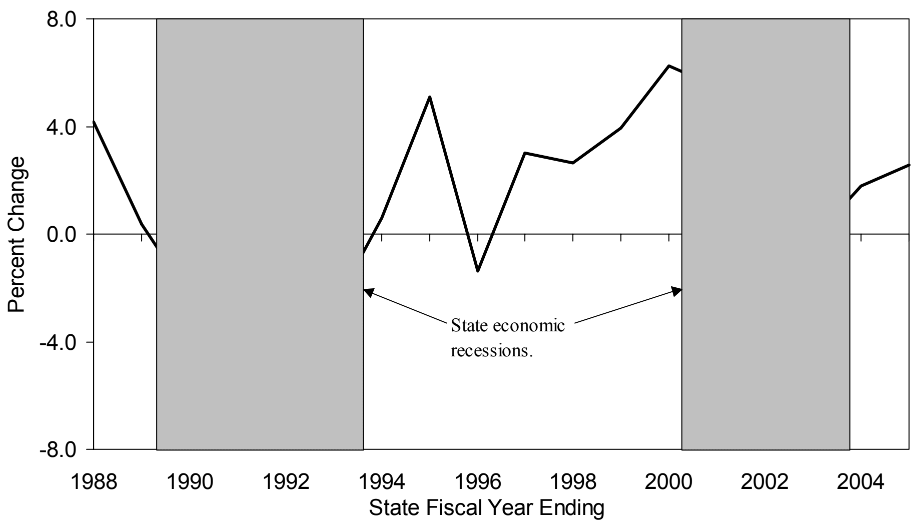
The increase is largely due to an expected rebound in national and State economic growth as well as to previously enacted and proposed tax law changes. Disposable income is expected to grow 5.3 percent and employment to grow 0.9 percent in 2004-05. Taken together, these factors help explain a projected growth in the sales tax base of 5.1 percent. The temporary 0.25 percent sales and use tax surcharge and the clothing legislation enacted in 2003 are projected to generate an additional $560 million and $103 million, respectively, in 2004-05.

Legislation submitted with this Budget proposes to eliminate the exemption on clothing and footwear priced under $110 and replace it with a $500 per item exemption effective during three separate weeks during 2004-05 and four weeks in subsequent years. This proposal is expected to generate an estimated $400 million in 2004-05. Additional legislation proposes a one-year extension of the sales tax exemption on alternative fuel vehicles. This proposal is expected to decrease 2004-05 receipts by $1.2 million. Increased sales tax receipts from the proposal to allow direct wine shipments to New York consumers (see the Alcoholic Beverage Taxes story) are expected to amount to $2 million.

Additional legislation proposes to impose a 3 percent State-only sales and use tax surcharge on currently taxable protective and detective services and a 4 percent State-only sales tax surcharge on currently taxable admission charges. The revenue from these surcharges will be deposited in a special revenue account to fund public security and safety activities. These surcharges are projected to provide $39 million in additional revenue in 2004-05.

The primary risk factor for the sales and use tax estimate is the economic forecast, which provides the basis for the projection of growth in the taxable sales base. Unexpected slowdowns in income or employment would affect consumption and thereby impact the level of taxable sales.

Real Sales Tax Constant Law Growth
1987-88 to 2004-05



General Fund

Direct deposits to the General Fund for 2003-04 are estimated to be $7,178 million, an increase of $850.4 million, or 13.4 percent, from 2002-03 receipts. All proceeds from the 0.25 percent surcharge are deposited in the General Fund. General Fund receipts in 2004-05 are projected to be $7,665.9 million, a 6.8 percent increase from the current year.

Other Funds

The Local Government Assistance Corporation (LGAC) was created in 1990 to help the State eliminate its annual spring borrowing. To pay the debt service on the bonds issued by LGAC, the State has diverted the yield of one-fourth of net sales and use tax collections from the 4 percent statewide sales tax to the Local Government Assistance Tax Fund (LGATF). Sales tax deposits to LGATF were $2,106.5 million in 2002-03 and are estimated at $2,244.5 million in 2003-04, and $2,364.0 million in 2004-05. LGATF receipts in excess of debt service requirements on LGAC bonds are transferred to the General Fund.

The Mass Transportation Operating Assistance Fund (MTOAF) was created in 1981 to finance State public transportation needs. MTOAF derives part of its revenues from the 0.25 percent sales and compensating use tax imposed in the Metropolitan Commuter Transportation District. MTOAF, which received $361.9 million in sales and use tax receipts in 2002-03, will receive an estimated $399.5 million in 2003-04, and $414.3 million in 2004-05.

As noted above, legislation proposed with this Budget would provide $39 million in 2004-05, which would be dedicated to the Public Safety and Security Account.

RECEIPTS BY FUND TYPE

SALES AND USE TAX RECEIPTS
(millions of dollars)

	Gross General Fund	Refunds	Net General Fund	Special Revenue Funds[1]	Capital Projects Funds	Debt Service Funds[2]	All Funds Net Collections
				Actual			
1995-96	5,036	41	4,995	293	0	1,666	6,954
1996-97	5,265	40	5,225	289	0	1,747	7,261
1997-98	5,467	24	5,442	306	0	1,814	7,562
1998-99	5,729	32	5,697	321	0	1,894	7,912
1999-2000	6,182	41	6,141	346	0	2,046	8,532
2000-01	6,311	39	6,272	368	0	2,092	8,732
2001-02	6,174	43	6,131	365	0	2,044	8,540
2002-03	6,390	62	6,328	362	0	2,106	8,796
				Estimated			
2003-04	7,218	40	7,178	399	0	2,245	9,822
2004-05							
(current law)	7,411	40	7,372	414	0	2,264	10,050
(proposed law)	7,726	40	7,666	453	0	2,364	10,483

[1] Mass Transportation Operating Assistance Fund and the Public Safety and Security Account.
[2] Local Government Assistance Tax Fund.

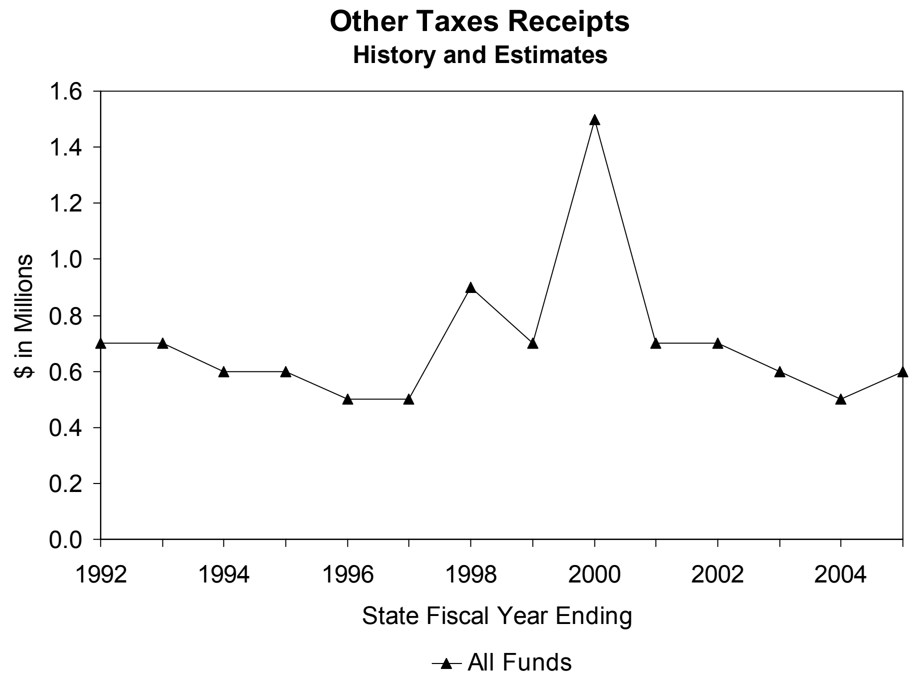
OTHER TAXES

SUMMARY

In 2003-04, All Funds collections from other taxes are estimated to be $500,000. This is a decrease of $100,000, or 16.7 percent, from the prior year, resulting from the expected reduction of the number of wrestling and boxing exhibitions compared to previous years.

