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THE CENTRIST COALITION'S DISAPPOINTING STIMULUS PROPOSAL

by Robert Greenstein

A "Centrist Coalition" stimulus package unveiled on November 14 by Senators John Breaux, Olympia Snowe, and several other senators has been presented by its sponsors as being the basis for a possible compromise on a stimulus package. The Centrist Coalition package, however, is a significant disappointment in some key respects. This is particularly the case with regard to its proposals to assist unemployed workers and the impact it would have on state budgets.

- The proposals in the Centrist Coalition plan fall short of what should be the minimum for assisting unemployed workers. Although it provides additional weeks of unemployment benefits for those who exhaust their regular benefits, it jettisons two significant temporary improvements in unemployment insurance benefits contained in the Senate Finance Committee stimulus plan. These temporary provisions, which represent effective stimulus policy, would make more part-time and recently employed workers eligible when they are laid off and provide for a modest increase in unemployment benefits.

- The Centrist plan also would exacerbate fiscal problems in the states; it would cause states and a few localities to lose nearly $4 billion in *state and local* tax revenue in the coming year, thereby necessitating nearly $4 billion in additional state budget cuts and tax increases. Actions by states to cut programs or raise taxes would further dampen economic activity and offset part of the stimulative effect that a federal stimulus package aims to have.

- The plan is particularly troubling in its approach to unemployed workers who fall into poverty during the downturn. Many of these individuals and their families likely would receive neither unemployment insurance nor health insurance under the plan, with unemployed workers who are ineligible for health insurance through COBRA being at a particular disadvantage. Some of these same individuals and families also could be adversely affected by the larger state budget cuts that would be a by-product of the plan.

A number of leading experts on the economy have identified the provision of additional unemployment insurance benefits and the provision of fiscal relief to states — so that balanced budget requirements do not force states to cut programs and raise taxes as much in the middle of a recession — as the two most effective stimulus measures that Congress can adopt.[1] The Centrist Coalition proposal does not adequately follow this counsel.

In addition, while the plan's tax provisions represent a substantial improvement over both the tax components of the House bill and the Administration's tax proposals, several of the plan's tax provisions raise significant concerns. These provisions would accelerate the phase-in of certain tax cuts enacted in June and would account for more than half of the plan's total cost over ten years (and 85 percent of its cost after 2002). Of particular note, four of every five dollars that these tax-cut acceleration proposals would provide in tax cuts would occur *after* fiscal year 2002 — in other words, in years after the economy is expected to be in recovery and when stimulus is no longer needed. Measures such as these are highly inefficient in stimulating the economy.

Such measures also would aggravate somewhat the budget crunch the nation will face after the recession ends and the need to restore fiscal discipline and hit certain budget targets returns. At a time when the Administration's budget director is issuing pronouncements that the federal budget is in such bad shape that programs not related to defense or counter-terrorism should be considered for cuts or elimination in coming years, it makes little sense to aggravate these problems by instituting measures that will reduce federal revenues further in years after the recession has ended.

I. Inadequate Unemployment Insurance Assistance

The Centrist Coalition plan drops two of the three temporary improvements in the unemployment insurance program that are part of the Senate Finance Committee bill. Like the Finance Committee bill, the Centrist Coalition plan provides an additional 13 weeks of benefits in all states to unemployed workers whose regular unemployment benefits run out before they can find a job. But unlike the Finance Committee bill, the Centrist Coalition plan provides no increase in weekly unemployment benefit levels. The Finance Committee bill raises unemployment benefits across-the-board through the end of calendar year 2002 by 15 percent or $25 a week, whichever is greater. This provision is significant because, on average, unemployment benefits replace less than half of workers' lost wages, making it difficult for many families with unemployed workers to pay rent or mortgage bills and also meet other family needs if they do not find new jobs fairly quickly. These additional benefits would, in general, be quickly spent and injected into the economy.

In addition, the Centrist plan fails to address two widely recognized problems in unemployment insurance rules that cause many deserving unemployed workers to be denied unemployment benefits. First, many unemployed workers who are available for work less than

[1] See, for example, the testimonies of William Gale and Peter Orszag, both of whom are senior fellows at The Brookings Institution, before the Senate Budget Committee, October 25, 2001.

