

AMERICAN JOBS PLAN



A Five-Point Plan
to Stem the
U.S. Jobs Crisis



ECONOMIC POLICY INSTITUTE

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December 2009

CONTRIBUTORS

Lawrence Mishel, Ross Eisenbrey, John Irons, Josh Bivens, and Ethan Pollack, with support from Andrea Orr, Kathryn Edwards, Andrew Green, Alexander Hertel-Fernandez, and Anna Turner.

The job creation tax credit proposal is based on the EPI Briefing Paper #248 by Timothy Bartik and John Bishop; for their full paper, visit <http://www.epi.org/publications/entry/bp248/>.

The school repair proposal is based on work by Mary Filardo of the 21st Century School Fund.

Edited by Tom Kiley.

We appreciate the financial support of the Ford Foundation; the Rockefeller Foundation; the American Federation of State, County, and Municipal Employees; and other generous supporters of EPI's research programs.

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ECONOMIC POLICY INSTITUTE
1333 H Street, NW
Suite 300, East Tower
Washington, DC 20005-4707
www.epi.org • www.AmericanJobsPlan.org

Manufactured in the United States of America

EXECUTIVE SUMMARY

Almost 16 million Americans are out of work. They are our husbands and wives. Our children, our parents. Our neighbors. The supply of willing workers is overwhelming, but we don't have the demand to match. Americans want to work. Putting the American people back to work is not only an economic imperative, but a moral one as well. Americans value hard work, independence, and personal responsibility. American workers are remarkably resilient and have an unrivaled work ethic. In the face of these challenging economic times, Americans who have jobs are working hard, gaining new skills, caring for their parents, and providing for their children. Americans who don't have jobs are doing everything they can to find work. Their quiet resilience has been a little-noticed source of our nation's strength and it can also be a wellspring for our nation's renewal.

- The United States is facing its worst unemployment crisis of the last 70 years. Nearly 16 million Americans are out of work, one-third of whom have been jobless for over six months. Another 9.3 million Americans are working part time because they can't find the full-time jobs they want and need. The jobs shortage is so severe that there are now six unemployed workers for every job vacancy—double the ratio in the prior recession of the early 2000s.
- The American Recovery and Reinvestment Act passed earlier this year helped to pull the economy out of its nosedive and to dampen mounting job losses. Still, the jobs crisis has persisted, and it is likely that unemployment will remain above 8% *even two years from now* in the absence of bold and decisive action to create jobs. The employment situation is an economic and moral crisis for the nation and requires an adequate, comprehensive response by the federal government. By itself, the private sector is unable to create jobs in the numbers the United States needs for a robust, full economic recovery.
- The Economic Policy Institute recommends a five-point American Jobs Plan to create jobs and stem the unemployment crisis. The plan calls for the nation to strengthen the safety net (including unemployment compensation, COBRA health coverage, and nutrition assistance); provide fiscal relief to state and local governments; make renewed investments in transportation and schools; support direct creation of public service jobs; and establish a new job creation tax credit.
- The American Jobs Plan is an efficient and effective way to create jobs. We estimate that the plan will create at least 4.6 million jobs in the first year, at a total first-year *gross* cost of roughly \$400 billion. This entire cost can be recouped within 10 years by enacting a financial transactions tax (FTT), which would take effect three years after enactment. An FTT is a highly progressive way to raise revenue by imposing a small tax on the sale of stocks and other financial products.

INTRODUCTION: THE JOBS CRISIS

The United States is facing its worst unemployment crisis in 70 years. In October, the unemployment rate reached double-digits for the first time in a quarter century; now nearly 16 million Americans are unemployed. Another 9.3 million are working part time even though they want full-time work. Overall, the nation has an *underemployment* rate of 17.5%, or 27.4 million people.

Among the 15.7 million jobless workers, one in every three has been out of a job for six months or more. These long-term jobless represent 3.6% of the total labor force, far exceeding the previous peak of 2.6% set in June 1983. More than 2 million workers have already been unemployed for more than a year. There is only one job vacancy for every six people unemployed.

Average unemployment rates mask an even bleaker reality for many Americans. Among African American and Latino workers, the unemployment rate has reached 15.7% and 13.1%, respectively. In Michigan, where the unemployment crisis has taken its toughest toll, unemployment reached 15.1% in October 2009.

Unemployment among men has reached 11.4%. Among blue-collar workers, unemployment is 50% higher than the national average. White-collar unemployment is 6.8%, which may seem low but is higher than all but the two worst months of the 1980s recession. And while college graduates have a comparatively low rate of unemployment (4.7%), it is still the highest jobless rate on record for that group.