In 2004-05, All Funds collections from other taxes are estimated to be $600,000. This is an increase of $100,000, or 20 percent, from the prior year, resulting from the expected return to more normal levels of boxing and wrestling exhibitions in the State due to the increased interest in this form of entertainment. Admissions to enter into racetracks and wrestling/boxing exhibitions are expected to remain fairly constant.

No new legislation is proposed with this Budget.



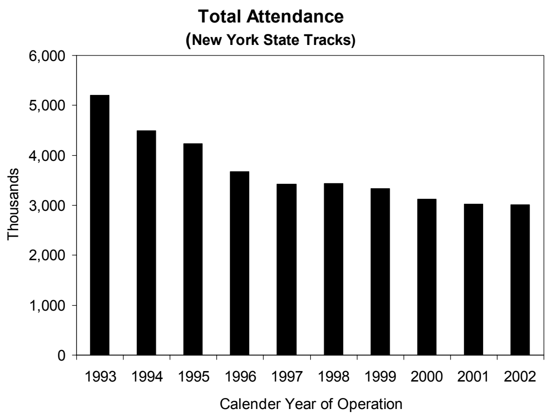
DESCRIPTION

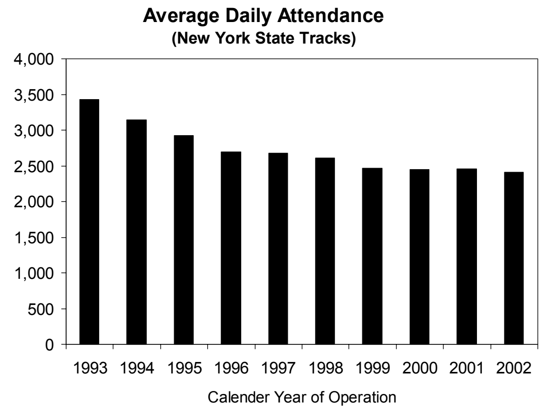
Tax Base and Rate

Racing Admissions Tax — A tax is levied on the charge for admissions to racetracks and simulcast theaters throughout the State. The increase in simulcasts at off-track betting locations with New York, expanded interstate competition, and the growth of casino activity in close proximity to New York residents, has led to declines in total paid attendance at tracks (see charts below) and in receipts from this source.

Boxing and Wrestling Exhibitions Tax — A tax is levied on gross receipts from boxing and wrestling exhibitions, including receipts from broadcast and motion picture rights. A heavyweight championship fight, which is an event of high spectator interest, can impact the yield of the tax substantially, causing receipts to vary considerably from year to year.

The racing admissions tax rate is 4 percent. The boxing and wrestling exhibitions tax rate is 3 percent.





Administration

In regard to the racing admissions tax, the New York State Racing and Wagering Board has general jurisdiction over all horse racing activities and all pari-mutuel betting activities, both on-track and off-track, in the State and over the corporations, associations, and persons engaged in gaming activities.

In reference to the boxing and wrestling exhibitions tax, the Department of Taxation and Finance is responsible for collecting the receipts.

Significant Legislation

In 1999, a cap was established for boxing and wrestling fees.

TAX LIABILITY

The major factor that affects racing admissions tax liability is the number of customers who attend on-track races; this is dependent on factors such as the weather and competition from other types of gambling or non-gambling entertainment.

The wrestling and boxing exhibitions tax can be affected by the importance of the events staged in a given fiscal year and by the degree of competition at other types of entertainment venues.

PROPOSED LEGISLATION

No new legislation is proposed with this Budget.

RECEIPTS: ESTIMATES AND PROJECTIONS

All Funds

2003-04 Estimates

Net All Funds collections to date are $486,202, a decrease of $12,645, or 2.5 percent below the comparable period in the prior fiscal year.

Total net All Funds receipts for 2003-04 are estimated to be $500,000, a decrease of $100,000, or 16.7 percent below last year. The decrease in receipts reflects the reduced number of wrestling and boxing exhibitions in New York City and the rest of the State compared to previous years.

2004-05 Estimates

Total net All Funds receipts are projected to be $600,000, an increase of $100,000, or 16.7 percent above 2003-04. The expectation is that the levels of boxing and wrestling exhibitions in New York City will return to prior levels.

RECEIPTS BY FUND TYPE

OTHER TAXES RECEIPTS
(thousands of dollars)

	General Fund		Special Revenue Funds	Capital Projects Funds	Debt Service Funds	All Funds Collections
	Admissions	Exhibitions				
	Actual					
1995-96	310	182	0	0	0	492
1996-97	272	232	0	0	0	504
1997-98	310	639	0	0	0	949
1998-99	294	400	0	0	0	694
1999-2000	280	1,220	0	0	0	1,500
2000-01	300	400	0	0	0	700
2001-02	300	400	0	0	0	700
2002-03	300	300	0	0	0	600
	Estimated					
2003-04	300	200	0	0	0	500
2004-05	300	300	0	0	0	600

MISCELLANEOUS RECEIPTS
General Fund

DESCRIPTION

Miscellaneous receipts cover a broad range of unrelated revenue sources with significant recurring income derived from abandoned property, investment earnings, fees, licenses, fines, and various reimbursements to the State's General Fund. Each year, the reported receipts are also affected by various nonrecurring transactions.

SIGNIFICANT LEGISLATION

The significant statutory changes since 1994 are summarized below.

Subject	Description	Effective Date
Legislation Enacted in 1994		
Assessments	Extended for one year the assessments on health facility providers.	April 1, 1994
Mandatory Surcharges	Extended for two years the mandatory surcharges pertaining largely to standing or moving violations of the Vehicle and Traffic Law.	October 31, 1994
Legislation Enacted in 1995		
Assessments	Extended for one year the assessments on health facility providers.	April 1, 1995
Love Canal claims	Provided for the deposit into the General Fund of moneys received from settlement of Love Canal claims.	April 1, 1995
Power Authority of NY	Provided for the one-time payment to the General Fund of $15.9 million in lieu of annual payments.	April 1, 1995
Legislation Enacted in 1996		
Assessments	Extended for one year the current assessments on health facility providers and imposed new assessments.	April 1, 1996
Power Authority, MMIA, Workers Compensation	Provided for the deposit into the General Fund of moneys from these entities, respectively: $50 million, $481 million, and $97 million.	April 1, 1996
Fees and Fines	Moved into the General Fund receipts previously deposited into various special revenue accounts.	August 31, 1996
Legislation Enacted in 1997		
Assessments	Provided for the collection of assessments for prior years from certain health facilities.	January 1, 1995
	Initiated a phase-out of the assessments on private health facility providers.	April 1, 1997
Mandatory Surcharges	Extended for two years the mandatory surcharges pertaining largely to standing or moving violations of the Vehicle and Traffic Law.	October 31, 1997
Legislation Enacted in 1998		
Assessments	Accelerated the phase-out of assessments on private health facility providers.	April 1, 1998
Legislation Enacted in 1999		
Assessments	Further accelerated the phase-out of assessments on private health facility providers.	April 1 1999
Mandatory Surcharges	Extended for two years the mandatory surcharges pertaining largely to standing or moving violations of the Vehicle and Traffic Law.	October 31, 1999
Legislation Enacted in 2000		
Assessments	Provided amnesty on interest and penalties for private health facilities that paid any outstanding assessments by March 31, 2001.	April 1, 2000
Legislation Enacted in 2001		
Mandatory Surcharges	Extended for two years the mandatory surcharges pertaining largely to standing or moving violations of the Vehicle and Traffic Law.	October 31, 2001

