P U B L I C   H E A R I N G

before

THE NEW JERSEY TAX POLICY COMMITTEE
TASK FORCE D
(REVENUE RESOURCES AND TAX INEQUITIES)

Held:
March 31, 1971
Assembly Chamber
State House
Trenton, New Jersey

MEMBERS OF TASK FORCE PRESENT:

Henry C. Lang (Vice Chairman)
Archibald S. Alexander, Jr.
Lawrence L. Lasser
Frank P. Reiche

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I N D E X

I N D E X (Cont'd)

HENRY C. LANG: (Acting Chairman): Good morning. This is a hearing conducted by Task Force D of the New Jersey Tax Policy Committee. It will cover the Retail Gross Receipts Tax, the Public Utility Franchise and Gross Receipts Taxes, the Railroad Franchise Tax, the Railroad Property Tax, and the Insurance Premiums Tax. In addition, we will also hear from speakers who will talk on behalf of the Sales Tax, whom we were not able to hear in our prior two Sales Tax hearings.

The speakers will be heard in the order of their registration with the Office of Tax Policy Committee.

In accordance with the rules, 25 copies of each speaker's statement should have been filed with the Committee Office or, if not, should be brought today and given to Mr. Martin Dyke who is sitting in the rear of the room here, on the right side, the Project Director of the Committee.

The oral presentation of each speaker will be limited to ten minutes and he will be timed in order to summarize his written statement. Then, after each presentation, the members of the Task Force, if they so choose, will question the speaker. If anyone has any questions from the floor, we would ask that they write them down and submit them to the Task Force hearing.

The first speaker we will hear today is Mr. Charles DeFoe of the New Jersey Retail Merchants' Association.

CHARLES T. DeFOE: Mr. Chairman, members of Task Force D, I am Charles T. DeFoe, Executive Vice President, New Jersey Retail Merchants Association. Ours is a statewide trade association representing some 2200 retail establishments in New Jersey. I appreciate this opportunity today to present the views of our members on the Retail Gross Receipts Tax, a tax the retailers of New Jersey consider to be the most discriminatory of all New Jersey taxes.

I am not going to read my statement. I would just like to make a few brief comments. You have my prepared statement. (See p 119)

The Retail Gross Receipts Tax which was enacted by the 1966 Legislature as part of the Chapter 51 amendments was that one part of the tax package that certainly, I think, everybody can agree was, for some unknown reason, added at the last moment and I don't believe anybody has been able to demonstrate the justification for the creation and imposition of the Retail Gross Receipts Tax.

What is the Retail Gross Receipts Tax? It's a tax imposed only on retailers. Retailers, like every other member of the business community, the industrial community in this State, pay all the various other taxes, yet for some unknown reason retailers, by the Act of 1966, were singled out to pay this one additional tax.

I like to use the story that business and commerce, industry in the State of New Jersey, we all pay taxes on the four wheels on the ground, then if you happen to be a retailer they also ask you to pay a tax on a spare tire. And, frankly, that's just exactly what it is. The Retail Gross Receipts Tax is not in lieu of another tax, such as corporations pay a tax and unincorporated business pays an unincorporated business tax; one is in lieu of the other, and so forth. But in the case of the Retail Gross Receipts Tax, it's not a tax as a substitute for some other tax that the retailers are not obligated to pay.

We feel, gentlemen, that this is very rank discrimination against the retailers of this State. The tax basically is discriminatory because it's only on retailers. Too, it is most discriminatory within the retail industry itself in that the base of the tax is gross receipts. And certainly on that basis no consideration is given to the fact that there are great profit marginal differences between one type of retailer and another, both at the gross level and at the net level. And this is certainly inequity. If a firm makes a normal profit, he pays at the same tax rate as a firm that makes no profit at all.

I would like to point out, and it has been noted on page two of my statement, that there is comparative information there about other states that impose a gross receipts or a retail gross receipts tax. And if you just briefly review the information contained there, you will see that again in those cases the retailer is not being singled out, such as in two of the states listed, Alaska and Delaware, there is no statewide sales tax.

I think the members of the Commission who are here today were here on March 3 when I discussed with you the retailer's cost on sales tax collections. Well, again, the retailers in Alaska and Delaware are not stuck with that tremendous cost, which we estimate in New Jersey as costing retailers some $15 million, - they are not required to expend those funds, and, of course, it's on all forms of business receipts in Alaska, and it's on merchants and manufacturers in Delaware. In Mississippi, you will notice, only on wholesale purchases; and in Washington State it's on all businesses but it is more or less in lieu of a corporate income tax. Indiana and West Virginia have gross receipts taxes, however, in both states the retailers pay either that tax or the corporate income taxes, whichever is higher. In New Jersey the retailer pays both.

As I indicated to you on March 3, retailers in this State are suffering a loss of somewhere between 5 and 20 percent of the sales tax collections that they make in administrative costs in collecting that tax. Some 22 other states directly compensate the retailer for these costs, at least a portion of those costs, and the majority of the total 45 states that impose sale taxes do allow the retailer to retain the breakage on sales tax collections.

In summary, I would just like to say that the retail industry recognizes the need for merchants and everybody else to pay taxes in order to finance the needs of the public through government but we feel, when it comes to Retail Gross Receipts Tax, that it's a tax that is asking more of retailers than is certainly justified in any manner or any means. We hope that this Task Force, along with the full Tax Policy Committee, will recommend that the Legislature continue its work on Assembly 634, which has already been passed by the Assembly, on April 20th of this year, by an overwhelming vote of 68 to 2 to repeal the Retail Gross Receipts Tax, and I hope your report will be directed to the early enactment by the Senate of that legislation.

That completes my formal comments, Mr. Chairman.

MR. LANG: All right, Mr. DeFoe.

Any questions from the Task Force?

MR. LASSER: I have a question. Mr. DeFoe, do you know how many retailers pay this tax? I note that there is an exemption of $150,000 of gross receipts. Does that mean that the number of retailers who pay it is narrowed down or is it still a large number?

MR. DE FOE: I would say, undoubtedly, there are a lot of momma-poppa type grocery stores and other small businesses that are not doing $150,000 volume. But, frankly, almost any type of an economic retail unit today that is not doing at least $150,000 has to be in the momma-poppa type arrangement, and the exact numbers I couldn't tell you. I am sure Mr. Glaser and the Revenue Department can. The taxes, last year, produced some $4 million. How many actual retailers are paying the tax - I know that they are requiring any retailers doing $125,000 volume to submit a return and then if they do over $150,000 in sales they pay the tax above the $150,000.

MR. LASSER: Do you think the result of this tax is that the tax is passed on to the consumer or do you think that the incidence remains with the retailer?

MR. DE FOE: I would say it's like any other cost of doing business. To sit down and say that a firm has paid $800 in retail gross receipts, I can't necessarily say that he runs out on the floor and adjusts the prices on certain items to compensate for that $800. It's much like our problems with shoplifting. We used to run around one, one and a half, or two percent maybe, at the most, in inventory shrinkage; today, in many stores, that's running up as high as five and seven percent. So, again, a factor is related to the cost of doing business for shoplifting, for retail gross receipts tax, and these various other sundry things, and prices are somewhat structured accordingly. Unfortunately, we can't pass on all of our increased costs, as you well recognize, because of the fact retailing has become so competitive.

MR. ALEXANDER: Does the Retail Merchants Association have a position with respect to how that income should be made up if the Retail Gross Receipts Tax were abolished? Do you support any particular program to make that up?

MR. DE FOE: This is a question that has been asked me by numerous Legislators and by many other people, particularly my own members, and I, for one, refuse to budge from my position on this that frankly I don't feel, when it comes to Retail Gross Receipts Tax, that our organization or the retailers of this State have any moral obligation to propose a substitute tax because we feel, first of all, this tax should never have been on the books, it's an additional tax, you're not asking any other element of the business community or any other element of society of this State to pay this type of a tax, this additional tax. And to be a little bit more positive, I would say this, that the revenue, as you gentlemen know, from the Retail Gross Receipts Tax and certain of the other taxes created in the 1966 tax package go into the save harmless fund. At the present time I understand that that fund is not solvent, that at the present time there are funds being taken from the State's general revenue funds to make up the necessary difference there in the save harmless fund, and I would say that $4 million additional could well be taken from the state coffers as a contribution, should we say, maybe toward some of this cost that retailers are experiencing in collecting the sales tax. I am sure that in your deliberations, as you review not only this tax but all of the other taxes that are up for scrutiny, there are going to have to be some adjustments made. I am sure there are going to be some increases as well as some repeal of taxes, and I am sure I wouldn't want to sit here and say add one-quarter of a cent on the sales tax or on corporate income tax or something like that. I think this is going to be a determination that the Tax Policy Committee will look at - what are you going to do away with and what new tax can you possibly create. But I think this $4 million that is currently being generated from the Gross Receipts Tax can probably fit into that picture somewhere rather readily. I wouldn't make any specific suggestion on it, Mr. Alexander.

MR. LANG: Mr. DeFoe, did you say that it cost the retailers $15 million to collect the sales tax? Is that your estimate of what it costs them to carry on the collection?

MR. DE FOE: This is an estimate that we have come up with. It's based upon studies that were conducted at Ohio State University and in New York and Colorado and several other states, South Carolina, and so forth, where there have been some very scientific studies conducted by impartial people as to the relative costs the retailer experiences in collecting and recording and auditing his sales tax collections. And these costs have been determined to range from five to twenty percent of the tax collected. We have taken the $550 million figure that the Revenue Department has estimated that New Jersey will take in on sales tax this current fiscal year and, right off the top of my head, I can't remember what the factor was but it came out around $16.5 million and we rounded it off at $15 million. I think our figure is conservative. If you will check the testimony I submitted on March 3, I submitted quite a lengthy detail as to the procedure that one of our members goes through in collecting, recording, auditing and transmitting the sales tax to the State of New Jersey. I think just from a review of that you will see that the cost to a retailer is quite extensive and certainly is equivalent to five to ten percent of the tax.

MR. LANG: That amounts to about three percent of the collection in the State. You said $550 million and you're looking at $15 million or $16 million, that's about three percent.

MR. DE FOE: I said it was a conservative figure. I could come in here and take the Ohio study and say, all right, let's take 8.3, I think it is, and, frankly, I'm sure, because of the composition of our business community here in New Jersey, even though we have a very complicated sales tax law where there are a lot of non-subject items that have to be taken care of especially, and so forth, it's a very complicated sales tax to administer at the retail level, - we have been conservative in our estimate.

MR. REICHE: Am I right in assuming that because of the nature of the tax there is no substantial cost associated for your folks in terms of its administration?

MR. DE FOE: You're speaking of the Retail Gross Receipts Tax?

MR. REICHE: Yes.

MR. DE FOE: No. Frankly, the form - I had the opportunity to work with the State Revenue Department when they were preparing their form, back in late 1967 and early '68, and the form is very simple as far as the annual report of the Retail Gross Receipts Tax.

MR. REICHE: Do you find that the imposition of this tax is a deterrent to business in New Jersey as opposed to other states which surround us, simply because there is no comparable tax in those other states?

MR. DE FOE: At the tax rate, as currently imposed by the Retail Gross Receipts Tax, no I would not say it is a deterrent. This is one of our great fears, of course, that the rate is rather low today but in the times we are going through today where constantly government is in need of greater funds we are constantly concerned about the possibility of the State looking at that tax and raising it, and then it would become a real, real burden on many of the existing retailers in the State and I am sure would be a deterrent to attracting further retail development in the State.

MR. REICHE: Thank you.

MR. LANG: Thank you, Mr. De Foe.

MR. DE FOE: Thank you, gentlemen.

MR. LANG: Mr. James M. Neilland of the New Jersey Food Council.

J A M E S M. N E I L L A N D: Good morning, Mr. Chairman and members of the Task Force. My name is James M. Neilland. I am the Executive Director of New Jersey Food Council which represents the State's food industry, its employees and its customers.

I would like to thank you, once again, for this second opportunity to present the Food Council's views on inequities which exist in New Jersey's tax structure.

I intend to address myself today to the Retail Gross Receipts Tax, which is included in the list of subjects you outlined for consideration during this hearing.

Additionally, however, I intend to call your attention to the recent action of the New Jersey Legislature in authorizing the City of Newark to impose a payroll tax upon all businesses operating in that city.

Both measures have striking similarities. Both single out the retailer, especially the food retailer, for unfair additional taxation- over and above those taxes apportioned among the rest of the State's corporate citizens.

Both levies bear no relationship to earnings or the ability of the taxpayer to pay the tax, requiring payment whether the end result of a firm's operations is a profit or a loss.

Frankly, both are shameful. Both should be stricken from the books of New Jersey law and this should be accomplished at the earliest possible date.

Retailers, like every other business in the state pay an income tax, a levy assessed against actual earnings -- at least in the case of corporations. This justice, incidently, is lacking in the case of the unincorporated business which must pay its corresponding tax based upon gross receipts, rather than earnings. We can assume, however, that the unincorporated business is earning a profit, for it could not continue to operate without it.

Retailers, like every other property-owning business in the state, pay property taxes to support local and county government and public education. I might point out, however, that retailers generally must be situated along main streets within a community or along main highways and both of these areas draw the highest in tax assessments. This contrasts with the manufacturing company which can successfully operate from lower priced land and, as a result, draw lower tax assessments for its land.

But the retailer, unlike the manufacturer, unlike the docter, unlike the lawyer, unlike any other business in the state of New Jersey, pays an added tax, a levy imposed against every single dollar which passes through his cash register on its way to paying for merchandise, salaries and a host of other costs, which, combined, can easily result in a net loss at the end of the year.

Certainly, it is an established fact that the retailer does not net the percentage of profits enjoyed by manufacturers, doctors, lawyers and other types of businesses in New Jersey.

And the food retailer, unlike other retailers, considers himself most fortunate today if he can retain a single penny from every dollar which passes through his hands.

And so I pose this question. Where was justice in New Jersey when the Retail Gross Receipts Tax was enacted? Obviously, justice had to take a back seat to expediency. As voters, retailers are a distinct minority, not worthy of undue concern in New Jersey's past.

Mr. Chairman, Members of the Task Force:

It may be absolutely true that retailers are not worthy of concern as voters. But I want to point out to you that retailers are New Jersey's third largest source of employment for the residents of this state, their taxes fund a substantial portion of the operations of government at every level and they are seeing that a large number of our children are properly educated.

But there is a more compelling reason why you must bring an end to the era which saw retailers -- and especially food retailers -- ignored. In every area of this state, among every segment of society and among thousands of persons involved in public service, there is a burning desire to see that justice is enjoyed by everyone.

All of us want justice to be something more than just a promise.

For years there have been promises. It is in your hands to deliver. The Retail Gross Receipts Tax, imposed as an added tax only upon retailers, must be repealed before New Jersey can end its shame for this injustice.

Am I being overly dramatic? I think not and I must reiterate.

It is bad enough that the retailer has been singled out for unfair additional taxation, over and above what is paid by other corporate citizens of the state. We made matters even more shameful by devising a tax which has absolutely no relationship to the ability to pay.

This levy requires the same tax payment of a retailer regardless of whether he shows a profit or a loss. It is shameful. I urge you to bury it and hope that everyone in New Jersey can forget that it ever existed.

As I direct your attention now to the Newark payroll tax, I ask you to note the similarities of injustice when compared to the Retail Gross Receipts Tax.

The payroll tax is levied against Newark employers. Its base is not the earnings, the spendable income of these employers. Rather it is the total amount of money which is paid to employees. With one simple illustration, it becomes readily apparent that the same amount of haste, the same lack of concern for retailers and justice which were evident in the 50's and 60's were still with us in authorizing Newark to enact this tax.

There are businesses which can net $50,000 in annual profits on a payroll of $10,000 or less. A food retailer, to net that same $50,000, would have a payroll as high as a half-million dollars. The first type of business would have a payroll tax of $100. The retailer's tax would be $5,000.

Where is the justice? Is this what New Jersey wants?

I think not. I think, once again, we pulled a monumental goof and, once again, it is the retailer who has been the victim of our haste.

Mr. Chairman, Members of the Task Force:

Let me assure you that New Jersey Food Council, its officers, its directors, its members and its staff are thoroughly aware of the financial needs of New Jersey, its counties, its municipalities and its school districts.

We are aware of the added needs of urban communities such as Newark.

I am not here to suggest that you ignore these many needs. But I am here to plead, to urge and to demand that New Jersey start apportioning responsibility for meeting these needs with a lot more fairness and justice than has been demonstrated in our past.

The Retail Gross Receipts Tax nets an estimated $4 million for the State of New Jersey. Members of New Jersey Food Council pay an estimated $1.5 million of that amount.

Ever since the tax was enacted in 1966, its injustice has been recognized. Retailers were asked to endure it for a little while and then, repeatedly, for a little while longer.

Last year, the State Assembly, with the sponsorship of the chairman of this Task Force, finally voted to repeal this tax. The bill has been stalled in the Senate with the same old answer:

"We can't replace it with some other tax."

This answer has never been a fair answer but, effectively, it has blocked repeal of this tax.

That answer today has even less merit. The New Jersey lottery is drawing far more revenue than its most optimistic supporters dared to anticipate. My personal estimate places the 1971 revenue at $100 million. from the lottery.

I can appreciate that your final recommendations will not be completed for several months. However, this need not deter you from submitting preliminary recommendations. And if there is one inequity which screams for immediate elimination, it is the Retail Gross Receipts Tax.

Accordingly, I urge this Task Force to recommend immediately that the New Jersey Senate vote final passage of A-634 and wipe the Retail Gross Receipts Tax from our books.

Secondly, I urge that you call for re-evaluation and subsequent rescinding of the authority granted by the Legislature to the City of Newark to impose the city's payroll tax.

It is true that both of these moves primarily will benefit retailers. But your action -- your courage -- will send out the word to every citizen in the State of New Jersey that when your work is completed, each of us can expect equal justice and a system of taxation which will be as fair as the mind of man can devise.

I am confident that your courage would be lauded by all our citizens if they can look forward to that kind of true tax reform.

Again, thank you for the opportunity to be with you today and I will be happy to answer any of your questions to the best of my ability.

MR. LANG: Thank you. Any questions?

MR. ALEXANDER: Mr. Neilland, don't you agree that at least we would have to wait before repealing the Retail Gross Receipts Tax until we knew how much money will be needed and where that money is coming from?

MR. NEILLAND: Mr. Alexander, I think you will agree that the subject of my presentation today is fairness. And I don't believe that it was fair that the retailer was asked to wait from the very day that tax was enacted. I don't believe it has been fair that he has had to wait each and every year as Legislators and State Officials and the Executive Branch told him, please wait until we have a broad base tax, and then wait until we expand or increase the broad base tax or come up with a new one. No, I don't believe it is fair for the retailer to wait any longer.

MR. LASSER: Mr. Neilland, has the imposition of this tax had any adverse effect upon retailers in New Jersey, that is their ability to serve their customers or to render the functions that they should render in our New Jersey economy?

MR. NEILLAND: Obviously not. There have been two main effects of this particular piece of legislation. In the retailing industry, I am sure all of you are aware, competition is the most extreme of any other type of business in this country. It has put a tremendous added pressure on the ability to net a satisfactory adequate profit at the end of the year. Secondly, it has given to the retailers of this State the tremendous feeling that the retailer means little. It is the retailer that can be put into the back seats and say, well, put this tax on him, put this on the retailer and put that on the retailer. I could sit here for the next two hours and tell you about inequities which the retailer must contend with in this state. This tax is the most major reason which gives that feeling among the retailing community that we don't count or they don't count. So, for these two very important reasons, we're talking fairness and justice and the ability to take off some of that pressure from the ability to net an adequate profit structure at the end of the year.

MR. REICHE: Mr. Neilland, I would like to comment just briefly on the role of this Committee at the present time. I do not believe that it is the function of this Committee to participate - and I think this has been, generally speaking, the view the Committee has taken -- to participate in on-going deliberative processes which were then in progress before the State Legislature. It is our function to eventually make a grouping of proposals, including which will be the continuation or non-continuation, as the case may be, of the Gross Receipts Tax. And, therefore, it would appear to me at the present time that the most efficient way of pleading your case, if you want the immediate relief which you seek, is through the Senate, since the Assembly has already passed it. And by that I am not saying that this Committee is not interested. I speak only as one. I don't speak for the Committee. But in the same breath, yes, it does have to be part of our long-range recommendation but I don't honestly think it is our function to become involved in what is being considered right now by the Legislature because, quite frankly, if we did, we then would be doing nothing else but that. And this is one of the ways in which the work of Tax Study Commissions in the past, I think, was broken down. And I just wanted to point that out. Any by that, please don't construe it as any lack of sympathy for your position or any lack of understanding, but I think our work should be put in its proper light.

MR. NEILLAND: I certainly would not have any intention of telling this Task Force how to do its job. You may recall, at my last presentation before you, I bent over backward to commend you for the willingness to serve and the willingness to put up with this monumental task you have before you. Certainly you will appreciate the fact that in a tax of this type I am going to try every means possible to get it eliminated at the earliest possible date. Any consideration which I can cause you to go through which may lead to your recommendation at this date to the Senate to move that bill can certainly only advance my cause of getting rid of this particular tax.

MR. LANG: Mr. Neilland, I think it would be very helpful to us if you feel it is true, this may not be so, that the New Jersey Food Retailers bear a higher proportion of the tax burden than food retailers in other states, taking into consideration all types of tax that they pay, be it corporate, an income tax, property tax, sales tax, gross receipts tax, if you will, - I think this is what we have to have some understanding of. It may be that even with the Retail Gross Receipts Tax in here the overall burden is comparable with some of the other states. Now, if you can show that this is not so, I think it would be very helpful to us in our deliberations and in making our recommendations to the full Tax Policy Commission. Is that possible?

MR. NEILLAND: Mr. Lang, we can certainly submit information along these lines. However, I would like to point out to you that we don't have to go beyond the State of New Jersey's borders to see just what kind of a burden the retailer is up against. When any man in business today can take home at the end of a year less than a penny out of every dollar that came through his hands, in comparison to four, five, eight and ten percent, and higher, that other businessmen in this State are taking in, something certainly is wrong and it is easily recognizable. But I will be happy to put together the type of information you've requested and submit it to the Task Force.

MR. LANG: I think that would be best. I can see some sympathy for the 1% of gross profit that you're talking about, however, they still remain in business and they're all over the State so they must be making some type of profit.

I think we've got to compare them with the burden that food retailers have in other states, as well as in our own State, and this is the type of information, if we could get it, that would be very helpful to us.

MR. NEILLAND: To that I can only add one comment, yes, we're still able to purchase food in the State of New Jersey today and I see no reason why we will not be able to purchase it for generations to come. I will point out, however, that the mom and pop store, the small supermarket chain, is fast disappearing. Constantly these companies are going out of business or being merged into larger operations because today in the food retailing industry if you're not big, that wolf is at your door every single day of the year.

MR. LANG: Thank you very much, Mr. Neilland.

MR. NEILLAND: Thank you, gentlemen.

MR. LANG: Mr. Al Lehman of the New Jersey Automobile Dealers Association.

A L N. L E H M A N: Mr. Chairman and members of Task Force D, my name is Al Lehman, and I am Executive Vice President of the New Jersey Automobile Dealers Association. Our membership represents approximately 800 franchised new car dealers in this State.

First, I would like to compliment Governor Cahill in his wisdom for creating this Tax Policy Committee. The need for such a study, in our opinion, has been long overdue and, believe me, we know your job is not an easy one. I also testified at your very lengthy hearing here just a few weeks back.

In accordance with your invitation, I would like to limit my comments today to the subject of the Retail Gross Receipts Tax and its effect on our industry. And may I add at this point that I heartily concur with my two predecessors in some of their comments and perhaps I can give you a few insights on, let's say, a large ticket item. The same theories, however, that I will express today will also be applicable to the Unincorporated Gross Receipts Tax, which you are also considering. But very few of our members are left that are small enough to be the mom-and-pop store, so to speak and most of them are corporations.