Table 1

Comparison of Senate Finance Committee and Centrist Coalition Plans

(in billion of dollars)

	Senate Finance Committee*		Centrist Coalition Plan**	
	2002	10-year	2002	10-year
Business tax cuts	19.4	2.4	31.4	2.9
Individual tax cuts:				
Supplemental rebates	14.2	14.2	14.2	14.2
Accelerate enacted tax cuts	—	—	11.5	57.0
Unemployment insurance	14.9	20.1	8.6	11.7
State fiscal relief	4.7	5.1	—	—
COBRA	4.8	7.0	3.2	4.7
Medicaid	2.1	3.2	—	—
National Emergency Grants	—	—	4.0	5.0
Expiring tax provisions	1.0	3.1	0.6	2.7
New York and distressed areas	1.8	5.3	—	—
Other	3.7	11.3	—	—
TOTAL	66.5	71.7	73.6	98.2

*Joint Committee on Taxation, "Comparison of Estimated Budget Effects of H.R. 3090, As Passed By the House of Representatives and As Scheduled for Consideration on the Senate Floor," JCX-85-01, December 5, 2001. Estimates are adjusted to reflect a modification made by the Manager's Amendment to the financing mechanism for the unemployment insurance provisions. Other modifications made by the Manager's Amendment, such as the addition of spending for homeland security, are not reflected; official cost estimates for these changes are not available.
**Centrist Coalition estimates, as modified by CBPP. See Appendix for details.

full time — such as mothers with young children who were working two-thirds or three-quarters time before being laid off, are searching for comparable employment, and meet all other criteria for unemployment benefits — are denied benefits solely because they are not available for full-time work. Second, because of state rules developed before the advent of widespread computerization, most states do not count wages that a worker earned in either the current or the previous calendar quarter when determining if the worker has earned enough to qualify for benefits. For an individual who was laid off immediately after the terrorist attacks and applied for unemployment benefits in mid-September, no wages earned *after last March* are counted. This disqualifies a substantial number of low-wage workers who entered the job market fairly recently, such as single working mothers who have worked their way off welfare.

The Finance Committee bill addresses these problems. It would provide benefits to unemployed workers who meet all other criteria for benefits but are currently disqualified solely because they are available for work on less than a full-time basis. It also would allow workers to use their earnings in the most recently completed calendar quarter when their eligibility for unemployment benefits is determined. Both provisions would be temporary, expiring at the end of 2002, and would be fully federally funded. The Centrist Coalition proposal includes neither provision.

Because it fails to include these provisions, the Centrist Coalition plan would fail to prevent many low-income parents who left welfare for work (or stayed off welfare to begin with) and have struggled to raise their children on low wages from being denied unemployment insurance benefits if they are laid off. The Finance Committee provisions that would address these problems are both equitable and sound stimulus policy, since they would ensure that unemployment benefits are available to hard-pressed, unemployed workers with low incomes, a group likely to spend nearly every dollar in unemployment benefits it receives.

II. Denying Fiscal Relief to States and Making Their Budget Deficits Larger

The Centrist Coalition plan eliminates all $5.1 billion in state fiscal relief that the Finance Committee bill would provide states. State fiscal relief ought to be an essential component of any stimulus package to guard against state actions that undercut federal efforts to stimulate the economy. Currently, states face sizeable budget shortfalls as a result of the economic downturn, and a majority of states are moving to cut programs or raise taxes to restore budget balance. (Nearly all states are required by their laws or state constitutions to balance their budgets, even in recessions.) It is undesirable for states to cut programs or raise taxes in a recession; such actions take money out of the economy and slow the economy further.

More than 30 governors already have begun planning or implementing budget cuts, while eight states have already imposed significant tax increases. This is likely to be just the beginning of such actions. Substantial additional budget cuts and tax increases are expected when state legislatures reconvene this winter. The National Governors Association projects that state budget deficits could reach $50 billion this year.