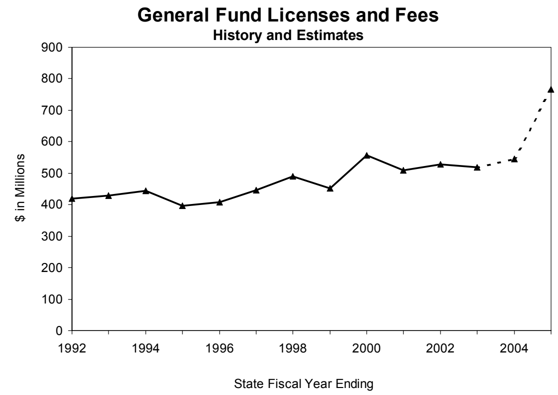
Subject	Description	Effective Date
Legislation Enacted in 2002		
Supplemental Wireless Service Surcharge	Increased from $0.70 to $1.20 monthly the State wireless communication service surcharge.	August 1, 2002
Legislation Enacted in 2003		
Abandoned Property	Reduced the time period for collecting abandoned property related to the demutualization of insurance companies, from five years to two.	January 1, 2003
Assessments	Increased cost recovery assessments' cap from $20 million to $40 million.	April 1, 2003
Criminal Fines	Increased criminal fines deposited into the Justice Court Fund from between $100 and $1,500 to $150 and $2,250.	April 1, 2003
Lobbyist Fee	Increased annual lobbyist registration fees to $100 (2004) and $200 (2005).	April 1, 2003
Uncashed Checks	Reduced dormancy period of uncashed checks from three years to one year.	April 1, 2003
Background Checks	Required holders of HAZMAT license endorsement to undergo criminal background check for a fee of $75.	May 15, 2003
Sex Offender Fee	Required sex offenders to pay a DNA databank fee of $50, a sex offender registration fee of $50, and a sex offender registration change fee of $10.	May 15, 2003
Data Search Fee	Increased data search fee by $1.	July 1, 2003
Court Motion Fees	Imposed a $45 motion fee on Supreme/County and Appellate Courts, a stipulation of Discontinuance Fee of $35 and increased all Civil Court Fees by 25%.	July 14, 2003
Oil and Gas Depth Fees	Increased Oil and Gas Depth fees by 50%.	August 1, 2003
Penal Bonds	Increased fee on penal bonds from $1,000 to $2,500.	October 1, 2003
DWI or DWAI Surcharge	Imposed a $25 surcharge on DWI or DWAI convictions.	November 12, 2003
Parking Surcharges	Increased parking surcharges from $5 to $15.	November 12, 2003

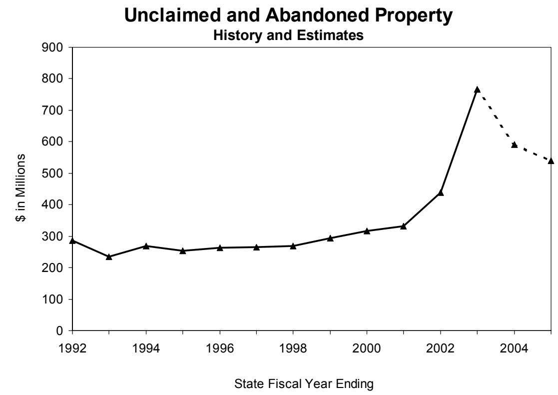
Proposed Legislation

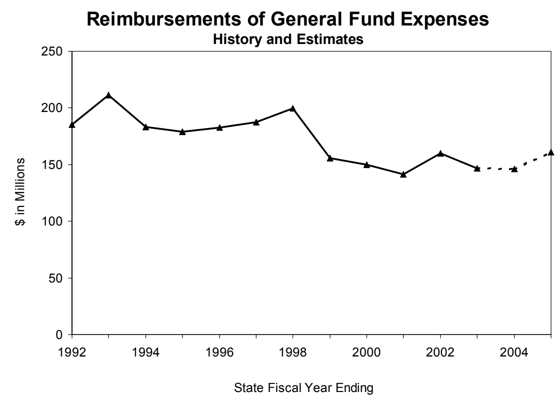
Legislation submitted with the Executive Budget proposes to add new charges and fees and to raise the amount of some existing charges and fees. The following is a table and summary of the proposals impacting General Fund Miscellaneous Receipts.

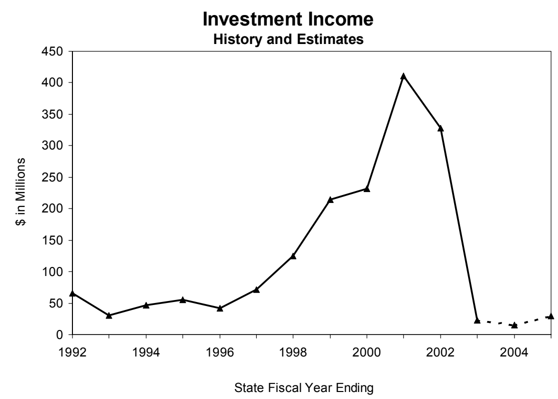
DESCRIPTION	CHANGE		VALUE IN 2004-05
			(millions of dollars)
Alcoholic Beverage License Filing Fees	Various		0.2
Banking Fees	From	$10 to $20 $5,000 to $10,000	2.0
Parking Ticket Surcharge	New	$15	7.5
Record Review Fee	From	$25 to $50	0.1
Work Zone Automated Speed Enforcement	New	$100	15.0
Tax Credit Application Fee	From	$100 to $200 $250 to $500 4% to 5%	0.5
ATV Registration Fee	From	$10 to $45	5.8
Driver Responsibility Program	New	$100 and $1,000	17.5
Federal Bed Capacity Contract	New	$30,000/bed	15.0
Divisible Load Permits and Fines	Various	$50 to $150	1.5
Waste Tire Fee	Extension of $2.25/tire		0.3
New State Land Gas Lease Sales	Various		0.8
Deceptive Trade Practices Penalty	From	$500 to $5,000	0.5
Snowmobile Fee	From	$5 to $10	1.0
Handgun License Fee	New	$20 to $100	31.0
Vehicle and Traffic Local Prosecution Program	Various		17.8

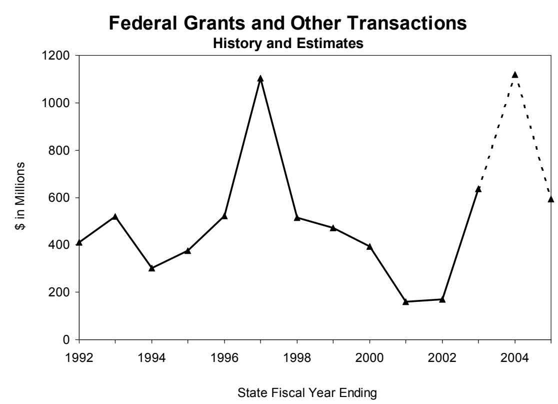
Components of Miscellaneous Receipts











Historically, General Fund Licenses and Fees revenues have grown modestly and fairly consistently, aside from minimal peaks and troughs associated with law changes. In 2004-05, these revenues are expected to increase as a result of fee increases proposed in the Executive Budget.