At the onset, gentlemen, please let it be understood that the membership of our Association is not against taxes per se. Although it's not a popular subject, those in business and government realize it is a necessity if services and programs for the citizens of this state are to be maintained and improved at all levels of government. As businessmen and citizens, we can only hope that these services are performed in the most efficient manner possible, thus avoiding unnecessary taxation. All of us, however, and I hope you would agree, must be concerned when any form of taxation is discriminatory.

Gentlemen, in 1966 the Legislature passed and Governor Hughes signed into law a package of four business tax reforms to replace the dual tax rate legislation applicable to Chapter 51. This legislation was recommended by a study committee appointed by Governor Hughes, assertedly representative of the business community. It is a matter of record, however, that of the 18 members on this committee, only one represented the retail community, and he was placed on the committee late in the deliberations almost as an afterthought.

In our opinion, the five-bill package enacted to replace Chapter 51 was hastily acted upon by the Legislature after introduction, and did not receive a thorough study and analysis to determine its impact upon New Jersey business. There were no public hearings on any of these measures before they became law. Those affected were not afforded any opportunity to voice what the effect of these tax measures would be on their industry.

Since this hearing is only interested in two of the five measures passed as a package, I must add that our membership was not opposed to the previous reform package, in theory. In fact, there were many aspects of this new concept of taxation we believed most desirable. For example, under the new concept all taxes were levied, collected and administered by the State before monies were returned to local municipalities who were previously responsible for these functions. In addition, the tax rate, depending on the type of tax imposed, became uniform throughout the State. We believe uniformity in taxation is highly desirable. It placed all those taxed on an equal basis, eliminating the possibility of favoritism or improper administration in any local jurisdiction.

With regard to the gross receipts tax, while the tax rate was uniformly established, that was where the equity ceased. In rounding out its new tax package, the Legislature enacted two pieces of legislation using a gross receipts formula - the tax on the gross receipts of unincorporated business, one-fourth of one percent, and the tax on the gross receipts of all retail stores, one-twentieth of one percent. The equity of both of these taxes should be an item of serious concern to this Committee.

And, gentlemen, I would like to pause right there from my prepared testimony and remind the members of this Committee, if you are not already aware of it, that when this package was originally introduced in the Legislature the rates on both of those taxes were exactly reversed. It started out, a proposal, with a gross receipts tax of one-quarter of one percent, and the unincorporated one-tenth of one percent. And just to give you an idea how fast economic pressures can come into the front before a tax is actually placed into law, - what I am trying to say is that I think this tax is a time bomb.

The Committee should be interested to learn that the membership of our Association was unique in that they were required to pay at least three of the four new taxes enacted in 1966. This package was supposed to round out the tax package but, you see, all franchised automobile dealerships have extensive service facilities and, therefore, we were still required to pay the machinery and equipment tax. Because we came within the definition of a retail store, all dealerships were required to pay the gross receipts tax, which was the new one. In addition, all automobile dealerships were required to pay either the increased corporate net income tax, recommended at that time, and since increased, or the special gross receipts tax levied upon unincorporated businesses.

If my information is still correct, the Committee should be knowledgeable of the fact that New Jersey is the only State in the United States to single out one class of businessmen for special taxation. Alaska, one of only seven states with such a tax, levies it on all forms of business receipts but has no sales tax. Delaware, which has no sales tax, imposes the tax on manufacturers as well as merchants. Mississippi levies its gross receipts tax on all wholesale purchases; while Washington's is on all businesses. Indiana and West Virginia allow retailers a choice of paying either the gross receipts tax or a corporate income tax, but they do not expect both. Connecticut imposes a gross receipts tax on incorporated businesses in lieu of the corporate tax.

In our opinion, the retail gross receipts tax is a highly discriminatory tax. It does not burden all segments of the business community equally, and it bears no relationship whatsoever with a business' ability to pay. The exemption of the first $150,000 presently in the law has meaning to some retailers, but not to the automobile dealer. The smallest automobile dealer in the State has annual sales of over $500,000 with perhaps a net profit of around $10,000. Compare this, gentlemen, with a jeweler or clothier with a profit of several times that amount on sales of $149,999 and no tax.

Under a gross receipts tax concept there is no concern whether the business paying the tax makes a profit. Under this concept a merchant could go bankrupt and still be forced to pay a tax. Merchants who sell a high price commodity, such as an automobile, operate on an extremely small margin of profit and suffer the most severe impact. For your information, here are some statistics compiled by the National Automobile Dealers Association which may be of interest to you and prove the highly competitive nature of our industry.

The average operating profit of new car dealerships before Federal taxes on total sales is as follows:

1969---1.9% of total sales

1968---2.2% of total sales

1967---1.83% of total sales

1966---1.8% of total sales

1965---2.1% of total sales

1964---1.8% of total sales

1963---1.9% of total sales

As far as 1970 was concerned, dealers were operating on approximately the same level as 1969 until the lengthy General Motors strike, which proved disastrous. This strike alone put out of business many marginal dealers and caused some of the most successful dealers to operate in the red for the year. The automobile industry is an excellent example of severe price competition at the retail level, especially so in an urban state like New Jersey. Obviously, in the above average figures there are dealers who operate below this figure and a substantial number who maintain only a marginal business.

If an automobile dealership sells fewer than 400 cars annually, the chance of failure in the business increases proportionately. Although New Jersey has more than its share of "large" dealers as compared with the rest of the nation, the average dealer in this state will sell approximately 300 new cars annually, which in terms of dollars, gentlemen, represents approximately 1.8 million dollars.

It is a generally recognized rule of thumb in our industry that for every new car sold the dealership will generate approximately $6,000 in retail sales from the car, its parts, service and other supporting components.

You can see that due to the nature of the products sold, the exemption granted under this tax means little or nothing. Accentuating the impact of the retail gross receipts tax is the lack of a trade-in exemption under the gross receipts tax law. As you might know, it is a normal practice to trade a car in when purchasing a new one. The sales tax law of this State takes this trade-in into account and assesses the tax only on the net payment. There is no provision under the gross receipts tax law for credit on trade-in merchandise. This Committee should at least recommend a trade-in credit for like merchandise received in trade. This is pure and simple double taxation as administered presently.

Our calculations will prove that the franchised new car dealers in this State, by themselves, pay more than 25 percent of the total tax to be collected under this law, and, gentlemen, that's considerable. This fact, alone, adds weight to our argument of extreme discrimination. New car dealers in New Jersey are responsible for merchandising approximately 375,000 new cars annually in this State, and maybe an additional 300,000 to 350,000 used cars each year. In addition, they are the primary source for automotive parts. Simple arithmetic will prove the accuracy of our calculations. And as I testified here a couple of weeks ago, all of our products are taxed, we have no exemptions under the sales tax law, and we pay three of the four taxes under the new package system of 1966.

It is interesting to note that at the same approximate time the retailing segment of New Jersey business was singled out to pay this gross receipts tax, they also became the unpaid collector and transmitter to the State of New Jersey of the new 3% sales tax, now 5%. Incidentally, as I testified before this Committee on March 3, 1971, automobile dealers are also the largest single collectors of the sales tax for the State. Here there is no small task involved. In view of the substantial burden placed upon the retailing industry in collecting and transmitting this tax alone, it seems most unfair that they should be selected to shoulder this additional gross receipts tax.

We think it is extremely important for this Committee to consider the relatively small amount of tax to be collected under this law at present levels. This tax is hanging over the retailers' head like a time bomb. How long will this rate remain 1/20 of 1%. It must be repealed as soon as possible.

MR. LANG: May I ask you to make a concluding statement? You've about run out of time and we have to keep the hearing moving.

MR. LEHMAN: Yes, Mr. Chairman.

Every year since this tax was proposed in 1966 it has been an item of concern with the Legislature and every year there have been bills submitted to repeal the tax. As you know, in previous testimony, this year it was supported by your own Chairman; it has passed the Assembly and it is sitting in the Senate.

Ironically, there are 22 sponsors in the Senate of an identical bill to repeal this tax. But so far, no action, because nobody knows where the money would come from.

I sincerely hope, gentlemen, that this Committee would agree with, let's say, your sister state of New York, that regardless of how badly a state or a local community needs money a gross receipts tax is not an equitable way to impose taxation.

I think I can answer any questions about our industry, if you are so inclined, and I will be glad to stop right there.

MR. LANG: Mr. Lehman, you know that in previous testimony, during the questioning, it was indicated that the State collects about $4 million under this Retail Gross Receipts Tax. How much of this do you feel the automobile dealers collect?

MR. LEHMAN: The average new car sold in this State, sir, will generate approximately $3400 for the new car. This takes in more expensive models and brings in less expensive models. The average is about $3400. The average used car sold will be about $1100. We sell approximately 375,000 new cars in this State and approximately 300,000 used cars in this State and there is a full Gross Receipts Tax, no credit for trade-in. I think you will find that we average somewhere between $2.25 million and $2.5 million of the $4 million. And those sales are a matter of record.

MR. LANG: Between the automobile dealers and the food retailers, then they make up the entire amount of the $4 million.

MR. LEHMAN: It's especially important, sir, on a large ticket item - and even though it wasn't part of my testimony, I noted a question you asked of Mr. DeFoe, could this tax be passed on to the consumer. In our industry the answer is a definite no. I am sure all of you gentlemen have purchased a car and you know, with the trade-in involved and the back and forth until you agree upon a price, you surely do not say at the end of your negotiations, we're going to pass on another three or four hundred dollars because the State has a Gross Receipts Tax. This is impossible. This is purely a tax the automobile dealer absorbs. On the other hand, if you were selling a loaf of bread or a bottle of ketchup, you might be able to add another penny to make it up. I don't know that much about that industry.

MR. LANG: On the other hand, looking at these figures that you submitted to us, where you show the average operating profit for the car dealerships, looking at 1966 through 1969 there really hasn't been any relevant change in the operating profit in spite of the fact that the Retail

Gross Receipts Tax was enacted in those years. So it would appear that it is being passed on, I would expect. I am not saying I'm in sympathy with the tax.

MR. LEHMAN: No. I would have to agree with my two previous colleagues who testified that under the present rates - and I have to stress this -- under the present rates, in terms of tax dollars submitted by our industry to the State, there probably is little or no difference. But, gentlemen, there is a theory of taxation involved. And in this particular case, at this particular time, I don't think it's the amount of dollars involved as much as the theory and what the amount of dollars could be sometime in the future. If the law had been enacted in its original form at one-quarter of one percent, look at the difference, for example.

MR. LANG: Any questions?

Thank you Mr. Lehman.

MR. LEHMAN: Thank you very much.

MR. LANG: Are the representatives of the New Jersey State Employees Association here? Mr. Circioni or Mr. Jack Silverstein? (No response)

Mr. Kozlowski of the New Jersey Furniture Association?

J O H N K O Z L O W S K I: Mr. Chairman, gentlemen, I am John Kozlowski, President of Park Lane Fruniture in Trenton, New Jersey. I appear today in my capacity as President of the New Jersey Furniture Association, an organization having a membership of more than 800 small and large retail furniture stores in the State of New Jersey.

I sincerely appreciate this opportunity to submit our views on a subject that is of utmost importance to the retail furniture dealers, and I am certain to all other retailers of New Jersey; that subject being the repeal of the New Jersey Retail Gross Receipts Tax.

The Retail Gross Receipts Tax, which was passed by the 1966 New Jersey Legislature undoubtedly constitutes one of the most discriminatory taxes that has ever been imposed upon an element of business in the history of our nation.

New Jersey retailers, already burdened with contributing more than fifteen million ($15,000,000) dollars in administrative costs in their services as the unpaid tax collector for the state's sales tax, have been singled out to make a tax contribution through the Retail Gross Receipts Tax in no manner imposed upon any other element of commerce or industry in New Jersey.

New Jersey business and industry, which includes retail furniture dealers and other merchants, pay a variety of state and local taxes; including real property, personal property, corporation and un-incorporated business taxes etc. In addition to all of these taxes, New Jersey Furniture Stores and other retailers have been singled out to pay an additional tax; a tax imposed solely upon the retail merchants of this state. This tax, the Retail Gross Receipts Tax, creates an unparalleled discrimination against a New Jersey industry, an industry that provides thousands of jobs, millions in state and local taxes and many other substantial contributions to the general well being of our state and its citizens. The New Jersey Gross Receipts Tax imposes upon retailing a most unfair tax burden when compared to the tax responsibilities of other New Jersey businesses, and when compared to the tax demands placed upon retailing in all other states. Besides representing an unfair additional tax burden upon retailing, the Retail Gross Receipts Tax creates a most discriminatory circumstance within the retail industry itself. Retail businesses enjoying a normal profit pay this tax on the same basis as a retail store having made no profit.

Since New Jersey Furniture Stores and other retailers do not ask for, nor receive, any services from state or local government not provided to all forms of business, is it fair to ask retailers to pay a tax not imposed upon the rest of the business community? Does the Retail Gross Receipts Tax not require more from retailing than its fair share of tax responsibility?

In 1965, when Governor Richard J. Hughes announced his intention to appoint a tax study committee, the Governor stated, and I quote, "In my opinion, the Business Tax is not a desirable one because it is not a fair measure of businesses capacity to pay". This statement of the Governor embodies the first objection retailers have to the Retail Gross Receipts Tax. That is, it is not a fair measure of businesses capacity to pay. This tax, confined to one segment of the business community, takes no account of earnings or net worth in its assessment formula. The marginal profit percentage differences between one kind of a retail store and another is often substantial, and certainly the Retail Gross Receipts Tax, as it is currently constituted makes no allowances for such differences.

The members of the New Jersey Furniture Association urges that the Tax Policy Committee carefully consider all of the testimony that I am sure will be presented here today calling for the early repeal of this onerous tax. I am confident by a careful review of all information provided you as to the unfairness and discriminatory features of this tax, that you will readily recognize the need for its complete and early repeal by the New Jersey Legislature.

The members of the New Jersey Furniture Association appreciate this opportunity to express their views on this most important subject.

MR. LANG: Any questions?

MR. REICHE: Do you have any idea of the extent to which this constitutes a burden on the furniture industry in New Jersey, that is the retail outlets?

MR. KOZLOWSKI: The burden that it's a nuisance tax.

MR. REICHE: In other words, the burden is not in terms of the overall financial impact. Is that correct?

MR. KOZLOWSKI: I don't know anyone in our industry who has mentioned that it's a burden to pay.

MR. LANG: Of the 800 furniture dealers you are talking about in the State, aren't a great number of these eliminated from paying this tax in view of the $150,000 exemption? Do you know how many there are?

MR. KOZLOWSKI: I don't think there are possibly 20 stores in the State of New Jersey that would have a volume of less than $150,000.

MR. LANG: Now, would you also tell us what the total amount of the burden is of the Retail Gross Receipts Tax on the furniture industry in the State, again thinking in terms of the $4 million total that's collected annually.

MR. KOZLOWSKI: As I mentioned, I don't know any dealer that has had a burden except it is considered a nuisance tax and an unfair tax, that is an additional tax to the other taxes imposed on the retailers.

MR. LASSER: Would you have any idea of the total volume of furniture sales in New Jersey?

MR. KOZLOWSKI: No, because some of the larger stores have included their figures in their total retail sales for the figures to be submitted and it's impossible for us to give you a figure for the State of New Jersey's furniture dealers.

MR. LASSER: And in the area of profit margins, the food industry talks about 1% and the automobile dealers talk about 2%, what do you think the figure would be in the furniture business?

MR. KOZLOWSKI: I do not think it would be a matter where it would be considered as an increase to the consumer or anything to that effect at the present time. We have not heard any dealer say he would have to raise prices because of the tax.

MR. LASSER: Is there some figure generally accepted in the furniture business as to what the percentage of profit margin would be on gross sales?

MR. KOZLOWSKI: Oh, yes.

MR. LASSER: What would that figure be?

MR. KOZLOWSKI: Gross, it would be about 38 percent.

MR. LASSER: Thank you.

MR. LANG: The profit margin is 38% on gross sales in the furniture business.

MR. KOZLOWSKI: Yes. That's if you get your regular mark-up.

MR. LASSER: That's the mark-up, I think, not the profit margin.

MR. KOZLOWSKI: That's supposed to be. And your net after dealers get through is 1.5.

MR. LANG: In other words, the 1.5 would be comparable to the 1% in the food retailers and approximately 2 for the automobile dealers. Is that right?

MR. KOZLOWSKI: When we consider gross, we do not consider freight problems which today run as much as from 15 to 20%, and the margin profit has been the same for, I guess, the past hundred years but today's expenses have narrowed that profit down to just about 1.5 net.

MR. LANG: Thank you, Mr. Kozlowski.

Mr. Harry Krausse of the Prudential Insurance Company.

HARRY A. KRAUSSE: Mr. Chairman and members of the Committee, my name is Harry Krausse. I am Director of Tax Administration for Prudential Insurance Company of America. I appear here today on behalf of four life insurance companies organized in the State of New Jersey: Bankers National Life Insurance Company, The Colonial Life Insurance Company of America, The Mutual Benefit Life Insurance Company, and The Prudential.

These companies account for more than 94% of the life and health premiums received from residents of New Jersey by all domestic life insurance companies and also about one-fourth of the life and health premiums received in New Jersey by all life insurers, both domestic and out-of-State companies.

The written study which we have submitted for your review describes the New Jersey taxes imposed on life insurance companies and compares their impact with the taxes of other New Jersey industries and the insurance tax systems of other states.

This morning I would like to summarize the findings of that study.

Although the life insurance industry is subject to various license and other fees and to franchise, income, and property taxes in the 50 states, the premium tax is the primary levy.

By the late 1800's and the early 1900's, most states had adopted some form of premium taxation as the principal means of taxing insurers. Until recently, the premium tax was also the principal tax burden of life insurance companies at all levels of government. Since 1955, however, federal income taxes have exceeded the state premium taxes. Any review of state insurance company taxation must recognize this relatively new force which superimposed an industry tax burden of $1.2 billion on top of state premium tax collections of over $540 million, in 1969, the latest year for which numbers are available.

During this same period, life insurance companies incurred an estimated $27 million for taxes in the State of New Jersey. Of this total, approximately $17 million was for premium taxes, including the local franchise taxes paid by domestic companies; over $8 million was represented by real estate taxes; and the balance of almost $2 million was for sales taxes, unemployment taxes, and various license fees.

The New Jersey companies' share of the total burden was more than $13 million and consisted of about $5 million for the premium and franchise taxes, real estate taxes in excess of $7 million, while all other taxes and fees amounted to some $1 million.

In general, a premium tax is determined by applying a flat rate to premiums received from the sale of policies. The premiums are usually reduced by various returns to policyholders in determining taxable premiums but no deductions are allowed the insurers for benefit payments or company expenses. Thus, the premium tax is a gross receipts tax which is unrelated to the insurer's profitability.

One of the characteristics of the premium tax system is its diversity from state to state. A variety of rates, deductions, exemptions, tax credits and retaliatory provisions are employed in determining the tax liability. A common characteristic is the favored tax treatment of home state companies. Typically, this is achieved by applying a lower rate to a domestic company or by exempting it altogether.

Since the premium tax is a special form of taxation applicable only to insurance companies, the Legislatures have recognized the need to relieve insurers from certain taxes applicable to corporations generally. Consequently, most states provides that the premium tax shall be in lieu of some other tax or taxes at the state and local levels, such as personal property and income taxes.

In most states non-profit hospital-medical insurance plans, such as Blue Cross-Blue Shield, are exempt from taxation even though they are in direct competition with insurance companies.

A major development affecting the insurance industry has been the growth of so-called self-insured employee benefit plans which are not subject to insurance regulation by the states or to the same tax obligations as are imposed on insurers.

The tax differential that favors the "Blues" and the self-insured plans impedes competition for the same business.

New Jersey imposes the same tax rate on domestic and foreign companies - 2% on life and individual health premiums, and 1% on group health premiums.

Annuity considerations and premiums received under plans which qualify for special treatment under the federal income tax law are exempt.

In most respects New Jersey's insurance tax system is quite typical.

Any review of a State's tax system must reckon with the retaliatory situation which is found in the insurance industry. In effect, the retaliatory laws found in 46 states say to other states, "if you tax our insurers in your state in excess of the levels we have set for your insurers here, we will tax your insurers to the same degree."

The retaliatory effect of increasing the rate above the most common rate of 2% can be substantial for domestic companies who do a nationwide business. For example, in one state it was recently estimated that for every additional $1.00 of tax to be raised from domestic companies by a proposed increase in the tax rate from 2% to 3%, such companies would be subject to $6.87 in retaliatory taxes.

The National Association of Insurance Commissioners has recommended the elimination of premium tax discrimination between domestic and foreign companies; the elimination of premium tax discrimination among types of insurance organizations or arrangements, principally the preferential treatment of the "Blues" and self-insured plans; and also the elimination of retaliatory premium taxes.

Excluding the retaliatory problem, a solution of which requires cooperation of all states, New Jersey goes a long way in meeting these NAIC anti-discrimination standards. The tax burdens on home-state and out-of-state companies are substantially the same in New Jersey. The exemption of annuity considerations and premiums under qualified plans and the lower rate on group health premiums are important factors in reducing the tax differential that favors the "Blues" and self-insured employee benefit plans.

The study also compares the impact of insurance company taxation with the taxes imposed on other businesses in New Jersey. One of the typical ways of comparing unlike taxes imposed on different industries is to measure the burden in terms of the ratio of taxes paid to the net income. When this is done in New Jersey, we find that the premium tax is the equivalent of a 17 to 18% tax on net income; the bank stock tax is equivalent to about 6.5% tax on net income; and the corporation business tax comes to about 6% of New Jersey net income.

While a 2% premium tax rate appears to be low, substantial tax revenue was generated because of the gross receipts' base to which the rate is applied. In terms of net income, however, life insurance companies are paying taxes at a rate which is almost three times that being paid by other corporations in New Jersey. Thus, we feel life insurance company taxes should be reduced in order to equalize the tax treatment of insurers with that of other businesses in New Jersey.

We appreciate this opportunity to appear here today and if you have any questions now or after you have reviewed our written submission, we will do our best to answer them.

MR. LANG: Thank you, Mr. Krausse.

Are there any questions?

MR. ALEXANDER: Yes. Mr. Krausse, in saying that our 2% insurance premiums tax is equivalent to a 17 or 18% net income tax, what income of insurance companies are you taking account of?

MR. KRAUSSE: We're using federal taxable income as the base allocated to New Jersey on the basis of premium receipts and then comparing the premium taxes to that base to get our 17 to 18%.

MR. ALEXANDER: Well, are you making any allocation of income from investments?

MR. KRAUSSE: The federal taxable income includes all income, investments as well as underwriting income.

MR. ALEXANDER: But you say you make the allocation based on --

MR. KRAUSSE: On premiums.

MR. ALEXANDER: -- premiums.

MR. KRAUSSE: Yes. This is done mainly because in the few states that do impose an income tax this is the method that is employed in allocation of total income to that particular state because it reflects more nearly the actual activity going on in the state. This is a common method employed.

MR. ALEXANDER: But, of course, the allocation formula you're talking about doesn't take account of investment income and, therefore, in a state where there was either no investment or a lot of investment income I suppose it would distort the allocation formula quite a bit.

MR. KRAUSSE: Of course all the investments flow from the initial premiums.

MR. ALEXANDER: No, but there are two separate components, clearly.

MR. KRAUSSE: Well, even if you don't allocate premiums to a particular state, you just look at total federal taxable income and total premium taxes paid by all companies, you come up with this same very high effective tax rate as compared with the rates normally imposed upon corporations, even forgetting the allocation problem.

MR. ALEXANDER: Well, what is the position of your company with respect to the insurance premium tax? Are you in favor of retaining it or would you rather see the corporate net income tax applied to insurance companies?

MR. KRAUSSE: The premium tax has been in effect, as I mentioned, for over a hundred years and it has certain advantages to the states as well as to the companies; it's relatively simple to compute and to administer; and it's a stable source of revenue. However, we do feel that the premium taxes are a substantial burden, as compared with the taxes other industries pay. And while I can't say that the company has a position currently on whether the income tax would be the type of tax that should replace the premium tax, all I can say is that we feel the premium tax is a substantial burden resulting in our paying more than other corporations and businesses in New Jersey.