The Centrist Coalition both fails to offer state fiscal relief and worsens the fiscal situation in most states by including a provision that would result in states losing significant tax revenue. A business tax cut that is part of all of the major stimulus packages — a provision that would allow firms to depreciate more quickly the costs of equipment and various other items they purchase — would result in 46 states losing revenues. Forty-four of these states conform their state's corporate and individual income tax rules to the federal rules in such a way that enlarging the depreciation deductions at the federal level automatically causes these deductions to grow larger at the state level as well. Two other states would lose revenues because of other effects this tax cut would have on their state tax codes. Since states already face budget shortfalls, instituting a federal tax cut that causes states to lose additional revenue in the coming year will necessitate deeper state budget reductions or tax increases.

Table 2

Estimated Loss of State Tax Revenues Due to Centrist Coalition Proposal (in millions of dollars)			
ALL STATES	**$3,630**		
Alabama	$37	Montana	$14
Alaska	47	Nebraska	22
Arizona	73	Nevada	not affected
Arkansas	36	New Hampshire	28
California	not affected	New Jersey	180
Colorado	58	New Mexico	26
Connecticut	66	New York	480
Delaware	21	North Carolina	130
Florida	140	North Dakota	10
Georgia	120	Ohio	130
Hawaii	14	Oklahoma	32
Idaho	21	Oregon	68
Illinois	240	Pennsylvania	230
Indiana	120	Rhode Island	13
Iowa	40	South Carolina	39
Kansas	38	South Dakota	5
Kentucky	49	Tennessee	73
Louisiana	38	Texas	220
Maine	20	Utah	29
Maryland	78	Vermont	7
Massachusetts	180	Virginia	92
Michigan	40	Washington	not affected
Minnesota	120	West Virginia	24
Mississippi	37	Wisconsin	93
Missouri	59	Wyoming	not affected
ADDITIONAL AFFECTED JURISDICTIONS			
District of Columbia	27	New York City	260

States would lose $3.6 billion from the depreciation provision in the Centrist Coalition plan. (See Table 2.) This is nearly twice the state revenue loss associated with the depreciation provision in the Finance Committee plan. (The Centrist Coalition plan results in nearly twice as large a state revenue loss because it contains twice as big a depreciation tax break as the Finance Committee legislation.) More important, while the Finance Committee bill accompanies its depreciation tax cut with a measure that provides $5.1 billion in state fiscal relief, the Centrist Coalition plan contains no such relief.

Under the Finance Committee legislation, $2 billion of the $5.1 billion in fiscal relief would offset the revenue losses the Finance Committee's depreciation provision would cause. Another $600 million would be used to prevent the federal share of Medicaid costs from *declining* in 29 states in fiscal year 2002; this decline is scheduled to occur under current law because the federal matching rates for 2002 are based on state per capita incomes in 1997-1999, a period when the economies of many states were growing robustly. The remaining $2.5 billion would be made available to states to reduce the magnitude of the budget cuts and tax increases they will have to implement. This approach follows recommendations from the National Governors Association (although NGA has called for a more substantial level of fiscal relief). By contrast, the Centrist Coalition plan would push states nearly $4 billion deeper into the hole without providing any offsetting relief. It thus would compel states to institute larger budget reductions or tax increases.

(Note: The Centrist Coalition plan would provide $5 billion to state and local workforce boards, as described below, but that is not fiscal relief. States would have to use this money to cover the costs of new expenditures on income support, health insurance, and job training for unemployed workers, not to ease the budget shortfalls they face. This $5 billion is included in the plan in place of key unemployment insurance and health insurance components of the Finance Committee bill.)

III. Inadequate Health Insurance Assistance

The Finance Committee plan contains two provisions to help unemployed workers maintain health insurance. The Centrist Coalition plan eliminates one of these provisions and substantially weakens the other. The Finance Committee bill would subsidize 75 percent of the cost of the cost of health insurance premiums for unemployed workers through COBRA. Under COBRA, individuals who lose their jobs can remain in their former employer's health insurance plan for 18 months after the job loss, provided the individual pays the full premium costs. The Centrist Coalition plan provides a smaller 50 percent subsidy for COBRA premium costs (which it would provide through a tax credit). With the costs of a family health insurance policy under COBRA averaging around $7,000, it is unlikely that many unemployed workers — particularly those with low or moderate incomes — would be able to pay 50 percent of COBRA premium costs.