Historically, Unclaimed and Abandoned Property revenue has remained relatively stable with minimal growth, aside from a spike in 2002-03 and 2003-04 resulting from a large amount of abandoned property released to the State of New York by the Office of the State Comptroller. This property was associated with the sale of stocks as well as a reduction in the dormancy period of uncashed checks. Unclaimed and Abandoned Property revenue is expected to return to more normal levels in the forecast period.

Historically, Reimbursements of General Fund Expenses Revenues have remained relatively constant. Reimbursements are expected to remain relatively constant over the forecast period.

The trends in Investment Income are directly related to the General Fund account balances and interest rates. For example, the large increase in 2000-2001 followed by the severe drop in 2002-2003 is a result of the impact of the economic growth and subsequent recession on the State's finances - balances declined and interest rates declined. The forecast for Investment Income is a slight increase in the outyears as interest rates increase.

Federal Grants and Other Transactions, excluding tobacco securitization proceeds, are an unrelated grouping of transactions and payments, which do not fall under the other Miscellaneous Receipts categories. Differences in collections year-to-year are the result of large, unusual payments to the State of New York. The increase in 2003-04 and its continuation in the forecast for 2004-05 is due to: Federal revenue sharing grants; Bond Issuance Charges on Tobacco Bond Proceeds; a supplemental wireless surcharge; and an increased number of Wall Street settlement payments to the State of New York.

2002-03 RECEIPTS

In State fiscal year 2002-03, miscellaneous receipts totaled $2,091 million. Major revenue sources in that year included: $767 million in unclaimed and abandoned property; $518 million in fees, licenses, fines, royalties, and rents; $150 million from the State of New York Mortgage Agency; $145 million in medical provider assessments; $145 million in reimbursements; $139 million in additional bond issuance charges; $67 million from the PASNY for the Power of Jobs program; $38 million from the New York State Housing Finance Agency; $28 million from the supplemental wireless surcharge; and $23 million in interest earnings on short-term investments and bank accounts (this amount is net of certain expenses incurred in providing banking services to various State agencies). In addition the receipts include, $6 million in Federal grants and $6 million from revenue maximization.

2003-04 ESTIMATES

Miscellaneous receipts are estimated at $6,615 million for fiscal year 2003-04, including $4,200 million in Tobacco Bond proceeds. With tobacco proceeds excluded, miscellaneous receipts are estimated to increase $323 million from the prior year. The estimate includes $652 million from Federal Revenue Sharing grants; receipts of $590 million in unclaimed and abandoned property; $546 million in fees, licenses, fines, royalties, and rents; $148 million in medical provider assessments; $146 million in reimbursements; $113 million in additional bond issuance charges; $69 million in extraordinary fines from various Wall Street firms; $58 million from PASNY for the Power for Jobs program; $56 million from the supplemental wireless surcharge; $15 million in net investment earnings; $11 million from a tobacco settlement; $9 million from the Port Authority of New York and New Jersey; and $3 million from petroleum overcharge recoveries.

2004-05 PROJECTIONS

Miscellaneous receipts are projected at $2,087 million in fiscal year 2004-05, a decrease of $328 million from the amount estimated for 2003-04, with tobacco proceeds excluded. This projection includes $766 million in fees, licenses, fines, royalties and rents; receipts of $540 million in unclaimed and abandoned property; $181 million from a transfer of tobacco proceeds; $161 million in reimbursements; $149 million in medical provider assessments; $101 million in bond issuance charges; $100 million from PASNY for the Power for Jobs program; $73 million from the supplemental wireless surcharge; $30 million in net investment earnings; $25 million in proceeds from ESDC privatization and $4 million in Federal grants.

MISCELLANEOUS RECEIPTS
GENERAL FUND
(millions of dollars)

	2000-01	2001-02	2002-03	2003-04	2004-05
	Actual			Estimated	Projected
License, Fees, Etc.	509	528	518	546	766
Federal Grants	4	4	6	652	4
Abandoned Property	333	439	767	590	540
Reimbursements	141	160	144	146	161
Investment Income	411	328	23	15	30
Other Transactions*	155	166	633	4,666	586
Total	1,553	1,625	2,091	6,615	2,087

* Includes proceeds from Tobacco securitization.

MISCELLANEOUS RECEIPTS
Special Revenue Funds

Miscellaneous receipts deposited to special revenue funds represent approximately 23 percent of total special revenue receipts, excluding transfers from other funds. These receipts include State University of New York (SUNY) tuition and patient income, lottery receipts for education, programs funded by HCRA, assessments on regulated industries, and a variety of fees and licenses, all of which are dedicated to support specific programs.

STATE UNIVERSITY INCOME

The majority of special revenue receipts that support SUNY's operations are provided by tuition, patient revenue, and user fees. SUNY's three teaching hospitals at Brooklyn, Stony Brook and Syracuse receive patient revenue from third-party payors including Medicare, Medicaid, insurance companies, and individuals. User fees, which include fees for food, parking, career placement and recreation, are generated from service users, including students, faculty, staff, and the public.

LOTTERY

Receipts from the sale of lottery tickets and proceeds from the expected implementation of VLTs at racetracks are used to support public education, as well as administrative costs associated with Lottery operations. The Lottery is discussed in detail in a separate section.

INDIGENT CARE

The Indigent Care Fund allows the State to claim Federal reimbursement for payments to hospitals that provide care for the medically indigent. The State makes payments in the first instance from a bad debt and charity care pool funded with non-Federal Medicaid dollars, and money from various payors including insurance companies and hospitals.

HCRA FINANCING

Receipts from the Tobacco Control and Insurance Initiatives Pool and the Health Care Initiatives Pool are used primarily to finance a portion of the State's Medicaid program, including expansion of programs such as Family Health Plus, workforce recruitment and retention, the Elderly Pharmaceutical Insurance Coverage Program, Child Health Plus, AIDS programs and community mental health expansion programs.

PROVIDER ASSESSMENTS

The provider assessment account receives moneys from a reimbursable assessment on nursing home revenues. The 2004-05 Executive Budget proposes an increase in the assessment on nursing home revenues from 5 percent to 6 percent and the reimposition of a nonreimbursable 0.7 percent assessment on hospital and home care revenues.

ALL OTHER

The remaining revenues in this category include fees, licenses, and assessments collected by State agencies, primarily to support all or specific components of their operations. Receipts from assessments primarily reflect reimbursements from regulated industries, which fund the administrative costs of State agencies charged with their oversight. State agencies funded entirely from assessments include the Banking Department, the Insurance Department, the Public Service Commission, and the Workers' Compensation Board.