MR. ALEXANDER: Well, then, is the position of your Company then that we should keep the premium tax but not change its rates? Is that what you're trying to say to us?

MR. KRAUSSE: What I have come to say to you is that we feel that we should go one step further than we did in 1966, when certain changes were made in the taxation of life insurance companies, to put them on more of a competitive base with the "Blues" and noninsured plans. And this was done by removing annuity considerations from the tax base and reducing the tax on group health plans to 1%. I would say we should go all the way and reduce the other 1% so that we would be on an equal tax footing with the "Blues" and non-insured employee benefit plans.

MR. ALEXANDER: Why shouldn't the other ones that are now favored be raised to 2%? Wouldn't that achieve the same result?

MR. KRAUSSE: If it was possible to tax the non-insured plans, and I'm not too sure that it is possible, -

if it was possible, this would be one means but I think it might present difficult problems if you try to do so. So to raise, let's say, the tax on the "Blues" would just add them to the list of companies that would have to compete unfairly with the noninsured plans.

MR. ALEXANDER: You think that the "Blues" now are in an unfairly favorable position compared to other insurance companies?

MR. KRAUSSE: Compared to insurance companies, as far as taxes are concerned, yes.

MR. ALEXANDER: Do you know of any reason why group insurance wouldn't be taxable? Is there any constitutional ground?

MR. KRAUSSE: Well, it has not up to this point been looked upon as insurance. I say "self-insurance", that's a misnomer, it's really noninsurance. An employer just says if any benefits are due we will pay them out of pocket and there is no insurance involved at all.

MR. ALEXANDER: Well, is this taxable as insurance now?

MR. KRAUSSE: Not when it's done by the employer without a contract with an insurance company, it's non-insured.

MR. ALEXANDER: All right. Well, I think that self-insurance describes that, as far as I'm concerned.

MR. KRAUSSE: Well, yes, O.K.

MR. ALEXANDER: But, right, it isn't the employee who is insuring himself.

MR. KRAUSSE: There really is no insurance. There is no one assuming the mortality or morbidity risks.

MR. ALEXANDER: But do we tax that kind of activity at all now, under the insurance premium tax?

MR. KRAUSSE: No state does.

MR. ALEXANDER: But you feel there's an equity problem there, do you?

MR. KRAUSSE: Yes, particularly in the group insurance field because this is probably the most competitive line of business in insurance. You are dealing with large employers who are very sophisticated and very cost conscious. And it has been borne out that a 2% premium tax rate as compared with no rate at all results in double the retention charge that an insurance company would have to charge. In other words, all other expenses add up to 2% and the 2% premium tax just doubles the charge, so a large employer says, "Why should I do it? I'll take care of this myself."

MR. ALEXANDER: Well, take the example of true self-insurance. Supposing an industry says, the premiums to insure us against a certain kind of risk, let's say theft by employees, - the premiums are so great that we're going to self-insure our own industry, we're going to pool our money and create our own insurance system. Do you think that as a matter of equity that kind of an arrangement should be taxed in the same way that insurance companies are taxed?

MR. KRAUSSE: If we're going to have equity between taxpayers, yes.

MR. LANG: How do you feel, Mr. Krausse, about the insurance company tax burden versus other corporate businesses? Do you feel that the insurance company is being discriminated against?

MR. KRAUSSE: From our studies --

MR. LANG: We haven't had a chance to look at this.

MR. KRAUSSE: Yes, our studies so indicate. On the basis that we made the computations, comparing the taxes paid by the various industries to net income, insurance companies have a higher effective tax rate.

MR. ALEXANDER: Can you point to any place in your study where you demonstrate this?

MR. KRAUSSE: Yes, it's in Chapter 5. There are three charts, charts four, five and six. Chart four shows the taxes paid under the corporation business tax; chart five is the bank stock tax; and chart six shows insurance premium tax for 45 life insurance companies. These 45 companies do about 85% of the business done in New Jersey.

MR. LANG: Well would the insurance companies, your company in particular, propose that the insurance companies be brought in under the corporation business tax?

MR. KRAUSSE: No, we are not proposing that at this moment.

MR. LANG: Even though you feel that the other corporate businesses are bearing less of a tax burden than the insurance companies.

MR. KRAUSSE: That's right. There are certain problems to be resolved that would have to be considered further, one of them, of course, being how do you define net income. For this purpose we would use federal taxable income.

MR. LANG: Then your problem lies with inequities within the insurance business itself. Your company, a life insurance company, as compared with the "Blues", as you call them, and the self-insurers? Is that what you're saying?

MR. KRAUSSE: Self-insurers.

MR. LANG: This is where the inequity lies.

MR. KRAUSSE: Right, and also in just looking at how we compare with other corporations generally, manufacturers, for example. To set the record straight, some people just look at the rate that we pay, 2%, and say, gee, that's lower than the rate being paid by other corporations; but ours is 2% on gross receipts versus the combination net worth and net income tax that general corporations pay which comes out to about 6% of net income where our premium tax, although it's 2% of gross, comes out to about 17 to 18% of net income.

MR. LANG: Are there any states that tax insurance companies under their corporate income tax as opposed to gross premiums tax?

MR. KRAUSSE: Yes. All the states have a premium tax; a few states also have an income tax; but, generally, they either provide that the income tax shall be a credit against the premium tax or the premium tax is a credit against the income tax so that basically --

MR. LANG: Pay the higher of the two, I guess.

MR. KRAUSSE: Yes, and the higher is always the premium tax. This is another illustration that we can point to to show that our burden is higher than what an income tax burden would be.

MR. LANG: I see. But at the same time you're not proposing that we consider brining insurance companies under the corporate income tax.

MR. KRAUSSE: This is something that has been under consideration in recent years, with rising taxes and rising costs. I don't believe - well, I'm quite sure the industry doesn't have a position on this yet and our company, I don't believe, has a position on this. It's being studied. One of the problems would be, since all the states have had premium taxes for so long, unless all states swung together over to an income tax we could result in a situation where we would have a few states with income tax and, depending upon the method of apportioning net income to those states while other states continue the premium tax, we could end up with greater taxes than we have now. For example, the three factor formula that is found in New Jersey - payroll, property and sales - now if a home state company had, let's say, 10% of its sales in its home state - premiums in this case - where 100% of its payroll and property was in the home state, you would come out with an average factor of about 70%. So 70% of its net income would be allocated to the home state. Now, if all of the other states continued on the premium tax basis they would still be paying 90% of their present premium tax burden to the other states plus 70% of their net income to the home state. So, overall, the burden would go up. This is one of the dangers of doing something piecemeal. If all states went on a net income, I think most companies would be for it because of the results we show here in our study. And also similar studies have been done in Alabama, California, Massachusetts, New York, and they all come to the same conclusion, that the premium tax, expressed in terms of net income, comes out to a higher rate than the normal corporate tax rate on net income found in each of the fifty states.

MR. LANG: This takes into consideration all the insurance companies that do business in the State, not necessarily those who are headquartered or incorporated in the State then.

MR. KRAUSSE: That's right. In fact our study here is 45 companies and there are only three domestic or home-state companies in that; the other 42 are foreign or out-of-state companies.

MR. LANG: I note, in reviewing some of the reports of similar tax policy or tax study groups in some of the other states, there has been some consideration given in a number of them to bring the insurance companies under the corporation income tax. I can't recall that it has actually been legislated but they have been considering this and I assume you are up on that.

MR. KRAUSSE: Yes, they have been considering this but currently there is no state that just taxes insurance companies on net income and not on premiums. They have this combination with credits or they have a net income base which comes up with some sort of minimum tax, fifteen dollars, twenty-five dollars, something like that. But I think what stops them in most cases is when they find if they apply the usual corporate rate to the insurance company's net income they will end up with less revenue, and this sort of kills the whole thing. But, as a matter of equity, if some of these problems of definition and apportionment can be solved, then I think the industry might be willing to propose it but I don't think they are ready at this moment.

MR. LANG: Are you considering any proposal that you might make to our Task Force or to the Tax Policy Commission?

MR. KRAUSSE: No. But because of your interest, I will pursue it and if we have a proposal to make we will send it down to you.

MR. LASSER: Mr. Krausse, about a year ago the State of Pennsylvania proposed an increase in their premium tax to 3%. I think it was enacted and then repealed. Do you have any information?

MR. KRAUSSE: That was a sales tax proposal on top of the premium tax. It was repealed within three days after enactment.

MR. LASSER: Can you tell us why? In other words, what was the impact on insurance companies and why the hasty retreat by the State of Pennsylvania.

MR. KRAUSSE: I think, first of all, it's certainly inequitable to tax prudent people who are seeking to protect themselves and their families from the hazards of life and death and also to save for the future. This would be a tax on thrift. Whereas other forms of thrift, such as savings in a bank account or securities are not subject to a sales tax. Also there is this problem of the non-insured plan and such a burden would only result in further movement to these non-insured plans with a loss of business to the insurance companies and a loss of tax revenues to the states.

Also one of the telling reasons was the fact that such a rate, sales tax rate on premiums, would have triggered retaliation in all the states in which - well, the other 45 states that have retaliatory statutes, and this would have put a tremendous burden on the domestic companies which they couldn't bear.

And also there is a further problem of - I guess it's a constitutional question - can a state impose a sales tax on premiums which are being paid under contracts which were issued many, many years ago and which have a fixed contractural premium stated in the contract. If policyholders refuse to pay the sales tax the companies themselves would have to bear it because they are under this contractural obligation to continue the policy so long as the premiums are paid. So the policyholders could say, "Here's the premium but I'm not paying any tax." So I think that basically the Pennsylvania Legislature realized that there were better ways of obtaining revenue for needed government services than by taxing thrift and self-reliance of the residents of their State.

MR. LASSER: There are other states that have a premium tax in excess of the 2% rate that we have.

MR. KRAUSSE: Yes.

MR. LASSER: Would it be possible for us to consider an increase in the premium tax in New Jersey and what effect would that have?

MR. KRAUSSE: Well, you are right. Premium tax rates run as low as a half of one percent and as high as four percent. We're right about in the middle and most companies also have a 2% rate. That's the most common rate. Once you get above that then you run into this retaliatory problem that the domestic companies, the home-state companies, would face when they're doing business outside the State, as I mentioned in my verbal presentation. In this one state that made the study, the state had proposed an increase in their tax rate from 2% to 3% and this was to be imposed on domestic and foreign companies, but for every dollar that they would have collected from the domestic companies, those domestic companies would have paid almost $7.00 outside the state. I forget the actual dollar amount but it was a ratio of one to seven. For every dollar that the home state collected from their domestic companies, the domestic companies would have to pay almost $7.00 to the other states through the operations of these retaliatory provisions that we find in the insurance industry. And, incidentally, those retaliatory provisions go back to 1826 when the first one was enacted. So it's something that has been in the industry for a long time and it's very difficult to get rid of. But this is what would happen if a state, especially a state with a substantial domestic industry that does a lot of out-of-state business as well, that's an exporter of business. These domestic companies would have a tremendous burden.

MR. LASSER: Is the fact that some states, such as Massachusetts and Connecticut, have a very large domestic life insurance industry due to any favorable tax climate in those states?

MR. KRAUSSE: Connecticut has - well, both of them have, I would say, a large domestic industry. As far as Massachusetts, they have not had favorable tax treatment. And actually in Connecticut the domestics pay a greater burden than the foreign companies. And they have been trying, and a recent Task Force recommended there that domestic and foreign companies be treated equally. But currently the domestic companies in Connecticut are paying taxes at a higher rate than the foreign companies operating in that State.

MR. LASSER: What about the mobility of life insurance companies? There are only four, apparently, in New Jersey.

MR. KRAUSSE: Oh, no. We have about 15 domestic life insurance companies.

MR. LASSER: Four major ones, I guess.

MR. KRAUSSE: Well, there are four here and they account for 94% of the premiums.

MR. LASSER: The other ones are mostly smaller companies?

MR. KRAUSSE: Smaller companies, yes.

MR. LASSER: Well, for instance, the Prudential has a program of decentralization, how difficult would it be for Prudential to make some other state its home state?

MR. KRAUSSE: I don't know. That's a legal question which is outside of my realm. But as far as premium taxes, it wouldn't make any difference because the base is how much you collect from within that state. If we moved to New York, we would still have, presumably, the same amount of premiums coming from residents of New Jersey.

MR. LASSER: Therefore, in our consideration the factor of either attracting more life insurance industry or discouraging or causing any to withdraw from our State is really not a factor to --

MR. KRAUSSE: Well, they could be encouraged by giving them domestic preference. We're not asking for that. You could attract companies to come in. You could get companies that just wanted to operate in New Jersey and, if you gave them a favorable rate as compared with another state, I am sure they would like to come in. But we're not asking for anything like that.

MR. LANG: May I ask a question? Before we go any further, Mr. Krausse, I notice that you have four companies listed in this report and I notice too that Mutual Benefit and Colonial Life are listed as having speakers. Are you speaking for them now or are they going to appear individually?

MR. KRAUSSE: They're going to appear individually. Although I think they endorse what is in this report but I think they have additional comments to make.

MR. REICHE: First, I want to make the comment that I think we might well wish to take you up on your offer of discussing it further after we've had an opportunity to assimilate the information you have in your study.

I have a couple of questions I would like to ask at this point. First, in terms of the impact of the premiums tax, would it be fair to assume that it is passed along to the insured or is it in any direct form or is it absorbed in the general cost.

MR. KRAUSSE: Well, certainly in determining the premium rate structure for companies they consider not only the mortality risk that they are insuring but also general expenses and taxes are figured in determining what that premium is going to be.

I might say this - and maybe Mr. Callahan, who will appear, might have something further to add to this - a stock company that does not do a participating business, in other words, it does not declare dividends to policyholders, it sets the premium and that's it, it could issue a policy in 1900 and premiums are being paid today. Certainly if any premium increases have come along in the meantime, that stock company is bearing those taxes because they were not considered in the original premium that was set many years ago.

In the case of mutual companies, although there probably is leeway in the premiums, certainly when we're talking about long-term contracts which may exist 100 years, they have to build something in there for a contingency. But if taxation got to the point - and inflation, which is a big problem today - and these ate up all those contingencies, certainly it would have to be passed along in the way of reduced dividends to policyholders.

MR. REICHE: This is a corollary of a question asked by Mr. Lasser but how significant a factor in the location of insurance business in New Jersey, in the extension of such business in New Jersey, is the tax imposed on the insurance industry as such?

MR. KRAUSSE: Well, certainly it must be one of the factors that any company considers. Since we've been here for a long time, we haven't had to consider it. But, you know, labor supply and taxes, they are just one of the factors. If all other things are equal, certainly the tax would be the variable which would probably decide against locating in one state versus locating in another. But, as I say, the New Jersey insurance tax system is quite typical as far as the most industrialized and populated states are concerned. So that if a company wanted to locate in a populous area, New Jersey would be one of those to be considered. But, then again, there are a number of very populous states, in the top ten in population, which give domestic preference, some states which don't tax the domestic companies at all.

So, as far as the amount of business they do in that state, that is a significant element in their decision. But if they are planning on doing a nationwide business, they would only have that benefit in the home state, they would still be subject to whatever taxes are imposed in the other states in which they operate. So it has a limited benefit to the state in which they operate.

MR. REICHE: This would appear to contrast with more mobile industries which are attracted or repelled, as the case might be, more readily, I would assume, by the tax structure of the state. Does that appear to be a fair statement?

MR. KRAUSSE: I really couldn't comment on other industries.

MR. REICHE: All right. Thank you.

MR. ALEXANDER: Mr. Krausse, I would like to get back to the question of comparing insurance companies to other corporations within the State of New Jersey. I take it that you are not suggesting that the comparison of the insurance premiums tax to the corporate net income tax with a rate comparison of about 4 1/4% to 17 and 18% --

MR. KRAUSSE: That's 6% with 17 and 18%.

MR. ALEXANDER: Right. That that would constitute a basis for making a comparison between the two types of entity.

MR. KRAUSSE: I'm saying it's an indication of their relative burden.

MR. ALEXANDER: You think it is an indication of it.

MR. KRAUSSE: Yes.

MR. ALEXANDER: But isn't it true that - well, one thing, that doesn't take account of the fact that insurance companies are exempt under the business personal property tax.

MR. KRAUSSE: Yes. And I should qualify that 6% rate. In my written summation, I do indicate that these other corporations are subject to the business personal property tax. I had no way of knowing how much corporations paid in the way of such taxes but if all of the business personal property taxes paid by everyone in business, individuals, partnerships, corporation, excluding those that are exempt, - if all of those taxes were added to those companies who are paying the corporation business taxes, it would increase their effective tax rate about 1.5%. So this gets it up to maybe 7.5%.

MR. ALEXANDER: Well, what if you add the net worth tax?

MR. KRAUSSE: This figures the net worth tax. What I did was to get the net income and then added the net worth and the net income tax and then divided that by net income to come up with 6%. That's why we don't come up with 4 1/4 but we come up with 6.

MR. ALEXANDER: Oh, you're adding the net worth in.

MR. KRAUSSE: Yes.

MR. LANG: O.K. Thank you, Mr. Krausse.

MR. KRAUSSE: Thank you.

MR. LANG: Mr. Charles Kappes of the Mutual Benefit Life Insurance Company.

C H A R L E S W. K A P P E S: Mr. Chairman and other members of the Task Force. I am Charles W. Kappes, Vice President and Counsel of the Mutual Benefit Life Insurance Company, one of the four companies on whose behalf the study has been presented, which you have just had the pleasure of discussing with Mr. Krausse.

I don't intend to take any of your time by adding anything. I would merely suggest that perhaps the discussion with Mr. Krausse has indicated the intense complexity of anything having to do with life insurance, finance and life insurance taxation.

As you gentlemen know, the Federal Government in its internal revenue code has a whole special act with respect to the federal income tax on life insurance companies. And not only is that applicable to all life insurance companies but it goes by phases, and some companies pay under phase 1 and some under phase 2, and so on, my point being that this is a very intricate and complex study. As you delve deeper into it, I am sure we would all be happy to discuss it at length and in depth because of those problems and I would like at this time with your permission to subject myself to whatever questions you might want to ask.

MR. LANG: Do you feel that New Jersey's tax structure, at least it's application to insurance companies, in any way acts as a deterrent to the locating of insurance companies, at least having them locate their headquarters here? There seem to be so few of them, as compared to some of the other states, such as Connecticut. What is the reason for that? Is it the tax structure that's preventing this?

MR. KAPPES: No, I don't think so, Mr. Lang. I think it's historical. You will find in the East that companies tend to be where they started initially, and this was long before taxation was an important factor. Life insurance, of course, in the United States started, essentially, except for a small company in Philadelphia, in the State of New York. And our Company, which was incorporated by the New Jersey Legislature in 1845, was incorporated over here because New York had just created the Mutual Life Insurance Company of New York. And so it went. In the various financial centers life insurance companies grew up. The larger companies tend to be nationwide in their activity, although there are, of course, many concentrated local companies. But if you move across you will find Texas, for instance, has many life insurance companies and rather large ones. So has California and Illinois. There are centers such as that. And I doubt whether taxation was much of a factor. Once a company is located in a particular place, I don't think, to carry on the answer Mr. Krausse gave you earlier - I don't think there is much opportunity for mobility. We have, as I said, a special charter from the New Jersey Legislature and for Mutual Benefit to move out of New Jersey, if it ever wanted to, would represent a lot of interesting questions for the lawyers.

MR. LANG: What do you consider a large insurance company?

MR. KAPPES: Well, any company larger than Mutual Benefit.

MR. LANG: Is there any way of categorizing "large" based on premiums or insurance issued or anything of that nature?

MR. KAPPES: No. "Large" is as indefinite a word in connection with life insurance companies as anything else when comparing. We have certain giants, as you know. The Prudential Life Insurance Company, from whom you have just heard, I guess is the largest in the United States. And there are some five companies, we would say, in the same general area, of which three are in New York City, - the Metropolitan, the New York Life, and the Equitable, and one, the John Hancock, is in Massachusetts. Then you come to sort of a second tier, I'll say from the fifth down to the twenty-fifth, which includes the Mutual Benefit and Mutual, the Northwestern in Milwaukee, and so on. And then they start going down. There are some 2,000 life insurance companies in the United States, you know, and many of them are rather small.

MR. LANG: That was the next question I was going to ask, how many are there in the U.S.

MR. KAPPES: Close to 2,000, Mr. Lang.

MR. LANG: And their headquarters are usually in metropolitan centers, I guess.

MR. KAPPES: Not necessarily. Some of these are highly specialized. There may be a company with just one client, for example, with one policyholder. There will be companies established for a special purpose, as a subsidiary of some business organization. You get a great spread in variety.

MR. LASSER: Would there be any justification in making a distinction in taxation between stock companies and mutual companies?

MR. KAPPES: Mr. Lasser, that is a problem that has infinite complications. As you know, in the Internal Revenue Code there is the difference of treatment between stock and mutual companies in many ways. And that's why those phases to which I referred were written into the code. So it can be done. And using the income tax approach, Congress found that in order to balance the distinctions it was necessary to do something like that. That is perhaps a good reason, one good reason, why the premium tax concept could well be concluded by you gentlemen to be a preferable one in New Jersey, because as soon as you start moving away from it you not only have to build in all of the elements that develop as between life and mutual companies but you trigger the retaliatory laws, as Mr. Krausse testified earlier. For example, as you gentlemen surely know, New York, which needs tax money too, has had for several years now before the Legislature proposals to increase the premiums tax but each year it is deferred in hopes that some satisfactory solution can be determined. Everybody is working on it and as of this date, to my knowledge at least, they have not been able to find it. So New York has refrained from increasing the premiums tax because of triggering the retaliatory laws and all sorts of other complications.

MR. ALEXANDER: Mr. Kappes, in looking at your Table of Contents, I note number 6, Tax Policy Considerations but I can't seem to find it inside there.

MR. KAPPES: I think you will find it way at the end, Mr. Alexander, which is 6-3 and work back to 6-1.

Those numbers are keyed to the index.

MR. ALEXANDER: I found it. Thank you.

MR. REICHE: Might I ask one question? With regard to the possibility of according preferential treatment to domestic companies, do you believe that this is justified?

MR. KAPPES: I don't think it's justified as a practical matter, as an equitable matter or as a matter of public policy. The overwhelming amount of life insurance business in this country is done by companies who are, if not nationwide, pretty much so, and I see no justification for an individual state treating its own companies differently from out-of-state companies in the area of premium tax. Of course, the domestic companies have all sorts of other taxes, as is indicated. We pay, I think, the four companies involved here, according to this study, some several millions more in real estate taxes than we do in premium taxes. And there are many other places where we are paying taxes. But when we speak of premium taxes, I don't see any justification for treating out-of-state companies differently from in-state companies. Most of the companies, as you will notice when you have an opportunity to review the chart here, most of the states do treat them relatively comparably, although some do put a heavier burden on domestic companies and some do put a heavier burden on foreign companies.

MR. REICHE: It's somewhat beyond the scope of our inquiry here but let me ask if I may, is the extent of local real property taxation a source of perhaps greater concern to insurance companies in New Jersey than is the insurance premium tax?

MR. KAPPES: I think I can properly answer that no.

MR. LASSER: Mr. Kappes, the retaliatory tax is apparently not triggered by the imposition of the real property tax.

MR. KAPPES: That is correct.

MR. LASSER: But would be triggered by other types of tax. If I remember correctly, the Newark payroll tax exempts insurance companies because of the retaliatory effect. Is there any way of determining which taxes will trigger the retaliatory tax and which won't?

MR. KAPPES: Mr. Lasser, that takes an extra law school course to learn that. This is something that there is always question on. As Mr. Krausse testified, when the sales tax was passed in Pennsylvania last year there was immediately the question of triggering retaliation. The retaliatory statutes vary from state to state, the wording varies, the provisions vary, and this is one of the complications of our life. So that I don't think it is possible to give you a categorical answer. A property tax is on real property, other types of property, and the retaliatory statutes generally apply to taxes in the nature of franchise taxes, privileged taxes, taxes based on the doing of business rather than owning property.