In addition, the Centrist Coalition plan drops a Finance Committee provision that would establish a new Medicaid option at an enhanced federal matching rate, under which states could provide Medicaid coverage to low-income unemployed workers who are not eligible for COBRA and use Medicaid funds to pay the remaining portion of COBRA premiums for low-income unemployed workers who are eligible for COBRA but are too poor to pay much for it. This component of the Finance Committee plan is essential if low-income unemployed workers are to be provided health insurance during the downturn.

- A recent Urban Institute study has found that fewer than one-third of all low-income workers are eligible for COBRA when they are laid off, in part because workers in firms with fewer than 20 employees do not qualify for COBRA.

- Many of those low-income workers who are eligible for COBRA cannot afford it. The Urban Institute study found that only one in 20 low-income workers — five percent — has COBRA coverage while unemployed.

The Centrist plan does include $5 billion in grants to state and local workforce boards through the National Emergency Grants program operated by the Department of Labor. These grants could be used to provide health insurance to unemployed workers not eligible for COBRA. This provision is taken from the Bush Administration stimulus plan, except that the Bush plan provides $3 billion rather than $5 billion.[2] This approach, however, has substantial drawbacks and would be of questionable effectiveness.[3]

- The National Emergency Grants program does not appear to provide an appropriate structure to help unemployed workers retain health insurance during a nationwide economic downturn. Under current law, National Emergency Grant funds are available to help a state respond to unexpected events that result in job dislocations, such as major layoffs, plant closures, natural disasters, and job losses stemming from federal actions such as defense downsizing. Grants are administered by local Workforce Investment Boards and currently may be used for job training, re-employment services, income support, and supportive services. This grant program is designed to address the need for job training and related services in individual localities where events that have caused significant job losses have occurred, not to respond to problems created in most or all states as a result of a national recession — or to provide health insurance for unemployed workers who lack it. In fact, the program has no experience in purchasing health insurance or providing health care coverage.

- Moreover, under the proposal, the workforce boards could use the new $5 billion for a number of other purposes — such as job training, income supplements, and related services for unemployed workers — as well as for health insurance. Since the state and local workforce boards are much more familiar with employment and training programs (and the contractors that operate such programs) than with health insurance, it is likely that many of these boards would use a large share of this new money for training and employment services programs, leaving too little money to meet the health insurance needs of more than a small fraction of low-income unemployed workers.

- Of particular concern, administrative difficulties are likely to hinder the speedy use of these funds to help unemployed workers with their health insurance needs. In some states, these funds could not be used until state legislatures met and made decisions on how to allocate the funds among various workforce boards in the

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[2] Under the Bush plan, one allowable use of the National Emergency Grants would be to provide subsidies for 75 percent of COBRA premium costs. The Bush plan contains no separate COBRA subsidy. In the Bush plan, $1 billion of the $3 billion for National Emergency Grants would not be available until FY 2003.

[3] For further discussion of the National Emergency Grants proposal, see Sandra Clark, "Do Proposals to Increase Funding for National Emergency Grants Provide an Effective Way to Meet the Health Insurance and Other Needs of Laid-off Workers?," Center on Budget and Policy Priorities, November 15, 2001.

state. Moreover, the state and local workforce boards are generally advisory or planning groups that have little administrative experience. There are serious questions about whether many of them have the administrative capacity to gear up to dispense these funds on a timely basis. It could take a substantial period of time — many months in a number of areas — before state legislatures acted, the workforce boards then made decisions on how to use the new money, and the workforce boards actually got local programs up and running. This is especially likely to be the case with regard to the provision of health insurance, something the workforce boards have never done before. There is substantial risk that in many areas, these programs would get up to full speed around the time the recession ended.