MISCELLANEOUS RECEIPTS
SPECIAL REVENUE FUNDS
(millions of dollars)

	2000-01	2001-02	2002-03	2003-04	2004-05
	Actual			Estimated	
State University income	1,656	1,824	1,944	2,240	2,303
Lottery	1,587	1,713	1,931	2,030	2,318
Indigent care	873	836	1,056	901	876
HCRA financing	854	1,072	2,086	2,477	2,756
Provider assessments	0	0	423	371	629
All other	1,676	1,684	2,130	2,377	2,596
Total	6,646	7,129	9,570	10,396	11,478

LOTTERY

SUMMARY

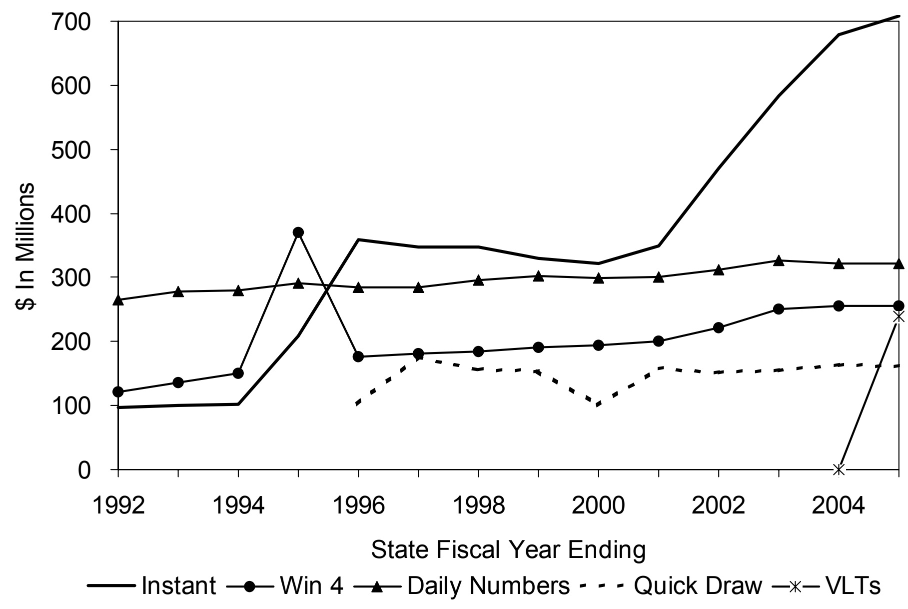
In 2003-04, All Funds collections from the Lottery Division are estimated to be $1,868.7 million. This is an increase of $42.5 million, or 2.3 percent, from the prior year, reflecting higher-than-expected sales in Instant Games, a full-year effect of the Mega Millions game, and improved sales in Quick Draw. The 2003-04 supplemental lottery appropriation sets disbursements to education at $1,835.1 million. The $33.6 million balance will be carried forward to 2004-05.

In 2004-05, All Funds current law collections from the Lottery Division are projected to be $1,767.7 million. This is a decrease of $67.4 million, or 3.7 percent, compared with 2003-04.

Legislation proposed with this Budget includes provisions to:

- Allow a VLT licensing program, which will allow up to 8 new facilities in New York State.
- The Quick Draw game expires on May 31, 2004. The Lottery Division proposes legislation to make permanent the authorization to operate Quick Draw. Estimated revenue, including administrative surplus, from Quick Draw for 2004-05 is $162 million. In addition, the proposed legislation will authorize the elimination of specific hours, space, and food requirements. This is expected to increase revenues from Quick Draw by $43 million.

Fixed Odds & Instant Game Revenues



DESCRIPTION

In 1966, New York State voters approved a referendum authorizing a State lottery, and ticket sales commenced under the auspices of the Division of the Lottery (the Division). Under the original lottery legislation, a lotto-type game was offered with 30 percent of gross receipts earmarked to prizes, 55 percent to education, and the remaining 15 percent representing an upper limit on administrative expenses. Since then, numerous games have been introduced with varying prize payout schedules to make them attractive to the consumer.

The Division manages the sale of lottery tickets, and operates as an independent agency within the Department of Taxation and Finance. The Division, pursuant to legislation enacted in 2001, is authorized to operate five types of games:

- Instant games, in which most prizes are won immediately;
- Lotto games, which are pari-mutuel, pick-your-own-numbers games offering large top prizes with drawings conducted eleven times weekly: seven 5-of-39 draws (Take-5), two 6-of-59 draws (Lotto 59) and two multi-jurisdictional drawings (Mega Millions). For the Lotto 59 game and the Mega Millions (multi-jurisdictional game), the value of any top prize not won is added to the top prize in the subsequent drawing;
- Daily numbers games, which are fixed-odds games with daily drawings where players select either a three-digit number (Daily Numbers), a four-digit number (Win 4), and Instant Win, an add-on game to Daily Numbers and Win 4;
- Keno-like games, which are pari-mutuel pick-your-own 10-of-80 numbers games with drawings conducted either daily (Pick 10) or every four minutes (Quick Draw) during certain intervals. The Division pays top prizes of $500,000 in Pick 10 and $100,000 in Quick Draw; and
- Video lottery games, which are lottery games played on video gaming devices. The VLTs, are currently authorized to be used only at selected thoroughbred and harness tracks.

The minimum statutory allocation to education for the Lotto 59 and Instant Win game is 45 percent of ticket sales; for the Mega Millions, Take-5, Win 4, Numbers and Pick 10 games, 35 percent; for Instant Games, 20 percent with three games authorized at 10 percent; for Quick Draw, 25 percent; and for Video Lottery Terminals (VLTs), 61 percent of net machine income. After the earmarking for prizes, the Division has available 15 percent of net sales for its administrative expenses, of which any unused portion is used to support education.

Distribution of Lottery Sales
(Percent)

	Prizes	Revenue Percent	Admin. Allow
Lotto	40.0	45.0	15.0
Lotto - Millenium Millions	40.0	45.0	15.0
Instant Win	40.0	45.0	15.0
Mega Millions 50% Prize Payout	50.0	35.0	15.0
Take 5	50.0	35.0	15.0
Quick Draw	60.0	25.0	15.0
Numbers	50.0	35.0	15.0
Win 4	50.0	35.0	15.0
Pick 10	50.0	35.0	15.0
Instant	65.0	20.0	15.0
Three Games 75%	75.0	10.0	15.0
VLTs*	92.0	4.9	3.1

*Applies to SFY 2004-05. The administrative allowance includes the commission paid to the track (1.62 percent), purses (0.6 percent), and Breeders' funds (0.1 percent), and the amount retained by Lottery for administration (0.8 percent).

Administration

The Lottery Division develops, advertises, distributes, and performs all required responsibilities necessary to operate an effective State lottery. Under current law, the Comptroller, pursuant to an appropriation, distributes all net receipts from the lottery directly to school districts. This aid includes special allowances for textbooks for all school children and additional amounts for pupils in approved State-supported schools for the deaf and the blind.

Significant Legislation

The significant lottery legislation enacted since 1994 is summarized below.