MR. LASSER: Was the exemption from the business personal property tax enacted on that same basis?

MR. KAPPES: On the payroll tax?

MR. LASSER: No, on the business personal property tax.

MR. KAPPES: I can't answer that. I don't know.

MR. ALEXANDER: Are you in favor of raising the tax treatment of the "Blues", raising the percentage that they will pay on their premium to 2% from 1%?

MR. KAPPES: Mr. Alexander, I know the very great problems that all governmental units have in providing themselves, through taxes, with the wherewithal to provide for the carrying on of government and the necessary services which the people require from government. But there is also a social end involved too. I think these organizations such as Blue Cross and Blue Shield were originally set up because of a need of the people for the kinds of coverage that they were to provide where people, as individuals, very often were unable to provide it for themselves. And I think that social purpose still exists and it still applies to these various coverages that commercial life insurance companies provide. So that the answer I would give you is, no, we should not add the burden on to the "Blues" but we should take into consideration inequities that may exist as between organizations such as Blue Shield and Blue Cross on one hand and commercial life insurance, as we know it, on the other, and the so-called self-insured plans that Mr. Krausse was talking about.

MR. ALEXANDER: Well, are you saying that there is or is not discriminatory treatment as between the "Blues" and commercial life insurance?

MR. KAPPES: Well, sure there is, although New Jersey a couple of years ago helped reduce the gap by reducing the tax on annuity considerations and on group health. But there is still a discrimination too. I thought the burden of your question though was whether I thought it would be desirable to eliminate that gap by raising or by imposing a tax on the "Blues" side rather than diminishing the tax on other life insurance companies.

MR. ALEXANDER: Yes, that was the way my question was phrased.

MR. LANG: And you would prefer lowering the tax on the other insurance companies. Is that it?

MR. KAPPES: Well, sir, as I read the charge to your task force, you have been asked to try to make an equitable distribution of the burden. And I realize this is a very difficult thing and, in the light of the fact that the premium tax is a relatively heavy imposition already, I would think that the fair thing in that area would be to move us down in the area of the "Blues".

MR. ALEXANDER: What would be the effect on the insurance industry of an across-the-board 1% increase in the premium tax?

MR. KAPPES: Well, let's speak of the domestic industry, the domestic companies, the 15 companies that are incorporated in New Jersey. This would immediately not only create the additional drain on our own resources that that tax would impose with respect to premiums from New Jersey policyholders but it would immediately trigger the retaliatory statutes in the 45 other states which have them. And I am not prepared to give you a dollar result but it would be a tremendous amount.

MR. ALEXANDER: Well, is there any reason to think that that would make the treatment of domestic companies more discriminatory than it now is, by raising the rate?

MR. KAPPES: Discriminatory against whom?

MR. ALEXANDER: As between domestic and foreign insurance companies.

MR. KAPPES: Well, we presently do not, New Jersey does not. New Jersey has the same rate.

MR. ALEXANDER: But other states have retaliatory provisions which are now in effect. Isn't that so?

MR. KAPPES: Right. Now, may I be sure that I understood what you hypothesized, that the New Jersey rate would go up from 2% to 3% for both New Jersey and foreign companies, on the premium tax. Was that your proposal?

MR. ALEXANDER: Yes, that would be part of it.

MR. KAPPES: Well, as soon as you raise the rate on the other states, companies who do business in New Jersey, that is what triggers retaliation. And then those 45 states would add our premium tax that we New Jersey companies pay to them by 1%. This would be a very burdensome and large thing and wouldn't do too much good for the revenues of the State of New Jersey because, the companies we are here concerned with, the great preponderance of our business is out of New Jersey.

MR. ALEXANDER: But if you are talking in terms of the revenues of the State of New Jersey, the vast majority of revenues from the insurance premiums tax comes from foreign corporations.

MR. KAPPES: Yes. That's very true. I think in this connection it is necessary to think back to the reason for these retaliatory statutes. In fact, I've often felt that the word "retaliatory" is very misleading. It sounds as though somebody is trying to discriminate against someone else, whereas the reason that the states enacted these was to try to maintain a balance and not have one state jump ahead with a large tax and discriminate against all the other states. And the retaliatory acts have very largely fulfilled their purpose by maintaining this general balance, although your chart, I think it's Chart 1, indicates there is a variety and Mr. Krausse said there are states that go up to 4% and down to .5%, but, by and large, we have a balance. And what I would like to suggest to the Task Force is that if you come up with a recommendation that is going to upset this tenuous balance that we have, please give it the deepest consideration because it could be very dangerous.

MR. LANG: Thank you, Mr. Kappes.

MR. KAPPES: Thank you, gentlemen.

MR. LANG: Mr. Callahan, Colonial Life Insurance Company.

GEORGE H. CALLAHAN: My name is George Callahan. I am Senior Vice President and Counsel of Colonial Life of East Orange. I primarily just want to be here to join with my colleagues, Mr. Krausse and Mr. Kappes, in the presentation that was made and the report that was filed and also to co-author the comments that they have made.

I would like, with the permission of the Task Force, to address myself to answering a question that was put by Mr. Reiche to Mr. Krausse. I must have been psychic in anticipating it because when I went over our material, the written material, I was prompted to want to make a comment, which I would like to do now, which is really not in the written report but it supplements it, with your indulgence.

In the written report, it has been pointed out that the gross premium of the life insurance company is not any evidence of its profitability and also that the life insurance companies in general in New Jersey now are paying taxes at a rate equivalent to three times that being paid by other corporations in New Jersey.

We wish to remind the Task Force that the commodity of these companies, life insurance policies and their related contracts, are sold in a highly competitive market. The constant trend of these companies making up this industry is to reduce premium rates to compete for a portion of the life insurance business. This is a rare industry where the cost of benefits to the insured over the years has continued to decrease. On the other hand, the ever-increasing costs, and especially tax costs, are making it more difficult for a company to maintain a competitive business with a reasonable return.

Size of premium income is deceiving and no measure of ability to pay taxes. Remember that current premium income is derived from policies sold not only this year but for many, many years past. This year's premium income is based upon past sales with premiums established based on actuarial assumptions for expenses, including taxes, deemed reasonable at the time when the policy was sold. The current spiraling increase in taxes has far exceeded the prior original actuarial assumptions built into the premium rates on policies sold in past years.

Colonial Life, as a life insurance company selling principally nonparticipating life insurance policies, is particularly affected by these rising tax costs. The non-participating, meaning non-dividend paying policies, sold by Colonial and other companies have a fixed premium rate with built-in cost assumptions which were established when the policies were sold. These premiums remain constant throughout the life of the policy without any means available to the company of offsetting these rising tax costs retroactively to prior sales where the original premium calculations have proved inadequate.

Colonial, for example, was founded in 1895, and we, today, have some premium income going back to that time, based on the value of the dollar in those days. Today's total gross premium is a composite of sales from yesterday back to 1895 for Colonial, with each individual premium based on assumption for expenses, including taxes, related to when the sale is made. Today's gross premium income from all of these prior years has not made adequate provision for today's inflation. I reiterate, to look at current gross premiums alone is misleading. The only way that we can offset these rising taxes is by increasing premiums; but, by so doing, the company becomes less competitive with a decreasing premium income subject to taxation. And it follows, likewise, that the benefits to its policyholders become more costly.

Thank you.

MR. LANG: Mr. Callahan, just to zero in on this retaliatory tax procedure again, I must admit I'm a layman in this field --

MR. CALLAHAN: I hope I can help you, sir.

MR. LANG: As an example, New Jersey has a 2% tax on gross premiums, now does your company do business in a 3% state, as an example, Mr. Callahan?

MR. CALLAHAN: On which chart, Mr. Lang?

MR. LANG: Well, I'm looking at chart 2.

MR. CALLAHAN: Generally, I can say that Colonial Life is authorized to do business in 46 states, the District of Columbia and Porto Rico.

MR. LANG: Well, let's take as an example, - suppose you did business in any of these six states that have a 3% tax on gross premiums, does that mean now that New Jersey levies a 3% tax on an Alabama Company, as an example, that does business in New Jersey? Is that how that works?

MR. CALLAHAN: Well, as was explained by Mr. Kappes, the way this works, as I understand it, and I'm not a real expert on it either, if New Jersey were to increase its tax say to 3%, as Mr. Alexander before suggested, then in the case of Colonial Life, if we go into another state which has a 2% rate, we then on that state, on sales within that state, would be charged 3% to offset what New Jersey is doing to the foreign companies selling within our state. In other words, even though they have in that state a 2%, as to other companies they will impose a 3% rate if that is the rate of your domestic state.

MR. LANG: Well then, that would be the case, in looking at this comparison chart here. I would assume that since Alabama, for example, would charge your company 3% on gross premiums in that state, then evidently any Alabama insurance companies, if there are any, doing business in New Jersey would be taxed 3% in New Jersey. Is that right?

MR. CALLAHAN: Well, supposing New Jersey went to 3% on all premiums --

MR. LANG: Let's stay with it where we are today. In other words, let's not talk about an increase. What is happening today between New Jersey and Alabama?

MR. CALLAHAN: I don't feel qualified. I'll put it this way, we're not in Alabama. That's one of the few states I know we're not in. But I would imagine if we had sales in that State we would pay 3%.

MR. ALEXANDER: But New Jersey has retaliatory provisions, does it not?

MR. CALLAHAN: Yes, it does.

MR. ALEXANDER: And, therefore, we are presumably "retaliating" against Alabama companies, if any, selling in New Jersey.

MR. CALLAHAN: Yes.

MR. ALEXANDER: That's the question.

MR. LANG: Mr. Krausse, can you answer that question?

MR. KRAUSSE: Three percent, I believe it is, the Alabama rate, against Alabama companies on the business that they do in New Jersey.

MR. LANG: These would be domestic Alabama insurance companies.

MR. KRAUSSE: Right.

MR. ALEXANDER: What is the sense in which "domestic" is used? the state of incorporation?

MR. CALLAHAN: Yes.

MR. ALEXANDER: So that a company could very well be incorporated in State A and State B have its principal office and all employees, or 99% of them, couldn't it?

MR. CALLAHAN: I don't think that's generally so, Mr. Alexander.

MR. ALEXANDER: But it could, though.

MR. CALLAHAN: I doubt it. I really do. I think you will find that in most cases, if not all, the insurance department of the state of incorporation would exert pressure that the principal office be in that state.

MR. ALEXANDER: Well, take a company like Prudential, does it have more employees in New Jersey or in Illinois?

MR. CALLAHAN: I really couldn't answer that.

MR. ALEXANDER: What is the home state of Prudential?

MR. CALLAHAN: The home state? It's a New Jersey corporation, to my knowledge.

MR. ALEXANDER: Right. What about comparing those employed by Prudential in New Jersey and those employed by Prudential in Massachusetts? Wouldn't it depend upon the size of their office, rather than the state of their incorporation?

MR. CALLAHAN: I believe that would follow. But I don't know, not being of Prudential, Mr. Alexander, I don't know what motivates their decentralizing in a given market.

MR. ALEXANDER: I'm just using them as an example.

MR. CALLAHAN: Yes.

MR. LANG: Do you know when was the last time a state, any one of the states, increased its gross premiums tax?

MR. CALLAHAN: I, personally, do not know. Maybe Mr. Krausse does.

MR. LANG: Have there been any recent increases in the gross premiums tax in any of the states?

MR. KAPPES: Montana had a temporary tax that they made permanent this year. It was made temporary year after year and now it's permanent. I'm just checking with Mr. Krausse here. I don't recall any this year.

MR. LANG: And this 4% rate in Oklahoma has been in effect quite a number of years. Is that right?

MR. CALLAHAN: Yes.

MR. ALEXANDER: Is Connecticut a major home state for insurance companies?

MR. CALLAHAN: Yes.

MR. ALEXANDER: I see. It meets the problem we're talking about by discriminating between domestic and foreign. That's one way of avoiding retaliation.

MR. CALLAHAN: I don't quite understand, Mr. Alexander, if it's a question.

MR. ALEXANDER: Well, by taxing foreign corporations low you avoid retaliation against Connecticut domestic corporations.

MR. CALLAHAN: True.

MR. ALEXANDER: You don't recommend that solution though, do you?

MR. CALLAHAN: No, sir.

MR. LANG: Thank you.

MR. CALLAHAN: I think it can be said, insofar as I would like to supplement an answer, I think given by Mr. Kappes before, that the possible effect of any increase in premium tax, it ties in with the statement I was making before, what the effect of it would be. The only way that you can really offset such an increase in that is through your premium structure. Now, your premium structure can only be prospective and not retroactive. And for a company of our size, where we are competing, - we are, I would say, a small company, competing against 2,000 companies, - to then have to increase our premium, it makes it most difficult, even more difficult than it is right now.

MR. ALEXANDER: Well, you know it would be interesting to know in specific terms, with respect to a specific New Jersey domestic insurance corporation, what its impact would be in terms of foreign premium taxes if we were to raise 1% in this State. It would just be interesting to see what the impact would be in dollar terms.

MR. CALLAHAN: Through the retaliatory effect.

MR. ALEXANDER: Right. I'm not sure that's a relevant consideration but it would be interesting.

MR. CALLAHAN: I think - my colleagues are saying yes that we would be glad to try to submit some material along that line to demonstrate to you what the effect would be. I think it's going to be quite an impact. I am quite sure it would be.

MR. REICHE: And if I may add, I think it would be very relevant to our consideration, too, to have that information, since one of our problems is obviously the magnitude of revenues to be raised.

MR. LANG: Thank you, Mr. Callahan.

MR. CALLAHAN: Thank you.

MR. LANG: Mr. Nasmith, Associated Railroads of New Jersey.

A U G U S T U S N A S M I T H: Mr. Chairman, I will try to follow your rules and will not read from the statement.

What we are trying to do is to provide a summary outline of recent history regarding the two taxes which are mentioned in your guideline, the railroad franchise tax and the railroad property tax, and on the last page of our memorandum we refer to Sales Tax Inequities, wherein we propose two minor amendments to the Sales and Use Tax.

In essence, we are attempting to point out in this brief statement that after an historical background of litigation over many years, allegations on our part of overassessment, litigation with municipalities, the subject of railroad taxation has been considered at length by the State Tax Policy Commission, and most recently in 1963 and

'65, and its studies were implemented by legislation which finally became effective in 1967, which we consider to have been a major tax reform that took into account our lack of ability to payand the needs of the municipalities wherein we have property in railroad use.

Part of the considerations in the last report was our poor financial condition. And, as we pointed out, unfortunately that is even worse than it was at the time the Eleventh Report was published.

I would merely like to point out as to the sales tax inequities. We propose that railroad track materials, communications, signal and power equipment should be exempt, in addition to the present exemption for sales of locomotives and rolling stock because this would afford railroads, in essence, the same exemptions as are afforded other public utilities for machinery, apparatus or equipment and cables for use in transmission or distribution of their services.

I might point out another minor amendment wherein certain repairs to trucks are exempt. We believe that same exemption should be incorporated for repairs of railroad equipment.

I will conclude by merely stating that I think the intent of the reform has been accomplished. It has worked fairly well, in accordance with what they intended, although the property tax revenues are now down, for 1970, slightly under $8 million. We have suggested a 5% decrease in the tax rate because this reduction has not come about from the tax rate but has come about from disposal of property.

That's about all of the time I would care to take, unless you have questions.

MR. LASSER: Mr. Nasmith, are there any problems in the property tax area outside of the Class II main stem problems? In other words, do the railroads experience any inequitable treatment or any particular tax problem on other than Class II property in its taxation?

MR. NASMITH: As far as I know, we have no problems that are not peculiar to the general taxpayer. You're speaking now of property owned by railroads but not taxed under railroad tax law because it is not used for railroad purposes. I know of your personal interest so I will put in a plug that improvements should be made in the field of tax procedure and we were quite interested several years ago and I, personally, am still interested in the creation of a tax court which would expedite appeals.

MR. LASSER: I really didn't mean to elicit that kind of an answer but I was curious as to whether railroads were still experiencing any non-mainstem tax inequitable problems.

If the sales tax were amended to provide an exemption for machinery and equipment primarily used in manufacturing which is the exemption that was removed back in March of 1970 - would the restoration of that exemption solve your problem with respect to the equipment you referred to?

MR. NASMITH: We don't believe so because I think it would take a strained interpretation to say that we're in the manufacturing business or that our construction of roadbeds or transmission equipment would be in a sense a manufacturing enterprise.

MR. LASSER: You feel that you would need special language, special exemption for railroads to cover that problem.

MR. NASMITH: Yes, and on the same theory that similar exemptions are given to other public utilities.

MR. LANG: You spoke of requesting a 5% reduction in the rate. Is that on the $4.75 for each hundred dollars of true value? Is that what you mean?

MR. NASMITH: Yes. We propose a rate of $4.50 which was originally considered in the drafting of the original legislation but because of the need for money at that time the final version was $4.75.

MR. LANG: In other words, that would bring about, I guess automatically, a 5% reduction in the revenues from this source.

MR. NASMITH: Yes.

MR. LASSER: Do we have any kind of a domestic versus foreign railroad problem in New Jersey? Are there foreign railroads that operate in this State profitably that we may not be securing revenue from that we should?

MR. NASMITH: No. There is no distinction in taxation of either intrastate or interstate railroads. We have other problems but not tax discrimination in that sense.

MR. ALEXANDER: What would be the revenue impact, or did you state it in your paper, of reducing the tax rate from $4.75 to $4.50?

MR. NASMITH: In round numbers, $400,000. That's taking 5% of $8 million actually, I think, in 1970. It's actually, I guess, now 5% of $7,500,000. I do not have available the loss of revenue under our proposed sales tax amendments but the estimates I have are in the neighborhood of between $100,000 and $150,000. It's not a very large item.

MR. REICHE: Do you still favor adhering to the tax mechanism of a tax on net railway operating income as opposed to other bases for a possible tax on railroads? In other words, does this seem to be the most equitable basis as far as the industry is concerned?

MR. NASMITH: Yes. A gross receipts basis would have an extremely adverse impact.

MR. REICHE: Well, I can see that that would.

MR. ALEXANDER: What about an effort to reach income from other than operating sources?

MR. NASMITH: Well, we come under the sales and use tax and we do pay some taxes there. I don't know what the nature is. The effort to tax us on any kind of an income basis other than franchise tax would not produce much revenue for the State of New Jersey since the railroads that belong to our Association are, with one exception, all in deficit operation.

MR. ALEXANDER: Well, do all the railroads involved in New Jersey have a corporate structure setup somewhat like what we've been reading about in the papers as far as the Penn Central goes, with a holding company which has interests in a whole variety of enterprises some of which may be simply holding land formerly used for railroad purposes, and all kinds of other things, some of which may be involved in investing in various kinds of enterprises, holding securities, and so on? Do the others, beside Penn Central, have that kind of a corporate structure?

MR. NASMITH: I think your original question was, do all railroads, and I think the answer can positively be no.

MR. ALEXANDER: All right.

MR. NASMITH: I believe there are some railroads - I'm not qualified to answer specifically - who do have at least subsidiary landholding corporations. I think those in the main are nonprofitable and any sales of land go directly to the parent. They are 100% owned subsidiaries so there is no siphoning off of assets.

MR. ALEXANDER: Do we reach in some way, are we able to tax? For example, let's take that example because it's usually an important one for railroads, - do we reach by taxation in this State the sale of land by a railroad holding company which land may well have been held for railroad purposes beforehand but which has been perhaps for some length of time held simply as an investment?

MR. NASMITH: The State of New Jersey reaches it, as it does any other land owner. That land being held by another corporation would not be taxed under the railroad tax act, it would pay the general tax rate for all local property, the same rate as other general property taxholders. If that land were sold, you eventually reach it under the franchise tax as, let's assume, a profit on the sale, as that is passed on.

MR. ALEXANDER: Well, I would question that. Isn't the franchise tax limited to operating revenues?

MR. NASMITH: You're correct, yes. So that statement is wrong in that sense.

MR. ALEXANDER: O.K. Thank you.

MR. LANG: Thank you, Mr. Nasmith.

We will adjourn the hearing for lunch and we will reconvene at 1:30.

(Adjourned for lunch)

(Afternoon session)

MR. LANG: We will reconvene the hearing.

First, this afternoon, we will hear from Mr. Robert O. Brokaw, Jersey Central Power & Light Company.

R O B E R T O. B R O K A W: Good afternoon, gentlemen: My name is Robert Brokaw and I am Assistant General Attorney for Jersey Central Power & Light Company and for New Jersey Power & Light Company. I appreciate this opportunity of speaking to you about certain of the Public Utility Gross Receipts and Franchise Taxes.

Public Utility Franchise and Gross Receipts Taxes affecting electric and gas public utilities have been in effect in New Jersey for over 60 years in one form or another and from time to time Chapter 5 of the Public Laws of 1940, the current basic statute, has been amended and expanded to include other utilities such as water companies and sewer companies.

The statute provided a complete scheme for the taxation of those utilities, including electric companies, which are subject to taxation under it, and so insured uniform tax treatment of such companies in lieu of an ad valorem tax on their property other than real estate. It was the purpose of the Act that such companies not be subject to different or discriminatory tax treatment or evaluations made by local assessors with respect to property other than real estate since the gross receipts taxes are in lieu of the former local ad valorem tax on property other than real estate.

The abolition of local personal property taxation of corporations has not diminished the desirability of this single scheme of taxation.

For the year 1970, Jersey Central Power & Light and New Jersey Power & Light Companies paid $19,029,870 under this law. Of this $1,382,579 represented local real estate taxes and $17,647,291 represented franchise and gross receipts taxes and surtax. The surtax was imposed temporarily in 1963 and made permanent in 1966. In 1970 it accounted for almost $2,000,000 of our taxes. While these amounts are high in comparison to our revenues, we believe that the present levies are at appropriate levels for providing tax revenues, particularly when growth is considered. We anticipate that, in any event, solely by our growth in electric sales, the 1971 taxes on revenues will be approximately $2,270,000 more than in 1970, or over a 10% increase. Any changes in tax rates would, of course, be reflected in electric rates to our 555,000 customers.

Our companies also believe the formula used to allocate and apportion the taxes to the municipalities wherein the companies' property is located is fair and reasonable and, in particular, it is consistent with the administration and method of assessment of property of large industrial tax payers who pay ad valorem real estate taxes on a particular industrial facility to the municipality where it is located.

I think, gentlemen, that generally concludes our presentation. I hope to be able to answer any questions you may wish to put to me.

MR. LASSER: Mr. Brokaw, have you any idea how your company would be taxed if you were taxed under the corporate franchise tax instead of having special gross receipts tax?

MR. BROKAW: I have no specific information to indicate any meaningful entity but my impression is that under these taxing schemes we would be paying more than we would under the corporation business tax.

MR. LASSER: That's my impression, as well, that that's the case.

MR. BROKAW: Considerably more.

MR. ALEXANDER: You say you would be paying more?

MR. BROKAW: We would, although I have no specific calculations to support that statement but that would be my impression that we would be paying considerably more under this gross receipts and franchise tax than we would under the business corporation tax act, as if we were taxed as other corporations.

MR. ALEXANDER: The only trouble I had was with your use of the conditional --

MR. BROKAW: Sir?

MR. ALEXANDER: Aren't you paying under these taxes now?

MR. BROKAW: No, sir. We are taxed only under this statute. There are no other taxes imposed on our property franchises or stock. This is an exclusive tax statute so far as electric and gas utilities and other utilities named in there, water companies, sewer companies, traction companies and so forth.

MR. ALEXANDER: You're taxed under the public utility franchise and gross receipts tax.

MR. BROKAW: Yes, sir.

MR. ALEXANDER: I know that. But you say that you are paying more under that tax than you would pay under --

MR. BROKAW: We believe we would be paying more under that tax statute than we would be under the general corporation and business tax act. We still pay local real estate taxes on our land and buildings to local municipalities.

MR. ALEXANDER: Just your use of the word "would" had confused me. You are paying more under the public utility franchise and gross receipts tax --

MR. BROKAW: We believe we are.