In contrast, the Finance Committee provision would enable states to provide health insurance coverage to low-income unemployed workers through Medicaid, a proven public program that provides health care coverage to lower-income individuals and has existing application processes and mechanisms, such as contracts with health care providers, for delivering health care services.

- Another problem is that the National Emergency Grants program has no formula for allocating funds among states. Under this program, states submit applications to the Labor Department, which considers applications as they arrive and decides which states get funded and in what amounts. This seems appropriate for the *current* National Emergency Grants program, which dispenses only about $220 million a year and does so in response to isolated emergencies, such as a large plant closing in a particular locality. This program does not appear to be a workable (or equitable) mechanism, however, for dispensing several billion dollars to assist unemployed workers in most or all states. The risk is high that under this approach, states in which a substantial increase in unemployment rates occurs late in the downturn could receive little or no money because most or all of these funds may have been granted by then.

Finally, many of the low-income workers who do receive some health care coverage (outside COBRA) as a result of these grants to state and local workforce boards might receive only skeletal coverage. This component of the Centrist Coalition plan apparently lacks any requirement that states establish standards for the health insurance they purchase with these federal funds. Given the limited federal dollars they would be provided, a number of states or workforce boards might find it attractive to use these funds to provide quite limited health benefits to workers who are laid-off or to pay for relatively low-quality private insurance policies that carry high deductibles and provide only limited coverage, especially if such policies are marketed by insurance companies with substantial political clout in the states or localities in question. This approach represents a sharp departure from the policies that underlie the Medicaid program, which has federal minimum standards for benefit packages to ensure that the medical needs of beneficiaries, especially beneficiaries with disabilities and chronic illnesses, are adequately met.

IV. The Tax Provisions

The tax provisions of the Centrist Coalition plan are a mixed bag. On the positive side, the plan's corporate tax cuts are all one-year provisions rather than multi-year or permanent provisions. The plan's principal business tax cut — a 20 percent partial expensing provision — is appropriately tied to new investment by firms. In addition, rather than permanently eliminating the corporate Alternative Minimum Tax, the plan contains temporary changes in the corporate AMT to ensure that the AMT does not reduce the value of any of the plan's other business tax reductions. The Centrist Coalition proposal also includes a provision common to virtually all major stimulus plans — a tax rebate for lower-income workers who received no or only a partial rebate this summer. These aspects of the Centrist Coalition plan are well-designed.

The plan also contains two other tax provisions, however, that are difficult to justify as effective stimulus. These two provisions account for more than half of the cost of the entire plan over ten years (including its non-tax provisions) and 85 percent of the plan's cost after fiscal year 2002. These provisions would accelerate to 2002 both a tax cut scheduled for 2008 — the widening of the 10-percent tax bracket — and the reduction scheduled for 2004 in the current 27 percent tax rate (to 26 percent). Four-fifths of the cost of these two provisions over ten years would occur after 2002, making the provisions inefficient and of limited effectiveness as stimulus measures. Moreover, one of these provisions — the reduction of the 27 percent rate to 26 percent — would affect only the top quarter of taxpayers and be of most value to the top five percent of taxpayers. Those are taxpayers who tend to save more (and spend less) of additional after-tax income they receive than do taxpayers at lower income levels.

Conclusion

While certainly preferable to the misshapen House stimulus package or the Administration's proposals, the Centrist Coalition plan is a significant disappointment. Its provision of unemployment and health insurance to unemployed workers is not adequate, and it not only fails to provide fiscal relief to states but enlarges state budget deficits and thereby compels states to institute larger budget cuts or tax increases. Finally, it contains provisions to accelerate tax cuts enacted in June that would have limited stimulative effects but worsen the budget picture in years after the economy has recovered.