Subject	Description	Effective Date
Legislation Enacted in 1994		
Limit on Draws per Day	The tickets for Pick 10, Take-5, and Lotto games are to be offered no more than once daily.	April 1, 1994
Unclaimed Prize Money	The use of unclaimed prize money to supplement other games by the Division is limited to 16 weeks per year.	April 1, 1994
Annual Plan	The Division is required to submit an annual report to the Legislature, the Governor, and the Division of the Budget each year.	April 1, 1994
Legislation Enacted in 1995		
Quick Draw	Authorized Quick Draw.	April 1, 1995
	Authorized a 60 percent prize payout.	
	Drawings for the game can be held no more than 13 hours each day, of which only eight hours can be consecutive.	
	If there is no license for the sale of alcohol, then the premises have to be a minimum of 2,500 square feet.	
	If there is a license to sell alcohol, then at least 25 percent of the gross sales must be from sales of food.	
Legislation Enacted in 1999		
Instant Games	Authorized a 65 percent prize payout.	April 1, 1999
	Reduced the percent dedicated to education from 30 percent to 20 percent.	
Legislation Enacted in 2001		
Multi-jurisdictional	Allowed the Lottery Division to enter into agreements to conduct multi-jurisdictional lotto games with a 50 percent prize payout.	October 29, 2001
Video Lottery Terminals	Allowed the Lottery Division to license the operation of video lottery machines at selected New York State racetracks.	October 29, 2001
Legislation Enacted in 2002		
Instant Games	Three 75 percent prize payout Instant ticket games may be offered during the fiscal year.	January 28, 2002
Legislation Enacted in 2003		
Quick Draw	Extended the operation of Quick Draw until May 31, 2004.	January 28, 2002
Video Lottery Terminals	Of the total amount wagered on video lottery terminals, 92 percent is paid out for prizes. Of the balance, the Lottery Division retains 10 percent for administration, 29 percent is paid to the racetracks as a commission, and 61 percent is dedicated to education. Of the commission paid to the tracks, the amount allocated to purses in years one through three is 25.9 percent; in years four and five, 26.7 percent; and in subsequent years, 34.5 percent. The Breeders' funds receive 4.3 percent of the commission paid to racetracks in the first through fifth years and 5.2 percent in the following years. The racetracks are allowed to enter into agreements, not to exceed five years, with the horsemen to reduce the percentage of the vendor fee allocated to purses. The program expires ten years after the start of the program.	May 2, 2003

LOTTERY DEMAND

Factors that affect the demand for Lottery games include: the price of the lottery tickets, the amount spent on advertising and marketing, the prize payout percentage, the development of new games that generate increased sales, the potential customers' attitude towards the Lottery Division and competition from other gambling venues.

PROPOSED LEGISLATION

- The VLT licensing proposal will allow the Lottery Division to authorize up to 8 licenses for VLT gaming locations in New York State. A separate license is required for each VLT facility. This proposal was developed, in part, to generate additional education revenue to fund Sound Basic Education (SBE). The licenses will be awarded on a competitive basis and each proposed VLT location will be approved by the Lottery Division. In New York City, no more than five VLT facilities will be allowed to locate in New York County (south of 59th Street), Kings, and Richmond. No licenses will be granted for locations that are within 15 miles of a licensed VLT facility at a racetrack. To preserve competitive balance no additional facilities will be permitted in Westchester, Putnam and Rockland counties
- The Quick Draw game expires on May 31, 2004. The Lottery Division proposes legislation to extend the authorization to operate Quick Draw. Estimated revenue, including administrative surplus, from Quick Draw for 2004-05 is $162 million.
- The proposed legislation will authorize the elimination of restrictions on the Lottery's Quick Draw game. Under current law, Quick Draw may only be offered: (1) at facilities licensed for the sale of alcoholic beverages for on-premises consumption if at least 25 percent of the gross sales of the business are sales of food; (2) at locations not licensed for the sale of alcoholic beverages for consumption on the premises if the premises are greater than 2,500 square feet in area; and (3) Quick Draw is allowed no more than 13 hours of daily operations — no more than 8 hours of which may be consecutive. The estimated additional revenue gained from the elimination of the Quick Draw restrictions are $43 million, in State fiscal year 2004-05.

RECEIPTS: ESTIMATES AND PROJECTIONS

All Funds

2003-04 Estimates

Net All Funds collections to date are $1,196.9 million, an increase of $80.8 million, or 7.2 percent above the comparable period in the prior fiscal year. Growth in revenue can be attributed primarily to better-than-expected Instant Game sales. To date, Instant Game sales are 14 percent above last year's sales. Recent legislation that increased the prize payout on instant ticket games; added up to three games each year with a 75 percent prize payout; and introduced new more popular game formats. All of these factors have contributed to sales growth.

Net All Funds collections for 2003-04 are estimated to be $1,868.7 million, an increase of $42.5 million, or 2.3 percent above last year. (See Table 1.) Total net All Funds sales for 2003-04 are estimated to be $5.9 billion that, in turn provides $1.6 billion in receipts for education. This is an increase of $84.5 million, or 5.6 percent, above last year. Unspent administrative allowances and miscellaneous income is estimated at $277.2 million. The 2003-04 supplemental lottery appropriation sets disbursements to education at $1,835.1 million. The $33.6 million balance will be carried forward into 2004-05.

A game by game profile reveals that:

Instant Games, as stated above, are experiencing increased sales. Total Instant Game sales are expected to increase by 19.5 percent and revenue from instant ticket sales is expected to increase to $536.8 million in 2003-04.

Lotto sales have declined over the past several years. The declines are attributable to: (1) a general dilution of interest in ordinary jackpots; (2) increased competition from gambling outlets in and around New York; (3) reduced consumer interest, based on the maturity of the game; (4) a decline in the number of very large jackpots — a reflection of reduced participation; (5) low interest rates which limits the size of jackpots at every prize level; and (6) competition from Mega Millions. Similar declines have been experienced in many states with similar Lotto structures.

Mega Millions sales are $331.5 million. New York State is proving to be a dominant state among the Mega Millions coalition. To date, there have been only three substantial jackpot roll-ups during this State fiscal year. Considering the sales experience in 2002-03, the average weekly sales for Mega Millions in 2003-04 are expected to remain constant.

Take 5 continues to be characterized by diminishing sales. Competition from Mega Millions and a maturing game life cycle has caused estimated sales to drop by 4 percent, compared to 2002-03.

Numbers and Win 4 games are still benefiting from the addition of a second daily draw that was begun by the Division on December 2001. Revenue from sales for the Numbers game is expected to increase marginally from $263.4 million, in 2002-03, to $264 million in 2003-04. The estimated increase in revenue from sales for the Win 4 game is $7.8 million over 2002-03. The estimated combined revenue effect for State fiscal year 2003-04 from the addition of the second daily draw is $61.7 million. Numbers sales are expected to increase by 0.2 percent and Win 4 sales are estimated to increase by 4 percent.

The Instant Win game was introduced in October of 2002. Instant Win is a terminal game that offers Daily Number and Win 4 players the opportunity to win prizes up to $500 for an additional $1 wager. Initial sales were promising but quickly deteriorated, reflecting only modest customer interest in this game. Revenue from sales are estimated to decrease by 15.2 percent in 2003-04 from 2002-03.

Pick 10 sales are expected to continue to marginally decline. Revenue from sales are estimated to remain constant at $11.9 million.

Quick Draw sales are expected to increase by 5 percent in 2003-04 over 2002-03. The primary reason for the improvement in sales is the increase in draws from every 5 minutes to every 4 minutes. The change in draws was made on February 23, 2003. Some Quick Draw vendors have boycotted Quick Draw sales as a protest over smoking restrictions. This has offset a portion of the gains associated with increased draws.