MR. ALEXANDER: -- than you would pay under the --

MR. BROKAW: That's correct. We believe we are, although I have no figures to support this.

MR. LANG: You've never made a study of that then, have you?

MR. BROKAW: We haven't made a study of that.

MR. REICHE: Do you have any comments to make with regard to the present system of assessment and collection, i.e., assessment by the State and then payment over to the municipality?

MR. BROKAW: No, sir. We find that it works well for us and has worked well for the municipalities, although I understand there have been some problems with apportionment allocations between respective municipalities as to where our property is located.

MR. REICHE: Well, this naturally results in some municipalities, simply by the very presence of a plant there, benefitting greatly whereas other municipalities benefit very little.

MR. BROKAW: Yes. But this would be true of any other taxpayer or large industrial taxpayer who might wish to locate in a particular municipality as opposed to another. They would receive those large tax revenues too.

MR. REICHE: This is true except, of course, the areas served by utility companies usually transcend municipal lines.

MR. BROKAW: This is true, very true. But by the same token, the product of an industrial manufacturer transcends municipal lines also. Their work product is transmitted and flows into commerce, as ours does, but ours is intrastate.

MR. LANG: Well, yes, your revenues are really more of a local nature than most manufacturing companies --

MR. BROKAW: Yes, sir, they are.

MR. LANG: -- they are interstate, more or less, rather that intrastate.

MR. BROKAW: That's true.

MR. LANG: Where yours are intrastate and locally. In other words, your company just serves a local area.

MR. BROKAW: My two companies serve all or parts of 13 counties in New Jersey.

MR. ALEXANDER: Well, you represent Public Service?

MR. BROKAW: No, sir, I do not. I represent Jersey Central Power & Light Company and New Jersey Power & Light Company.

MR. ALEXANDER: Is it Public Service that has the large generating plant in Hamilton Township?

MR. BROKAW: I believe so. They're here today. We have one large generating plant in - well, we have three generating plants.

MR. ALEXANDER: And your rationale for having the gross receipts tax being paid to that municipality is that its revenues come from that municipality?

MR. BROKAW: No, sir. No. I don't mean to imply that. I say we're in no different position in that respect than the large industrial taxpayer. There are certain municipal services which we have an impact on, as does any large industrial manufacturing plant incurs expenses so far as municipal services are concerned, and that depends upon the size of the facility.

MR. ALEXANDER: That's true, but the other enterprises don't pay a gross receipts tax for municipal use.

MR. BROKAW: But they pay ad valorem taxes.

MR. ALEXANDER: On personal property?

MR. BROKAW: Well, no, that would go to the State under this new business and personal property tax.

MR. ALEXANDER: Right.

MR. BROKAW: But what is considered real estate, with respect to a large industrial taxpayer, is different than what is considered real estate with respect to electric and gas utilities. The definition of real estate is defined.

MR. ALEXANDER: Well, supposing you take the Public Service Plant in Hamilton Township, just as a hypothetical example. If it were paying to that municipality real estate taxes wouldn't they be substantially less than what it is paying in utility gross receipt taxes?

MR. BROKAW: To that particular township?

MR. ALEXANDER: Yes.

MR. BROKAW: It's possible this could be so. I am not familiar with that plant. But, as I pointed out, the only thing that's taxable locally and assessable locally, under this act, with respect to electric and gas companies, is its real estate, and its real estate is defined as land and buildings, notwithstanding the machinery, apparatus or equipment that may be attached to it. So, the law of fixtures doesn't apply to us where it would necessarily apply in large measure to large manufacturing plants because its permanently affixed to the building. So part of that may be included in real estate, with respect to a large manufacturing facility, and not with respect to us.

MR. REICHE: Have you any comment on the dual nature of the public utility tax, i.e., the division of gross receipts on the one hand and the franchise tax on the other?

MR. BROKAW: No, sir. I am not prepared to comment with respect to that. One is a franchise tax which is a privilege tax for our use of the public streets for our facilities. That's the 5% tax. And the other is a gross receipts tax on our business from all our lines and mains throughout the State.

MR. REICHE: What I am concerned about here is the fact that we have heard testimony by various businesses, albeit different from yours, indicating some dissatisfaction with the gross receipts tax as a viable measure for taxing, simply because it is not always, perhaps, an indicator of the profitability of the business. And I am just wondering whether this is a sentiment which you perhaps share.

MR. BROKAW: I do not think we share this. What we're particularly concerned about is the treatment we would have received, and before this gross receipts and franchise tax was enacted, was the variable treatment that we got from local assessors when these same items of property were taxed in different municipalities. What this statute and its predecessor did for us, where we have widespread lines and poles and large plant distributed throughout a large area, was establish uniform treatment with respect to those items. So this became an in lieu tax. This was the theory behind the tax and we are happy with that, as far as I can understand.

MR. REICHE: In other words, one of your major problems had been the differences between administration in one municipality as opposed to another.

MR. BROKAW: Correct. And this statute was designed to overcome that and it has worked well in that respect.

MR. ALEXANDER: Mr. Brokaw, in computing your rate base, what account is taken of the gross receipts tax?

MR. BROKAW: These are charged in the expense accounts in computing rate base, so that any increase would be reflected ultimately in the customer's rate.

MR. ALEXANDER: That's a very direct form of passing it on.

MR. BROKAW: Yes, it is. Of course, we are regulated in what we can earn and it's not like the ordinary industrial enterprise where they are in the open market and their prices and profits are determined by competition. We have so-called franchise areas or service areas, and we are regulated in what we can earn on our invested capital.

MR. ALEXANDER: This is why you might not be so concerned as some of the gentlemen that spoke this morning about the --

MR. BROKAW: This is so.

MR. ALEXANDER: -- if you want the regressive character, the fact that a gross receipts tax doesn't take account of ability to pay.

MR. BROKAW: That's correct.

MR. LASSER: Let me ask a question along those lines.

What we're really talking about is how much the consumer should pay for his electricity. And if additional taxes are imposed on public utilities, those will be passed on to the consumers.

MR. BROKAW: These are factors that are taken into account by the Public Utility Commission in determining a fair and reasonable rate, once the rate base is established, that is rate based on expenses and determine a return.

MR. LASSER: And that also has a bearing on the fact that electricity and other public utility rates are exempt from the sales tax.

MR. BROKAW: Yes, sir.

MR. LASSER: In other words, the end result, apparently, up to now has been how much the consumer will pay for this bundle of charges, including taxes.

MR. BROKAW: Yes, sir.

MR. LASSER: Have you any experience on what may have happened in other states when taxes on public utilities were increased? Does it just automatically result in higher cost to the consumer or does it have another effect?

MR. BROKAW: I would assume - I have no particular experience in that respect but I would assume it would because generally rate base is determined in most states along the same general lines - plant investment, revenues and expenses.

MR. LASSER: And what was the experience when the surtax was put on in New Jersey? That just added more cost to your company --

MR. BROKAW: That's right, it did.

MR. LASSER: And was that passed on to the consumer?

MR. BROKAW: Well, that was not because Jersey Central had never had a rate increase until just recently when we concluded rate hearings before the Commission. So that wasn't passed on at that point.

MR. LASSER: So there is a lag.

MR. BROKAW: There is a lag, a definite lag. But when I say it's carried on or passed on, when and if a rate application is made these taxes, of course, are ground into the expenses which the company incurs and shows on the financial statements, which are submitted as part of the rate case.

MR. LASSER: If it were determined that it was necessary for the State to raise more revenues, how would you feel about using the public utility tax as a method of adding to those increased revenues?

MR. BROKAW: I think we would consider it unfair, sir, because we feel we're paying a lot and we feel we're paying really more than our share now, although we're willing to live with it as it is.

MR. LASSER: Well, when you say "we", you're really saying the consumers, I think, the consumers of electricity are paying as much as they should for electricity because it does get passed on.

MR. BROKAW: Well, if there happens to be a rate application - and these don't occur too often, except recently there have been a rash of rate applications because of increased construction costs, and so forth, and operating costs have increased to the extent that a good many utilities are not gaining a fair return on their investment, and this has been the reason for these rate applications -- but, as you pointed out, there is in a good many cases a lag of a good number of years before these impositions are reflected in rates to customers. We don't have a tax adjustment clause in our rate whereby if a tax imposition goes into effect we can immediately pass it on to our customers. We can't do this until the time comes when it becomes necessary to apply for rate relief.

MR. LASSER: Do you have any idea how New Jersey stands, compared to other states or similar states, in taxing public utilities? about average? heavier? lighter?

MR. BROKAW: I'm not prepared to say that. I am not acquainted with what other states do.

MR. LASSER: All right. You made reference to the personal property - real property distinction. Is there any problem in administering the present law with respect to definition of personal property and distinguishing it from real property?

MR. BROKAW: Yes, sir, there is. We have run into problems. We have now before the Division a case involving easements which we claim are not land. I didn't want to open up this can of worms with you folks today because I didn't think it was the proper place, but there has been and there is litigation with respect to the interpretation of what constitutes land and what constitutes building, taxable under this statute by the municipalities.

MR. LASSER: I know in a number of instances where easements are being taxed as real property and the reason I raised the question is because this Task Force is concerned with these taxes, with the administration of the taxes, and any possible inequities that may result from the administration of these taxes. So if there is an area where there is either a conflict or some inequity, we would like to know about it so that we can perhaps do something about it.

MR. BROKAW: Well, this is under serious contention now. The New Jersey Power and Light Company has a case before the Division now, yet undecided, and I believe Public Service has now. And if the easements are defined as land, which we claim they are not, this would have a considerable impact upon the tax imposition that we now are faced with, concertedly, and it would involve another $2 million, at least, for our companies in tax revenue, and that's a conservative estimate and it could go higher. I am not prepared to say how high because we haven't made a study but that's just an off-the-cuff opinion. At least for our companies it would involve that much more in the way of a tax imposition if this type of interest in land were included. We take the position that land means land itself and not just an interest in land which is what is what an easement is. We have not been assessed, except in one or two places where the dollars didn't amount to much where it wasn't worth a fight. In Tewksbury Township they've assessed some six miles of electric transmission line right-of-way and the dollars are substantial, and we are now contesting it. And we think there should be some further clarification to put this thing at rest. But we are litigating it now and if the Committee wants to consider it, we would be happy to have it at least consider some further clarification.

MR. LASSER: Either this Task Force or possibly Task Force C, which is concerned with real property, both of us are concerned with inequities in the tax law.

MR. BROKAW: Well, we are taxed under this statute and our real estate is taxed under this statute, and our real estate is defined in this statute differently than it is defined under the general tax act, and it's that situation which causes the problem that we find in its administration.

MR. LASSER: Thank you.

MR. LANG: Has the State set a maximum rate of return on invested capital in the State? Could I infer that that's what you said?

MR. BROKAW: The Public Utility Commission usually arrives at a rate of return which give a fair return on invested capital.

MR. LANG: Is that a flexible thing, a fair return on invested capital?

MR. BROKAW: Well, traditionally, it has been around 6%; now it is going higher in the recent rate cases. I wasn't involved in the rate cases for our company and Public Service is currently conducting a rate case. And what the rate increases our companies got resulted in in the way of a rate of return, I am not sure but it was in excess of 6%, I know that. But that used to be the traditional, the magic number, but the regulatory bodies are becoming more realistic so far as allowing larger rates of return. But they are not the kind of rates of return you find on invested capital with respect to other types of industry.

MR. LANG: Manufacturing runs somewhere around 10%, I believe.

MR. BROKAW: Right. We're nowhere near that.

MR. LANG: Well, the initiative for filing these applications for rate increases, does this come about when you feel you are not earning a fair return on your invested capital?

MR. BROKAW: Not only that, it has affected our ability to finance our construction program. We're growing at a fantastic rate and we have to increase plants to meet the demands on our system and you have to have earnings to go into the money market. And our position in these rate cases has been that our earnings are not what they should be so that we can get decent financing to finance the programs that we are obligated to finance, to produce the service that we're obligated to produce.

MR. LANG: I gather then that the applications for rate increases precede any expansion of your facilities. Is that right? Or will they follow?

MR. BROKAW: No. They go hand in hand and in a good many cases we reach the point where we can only go so far with the capital we have and we've got to go out and look for capital to finance these projects. And if our earnings are not high enough, we have difficulty financing and then we have to seek rate relief so that our earnings are such that investors will invest so that we can get the funds we need to finance our expandion program. The electric utilities are expanding at a fantastic rate in New Jersey because of the growth that we're experiencing. And construction costs, labor costs, have increased fantastically. And these, of course, reduce earnings and affect this whole problem.

MR. LANG: I gather then that you are satisfied with the method of taxation in New Jersey, in other words, basing it upon gross receipts?

MR. BROKAW: We'd like to see it reduced but we know that can't be.

MR. LANG: I'm talking about the method rather than the --

MR. BROKAW: The method? We're satisfied with the method.

MR. LANG: Thank you, Mr. Brokaw.

Mr. Ferrara, New Jersey Gasoline Retailers Association.

J E R R Y M. F E R R A R A: I have to apologize for not having a written statement. We had them. Unless you want to read the means of franchising to us - that's the folder I have with me for a hearing tomorrow, so tomorrow I will try to switch it around. I guess my secretary took it a little too literally that you didn't want anything about a statement.

My appearance before the Tax Policy Committee is --

MR. LANG: What is your position?

MR. FERRARA: I am Executive Director of the Gasoline Retailers. Our office is at 66 Morris Avenue, Springfield, if you need it for the record.

Our position here today is basically on the unincorporated business tax and, as an aside, on the gross receipts tax, as you had testimony here this morning.

The unincorporated business tax for us - I've heard the term "regressive" used consistently in all types of hearings but I would like to use the term of the little businessman and call it "oppressive" to the extent that it has put a tax on earnings that are not net earnings, on earnings that are taxed beyond what is reasonable. I would like to refer particularly to the gasoline industry.

The unincorporated business tax as applied to the gasoline industry results in approximately a 5% net increase on personal income because of the fact that included in gasoline is a large amount of tax on a gallon of gasoline.

The gross income of a service station is approximately a minimum of 65 to 75% obtained from the sale of gasoline. Gasoline in itself includes 11¢ tax, presently - a 10¢ tax when this unincorporated business tax went into effect - which, in essence, is about 29% of the retail price of a gallon of gasoline. This, in effect, puts a tax on tax.

We appeared before a legislative committee, back about three years ago at this particular time, opposing the tax. The whole tax was originally passed in haste. It was a tax of necessity. The Legislature in 1966 approached me and asked me what I thought of the whole unincorporated business tax and admittedly felt it was wrong but it was a necessity. Now a necessity to tax the little businessman doesn't make any sense.

Originally, it was proposed to bring in $26 million. The first year it brought in $11 million. By putting a task force out to really beat the little grocery store and little businessman over the head, we finally brought it up to approximately $18 million.

Now, for the amount of effort and the amount of heartache that it causes the little businessman, I can't see even the necessity of the unincorporated business tax. We hear, in the future, about a broad base tax. I would say if I were to approach any gentleman and tell him that we were adding 5% to his net income, he'd fly off the handle. But this, in effect, is what this did.

I made some notes here. It really boils down to, of the total amount of tax paid in, approximately, our business pays 10% of the unincorporated business tax. The gross receipts tax, as such, affects us but only on a minimal basis because the gross that's set - very few of our stations attain that, and the gross receipts, per se, allows deductions for service and labor which, again, would lower it. If we did $250,000 and deducted service and labor - very few of our stations come in under this.

Without going any further, my prepared statement for your research force will be available tomorrow. I would like to appeal to this Tax Commission to take into consideration the problem of the little man. Originally, when I testified, the question was thrown at me - what would I suggest, and when I suggested - they had the nerve to appoint a bipartisan commission, not a convention, to honestly restructure the whole tax base so that everything would fall into its proper context, whether it be corporate tax, property tax, small business tax. We're not saying that we don't want to be taxed but we think that this particular tax is unfair and I am hoping that this Commission will see that some adjustments are made on the whole tax structure but particularly on this one.

MR. LANG: Thank you, Mr. Ferrara.

MR. LASSER: If I could ask Mr. Ferrara a question. I have to admit that I always thought that the unincorporated business tax, as it relates to gasoline dealers, caused a problem because of the large volume of sales that they do and the fact that it's a gross receipts tax. Would you feel the same way about it if it wasn't a gross receipts tax but if it was a net income tax?

MR. FERRARA: I think a net income tax would be more viable and more fair, yes.

MR. LASSER: Has the unincorporated business tax resulted in many of your members incorporating in order to avoid the effect of the tax?

MR. FERRARA: That's strange, we had a lot of offers from a lot of attorneys to do it on a mass basis. We've had some go into the corporate structure. However, the small businessman is not in a position to take a real advantage of the corporate tax, whatever tax advantages he can gain by it in the form of deductible expenses. He's not in that position. But we're seriously thinking of doing it on a mass basis, yes.

MR. LASSER: The other tax that you referred to was the retail gross receipts tax.

MR. FERRARA: Yes, sir.

MR. LASSER: Are the service stations that you represent most independent stations or are they company owned stations as well?

MR. FERRARA: Well, actually, our business is what you call company owned stations. There are very few stations actually operated by a company. This, of course, is for my tomorrow's hearing - I'm enjoying this. Our stations, propertywise, are usually owned either by a private owner who, in turn, leases to a company who, in turn, leases it to a dealer-operator, and 90% of the stations in New Jersey are probably dealer-operated under that context, not company, so that he is classified - we have opinions of whether he's really an independent businessman, but he is classified as an individual, not company.

MR. LASSER: But, at any rate, you're talking about the operators of the service stations. There are quite a number of service stations that do a million dollars in volume on the major highways in the State.

MR. FERRARA: That's surprising. There are very few. You take on the Turnpike and the Parkway, and that's about where you go with a million dollars worth, if you find even those stations doing a million dollars worth of volume.

MR. LASSER: Say between $500,000 and $1 million. Do they get much benefit from the service and labor deductions on that tax, or do they turn out to pay substantially.

MR. FERRARA: Well, on the Parkway, they still pay substantially, although on the Parkway, when you get into that $500,000 category, a lot of this is road service and service, because outside the Parkway I don't think I could count five stations in the State of New Jersey that would come anywhere near a half million. In fact, in checking with the Department of Internal Revenue and the Labor Department as to the question of where we stood on labor statutes, he wanted to bet me that one in three come over $250,000 in gross on the level -- you see, the Federal Labor Department does the same thing you do in gross receipts, they allow deductions for service, etc., when they are considering the gross receipts per se.

MR. LASSER: So the retail gross receipts tax doesn't - it may be a nuisance but it doesn't really provide any difficulty for you.

MR. FERRARA: It's a nit, using that expression, versus a cockroach.

MR. LANG: Do you know what the experience is in New York where they have unincorporated business tax as well as a personal income tax? Do these dealers pay both of those taxes? Do you know?

MR. FERRARA: No. I am not so sure as to the correct answer there, although I do know everything there is considered on a net basis. We only have about five states that have unincorporated business tax in the realm that we have it, based on gross receipts.

MR. REICHE: Are there any problems associated with the enforcement of this tax, of the unincorporated business tax, as far as your industry goes?

MR. FERRARA: Yes, there was a basic problem. In fact, I think perhaps the consolidation of the auditing might have been the result of my screaming and hollering and the result of a task force from the State here. Initially, an inspector went out and it was like holding a gun to the man's head. He told them either pay or they would close them up. And a lot of people were unaware of the whole thing. In the first year we do go on sort of a tax rebellion, we refused to pay the portion of tax on tax. In fact, there is a law suit in my name pending. It has taken three years and we are just reaching the court hearing stage now. But since then, there seems to have been a little bit more sense used in going around and collecting. We've also been approached by many small businessmen who heard of our case, those who were not organized in any shape or fashion, asking us to plead their problem. Of course, to get into their details, except in a broad sense, I wouldn't have the time.

MR. LANG: Thank you, Mr. Ferrara.

MR. FERRARA: Thank you.

MR. LANG: Mr. Massarano of the New Jersey Bell Telephone Company.

J O H N   M A S S A R A N O: Good afternoon, gentlemen. My name is John Massarano and I am the General Accountant for the New Jersey Bell Telephone Company. We take pleasure in being here this afternoon. We are only involved in one particular tax that your Task Force is involved in and that's the New Jersey Public Utility Franchise Tax.

In the way of general information, I might say that in 1970 New Jersey Bell paid about $17 million in franchise tax, about $13.6 under the basic tax law and about $3.4 million under the surtax.

As an aside, the gentleman who drafted the surtax legislation at one time is now our Vice President of Public Affairs. You never know how this thing is going to come back and hit you but Bill Kirchner is the individual I am talking about. I am here as a stand-in for him today.

Our written presentation goes on to outline the mechanics under which the tax is computed, which we hope will be informative, but I would like to move on to some of the other points that we have made in here.

Franchise tax, as the name implies, is a tax upon the right to do business which, in our case, includes our right to the use of and to have access to the public streets and highways. This is true in each municipality that we operate in.

Our franchise, we recognize, imposes a responsibility on us to provide service under any and all conditions. This responsibility has come to include the rearrangement of telephone plant when necessitated by certain public projects - for instance, the rearrangement of a pole line in connection with street widening. Thus, in addition to paying a franchise tax to the municipalities, we must bear what can be termed a hidden tax, and at the rather significant cost, at times, of rearranging our plant in such circumstances. Even more importantly than this, and as distinguished from other utilities, the telephone and telegraph companies pay to the municipalities a business personal property tax on the same plant.

I won't dwell on the business personal property tax because that's not one of the taxes you're studying. But the fact of its existence brings me to one point that I think we should stress.

New Jersey Bell's personal property tax liability has almost doubled in the past five years from $21.5 million in 1965 to $38 million in 1970. Putting aside the question of whether this is a fair burden or an unfair burden, we feel that a proper review cannot be made of the role of New Jersey Bell, as a taxpayer in this State, by looking at the effect of one particular tax on the company. Rather, we think that New Jersey Bell, in its role as a corporate citizen, whose total tax assessment toward the cost of state, county and local government climbed to about $65 million in 1970 - and, without any revisions in existing tax structure, we think this may be increased by about 18% in 1971.

Now I agree this is not the place to argue as to whether this is or isn't a fair tax burden or an overtaxing for New Jersey Bell, for that matter all utilities in this State, but this increase in our tax burden over the recent years does prompt an observation concerning the true identity of the utility tax and who pays it, and that's the telephone consumer, from whom we just heard recently here.

The telephone consumer pays for these taxes. They are not directly passed on, as was pointed out, in the sense that this term is used in our present day tax legislation, but they are hidden taxes that in most cases the individual consumer cannot avoid. Stating this in another manner, in our case about 10¢ out of every dollar the customer pays for telephone service goes for state and local taxes. Our ability to pay a business personal property tax, then, is derived from the ability of our customers to pay the tax.

We, and I think I can speak for all utilities, recognize that our responsibility as corporate citizens includes the assumption of our fair share of the total tax burden at all levels of government. We repreat, however, and I believe that this point cannot be stressed too strong, that the impact of state and local taxes on the public utility community cannot be studied in one area alone, but rather must be viewed in the overall. I think this is true not just from our point of view but for the good of the consumer and the various levels of government who look to us for major sources of revenue.

One last point that maybe we can cover and that is to just talk about the difference in tax treatment between telephone companies and other utilities. As you are probably aware, in 1963 the State Tax Policy Commission recommended extensive revisions in the State's entire tax structure.

The revisions proposed included, among other things, a recommendation that the telephone companies be removed from ad valorem taxation of personal property and brought under the 7 1/2% gross receipts tax which already applied to all other utilities. We resisted the proposal at that time because of a real concern over the establishment of a workable formula which would be universally acceptable for the redistribution of such state collected taxes back to the municipalities.

Again, in 1965, a broadly-based Governor's Commission on Chapter 51 looked again at this situation at the time it was repealing the general business personal property tax provisions and replacing them with a package of new business taxes. Legislation was enacted preserving the taxation of business tangible personal property of telephone companies on the local level at real property tax rates. Here again our basic concern was with the likelihood of local dissatisfaction with any redistribution formula that might be adopted.