Appendix

Comparison of the Centrist Coalition Plan and the Reported Senate Finance Plan

in billions of dollars

	Finance Committee Bill, as reported*		Centrist Coalition Plan, as presented**		Centrist Coalition Plan, re-estimated		
	2002	10-year	2002	10-year	2002	10-year	
Supplemental rebates	14.2	14.2	14.2	14.2	14.2	14.2	**
Special depreciation	14.0	2.2	26.0	26.0	26.0	2.7	**A**
Sec 179 expensing	0.9	0.1	0.9	0.1	0.9	0.1	**
5-year carryback	4.6	0.1	4.6	0.1	4.6	0.1	**
Expand 10% bracket to $7K/$14K			5.0	30.0	5.0	30.0	
Reduce 27% bracket to 26% in 2002			6.5	27.0	6.5	27.0	
Expiring tax provisions	1.0	3.1	0.6	2.7	0.6	2.7	**
COBRA	4.8	7.0	4.7	8.5	3.2	4.7	**B**
Medicaid	2.1	3.2					
State fiscal relief through an FMAP increase	4.7	5.1					
Unemployment insurance	14.9	20.1	8.0	8.0	8.6	11.7	**C**
National Emergency Grants			5.0	5.0	4.0	5.0	**D**
New York and distressed areas	1.8	5.3					
Amtrak, etc.	0.6	5.4					
Other health insurance provisions	0.3	0.4					
Agriculture provisions	2.8	5.5					
TOTAL	66.5	71.7	75.5	121.6	73.6	98.2	

* These estimates are adjusted to reflect a modification made by the Manager's Amendment to the financing mechanism for the unemployment insurance provisions. Other modifications made by the Manager's Amendment, such as the addition of spending for homeland security, are not reflected; official cost estimates for these changes are not available. Estimates are from the Joint Committee on Taxation, "Comparison of Estimated Budget Effects of H.R. 3090, As Passed By the House of Representatives and As Scheduled for Consideration on the Senate Floor," JCX-85-01, December 5, 2001.

** The Centrist Coalition Plan includes a number of items that appear to be identical to items in the Senate Finance Plan as reported. These items are designated by **. For these items, the table prepared by the Centrist Coalition rounds their dollar costs, while the middle column of this table uses the unrounded costs reported by the JCT. For that reason, the totals in the middle column of this table differ very slightly from those presented by the Centrist Coalition; the Coalition shows total 2002 costs of $75.2 billion and ten-year costs of $121.3 billion.

(A) The figure shown by the Centrist Coalition as the ten-year cost of this proposal appears to be in error. The ten-year cost of any temporary proposal to accelerate depreciation, such as this proposal, is far less than the first-year cost; if firms are allowed to "expense" a greater portion of their investment expenditures up front (and therefore pay less taxes up front), they will have a smaller portion of their investment expenditures available as deductions against their earnings in later years. Therefore, they will pay more taxes than they otherwise would in later years. Our estimate of the ten-year cost of this provision is consistent with the Joint Tax Committee's estimate of the ten-year cost of a comparable provision in the Finance Committee bill.

(B) The Centrist Coalition estimates for the COBRA provision appear to be too high, given the CBO estimate of the Finance Committee's COBRA provision. The 10-year cost of the Finance provision, which would provide a 75 percent subsidy, is $7.0 billion, while the Centrist Coalition estimates the cost of its 50 percent subsidy is $8.5 billion. One would expect that, with a lower subsidy rate and no accompanying Medicaid provisions to encourage enrollment in COBRA among the low-income unemployed, the Centrist's COBRA provision would cost at least one-third less than the Finance provision. The adjusted Centrist estimate used here consequently equals two-thirds of the cost of the Finance Committee's COBRA provision.

(C) The Centrist Coalition estimate of the cost of providing 13 additional weeks of unemployment benefits, a provision of the Finance Committee bill, has been adjusted to reflect CBO's outlay estimate of that provision as well as an estimate of the effect of combining extra weeks of unemployment insurance with a COBRA subsidy.

(D) The figures that the Centrist Coalition issued imply that all the $5 billion that would be made available in National Emergency Grants would be spent in FY 2002. This seems unlikely. As this analysis explains, some implementation delays are virtually inevitable. The cost estimate in the third column assumes that 80 percent of the fund would be spent in FY 2002 with the remainder being spent in FY 2003. Even the 80 percent estimate is probably too high.