Despite several challenges, conflicts, and delays encountered with the VLT program, the Division has made substantial progress towards the opening of VLTs at authorized New York State racetracks. A central computer system is in place; all required contracts with VLT vendors and other related business entities are now approved by the Comptroller's office; and the initial gaming floor layouts have been received from most of the racetracks.

Due to the delays in the initiation of the VLT program, the Division of the Budget is not including any revenues from VLTs in the 2003-04 Financial Plan.

2004-05 Projections

Total net All Funds receipts are projected to be $1,767.7 million, a decrease of $67.4 million, or 3.7 percent, below 2003-04, with lottery base sales for 2004-05 estimated to be $5.9 billion. This figure includes $1,488 million in revenues from sales, $246.1 million in unused administrative surplus and miscellaneous receipts, and a $33.6 million carry-in from 2003-04.

Game by game estimates can be summarized as follows:

Instant games revenues are expected to increase by $26.2 million, in 2004-05. The higher payout games are projected to be entering a mature cycle.

Lotto game revenues are estimated to decline by $8.8 million. The continuing drop in Lotto sales reflects the increased competition from other gambling options, (e.g., casinos and VLTs) and continued cannibalization from the Mega Millions game.

Net receipts from Mega Millions is expected to drop by 1 percent, to $145.6 million in 2004-05. The game has gained a customer base, but the jackpots have yet to attain the anticipated lofty levels that its competition, the Powerball game, has achieved.

Revenues from Take-5 games are projected to drop by $12 million. The negative impact of competition from Mega Millions and the anticipated continuation of the game's maturation cycle will contribute to continued declines in sales.

Daily Numbers and Win 4 are estimated to remain roughly constant from State fiscal year 2003-04.

The Instant Win revenues are projected to decline by $0.6 million in State fiscal year 2004-05.

Revenues from Pick 10 are expected to decrease by $1 million, due to competition from the more popular Instant and Take-5 games.

The Quick Draw game is projected to decline $104 million, or 84 percent, in State fiscal year 2004-05, if the game is allowed to sunset on May 31, 2004. The estimated administrative surplus for 2004-05 will be further reduced by $31.6 million, because Quick Draw will only be operating the first two months of the State fiscal year. In addition, base sales are expected to drop because of competition from other games, restrictions on locations that can operate Quick Draw games, a maturing sales cycle, and continued diminished sales due to the recent smoking restrictions.

The current VLT program is estimated to generate $240.1 million in incremental revenues in State fiscal year 2004-05. All receipts from the VLT program are to be deposited in a separate Lottery account, not co-mingled with existing Lottery receipts, to help fund SBE. Despite anticipated construction and administrative delays, the following racetracks are expected to be operating in 2004-05: Saratoga Equine Sports Center, Buffalo Trotting Association, Inc., Finger Lakes Race Track, Monticello Raceway Management, Inc., and Batavia Downs. The proposed expansion of VLT facilities included with the Budget is expected to have no revenue impact in 2004-05. However, any receipts received from this expansion would also be deposited in the new account earmarked for SBE.

TABLE 1
COMPONENTS OF LOTTERY RECEIPTS
(millions of dollars)

	1999-2000 Actual	2000-01 Actual	2001-02 Actual	2002-03 Actual	2003-04 Estimated	Current Law 2004-05 Projected	Proposed Law 2004-05 Projected
Instant Game	272.7	283.0	377.1	465.7	536.8	563.0	563.0
Lotto Games[1]	339.5	304.6	254.8	175.7	162.3	153.5	153.5
Mega Millions				129.0	147.1	145.6	145.6
Take-5	114.8	135.0	152.2	133.5	128.5	116.3	116.3
Daily Numbers[2]	246.7	247.4	256.8	267.0	267.2	265.7	265.7
Win-4[2]	159.6	164.5	182.4	205.6	212.8	212.6	212.6
Pick 10	15.1	14.5	13.2	11.9	11.9	10.7	10.7
Quick Draw	82.2	126.7	121.8	118.6	124.9	20.6	156.6
Subtotal	1,230.6	1,275.7	1,358.3	1,507.0	1,591.5	1,488.0	1,624.0
Administrative Surplus[3]	119.1	159.8	193.2	281.9	277.2	246.1	287.8
Current Receipts Subtotal	1,349.7	1,435.5	1,551.5	1,788.9	1,868.7	1,734.1	1,911.8
Carry-In	0.0	4.7	47.2	37.2	0.0	33.6	33.6
Net Receipts for Education	1,349.7	1,440.2	1,598.7	1,826.2	1,868.7	1,767.7	1,945.4
Carry-Out	(4.7)	(47.2)	(37.2)	0.0	33.6	0.0	0.0
Disbursements for Education	1,345.0	1,393.0	1,561.5	1,826.2	1,835.1	1,767.7	1,945.4
VLTs						240.1	240.1

1 Includes receipts from Lotto and Millennium Millions (Millennium Millions on December 1999 and October 2000).
2 Includes Instant Win
3 Reflects miscellaneous income and the balance of the 15 percent administrative allowance, after deduction of actual expenses, vendor allowances, and agent commissions.

The continuation of Quick Draw and removal of restrictions on Quick Draw; and the continued positive influence of Instant Game sales results in total sales of lottery games of an estimated $5.9 billion. This will provide net lottery receipts of $1,624 million. An additional $240.1 million expected from VLTs is to be deposited in a new separate Lottery account for the purpose of funding SBE. Additionally, $287.8 million from surplus administrative funds and miscellaneous receipts, and a $33.6 million carry-in from 2003-04, result in net lottery receipts for education of $2,185.5 million.

TABLE 2
NET LOTTERY RECEIPTS FOR EDUCATION
(millions of dollars)

---------- Actual ----------	
1995-96	1,441.3
1996-97	1,533.2
1997-98	1,533.9
1998-99	1,442.4
1999-2000	1,349.7
2000-01	1,440.2
2001-02	1,598.7
2002-03	1,826.2
---------- Estimated ----------	
2003-04	1,835.1
2004-05	
(current law)	2,007.8*
(proposed law)	2,185.5*

Includes $240.1 million in VLT receipts to be deposited in a separate Lottery account to help fund SBE.

MISCELLANEOUS RECEIPTS
Capital Projects Funds

Miscellaneous receipts in the Capital Projects Fund type include reimbursements from the proceeds of bonds sold by public authorities, fees, and other sources of revenue dedicated to specific funds, primarily for environmental or transportation capital purposes. The Miscellaneous Receipts table reflects an accounting adjustment for capital activity that is not reflected by the Comptroller's accounting system, but which is included in the Five-Year Capital Program and Financial Plan.

REIMBURSEMENT FROM AUTHORITY BOND PROCEEDS

Pursuant to statutory authorizations, State agencies enter into contractual arrangements with public authorities to provide for the financing of State capital projects. The State makes payments directly for projects and is reimbursed by the public authority from the proceeds of bonds. The amount of reimbursements received annually is a direct result of the level of bondable capital spending in that year and the timing of bond sales. As bondable spending fluctuates with the progress of capital programs, so do the bond receipts reimbursing such spending. Reimbursements from authority bond proceeds will account for approximately 94 percent of all miscellaneous receipts flowing to Capital Projects Funds in 2003-04 and 2004-05.

STATE PARKS REVENUES

User fees and other revenues generated by State parks are deposited into the State Parks Infrastructure Fund. These revenues, which are projected at $22 million in 2004-05, will be used to finance improvements in the State's park system.