The statewide nature of the Company's operation involving personal property is important to us and, we believe, to the Legislature. New Jersey Bell does business in and derives revenues from almost all of the municipalities in the State. However, the source of gross revenues may bear little relationship to the location of the Company's real property.

I can illustrate this by saying that many of our switching operations, which are major investments, are centered in the large cities. Improvement and growth of these operations necessarily demand a constant expanding construction program. The municipalities housing these operation centers are well aware of the growth of these centers and have come to expect and anticipate a continuing increase in the ratables generated by this construction program. The larger cities, understandably, would view with apprehension any approach which would reduce their allotment of the total tax.

At the risk of overburdening you at this point, that is with the concern for apportionment and the problems inherent in the centrally collected taxes, just one theoretical example might be to say, in 1970 New Jersey Bell paid about one-third of its total personal property tax bill to ten municipalities of the State directly. That's about $13.2 million. And if, again just theoretically, we were to say that the franchise tax allocation factors were applied to the total personal property tax bill, for those cities, those cities alone would have lost about $7 million in revenue, which points up the apportionment problem here. And Newark and Jersey City, alone, would have lost about $4.3 million. Admittedly, that's just a theoretical approach but it illustrates the problem.

In conclusion, let me acknowledge that we have touched on only a very small segment of the overall problems associated with the formulation of tax policy. We have done so in an attempt to indicate why groups, like your Task Force, must take the broadest of viewpoints if we are indeed to find solutions to our tax problems. We are well aware that the goal of developing sound tax legislation can be impeded by exposure of the problems to the legislative process before opportunity and resources calculated to develop an adequate background of study has been provided. In that connection, New Jersey Bell will continue to hold itself available to this Task Force, and to the Tax Policy Committee, for such assistance as we can render in the area of tax research.

MR. LANG: Thank you, Mr. Massarano.

Any questions?

MR. LASSER: Mr. Massarano, the usual question we ask is, how would you fare if you were taxed under the New Jersey Corporate Franchise Tax? Have you made any calculations along those lines - a tax on net worth plus a tax on income, instead of the gross receipts tax that you pay?

MR. MASSARANO: Not definitively. I think that we feel it would be higher. And I think we are concerned about the total picture again that we're trying to emphasize here. We are paying, of course, the business personal property tax to each municipality.

MR. LASSER: Well, of course, every other manufacturing concern is paying both the corporate income tax, net worth tax, and the business personal property tax. Your guess is that probably you would be paying more under the corporate income tax.

MR. MASSARANO: Not having any exact figures, I would withhold judgment but I think it might be more.

MR. LASSER: The figure that you refer to as being your obligation under the New Jersey Business Personal Property Tax of $38 million seems like quite a large figure. The figure that I note as the total collections from that tax is $45 million in 1970.

MR. MASSARANO: I think that included real property as well.

MR. LASSER: Your $38 million figure?

MR. MASSARANO: This is personalty only.

MR. LASSER: Well, the total collections from the business personal property tax from all sources is $45 million in 1970. You have a prompter.

MR. MASSARANO: Yes, I'm hearing something here on the side.

MR. LASSER: I just question whether your $38 million figure in 1970 - whether that is solely the business personal property tax.

MR. MASSARANO: Yes, it is.

MEMBER OF AUDIENCE: Larry, I think the difference is that ours is paid directly to the municipalities, not to the State like other business personalty tax.

MR. MASSARANO: Oh, I thought we made that point, to the municipalities.

MR. LASSER: Oh, excuse me. We're talking about a different tax then.

MR. MASSARANO: Yes. Oh, I'm sorry. We pay that directly to municipalities, and that has been our position.

MR. LANG: You find no fault, then, with the present method of taxation, the use of gross receipts as a base.

MR. MASSARANO: We find no fault in the sense that there is a distribution of the taxes in municipalities. And, again, I guess we would have to say that that tax must be rated in consideration to any changes to all other taxes. That position we feel very strong about, a re-allocation problem here would be just significant to us. Generally, I would say no, we don't.

MR. LANG: You have the same rate problems as the electric and gas companies?

MR. MASSARANO: Yes. I was interested to hear that dialogue. We have the same problems, the taxes, our operating expenses and the rate base situation for us as well.

MR. LASSER: Something that I am interested in considering and that is, to the extent that we would increase taxes on any public utility, we would be increasing the cost to the consumer which would be non-deductible by the consumer and, therefore, would reduce our chances of picking up some income from the Federal Government, that is to the extent that a taxpayer pays a tax to the State of New Jersey, deducts it from the Federal tax, and, therefore, we do the Federal Government out of some revenue and bring it to the State. To the extent that we would increase any tax on public utility, rather than putting the tax directly on the consumer, we deprive the State of New Jersey of funds which are deductible by that consumer. I don't know whether that is an argument that you have heard made on behalf of a public utility but I would be interested in your examining it to see if it has any validity.

MR. MASSARANO: It has validity and I think we do make that point that it's a hidden tax. One of the elements, of course in our current rate case, in any utility's current rate case, is its operating expenses, taxes being one of them. When the rate of return on investment, including the deduction of net earnings as a result of taxes, slides, a rate application is made. The telephone consumer ultimately will absorb the cost of that expense as well as any other expense that's granted, as an increase in rate.

MR. LANG: And the contrary, to the extent that we would propose an increase in the tax on gross receipts, to the extent that that is passed on to the consumer, and further to the extent that the Federal government levies an excise tax on those charges, then, in effect, you are increasing the coffers of the Federal Government.

MR. MASSARANO: Right.

MR. LANG: All right. We have asked the New Jersey Power & Light, rather Mr. Brokaw, some of these questions that fall into your same area. I think that's all we have, Mr. Massarano. Thank you.

Mr. Arthur Fisk, Public Service Electric and Gas Company.

A R T H U R F I S K: Yes, sir. I am Arthur Fisk and I am Tax Manager of Public Service Electric and Gas Company, and I am hear on behalf of the Company to express our views relating to the existing public utility taxes incurred by our Company.

I might say now, after listening to Mr. Brokaw and to our Telephone friend, that we have parallel problems, of course, and I think Mr. Brokaw answered as I would have answered as far as an electrical company is concerned. What I will do now is repeat some of those things, which is like underscoring his views, and bring in amounts of money to show what kind of taxes our Company really pays to the State of New Jersey.

Under Revised Statutes 54:30(a)-54, also known as Chapter 5 of Public Laws of 1940 the Utility Tax Law, Public Service incurs a tax computed at the rate of 5% of the gross receipts for the privilege of exercising its franchise in the public streets, highways, roads and other public places in the State of New Jersey. In 1970, the tax incurred amounted to $29,285,884, which was apportioned back from the State to the various municipalities wherein our lines are located.

Public Service also incurs a tax at the rate of 7 1/2% on the gross receipts of this Company from its business carried on through its lines or mains throughout the State of New Jersey. This tax is known as the "Tax in Lieu of Personal Property Tax". The amount incurred in 1970 was $50,627,694, which, of course, was apportioned back to the municipalities where our facilities are located.

Prior to the passage of this law, the assessment of utility company facilities was made on a local basis and the values were forwarded to the State for tax apportionment. The resulting assessments against similar equipment varied greatly among taxing districts and, in general, chaotic conditions existed. Since the Revised Statute became effective in 1940, the law has worked smoothly and tax dollars have been apportioned equitably throughout all municipalities.

Under Chapter 42 Public Laws of 1963, a surtax is imposed on the local franchise tax amounting to 0.625% of the gross receipts of the Company. This is paid directly to the State for State purposes. There is also a surtax at the rate of 0.9375% of the gross receipts of the Company which is also payable to the State for State purposes. These surtaxes, incurred by Public Service, in 1970, amounted to $3,768,997 and $6,356,535, respectively.

As Mr. Brokaw pointed out, the law of 1963 covering the surtaxes was an emergency measure meant for a period of three years only and, since then, it has developed into a permanent tax.

The total taxes, shown above, amounted to $90,039,110, for 1970.

It is interesting to note that if Public Service were to be assessed under other existing laws, such as the Corporate Business Tax Act and the Business Machinery and Equipment Law, instead of Chapter 5, the taxes incurred during the year 1970 would have been but approximately $18 million. These monies, of course, would be paid directly to the State and apportioned back to the municipalities by a formula established by law. Under such laws, it is immediately apparent that the municipalities and the State would have received far less money than they presently do under Chapter 5 of the Laws of 1940.

Other taxes, both State and local, are incurred by Public Service. During 1970, these taxes amounted to: Real Estate Taxes - $7,275,285; Sales and Use Taxes - $1,381,222; State Unemployment Tax - $454,456; and other minor taxes - $270,536; making a grand total of $99,420,610. In addition, Public Service incurred an assessment of $684,050 for its share of the State Public Utility Commission expenses. All in all, there is over $100 million. All of this, of course, does not include any federal taxes for which Public Service was obligated for the year 1970.

It is our position that public utilities, such as Public Service, are now paying a greater share of the cost of government than other businesses and that, if possible, the existing laws should be amended to provide a more favorable tax position so that utilities may attract new businesses to our State. The taxes incurred by a utility must be reflected in the rates charged to consumers and it has been the experience of Public Service that when a business venture of major proportions is seeking a new area to develop and establish its operations, a principal concern in its determination is the availability of utility services and, of course, the rates charged for such services.

Thank you, gentlemen.

MR. LASSER: Mr. Fisk, how do utility rates compare in New Jersey to our competitor states, competitors for business and manufacturing?

MR. FISK: Well, I am not prepared to say that and I don't know.

Now, I have a couple of Associates here with me who are very much involved in these franchise and gross receipts taxes and one of them may have that information.

MR. McDONALD: We do not have any recent studies on this. We did some a few years back and we were considerably higher than other states.

MR. LASSER: Because one of the things that we hear from people who testify before this Committee is that it's more expensive to do business in New Jersey than in some other states in the United States and, naturally, we are concerned with keeping and attracting business to the State. That's why I would personally be interested in hearing how competitive or noncompetitive our utility rates are.

MR. FISK: Well, I am not prepared to say that now but I will check up on that and see that you get that information.

MR. LASSER: That would be fine.

MR. REICHE: What would be your preference as to the taxation of public utility companies? I mean, you've pointed out the total taxes which you pay but what suggestions do you have as to ways in which you would change the taxation?

MR. FISK: Well, might I say this, that we are content to live with the gross receipts and franchise taxes that now exist. And we are doing, as we think, our fair or more than fair share of taking care of the taxes that way. We don't have any suggestions.

MR. REICHE: Are there any suggestions with regard to the administration of the taxes?

MR. FISK: I might say, we're perfectly satisfied with the administration of the taxes as it is.

MR. REICHE: And you would prefer taxation under these two as opposed to, for example, corporation business tax?

MR. FISK: Well, as I pointed out, the corporation business tax would mean a lot less taxes for us but we are satisfied to continue as we are, and do our share.

MR. REICHE: I realize you made that point.

MR. LANG: Do you come under the general Federal Income Tax Laws or is there a special section of the Federal Income Tax Law that utilities come under?

MR. FISK: I can't really say.

MR. McDONALD: Public utilities, as I understand, do come under the general Federal Income Tax Law.

MR. LANG: Now the gross receipts taxes you pay to the State of New Jersey, you deduct these under the Federal return?

MR. McDONALD: Yes.

MR. LANG: So they are treated no different than a New Jersey Croporation in income tax, as an example? You still get the deduction.

MR. McDONALD: With that understanding, yes, that's right.

MR. FISK: Excuse me, gentlemen, this is Mr. John McDonald, our Assistant Attorney.

MR. LANG: Thank you.

MR. LASSER: Does Public Service Coordinated Transport also come under your jurisdiction or is that a different department?

MR. FISK: That's a different department.

MR. McDONALD: It's a subsidiary corporation.

MR. FISK: Our department has no dealings with it. They have their own separate tax department.

MR. LANG: O.K. Thank you very much, Mr. Fisk.

MR. FISK: Thank you. And I will see to it that you get that, Mr. Lasser.

MR. LASSER: That would be fine.

MR. LANG: Mr. Henry Peterson, Rockland Electric Company.

H E N R Y P E T E R S O N: My name is Henry Peterson. I am Vice President of Accounting and Services for the Rockland Electric Company.

As representative of the Rockland Electric Company, I would like to thank this Task Force for the opportunity to express our opinion on the existing laws under the present levies of the public utility tax laws.

In order to conserve the time of these hearings, it can be generally stated that Rockland Electric Company's taxes, although considerably less than those taxes paid by the Public Service Electric & Gas Company, mainly due to our size, nevertheless are comparable percentagewise.

We concur with the representative of the Public Service Electric & Gas Company that since the enactment of the 1940 tax law, the apportionment of taxes based on the assessment of the utility facilities is more equitably distributed among the municipalities.

Also based on the financial position of utilities, we find ourselves at this time, from a rate of return standpoint, - which has resulted in a rash of rate increase petitions being filed, but we believe that utilities generally are paying more than their fair share of the taxes in comparison to other businesses. A more favorable tax climate for public utilities would certainly help to keep consumer rates down and thus provide a greater incentive for business to locate within the State.

Are there any questions?

MR. LANG: Is your company a Jersey company or is it a New York company?

MR. PETERSON: It's a New Jersey company.

MR. LANG: Rockland Electric?

MR. PETERSON: Rockland Electric Company.

MR. LANG: I see. It has nothing to do with Rockland County, then?

MR. PETERSON: No, it has nothing to do with Rockland County. It's all within the State of New Jersey. It's just unfortunate that the name, Rockland Electric, and Rockland County do get associated.

MR. LANG: And the area in which you operate is in Northwest Bergen County, is that it?

MR. PETERSON: The Northern New Jersey area.

MR. LANG: I see. But all within the State of New Jersey.

MR. PETERSON: All within the State of New Jersey.

MR. LANG: I don't know where I got the idea, I guess because of the name, that you were operating in Rockland County too.

MR. ALEXANDER: Is there any comment that you would have on the question of discrimination among utilities under the present tax structure?

MR. PETERSON: No. I think that Mr. Fisk stated very well that we are paying what we feel is a greater share than we would like and it is certainly being reflected in the position we're in now, as far as rate hearings and financing are concerned. It's one of four items that have contributed to these conditions.

MR. ALEXANDER: I guess you didn't realize my question wasn't directed to that but was to any inequality of treatment as among utilities.

MR. PETERSON: As among utilities? No.

MR. ALEXANDER: As I understood the man who testified, Mr. Massarano, for the New Jersey Bell Telephone Company, he indicated that he felt that his company would be paying more were it taxed under the corporate franchise act.

MR. PETERSON: Let me say that when you said among utilities, I was thinking of electric utilities. Now, I am not cognizant of the facts, of the composition of the Telephone Company or another utility, so I would like to withdraw that statement. But among electric utilities, there is no problem as far as fairness is concerned. He indicates that their tax would go up and I have no way of agreeing or disagreeing with that.

MR. ALEXANDER: Do you agree with Mr. Brokaw's testimony on that point?

MR. PETERSON: Mr. who?

MR. ALEXANDER: Mr. Brokaw. He testified on behalf of Jersey Central Power and Light Company, and he said that they are paying more now, under the present tax system, than they would if they were to pay under the corporate franchise.

MR. PETERSON: I would say that right now we are paying considerably more under the present than we would under the corporate tax.

MR. LANG: I wonder if you - and I don't know whether you have any kind of an organization of the public utilities - might consider doing what the insurance companies have done, in other words, converting your tax burden, as a result of this gross receipts tax base, into a comparable rate if you were taxed under the corporate income tax; or, in other words, what is your comparable income tax rate under the gross receipts tax method as opposed to what it would be for those just paying it under the corporation business tax. They have something like 17% that they showed is their effective income tax rate as opposed to approximately 6% for other business corporations. Could that be done so that we could get some kind of a feeling as to just how much you are overburdened?

MR. PETERSON: I'm sure it could be done, yes. If I understand you correctly, convert our existing taxes into an effective rate under the corporate tax structure. Is that right?

MR. LANG: Yes, but not all the taxes that you are paying but just the gross receipts tax.

MR. PETERSON: Just the gross receipts, not the franchise, just the gross receipts.

MR. LANG: Those that are measured by gross receipts.

MR. PETERSON: Sure, it could be done, and we could probably work it together as an industry.

MR. LANG: I think something like that would be helpful to us and we could get sort of a feel as to the extent of this excess tax that you people feel you are paying.

MR. PETERSON: Now, do we have a target date that we could be working toward?

MR. LANG: Well, it's hard to say, but the sooner, the better. We have to move on to other things, but the sooner the better. We would appreciate that. It would be very helpful to us.

MR. PETERSON: And should we direct it to anyone in particular?

MR. LANG: Direct it to the office of the Tax Policy Commission, across the street.

MR. PETERSON: We will get together and present something to you.

MR. ALEXANDER: I am sure if you could do it within a month you will be plenty quick enough.

MR. PETERSON: There's no problem, I'm sure.

MR. LANG: Thank you very much, Mr. Peterson.

That concludes the testimony insofar as the Retail Gross Receipts Tax, Public Utility Franchise, and Gross Receipts Taxes, Railroad Franchise Tax, Railroad Property Tax and Insurance Premium Tax are concerned. And we will now move into the Sales Tax Area and we will hear from Mr. Joseph DiBella, President of Local 461 of the International Union of Electrical, Radio and Machine Workers, AFL-CIO.

J O S E P H   D i B E L L A: Mr. Chairman and Committee members, my name is Joseph DiBella. I am the President of Local 461 of the International Union of

Electrical, Radio and Machine Workers, AFL-CIO, representing over 2,200 members at the Singer Company in Elizabeth, New Jersey.

I am here to testify on the need to exempt from the sales tax on capital expenditures, companies which are in stiff competition with foreign manufacturers, since such competition has led to wide-scale reduction in employment at our plant and others, throughout the State.

In the past 20 years, employment at the Elizabeth plant has shrunk by over 6,000. The prime reason for the reduction in employment has been competition from abroad, not only from Japanese manufacturers, which have captured a substantial share of the sewing machine market, but from our own company, which has large plants in Scotland and Italy.

The fact is, that in 1969, two-thirds of all sewing machines sold in the United States were imported from abroad. The Singer Company, itself, has a plant in Germany, which manufacturers the identical model we make in Elizabeth. It is this model which keeps our 2,200 people employed. Any significant increase in the cost of producing here could tip the balance in favor of manufacture at Singer's Germany plant and result in substantial layoffs in Elizabeth and even the eventual shut-down of our facilities.

The introduction of a new generation of sewing machines at the Elizabeth plant would require heavy capital expenditures by our company. The additional cost, which would be imposed by the application of the 5% sales tax, could very well be the straw that would influence a company decision to manufacture these new models in Germany. An investment of $10 million, for example, would bring with it an additional cost of one half-million in sales taxes and might firm up a company decision to transfer operations abroad.

If it seems strange that we are concerned about additional taxes on our company, it should not be, since their decision to invest or not invest in our plant spells out jobs, our bread and butter, and the security of our families.

Latest statistics released by the State Department of Labor and Industry, report a 7.3% unemployment figure in the State of New Jersey. This means that 60,000 more workers in this State are unemployed over and above last year at this time. According to the Labor Department, New Jersey unemployment will probably get worse.

A significant percentage of those thrown out of work in our State is the result of foreign imports. For example, the Emerson Radio and TV plant in Jersey City, shut-down on June 30th, with a loss of 1,500 jobs, because the company made the decision to have its TV products imported from Taiwan. Over 1,000 people have lost employment at the General Instrument plant in East Newark for the same reason. The Westinghouse Corporation shut its plant just two years ago in Metuchen, New Jersey to the production of television sets, and now imports them, eliminating 2,000 jobs. The large RCA plant in Camden has been similarly hit. So, we see the threat of imports and competition from abroad as an extremely serious one, with which workers at the Singer-Elizabeth plant have suffered enough!

Our proposal, therefore, is that any company which demonstrates that its business is in competition with foreign imports, be exempt from the 5% sales tax on capital expenditures. This proposal, we feel, will address itself to the most serious problem our economy faces today, that is, the loss jobs due to the avalanche of imports, which have hit the United States.

On behalf of our 2,200 members and the thousands of Singer employees who have been laid off due to imports, we urge that this exemption be made.

MR. REICHE: I assume you are referring to machinery and equipment.

MR. DiBELLA: Machinery and equipment, and I might also add that the Singer Company has been in business for almost a hundred years and that some of the present factory is very old, and I would also ask that the demolition of a building, which could be replaced by a new building, in Elizabethport might also be exempt from the sales tax.

MR. LANG: Well, you are asking for a much broader exemption than we would conceive of under the machinery and equipment provision. In other words, according to your statement, if it is proven that a business is in competition with foreign imports, and I can see a lot of problems in that area, and you are proposing, Mr. DiBella, that this company be exempt from sales tax on any capital expenditures, no matter what they may be, - of course the sales tax only applies to tangible personal property, so it would not apply to building, and that type of thing. But it is a little broader than we would conceive under the regular machinery and equipment exemption.

MR. DiBELLA: Yes. It must be understood that Singer Company, some years ago, built some plants in South Carolina, simply because the climate with respect to taxes was much more favorable than that here in New Jersey. And it could very well be considered that if the company had to build a new factory or an addition to the factory that they presently have, the 5% sales tax that would be applied for building might influence the company to put this factory up in another state or another country. This is what I am implying.

MR. LASSER: Mr. DiBella, we are both concerned with the loss of industry in New Jersey. Some people say that taxes are an important consideration and some people even say that labor is. The problem is probably not one that can be traced directly to either one of those subjects but is there any way, other than by dealing with the tax problem, that anything can be done to avoid the loss of industry in New Jersey. We are aware of the loss of electronic plants because of those companies going to Mexico and Hong Kong and Taiwan and Korea. Taxes really won't bring them back, I don't think. Is there any other way that has been proposed to keep them here?

MR. DiBELLA: Well, of course, my primary concern is to keep any industry here and to fight it with any means possible when we are faced with foreign imports. But I can't speak for the company, and I don't know what their position would be, but as an alternative I might suggest, rather than a front-load tax that tax could be applied at a later date if and when this machinery begins to develop the product that it was bought to build and it starts making money. It could be assumed now that if the company planned to invest something like $10 million in capital expenditures throughout the State that this would mean a half million dollars that the company might be able to use better to purchase additional machinery and to add more jobs; then at a later date, when the machinery is productive and does produce, at that time the tax may be applicable. This is only a suggestion. I don't know the company's feeling on this but it's merely an alternative.

MR. LANG: You, of course, are asking for just manufacturing exemption and, as Mr. Lasser said, we are interested, I must admit very seriously, in retaining manufacturing business in this State and, at the same time, attracting new business, we would hope. At the same time it isn't just the tax problem. We found that out in our hearings. There are many other things that contribute to the problem of the State in retaining manufacturing industry. And I assume that the labor people are willing to do their part too in this common project we have of retaining and attracting business in our State. Is that right, Mr. DiBella?

MR. DiBELLA: That is correct. With respect to my Local, we have done almost everything possible to make sure that the Singer Company remains in E-Port because it is the last sewing machine plant in the United States. Years back, we did lose quite a bit of that plant to foreign imports. As a matter of fact, only recently, not too many years back, the Singer Company was one of the largest domestic sewing machine needle manufacturer in the Country and we lost that industry to England because of the favorable tax structure in that Country. And this was the motivating reason for moving that particular part of the industry that we had in E-Port to Scotland. And almost every model machine that we now manufacture, a like model is manufactured in a foreign country. So that if the Company feels that there is an unfavorable climate, as far as cost is concern, it would be no problem for them to close the door and have the item imported from the factory that they are presently building in a foreign country.

We are concerned about saving what we have and adding on to what we have. But it must be understood that we can only do this through a cost reduction program. And anytime taxes are raised, it raises the cost of the item and we no longer remain competitive. This is our main and primary concern - we don't want to lose what we have, we want to keep it here.

MR. LANG: Thank you very much, Mr. DiBella.

MR. DiBELLA: Thank you, gentlemen.