ENVIRONMENTAL REVENUES

Miscellaneous receipts from environmental revenues are projected to decrease from $91 million in 2003-04 to $60 million in 2004-05. This decrease is attributable to changes in reimbursements for advance spending for various projects, which have been or are anticipated to be completed in 2003-04.

Environmental revenues also include receipts that are deposited to the Environmental Protection Fund from the sale of surplus State lands, leases of coastal State property, settlements, and the sale of environmental license plates. Other environmental revenues from settlements with individuals and other parties who are liable for damage caused to State environmental properties are deposited in the Natural Resource Damages Fund.

ALL OTHER

Various other moneys are received in the Capital Projects Funds to support capital programs and to reimburse the State for capital spending on behalf of municipalities and public authorities, such as the Housing Finance Agency. The remaining receipts are repayments of moneys advanced or loaned to municipalities, authorities, and private corporations.

MISCELLANEOUS RECEIPTS
CAPITAL PROJECTS FUNDS
(millions of dollars)

	2000-01	2001-02	2002-03	2003-04	2004-05
	---------- Actual	----------	----------	---------- Estimated	----------
Authority Bond Proceeds					
Transportation	875	710	473	1,752	1,221
Public Protection	197	140	295	188	188
Health and Social Welfare	0	0	0	23	29
Education	413	266	283	646	735
Mental Health	40	63	86	248	198
Econ. Develop./Gov. Oversight	12	101	260	347	790
General Government	0	12	23	47	152
Other	42	68	96	226	198
State Park Fees	16	23	23	22	22
Environmental Revenues	28	20	38	91	60
All Other	51	41	102	96	149
Total	1,674	1,444	1,679	3,686	3,742
Accounting Adjustment				(995)	(1,310)
Financial Plan Total				2,691	2,432

MISCELLANEOUS RECEIPTS
Debt Service Funds

Miscellaneous receipts in the Debt Service fund type include patient revenues, fees, interest income, and other revenues. These revenues are dedicated in the first instance for the payment of lease-purchase agreements, contractual obligations, and debt service, and support about 16 percent of the State's debt service payments. These revenues have been pledged as security for bonds issued for mental hygiene and health facilities, and dormitories, or are used by the State to pay debt service on general obligation housing bonds. After such requirements are satisfied, the balance of most miscellaneous receipts, together with other receipts and transfers, flow back to the General Fund or to Special Revenue funds which are used to offset the cost of State operations.

MENTAL HYGIENE RECEIPTS

Payments from patients and various third-party payers, including Medicare and insurance companies, for services provided by the mental hygiene agencies are deposited in the Mental Health Services Fund as miscellaneous receipts. Additionally, portions of State and local assistance and Federal Medicaid payments to not-for-profit community facilities are earmarked to pay their share of debt service, and are also deposited as miscellaneous receipts in the Mental Health Services Fund. These receipts, together with the transferred Medicaid money, secure bonds sold by the Dormitory Authority (DA) for State and community mental hygiene facilities.

DORMITORY FEES

Miscellaneous receipts in the State University of New York (SUNY) Dormitory Fund are composed primarily of fees charged to SUNY students for room rentals in the dormitories. The receipts of the Fund are pledged for debt service on bonds sold by the DA for the construction and improvement of the dormitories pursuant to a lease agreement.

HEALTH PATIENT RECEIPTS

Patient care reimbursements at the Department of Health's hospitals (Roswell Park Cancer Institute Corporation and the Helen Hayes Hospital) and veterans' homes (Oxford, New York City and Western New York) are deposited into the Health Income Fund. Similar to mental hygiene receipts, these receipts are composed of payments from Medicaid, Medicare, insurance, and individuals and are pledged as security for bonds sold by the DA for the construction and improvement of Health Department facilities.

ALL OTHER

The all other miscellaneous receipts category primarily includes receipts from local housing agencies to finance the debt service costs on general obligation bonds. All other receipts for 2003-04 also include receipts to the Debt Reduction Reserve Fund (DRRF).

MISCELLANEOUS RECEIPTS
DEBT SERVICE FUNDS
(millions of dollars)

	2000-01	2001-02	2002-03	2003-04	2004-05
	Actual			Estimated	
Mental hygiene patient receipts	258	248	407	232	228
SUNY dormitory fees	224	247	269	284	299
Health patient receipts	87	91	102	93	98
All other	291	28	29	85	22
Total	860	614	807	694	647

FEDERAL GRANTS

To qualify to receive Federal grants, the State must comply with guidelines established by the Federal government. Each Federal grant must be used pursuant to Federal laws and regulations. Also, the State is required to follow specific cash management practices regarding the timing of cash draws from the Federal government pursuant to regulations for each grant award. In most cases, the State finances spending in the first instance, then receives reimbursement from the Federal government.

Total receipts from the Federal government are projected at $37.19 billion in 2003-04 and $36.26 billion in 2004-05. These revenues represent approximately 37 percent of total receipts in governmental funds, excluding general obligation bond proceeds, and are deposited into the Special Revenue and the Capital Projects fund types. The projections for both fiscal years include the flow-through of Federal aid to localities for World Trade Center disaster costs which amount to $1.47 billion and $1.68 billion in 2003-04 and 2004-05, respectively.

SPECIAL REVENUE FUNDS

Federal grants account for approximately three-quarters of all special revenue receipts and are used to support a wide range of programs at the State and local government level. Medicaid is the single largest program supported by Federal funds.

Medicaid finances care, medical supplies, and professional services for eligible persons. The State receives moneys from the Federal government to make payments to providers for both State-operated and non-State-operated facilities. The State-operated category includes facilities of the Offices of Mental Health and Mental Retardation and Developmental Disabilities. These facilities receive Medicaid funds for the delivery of eligible services to patients. Receipts for State-operated facilities represent 11 percent of total Federal Medicaid reimbursements, while receipts for non-State-operated facilities represent the remaining 89 percent.

Other Federal grants in the Special Revenue Funds support programs administered primarily by the departments of Education, Family Assistance, Health, and Labor. These programs include Welfare, Foster Care, Food and Nutrition Services, and Supplementary Educational Services.

CAPITAL PROJECTS FUNDS

Federal grants in the Capital Projects fund type finance transportation planning, engineering, and construction projects. Federal grants also support local wastewater treatment projects financed through the State's Revolving Loan Fund. Other Federal grants are for the rehabilitation of state armories, eligible housing programs, and other environmental purposes.

FEDERAL GRANTS
(millions of dollars)

	General Fund	Special Revenue Funds: Medicaid	Special Revenue Funds: Welfare	Special Revenue Funds: All Other	Total Special Revenue Funds	Capital Projects Funds	Debt Service Funds	Total All Funds
	Actual							
1997-98	0	13,118	2,219	5,174	20,511	1,132	0	21,643
1998-99	0	13,552	1,488	6,382	21,422	1,219	0	22,641
1999-2000	0	14,432	1,017	6,735	22,184	1,381	0	23,565
2000-01	0	15,203	1,450	7,620	24,273	1,509	0	25,782
2001-02	0	16,324	1,975	8,399	26,698	1,423	0	28,121
2002-03	0	19,021	2,307	10,356	31,684	1,567	0	33,251
	Estimated							
2003-04	645	21,799	2,049	11,073	34,921	1,621	0	37,187
2004-05	0	21,749	1,979	10,697	34,425	1,840	0	36,265