MR. LANG: Mr. Gerald Hall, who will speak for the New Jersey State Chamber of Commerce as well as the New Jersey Industrial Developers Association.

G E R A L D D. H A L L: Mr. Chairman and members of the Committee. My name is Gerald D. Hall. I appear here today in my capacity as Director of Governmental and Economic Research for the New Jersey State Chamber of Commerce, headquartered in Newark.

For the record today, may I state briefly that the Chamber is a membership organization of business and industrial concerns throughout New Jersey. At the time of its founding back in 1911, the Chamber incorporated within its organization the former Bureau of State Research. Through this incorporation, it is possible to say that our organization's interest in the patterns of governmental revenues and expenditures in New Jersey literally spans all of this century.

Among the Chamber's many committees of businessmen (which help to evolve its policy determinations) there are two which are directly concerned with the matters I am about to discuss -- our Industrial Development Committee and our Cost of Government Committee. The latter Committee, I might add, had always directed its full attention to taxation and spending by government at all three levels in New Jersey while the former Committee has long played a leading role in the premotion of New Jersey's orderly and beneficial economic development.

And now, for the Chamber I shall comment upon four separate but related matters falling within the purview of Task Force "D" and the purpose of today's hearing concerning the Sales and Use Tax:

Before so saying, though, I would like to ad-lib here that it heartened me greatly to hear the immediate previous speaker, representing apparently organized labor, urge specific treatment of problems via the tax route. We have urged for many years that labor recognize the fact that what might prove harmful oftentimes to business also affected labor. And we cannot agree with them more in this particular case.

I. THE EXEMPTION OF BUSINESS MACHINERY AND EQUIPMENT

Anyone attempting to assay New Jersey's Sales and Use Tax law will quickly become concerned with the very adverse impact upon our State's economy that has come about as the inevitable result of the Legislature's action on March 1, 1970, eliminating the former exemption of machinery and equipment used in production under the sales tax law.

New Jersey has experienced ill effects that are both immediate and long term in nature. We know, for example, of situations entailing the purchase of millions of dollars worth of new equipment to perform production contracts in New Jersey -- contracts entered just prior to the Legislature's repeal of the exemption. But the companies concerned, faced with the added 5% cost if the machinery were brought to New Jersey, shifted the sites for production to other states to avoid this added tax cost. With the shift, of course, went the jobs that go with the machinery. And because it would be uneconomical to move the machinery again, it is obvious that such investments and jobs are lost irretrievably to New Jersey.

We know, too, of many instances of like economic impact wherein businessmen, noting the removal of the machinery and equipment exemption, have refused to locate new manufacturing facilities in New Jersey; have dropped plans for expansion of existing manufacturing facilities here, or have refused to modernize their New Jersey productive capacity. In each of these cases the effect is the same: Badly needed jobs are not created; the economy suffers, and the tax base falls behind ever-increasing demands placed upon it for public service.

Only yesterday we checked with one of America's largest manufacturers which suspended planning last year for a proposed New Jersey investment running to tens of millions of dollars. Their answer is still: "Unless the machinery exemption is soon restored, the investment will go into a more 'friendly' state"!.

The most unfortunate aspect of removing this exemption is that it represents another manifestation of the anti-capital bias that appears to be a central philosophy of the New Jersey business tax structure. In addition to the well-known and documented heavy burden of the State's generally high real property taxes, New Jersey business caiptal labors under (1) the net-worth feature of the corporation business tax, (2) the tax on business personal property, and now, (3) the tax on the purchase of production equipment, all burdening the same capital.

Our neighboring Middle-Atlantic region states -- with whom we are in the most direct competition for business investment and the jobs and economic activity created by such investment -- do not tax business capital in the intensive manner that New Jersey does. These competitors do not generally tax net worth (or at least they give special treatment to manufacturing activities); for the most part they long ago gave up the taxation of tangible business personal property; they exempt productive machinery from their sales taxes; and they frequently have property taxes less burdensome than New Jersey's. Our pronounced bias against capital is reflected, in part, in the secular decline of manufacturing as a major component of the New Jersey economy. This picture is in contrast to growth rates of manufacturing activity and employment in many other states. We have just been fortunate that other factors have been operative in New Jersey to help keep our economy abreast of the burgeoning population and its economic requirements.

However, if the expansion and long-term health and stability of New Jersey's economy is to be given adequate assurance, the anti-capital bias of the tax structure, which militates against manufacturing investment in the State, must be reduced. A major first step in this direction should be restoration of the sales tax exemption on machinery and equipment.

Modern competitive conditions, wrought by manufacturers and businesses within other states (and, increasingly, from other nations as well), require that New Jersey-based industry constantly keep abreast -- or ahead -- of rapidly changing technology and to search constantly for means toward more efficient operations. The company that fails to do so inevitably will fail to meet competition both here and abroad. Yet a tax upon investment, such as the machinery sales tax, inhibits New Jersey companies from making such necessary investments or it serves to encourage them to locate their investments -- and jobs -- elsewhere.

If geographic or market considerations are important to a company, consider how attractive neighboring Delaware can be, lacking as it does a sales tax on either production equipment or purchases of any other business needs -- all of which are taxed in New Jersey. And in New York, not only is production machinery exempt of sales tax, but the state also makes available various investment incentives including a credit against corporation tax. And in neighboring Pennsylvania, long-standing investment incentives continue in effect. Within the past few weeks, moreover, a proposal there to discontinue the production equipment sales tax exemption was rejected -- an expression of official recognition of the essentiality of the machinery exemption to the long-term economic health of the Commonwealth. Obviously, the Keystone State has learned well from its bitter tax lessons of the 30's and 40's! Incidentally, a similar proposal to withdraw the machinery exemption in Massachusetts was very recently turned down out of concern over the economic consequences of such a move.

New Jersey, therefore, can hardly afford to continue to penalize its manufacturing and business concerns through a tax policy which serves to inflate the costs of their goods and thereby prevents their competing successfully in the world's marketplaces.

Given very hard competitive pressures from abroad plus the rising costs of all domestic production ingredients -- most particularly labor costs -- New Jersey's manufacturing concerns must constantly and urgently seek offsetting productivity improvements. With the current trends toward a decreasing supply of capital yet increasing production costs, decisions of where or how to invest in new productive facilities are made only after the most careful and thorough analysis of all of the alternatives.

Modern productive improvements and automation make it almost obligatory that plants be laid out on efficient, straight-through, in-line manufacturing concepts and that the most modern, sophisticated automatic machinery be employed throughout. Despite the many modern manufacturing plants one sees about our State, the fact remains that a large share of the State's manufacturing capacity is elderly and, more often than not, housed in antiquated, multi-story plants that do not lend themselves to conversion to modern manufacturing concepts except at prohibitive cost. As a result, modernization can often be met only by a wholly new plant in a wholly new location. New Jersey's imposition of the 5% sales tax on much of such investments, plus our other capital taxes, plus all of the other "disincentives" found here such as our high labor and construction costs, can and do -- influence many a company's decision to locate elsewhere. The true cost of this tax, therefore, must be measured in terms of the economic stimulus lost with the loss of these jobs to other states.

II. THE ADVERTISING MATERIALS AND SERVICES EXEMPTION

We must also express to the Committee our hope that the former sales tax exemption for certain advertising services and materials will be re-instated. This tax is basically wrong. It applies directly and adversely to the very efforts to solicit sales and thereby to increase the amount of merchandise sold which is taxable under the sales tax. It is, in other words, a counter-productive tax.

It is clearly discriminatory, moreover, to place a tax upon catalogs, display material and direct mail advertising, when other sales media are exempted. The move to tax such materials has proven to be a heavy blow to what had been a very rapidly-growing industry in New Jersey -- advertising, printing and allied distribution activities. Inasmuch as such advertising materials are taxed in New York, for instance, only to the extent that they are used in that state (in contrast to the New Jersey practice) it is all too easy to make such purchases there and mail the resulting advertising materials directly from there -- with a corresponding rather substantial loss to New Jersey's economy.

III. EXEMPTION FOR POLLUTION CONTROLS EQUIPMENT

We urge this Committee to espouse the concept of a sales tax exemption (or refund) for equipment or facilities installed and approved by the Department of Environmental Protection as necessary solely for the control of air or water pollution.

Our Chamber has long supported legislation to this end as being at once: (1) an incentive to business to invest in (and to bear the subsequent costs of up-keep) of such facilities in furtherance of the public policy of protecting the environment and (2) recognition of the very substantial costs to business of purchasing, operating and servicing such equipment as required by that public policy. Most people simply do not realize the full extent of the costs involved. Often they also include resulting uneconomic higher processing and manufacturing costs -- expenses that are not borne by competitors in states where pollution control standards are far lower than those being applied in New Jersey.

Such a pollution equipment exemption (already granted by 21 other states) would redress, at least to a degree, this difficult competitive situation. We have urged before, and we repeat again here, however, that any such sales tax exemption should follow the same format of certification by the environmental authorities as will be found under the present property tax exemption. This will assure that public policy is being adequately served in all respects.

IV. COMPENSATION FOR VENDORS

In connection with Item #3 of the agenda proposed for today's hearing, we would like to repeat our oft-stated recommendation for granting either a discount or compensation for vendors in at least partial recognition of the very substantial sales tax collection costs that they have been saddled with by the State.

With the inception of the sales tax, most vendors were forced to make substantial investments in the purchase of new or additional cash registers and allied accounting systems. Additionally, they were forced to retrain their personnel to handle the collection of the tax for the State.

Moreover, vendors in New Jersey are liable for the tax on a gross taxable sales (less returns) basis. Because of the complexities of the New Jersey tax -- its many ill-defined areas of taxable versus exempt items, and the sheer magnitude of the problem of hiring and training employees to grapple with the interpretive technicalities involved in collecting the tax -- these factors cost New Jersey retailers hundreds of thousands of dollars in additional tax payments each year because their employees often cannot make, at the brief moment of the sale, a completely accurate determination of the tax they should be collecting but which he has to pay even if it isn't collected.

In view of these very considerable burdens, we urge that a provision be made for payment of a fee to retailers that will partially reimburse them for the collection and accounting services they are now providing the State. There is ample precedent for this in that at least twenty-two states already have such provisions in their sales tax laws. Under New Jersey's current system of no reimbursements, retailers are, in effect, paying an extra tax on sales in addition to the mercantile gross receipts tax -- neither of which is borne by any other type of business in the State.

MR. LANG: Thank you, Mr. Hall.

MR. ALEXANDER: Mr. Hall, you mentioned the "anti-capital bias" of New Jersey taxes. If we were to eliminate the business personalty tax and reduce realty taxes and the net worth tax, that would have a significant impact on the anti-capital bias, wouldn't it?

MR. HALL: If you would eliminate it, it would take care of it, yes.

MR. LASSER: Mr. Hall, I was interested in the advertising materials and services exemption problem. There obviously appear to be inequities in that area. Would a solution to the inequities be to impose the tax on those advertising materials and services which are presently exempt? Could the inequity be eliminated, in other words, by taxing those people who are not now taxed, in addition to taxing the catalogs and display material and direct mail advertising?

MR. HALL: That removes the inequities insofar as printers and preparers of this and purchasers, of course, of this type of material. It may be, as we have urged upon the tax authorities, that they follow the New York pattern, if they're going to continue the tax, if it's unacceptable to remove the tax now placed on these people, that it apply to those purchases used within New Jersey - parallel the New York system - and that anything mailed outside the State be non-taxed.

MR. LASSER: The problem that I see with it is that it's kind of a mixed bag of services and goods.

MR. HALL: Very much so. Very ill-defined, apparently, too.

MR. LASSER: That the general theory of the sales tax, we're taxing the sale of tangible personal property.

Generally, it's not a tax on services. But when you get into this advertising area, you're mixing up services and goods and either you're going to have to exempt all of them or you are going to have to tax all of them. I don't know whether there's any better definition of the problem than just the fact that we have this mixed bag.

MR. HALL: I think it was the result of a hasty political decision in search of new revenue and this was picked without too much thought of the administrative problems or the economic consequences of it.

MR. LASSER: In connection with the exemption of pollution controls equipment, if that exemption were not granted, would there be any effect on the installation of pollution controls?

MR. HALL: None, I don't think, where a company will put it into effect because by and large those that are doing so are being urged by the environmental authorities to do so. There's an element of timing involved here and so on. That's why we say it is a two barrel thing that we're urging: one, to urge more voluntary compliance with public policy in this regard; secondly, a public recognition that these firms, in furtherance of that public policy, are being either voluntarily or forced to assume a very considerable additional cost burden.

MR. LASSER: Generally, I think you would probably agree with this, that exemptions are to be avoided in taxing statutes. In this case, would the failure to grant an exemption for pollution equipment put this State at a competitive disadvantage, a similar competitive disadvantage to the competitive disadvantage mentioned in the failure to exempt machinery and equipment?

MR. HALL: Very much so. Very much so, because we have every conviction that the enforcement activities in New Jersey, the laws and the administration thereof, are far more stringent than found in most any of the other states. And to the extent that any states within the general economic region, let's say, in terms of competitiveness, are more lax in this regard, a major plant faced with a multimillion dollar cost of equipment for control only, or modification of equipment to allow control, or very, very substantial additional costs of operation because they have to alter the way they do things, because of control requirements, might very well wander off to West Virginia or someplace and put it where nobody is going to bother them in this regard.

MR.LANG: The pollution control equipment would not be covered if the Task Force gave consideration to recommending restoration of machinery and equipment exemption, I gather.

MR. HALL: We had a very distinct problem with that which we sought to resolve by the introduction of legislation to grant this exemption. We found that in many cases, of course, at that time production machinery and equipment was exempt. Then came the necessity to make modifications or installations of new equipment, and so on, parallel, that were not for production or might not be deemed for production by the tax authorities but only for pollution control and, therefore, that was taxable. And one facet of our effort in this regard was to straighten out this confusing area which we found ourselves in.

MR. LANG: So then there would be two exemptions required. If the machinery and equipment exemption was reinstated, there would also have to be one to provide for exemption of pollution controls.

MR. HALL: We would hope there would be the parallel exemption for pollution equipment.

MR. LANG: With regard to the vendor's compensation, does the Chamber recommend any amount or rate that might be considered reasonable?

MR. HALL: We're not prepared to suggest a figure. It would appear from what is the practice in the other states that 2 or 3% is the common one. It runs from 1 to 5%.

MR. LANG: The trouble I find with using a percentage for either a discount or a vendor's compensation, or whatever you might want to call it, is that as soon as the rate is increased then automatically the collector's allowance is increased even though he might not incur one cent more in collection costs. So it seems to me if a collection allowance was proposed that there would have to be some compensation for that type of happening. In other words, as an example, if there is a 3% sales tax, let's say, and a 2% collection allowance and that's raised to 4%, the rate, and 2% collection allowance remains the same, then the collector gets an automatic increase.

MR. HALL: Right. I know exactly what you're referring to. As you perhaps know, the State already gives, in the area of the cigarette tax, the wholesalers who affix the stamps a percentage for their service in doing so. This is not the case in liquor or gasoline but in the cigarette area. And each time that the rate of tax is changed, that percentage of retention is adjusted by the Legislature.

MR. LANG: Oh, I see. Is that by law?

MR. HALL: Yes. It's done, generally, in the same statute as they raise the price per pack.

MR. LANG: Then the retailers wouldn't object to this type of thing, I don't imagine.

MR. HALL: I don't think they would.

MR. REICHE: You've spoken about the generally heavy burden which is placed upon industry in the State of New Jersey, and you've made specific reference to the two components of the corporation business tax, business personal property, the exemption that we're discussing right now, which is not currently in effect on machinery and equipment. As you examine the overall climate for the location of industry or the continuance, as the case might be, of industry in New Jersey, what do you consider to be the most, shall we say, significant pieces of that puzzle in terms of their burdensome nature upon industry? In short, which of those are the most onerous?

MR. HALL: I think, at this point in time, speaking in terms of attracting or retaining industry or modernization of industry, and so on, that the machinery and equipment sales tax exemption probably is the important one at this time. It's not necessarily, in terms of dollars of revenue to the State; I think that the net worth tax is somewhat larger than that. We've lived with the net worth tax for a long time. There are a number of segments of business that feel that it would be desirable to place the net worth and net income taxes on an alternative basis. That's another subject for another time.

MR. LANG: There are sort of mixed opinions, as you know, on the part of business as to whether on not there should be a compensating increase in the corporation business tax rate if there is the enactment of exemption for machinery and equipment sales tax. There are some businesses that say, yes, they can live with this type of thing, and others say, no, they couldn't. So I gather the Chamber did not take a position on this.

MR. HALL: You're very right. Actually, that question cuts in three different directions. You have the business which is not only maybe making new investment but is constantly upgrading its investment and, therefore, they are repeatedly paying a sales tax year in and year out, a large figure, on their investment. They, of course, depending upon their profitability, would have to weigh this. There are companies who do not necessarily too often make this investment or it's not a great amount but their profitability may be considerable so that they would have their own views on that. And then there is a large group that has never enjoyed the machinery and equipment exemption, service people, retailers, and so on, and they look askance at any effort to raise the corporation tax in that regard because they do pay that tax. So that you find the three camps.

Mr. Lang, I would like at this point, off the top of my head, now that we're discussing the facets of the thing, to suggest, of course, that your Committee hopefully will look at all aspects of the total business picture here. And I don't know that part of your charge is involved in what I was to say but you know that a major component of the costs of business in New Jersey, of course, is the statutory benefit programs which are tax-like in character in many respects. And one would hope that in the course of your deliberations that you would give some consideration to these. I don't think it was intended at the time that you do so but they are a major ingredient along with the tax picture in the developmental aspects of the entire State.

MR. LANG: I think that's a good suggestion.

May I suggest that the statement of Mr. Robert H. Franklin of the New Jersey Industrial Development Association be made a part of the official record of the hearing, rather than have you read it?

MR. HALL: I am all for that. I would like to take a second to point out that the New Jersey Industrial Development Association, commonly called "NJIDA", is made up of the representatives of the water, electric, gas, and telephone utilities, the banks, the railroads, real estate industrial developers, and the county and municipal industrial development commissions, planners. This is an active group that has worked for many years toward economic development of the State and their concern is grave as to the aspects particularly of the machinery and equipment exemption, and they are in a peculiar position of dealing with the people. They go out and beat the bushes to get people to come to New Jersey and they are well aware of those facets of the tax picture here that are troublesome. So I think it gives considerable weight to their statement which will be put in the record, if you please.

MR. LANG: Thank you, Mr. Hall.

Is there a Mr. Edward Burke in the Chamber? (No response)

A statement received from the Union Paving Company of Pennsauken, New Jersey, will be made a part of the official record of this third session of the Sales and Use Tax Hearings of Task Force D.

The hearing is now adjourned.

(Hearing concluded)

STATEMENT OF
NEW JERSEY RETAIL MERCHANTS ASSOCIATION
BEFORE
TASK FORCE D, NEW JERSEY TAX POLICY COMMITTEE
MARCH 31, 1971

Mr. Chairman, members of Task Force D, I am Charles T. DeFoe, Executive Vice President, New Jersey Retail Merchants Association. The NJRMA is a state wide trade association representing more than twenty two hundred (2200) small and large retail establishments in New Jersey. I appreciate this opportunity to present the views of our members on the Retail Gross Receipts Tax, a tax, the retailers of New Jersey consider to be the most discriminatory of all New Jersey taxes.

The Retail Gross Receipts Tax was enacted by the 1966 Legislature as a part of the tax package which revised the existing business personal property taxes, as provided for under Chapter 51 of the Laws of 1960. Although there were several existing tax in-equities that were eliminated by the tax revisions enacted by the 1966 Legislature, this same tax package created, what I am sure is the most discriminatory tax to ever exist in New Jersey. The Retail Gross Receipts Tax imposes upon the retailers of New Jersey, a tax, that is both discriminatory within the retail industry, and discriminatory to all retailers when related to the taxes imposed on all other business and industry in New Jersey.

New Jersey retailers pay all of the various taxes imposed upon New Jersey businesses, but then, they are singled out to pay a special additional tax, the Retail Gross Receipts Tax. It could be said, that retailers pay a tax on the spare tire, as well as the four wheels on the ground; while all other New Jersey businesses are taxed only for the wheels on the ground. This added burden of the Retail Gross Receipts Tax is most discriminatory when compared to the tax burden of other New Jersey businesses, with all other states, and within retailing itself. The tax in no way reflects the gross or net profit differences between the various types of retail business; nor is it in any way based upon the capacity of the retailer to pay the tax. A store operating without a profit is taxed on the same basis as a store with a normal profit.

When compared with other states that impose a gross receipts tax the in-equities of New Jersey taxes upon retailers is clearly demonstrated.

States Imposing a Gross Receipts Tax

Alaska (1)	On all forms of business receipts
Delaware (1)	Merchants and Manufacturers
Mississippi	On all wholesale purchases
Washington (2)	On all business

(1) No state wide sales tax
(2) No corporate income tax

Indiana and West Virginia have Gross Receipts Taxes, however in both states, retailers pay either that tax or corporate income taxes, which ever is higher; retailers pay both taxes in New Jersey. Connecticut imposes a gross receipts tax on unincorporated business in lieu of corporate income taxes.

Our complaint is especially urgent since we have already been burdened with the task of being the unpaid collector of the New Jersey Sales and Use Tax. This very substantial contribution to the State might well be termed another form of taxation. Authoritative studies on the cost to the retailers of collecting the Sales Tax have shown that such costs involve from 5% to more than 20% of the tax collected. These costs are incurred because of the required changes in cash register equipment, record keeping requirements, sales person training, record auditing etc. Since New Jersey has one of the most complicated and extensive system of tax exemptions, we unquestionably rank among the highest in collection costs to the retailer, of any state. Twenty two (22) other states have recognized this cost by permitting the retailer, as a tax collector, to retain from 1% to 3% of the tax collected. New Jersey has ordained that the retailer absorb the full cost of this collection. Based upon the authoritative studies conducted on sales tax collection costs for retailers, New Jersey retailers are contributing more than $15 million dollars annually in serving as the collector of the State's Sales Tax.

The New Jersey retailers recognize the many demands that are placed upon government for providing a great variety of services for our citizens, and we further recognize that various forms of taxes must be imposed to finance these services. We do not appear here today to question any of the basic concepts of taxes or spending by any level of government. The retailer pays his fair share of all local and state taxes. If he is incorporated he pays, as the other incorporated business in the state, his share of the Corporate Income Tax; and if he is an un-incorporated business, he pays the Un-incorporated Business Tax, like all other un-incorporated business. The retailer also pays, as does other businesses within New Jersey, the Machinery and Equipment Tax. As a matter of fact, the retailer pays a much greater percentage of this tax than was ever projected he would by the 1966 Governor's Committee on Local Property Taxation. Retailers are paying their just share of taxes and we can not see any justification for the Retail Gross Receipts Tax ever having been enacted, what less, why it should not be immediately repealed.

New Jersey retailers have accepted their responsibility to pay their share of the taxes needed by New Jersey governments, but object when they are singled out to pay more than their fair share. The Retail Gross Receipts Tax requires more from retailing than its fair share of the tax responsibility. The retailers of New Jersey ask your consideration of these views and solicit your support in securing the early repeal of this un-fair and discriminatory tax.

Mr. Chairman, we appreciate your time and interest and for this opportunity to present these views.

Statement of Augustus Nasmith on behalf of

ASSOCIATED RAILROADS OF NEW JERSEY

to
Task Force D (Revenue Resources and Tax Inequities)
of the
New Jersey Tax Policy Committee
at a Public Hearing

Assembly Chambers, State House
Trenton, New Jersey

March 31, 1971

We desire to submit to this Committee a brief review of railroad taxation---a subject which has been examined three times by the Commission on State Tax Policy in the following reports:

Third Report (1948) entitled

"The Taxation of New Jersey Railroads"

Tenth Report (1963) entitled

"Increased State Aid to Public Schools and Distribution of the Cost of Expanding Public Services." pp. 111-117

Eleventh Report (1965) entitled

"Railroad Taxation in New Jersey---The End of an Era."

A. RAILROAD FRANCHISE TAX

The railroad franchise tax originated in 1941, and its operation from 1941 through 1947 was evaluated in the Third Report of the Commission on State Tax Policy (pp. 41-47) which recommended that it be changed to provide: "A franchise (income) tax measured by net railway operating income allocated to New Jersey according to all track miles at the rate of 10 per cent."

This was done in 1948 (Ch. 40, L. 1948) and the present Railroad Franchise Tax exists in that same basic form. R. S. 54:29A-13. The Eleventh Report (1965) of the Commission on State Tax Policy did not recommend any substantial change in the tax nor the rate.

Since the franchise tax was designed to tax the railroads in accord with their capacity to pay---and their financial condition has been critical over the past several years---this tax has not recently been a significant factor in overall State revenue.

We respond to the three questions in the Guidelines for this hearing as follows:

1. Although it is not a significant revenue source, we do not ask that the Railroad Franchise Tax be eliminated, because it has been a fair tax, both in principle and in operation.

2. There is no need for modification of existing exemptions.

3. We would prefer the rate of tax be reduced to 5%.

B. RAILROAD PROPERTY TAX

The Third Report recommended changes in the existing 1941 Railroad Tax Act (summarized at page 58 of the Eleventh Report) designed to provide total railroad tax revenues of $16 million, as opposed to the existing (1941-1947) level of $18.775 million. These recommendations were enacted.

In discussing the Future Tax Burden of the Railroads, the Commission stated (page 24):

> "...that the economic condition of the railroads as a group, or at least those railroads which serve New Jersey, and the comparative tax burden imposed in other states, would normally warrant a reduction in the railroad tax imposed in this State. A reduction connot be recommended, however, at a time when all other property owners are being required to increase their contributions to the cost of government, and at a time when the State is faced with the need for additional new revenue. By the same token it is a much better time, when the revenue structure is being revised, to take advantage of the opportunity to adjust State finances to declining railroad tax revenues."

The Tenth Report found it quite clear that there had been no improvement in the economic status of the railroads since 1948 (p. 113). The Commission recommended as follows (p. 117):

> "As a first step toward a rational solution of the railroad tax problem the Commission recommends that all railroad taxes be for State use and that the State provide replacement revenue for the municipalities to save them harmless as a result of this change in tax policy. The replacement revenue could be derived partially from the continued taxation of railroads and partially from any new tax source which the State may adopt."

The Commission did not have the time to resolve the adjustment problems involved in this change in tax policy and stated that if the recommendations were acceptable in principle they could be remanded to it for further study and report. The Legislature did so by JR - 7, approved June 6, 1963.

The Eleventh Report was in two parts. An interim report of May 18, 1964 was issued because the Commission felt immediate tax relief was necessary and desirable; it recommended reduction of $2.5 million by elimination of the Class I tax on main stem (right-of-way) and the Class III tax on tangible personal property (primarily rolling stock). These recommendations were enacted on December 29, 1964, but the effective date was postponed until January 1, 1966.

The Commission's final report submitted in December, 1965 recommended that all Class II property (all real property in railroad use other than main stem) in passenger service be exempt from taxation; and that remaining Class II railroad property---after a transition period at a higher level---be taxed at a flat rate to reduce the total railroad property tax burden to $8 million.

These recommendations were again implemented and the total railroad property tax burden did reduce to $8 million in 1968.

In discussing the Need for Tax Reduction, the Commission considered the aggregate annual net deficits and working capital deficits of New Jersey railroads, set forth in Tables 5 and 6 on page 12.

The largest net deficit shown was ($63,782,764.) for 1961; largest working capital deficit ($64,275,539.) for 1963. Unfortunately, the comparable figures for the year 1969 are ($114,891,393) and ($150,819,518), as shown on Appendix A, attached.

Since publication of the Eleventh Report, the Central Railroad Company of New Jersey went into reorganization under the Bankruptcy Act on March 22, 1967; and Penn Central and Lehigh Valley did so in the summer of 1970. It is again quite clear that the economic status of the railroads has declined.

Conclusion

The Commission on State Tax Policy in its summary of the Eleventh Report (pp. vii and viii) stated:

> "2. To achieve such tax reform, it is desirable at this time that the State take over the taxation of Class II railroad property. <u>This will make possible the adjustment of the Class II tax level in the future as circumstances may require without adversely affecting individual municipalities."</u> (emphasis supplied)

We answer the Guideline questions as follows:

1. We concede it is necessary for the State to continue the Railroad Property Tax as a revenue source.

2. No modification of exemptions in this tax are appropriate at the present time.

3. As stated in our Conclusion, above, we believe that present circumstances warrant a reduction from the present tax rate of $4.75 for each $100. of true value (R.S. 54:29A-7) to a rate of $4.50.

C. SALES TAX INEQUITIES

Under the Sales and Use Tax we propose two amendments:

1. Railroad track materials, communication, signal and power equipment should be exempt, in addition to the present exemption for sales of locomotives and rolling stock (R. S. 54:32B-8 (bb).

This would afford railroads the same exemption as gas, electric and telephone utilities have for machinery, apparatus or equipment and cables for use in transmission or distribution of their services (R.S. 54:32B-8 (m).

2. Railroads should have the same exemption for repairs to locomotives and rolling stock as is afforded for repairs to trucks and trailers under Sec. 3 (b) 2 (iii).

Respectfully submitted,

Augustus Nasmith

Augustus Nasmith

Appendix A

System Net Income or Deficit* 1969

Jersey Central System		($ 9,042,400)
Erie Lackawanna (Includes New Jersey and New York)		1,258,859
Lehigh and Hudson		(96,928)
Lehigh Valley		(7,539,684)
Penn Central Company (Former Pennsylvania Railroad Company and New York Central)		(91,631,726)
Penn-Reading		(4,526,679)
Reading		(3,312,835)
	Total	($114,891,393)

* ( ) Denotes deficit.

Working Capital* 1969

Jersey Central		($ 6,665.527)
Erie Lackawanna (Includes New Jersey and New York)		(13,957,113)
Lehigh and Hudson		(21,939)
Lehigh Valley		(2,816,280)
Penn Central Company (Former Pennsylvania Railroad Company and New York Central)		(111,698,340)
Penn-Reading		(3,795,378)
Reading		(11,864,941)
	Total	($150,819,518)

* Includes material and supplies and debt due within one year

( ) Denotes deficit.

STATEMENT OF

NEW JERSEY BELL TELEPHONE COMPANY

BEFORE

TASK FORCE D OF THE NEW JERSEY TAX POLICY COMMITTEE

Mr. Chairman and members of Task Force D, I am John Massarano, General Accountant of the New Jersey Bell Telephone Company. We appreciate this opportunity to present a very brief statement concerning the New Jersey Public Utility Franchise Tax -- the only one of those taxes with which this Task Force is concerned that has application to my Company.

For the benefit of those who may not be familiar with it, let me describe briefly the franchise tax and its operation with respect to our situation.

New Jersey Bell Telephone Company paid about $17 million in State Franchise taxes for the year 1970 ..... $13.6 million under the basic tax and about $3.4 million more under the surtax.

Essentially, the Franchise Tax is based on the previous year's intrastate gross receipts related to the ......

"business over, on, in, through or from the lines of the company which are located in or over any public street, highway road or other public place."

Taxable gross receipts are determined by applying (a) the ratio of telephone lines (in miles) along public highways, etc., to total length of lines of the Company (this ratio was 79.86% in 1970) to (b) the difference obtained by subtracting non-taxable revenues (principally interstate revenues in our case) from total Company revenues.

The basic tax rate is 5%. Effective in 1964, however, a surtax was imposed on us by the Legislature. The surtax is based on .5% of the previous year's intrastate gross receipts plus .625% of such receipts apportioned to public highways. Parenthetically, that surtax was originally enacted for a period of two years only; however, in 1966, the expiration date on the surtax was eliminated.

An independent computation of the basic tax and surtax is made by the State on the basis of data furnished by us in an Excise Tax Report forwarded by February 1 of each year, as follows:

1. Adjusted gross receipts from Intrastate revenues for prior year ending December 31.
2. Total line mileage as of July 1 of prior year.
3. Total line mileage on public highways, streets or other public places as of July 1 of prior year.

The total amount of basic franchise tax to be paid is indicated on a Certificate of Apportionment (Franchise Tax). The certificate which is received on April 30 of the current year also shows the portion to be paid each municipality. The apportionment is based on data furnished to the State in a "Line and Wire Mileage Report" forwarded on or before September 1 of the prior year. The report is prepared from the Company's continuing property records.

and reflects the single miles of aerial and underground wire in each municipality as of July 1 of the prior year. The two classes of wire have separate valuation rates ($11. for aerial and $6.50 for underground). The values are totaled and related to the grand total valuation. The percentages arrived at are used for distributing the basic franchise tax to the municipalities as shown on the Apportionment Certificate.

The total tax due each municipality is paid in three equal installments on June 1, September 1 and December 1.

The amount of surtax to be paid is indicated on a Certificate of Excise Tax for Use of the State which is received prior to May 1 of each year showing the computation and the amount due which is paid in total on May 1.

During 1970, the regulated New Jersey public utilities paid $140.4 million in Gross Receipts and Franchise taxes; in the same year, the statewide average real property tax rate was $5.397 per $100 of assessed valuation. Relating these tax statistics, we find that if it were not for this $140.4 in Franchise and Gross Receipts tax the average real property tax rate would have been 28¢ higher or $5.678.

The franchise tax, as its name implies, is a tax upon the "franchise", upon the "right to do business" which in our case includes our right to the use of and to have access to the public streets, highways, etc., in a particular municipality for our facilities. Our franchise imposes a responsibility to improve .

service under any and all conditions. This responsibility has come to include, I might add, the very considerable cost of rearranging telephone plant when necessitated by certain public projects, e.g., the rearrangement of a pole line in connection with a street widening. Thus, in addition to paying a Franchise tax to the municipalities, we must bear a hidden tax, the significant cost of rearranging our plant in such circumstances. Even more importantly, and as distinguished from other utilities, the telephone and telegraph companies pay to the municipalities a Business Personal Property Tax on the same plant.

Last year this amounted to $44.3 million paid directly to the 567 municipalities by such companies. While I do not intend to dwell on the Business Personal Property Tax, because it is not one of those taxes which you are studying, the fact of its existence brings me to the first point I want to stress to you. As the chart attached to my filed statement indicates, New Jersey Bell's liability under that tax has almost doubled in the past five years -- from $21.5 million in 1965 to $38.0 million in 1970. That is, I think you must admit, a very substantial increase in tax liability. Putting aside the question of whether it is a fair burden or an unfair burden, I suggest it is nonetheless an experience which this Task Force must keep in mind as it considers possible changes in any one other tax affecting us.

I submit that no proper review can be made of the role of the New Jersey Bell Telephone Company, as a taxpayer in the State of New Jersey, viz a viz the effect of one particular tax on the Company. Rather, one must view my Company as a corporate citizen whose total tax assessment towards the cost of State, County and Local government climbed to about $65 million in 1970 ..... and, without any revisions in existing tax structure, this amount can be expected to increase by about 18% in 1971.

I shall not use this forum to argue that there is an overtaxing of New Jersey Bell and, for that matter, of all utilities in the State; but the dramatic increases in our tax burden over recent years does prompt an observation concerning the true identity of the Utility Tax - payer.

The telephone consumer, and most of our customers are individuals, pays for these taxes. They are not directly "passed-on" as defined under present day tax legislation, but are hidden taxes that in most cases the individual consumer cannot avoid. Stating this in another manner, about 10¢ out of every dollar the customer pays for telephone service goes for State and Local taxes ..... our ability to pay a business tax, then, is derived from the ability of our customers to pay the tax.

We, and I think I can speak here for all utilities, recognize that our responsibility as corporate citizens of the State includes the assumption of our fair share of the <u>total</u> tax burden at all levels of government. We repeat, however -- and I believe that this point cannot be stressed too strongly -- that the impact of State and Local taxes on the public Utility community cannot be studied in one area alone, but rather must be viewed in the overall ..... for the good of the telephone consumer as well as Local, State and County governments who look to the utilities as a major source of revenue.

The last point that I want to cover concerns the difference in tax philosophy and tax treatment between telephone companies and other utilities. As you may be aware, in 1963 the State Tax Policy Commission recommended extensive revisions in the State's entire tax structure. The revisions proposed included, among other things, a recommendation that telephone companies be removed from ad valorem taxation of personal property and brought under the 7½% gross receipts tax which already applied to all other utilities. We resisted the proposal at that time because of a real concern over the establishment of a workable formula which would be universally acceptable for the redistribution of such State collected taxes back to the municipalities.

Again, in 1965, a broadly-based Governor's Commission on Chapter 51 looked again at this situation at the time it was repealing the general business personal property tax provisions and replacing them with a package of new business taxes. At our behest, legislation was enacted preserving the taxation of business tangible personal property of telephone companies on the local level at real property rate. Here again our basic concern was with the likelihood of local dissatisfaction with any redistribution formula that might be adopted.

The statewide nature of the Company's operation involving personal property is important to us and, we believe, to the Legislature. New Jersey Bell does business in and derives revenues from almost all of the municipalities in New Jersey. However, the source of gross revenue may bear little relationship to the location of the Company's real property. Many of our switching operations are centered in the large cities. Improvement and growth of those operations necessarily demand a constant expanding construction program. The municipalities housing these operation centers are well aware of the growth of these centers and have come to expect and anticipate a continuing increase in the ratables generated by this construction program. The larger cities, understandably, would view with apprehension any approach which would reduce their allotment of the total tax.

In some states, taxation of telephone personal property is accomplished by centralized statewide assessment. This approach, as in the case of the gross receipts tax, presents identical apportionment problems. Such difficulties, in fact, are avoidable only in an approach which preserves the existing ad valorem treatment of the company property with assessment and collection of applicable tax revenue at the local level.

At the risk of overburdening you with our concern in this respect, let me try to illustrate it with one example.

If the right to "settle" with each municipality with respect to New Jersey Bell's personal property tax payments, were repealed and a single payment t x approach were assumed the difficulty of working out an acceptable formula must again be pointed out ..... for example -

New Jersey Bell paid bout one-third of its total personal property ta bill directly to 10 municipalities ($13.). If the factors presently used to al cate our Franchise Tax payments were use to allocate our total personal property ta bill to each municipality these 10 municipalit s alone would receive $7 million less in ta revenue (Newark and Jersey City account for $4.? million).

For my conclusion, let me acknowledge that we have touched on only a very small segment of the overall problems associated with the formulation of tax policy. We have done so in an attempt to indicate why groups like your Task Force must take the broadest of viewpoints if we are indeed to find solutions to our tax problems. We are well aware that the goal of developing sound tax legislation can be impeded by exposure of the problems to the legislative process before opportunity and resources calculated to develop an adequate background of study has been provided. In that connection, New Jersey Bell will continue to hold itself available to this Task Force, and to the Tax Policy Committee, for such assistance as we can render in the area of tax research.

NEW JERSEY BELL TELEPHONE COMPANY

State and Local Operating Taxes....	1950	1955	1960	1965	1970
	(Millions of Dollars)				
Personal Property	$ 6,443	$10,630	$18,517	$21,549	$38,993
Real Estate	1,109	1,800	2,851	3,717	6,922
Gross Receipts (Franchise)	3,838	5,412	8,042	12,865	17,034
State Temporary Disability	31	31	24	43	101
State Unemployment	444	686	1,038	530	887
P.U.C. Assessment	-	-	-	-	[illegible]
Total	$11,865	$18,559	$30,472	$38,704	$64,406

Note: Motor Vehicle (Registration and Fuel Tax) and State Sales Tax data are unavailable.

The City of Newark Payroll Tax is estimated to be $500,000 effective with the year 1971.

Statement Before The
NEW JERSEY TAX POLICY COMMITTEE
TASK FORCE "D"
(Revenue Resources and Tax Inequities)
Presented by the

NEW JERSEY INDUSTRIAL DEVELOPMENT ASSOCIATION
Robert H. Franklin, President

Assembly Chamber, State House
March 26, 1971 at 10:00 a.m.
Trenton, New Jersey

****

Members of Task Force "D", my name is Robert Franklin. I am General Manager of Urban Affairs and Area Development of Public Service Electric and Gas Company, Newark, but I am appearing before you today in my capacity as President of the New Jersey Industrial Development Association. This is a voluntary organization comprised of some 80 professionals in the field of economic development and industrial plant location and our members are employed by firms and organizations throughout New Jersey that have a direct stake in the development of jobs for New Jersey citizens -- railroads, banks, utilities, Chambers of Commerce, municipal and county governmental development commissions, etc.

Our organization -- "NJIDA" as it is usually called -- was founded in 1953 not only to unite New Jersey's full time practitioners in this field for professional advancement, but also to (a) pool our collective experience and talents for more effective promotion of New Jersey as a site for the most desirable types of job-providing industries and (b) to maintain a watch upon developments within New Jersey's total "climate" for business and industry which have a direct effect upon our State's attractiveness as a site for business and industry.

Over the years, we have experienced many facets of the often intense competitive pressures which New Jersey's various neighboring States have exerted in order to lure new or expanding industrial operations within their borders. For example, New Jersey's plant location specialists, by and large, resisted the temptation to seek in New Jersey a counterpart of the publicly-financed low interest cost plant financing schemes which have been practiced by a number of our industrial neighbors. We have resisted this temptation because we have felt that, in the long run, it was simply not in the public's best interest that taxpayer monies be tied up for long periods of time in funds being loaned at extremely low interest rates to private industrial concerns. It has been our belief that, advantageous as the availability of such low-cost money might seem to a company seeking a new plant site at the time, that company's long term best interests (as well as those of the citizens of our State) were best served by a business climate that (a) used none of these artificial stimulants to economic growth and (b) confined taxpayer costs to the direct needs of State and local government.

As the result of this firmly adhered to belief (which resulted in New Jersey's losing some rather attractive industrial prospects to neighboring States during the past decade), the members of NJIDA have maintained an intense interest in the total picture of governmentally imposed costs upon business and industrial firms in New Jersey -- not only how our taxes compare with those of our industrial neighbors, but such other factors as statutory employment benefit costs (unemployment compensation, workmen's compensation, etc.), and pollution control obligations (which are both substantial and growing).

We recognize that all industry seeking to do business in New Jersey must accept its obligation to uphold its share of New Jersey's rather high standards of governmental services, etc. But at the same time, we hope that, in considering changes in New Jersey's present tax structure, the members of the State Tax Policy Committee and the members of this Task Force in particular, will recognize that some forms of taxation can do a great deal of harm to New Jersey's extremely sensitive position competitively with respect to attracting new or expanding industrial plants. And with the projected growth of New Jersey's population, it is vital that good jobs be created almost continually in order to support that population growth.

The main point we wish to make in this statement is that, within New Jersey's sales tax, the loss last year of the exemption on machinery and equipment used in production did serious harm to New Jersey's attractiveness for some of the most desirable types of manufacturing enterprises.

We must emphasize that none of New Jersey's industrial neighbors levy a tax of this kind. And what it tends to do is to head off the types of industry that require large investments in production machinery and equipment. Yet, by and large, these are the most desirable types of industry for New Jersey because, once they have located here, they are far less likely to be lured away again later by competitive wiles such as the low-cost plant financing schemes I have already mentioned.

In other words, removal of the machinery and equipment exemption put a heavy damper on large capital-type industries locating in New Jersey, but it had relatively little effect upon low-capital types of enterprises (often, but not always, firms employing much minimum-pay labor and operating sometimes on a highly seasonal basis).

We feel quite strongly that such a situation is not in the best interests of economic stability in New Jersey. Low-capital enterprises are often most prone to relocation "deals" because there is relatively little involved physically to moving to another State. And, by contrast, heavy-capital industries, because their roots are much deeper wherever they locate, tend usually to become highly responsible corporate citizens of their community and State, and a source of leadership on many community and civic matters, as well as substantial contributors to the economy of the region both in terms of taxes and payrolls.

Because the loss of this sales tax exemption on production machinery and equipment is presently, in our experience, such a glaring obstacle to New Jersey's ability to attract the most desirable types of industrial enterprises, and because New Jersey does face the need for a continuing influx of worthwhile industrial jobs to keep pace with our continuous population growth, it is the hope of the members of the New Jersey Industrial Development Association that the State Tax Policy Committee will recommend strongly that this exemption be reinstated.

609-662-7132
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UNION PAVING COMPANY

FOUNDED 1912
RIVER & COVE ROADS
PENNSAUKEN, N. J. 08110

LOUIS F. ESOLA
VICE PRESIDENT

MEMBER OF
ASSOC. GENERAL CONTRACTORS OF AMERICA
AMERICAN ROAD BUILDERS ASSN.
ASSOC. PENNSYLVANIA CONSTRUCTORS
ASSOC. GENERAL CONTRACTORS OF NEW JERSEY
CONTRACTORS ASSN. OF EASTERN PENNA.
NATIONAL ASPHALT PAVEMENT ASSN.

March 1, 1971

The New Jersey Tax Policy Committee
Assembly Chambers
Trenton, New Jersey

Re: New Jersey State Sales & Use Tax

Gentlemen:

We ask your vigorous effort to restore the Sales Tax Exemption on Machinery and Equipment used in manufacturing that was eliminated through the passage of Assembly Bill A416.

Considering the large investment that any replacement of our three New Jersey Asphalt Plants would represent vs. the fact that adjoining States have applicable exemptions, we feel the present law is inequitable.

Very truly yours,
UNION PAVING COMPANY

Louis F. Esola
Vice President

LFE:jmc

CLANCY AND CALLAHAN
COUNSELLORS AT LAW
11 COMMERCE STREET
NEWARK, N. J. 07102

JOHN J. CLANCY
EDWARD M. CALLAHAN, JR.

AREA CODE 201
622-4477

April 20, 1971

New Jersey Tax Policy Committee
Task Force D
134 W. State Street
Trenton, New Jersey 08625

Attention: Honorable Richard W. DeKorte, Chairman

Gentlemen:

Please be advised that this law firm represents the New Jersey Chapter, Inc. of the National Electrical Contractors Association which is comprised of over 200 of the principal union electrical contractors having offices within the State of New Jersey as well as approximately 40 out-of-state union electrical contractors who are presently engaged in construction projects within the State. These contractors employ approximately 6,500 men and in addition, engage in over 13 apprenticeship training programs in cooperation with the International Brotherhood of Electrical Workers (I.B.E.W.) involving approximately 700 apprentices who are engaged in schooling and on-the-job training. The total value of electrical services performed by these members within the State aggregates approximately 72 million dollars and comprises 85% of all electrical construction within the State.

This Association wishes to state to your Committee its concern regarding the deletion from the New Jersey Sales and Use Tax of the exemption on machinery and equipment used in manufacturing and the deleterious consequences of same upon the growth and expansion of commerce and industry within the State of New Jersey. The New Jersey Chapter of the National Electrical Contractors Association wishes to join with other interested parties who have appeared before your Committee and voiced their opposition to the deletion of this exemption. While we understand that the purpose of a deletion of this type is hopefully to provide additional tax revenue to the State, the consequences of this particular amendment have been quite the opposite, in that new industry and existing industry within the State have been discouraged from making major capital investments by way of construction

RECEIVED APR 22 1971

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AREA CODE 201
622-4477

of new facilities or improvements to existing facilities within the State because of this additional tax burden. Consequently, these manufacturers have sought sites in areas other than our State and therefore have caused, and will in the future, cause, a significant reduction in construction within the boundaries of New Jersey resulting in a serious threat to the economic welfare of the contractor members of our Association and the labor forces which they employ, all of whom are tax payers to the State of New Jersey.

In the light of all of the above, the New Jersey Chapter of the National Electrical Contractors Association respectfully requests that your Committee recommend the reinstatement of the exemption for machinery and equipment from the effect of the New Jersey Sales & Use Tax an action which we submit will be to the best interest of the economic well-beling of the State of New Jersey and its citizen-tax payers.

Respectfully,

CLANCY& CALLAHAN
Attorneysfor N.J. Chapter, NECA

By Edward M. Callahan, Jr.

EMC:jj

CC:

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