Unemployment would be even higher had there not been an actual drop of 903,000 in the size of the labor force over the last year when normally we would expect labor force growth of nearly 1.5 million. A primary reason for this contraction is that the dismal labor market convinced many people to give up looking for work; these labor force dropouts are therefore no longer counted among the unemployed. Nevertheless, the steep rise in unemployment, up 5.3 percentage points since the start of the recession, is even greater than the rise in unemployment in the deep recession of the 1980s.

The United States has lost 8 million jobs (5.9% of all jobs) during the recession so far, the sharpest drop since World War II. But bringing back even 8 million jobs would not return us to the pre-recession unemployment rate of 4.9% because the population has grown since then. Each month we need to create 127,000 jobs just to keep unemployment from rising. Therefore, we actually need 10.9 million new jobs to get us back to 4.9% unemployment.

The Economic Policy Institute anticipates that unemployment will keep rising until mid-2010 or even until the end of 2010, topping out at 10.5% or higher. According to some forecasts, the unemployment rate may still be as high as 8% at the end of 2011. To offer some context, at no point in the 25 years preceding this recession did the unemployment rate reach 8%. It is an unacceptably high unemployment rate that policy makers must address.

Since people flow into and out of unemployment, over a third of the workforce will experience a spell of unemployment or underemployment during 2010. Among African Americans and Latinos, about 40% of workers will be unemployed or underemployed at some point in 2010.

Wage deceleration and lost income

High unemployment hurts even those who retain their jobs because wages grow more slowly and furloughs, reduced hours, and losses in benefits become more common. Gallup reports that a third of workers fear their wages will be reduced. A September 2009 survey of voters' views on the recession, jobs, and the deficit, conducted for the Economic Policy Institute by Hart Research, found that 44% of households have already experienced job loss or cuts in pay or hours.

The recession will reduce incomes for families at all income levels, but it will hit low-income families the hardest. Over the four years from 2008 to 2011, average low-income families will see their incomes decline by \$1,200 a year, for a four-year total income loss of \$4,600, compared with what they earned in 2007, before the recession began. In other words, low-income families will have earnings in 2011 that are 7.2% lower, on average, than their 2007 earnings. An average middle-class family will see losses of roughly \$3,500 a year for those four years, with incomes in 2011 worth 5.6% less than their 2007 levels.

Widespread economic hardship and harmful scarring

Economic recessions are often portrayed as short-term events. However, as a substantial body of economic literature shows, the consequences of high unemployment, falling incomes, and reduced economic activity can have lasting consequences. For example, job loss and falling incomes can force families to delay or forgo a college education for their children. Frozen credit markets and depressed consumer spending can stop the creation of otherwise vibrant small businesses. Larger companies may delay or reduce spending on research and development.

In each of these cases, an economic recession can lead to “scarring”—that is, long-lasting damage to individuals' economic situations and the economy more broadly. More specifically, recessions can cause long-term hardships for families and lasting economic damage in the following areas:

- *Educational achievement:* Unemployment and income losses can reduce educational achievement by threatening early childhood nutrition; reducing families' abilities to provide a supportive learning environment (including adequate health care, summer activities, and stable housing); and by forcing a delay or abandonment of college plans.
- *Opportunity:* Recession-induced job and income losses can have lasting consequences on individuals and families. The increase in poverty that will occur as a result of the recession, for example, will have lasting consequences for children, and will impose long-lasting costs on the economy. High and rising unemployment could drive up the child poverty rate from 18% in 2007 to around 27% over the next few years. For black children, poverty could rise from the already dismal level of one-third in 2007 to more than 50% in the year or two ahead.
- *Private investment:* Total nonresidential investment is down by 20% from peak levels through the second quarter of 2009. The reduction in investment will lead to reduced production capacity for years to come. Furthermore, since technology is often embedded in new capital equipment, the investment slowdown can also be expected to reduce the adoption of new innovations.
- *Entrepreneurial activity and business formation:* New and small businesses are often at the forefront of technological advancement. With the credit crunch and the reduction in consumer demand, small businesses are seeing a double squeeze. In 2008, for example, 43,500 businesses filed for bankruptcy, up from 28,300 businesses in 2007 and more than double the 19,700 filings in 2006. Only 21 active firms had an initial public offering in 2008, down from an average of 163 in the four years prior.

A recession, therefore, should not be thought of as a one-time event that stresses individuals and families for a couple of years. Rather, economic downturns will affect the future prospects of all family members, including children, and will have consequences for years to come. On the flip side, spending now to create jobs has beneficial effects that ripple over the long term.

The American Recovery and Reinvestment Act

The American Recovery and Reinvestment Act enacted in February 2009 was by necessity the largest economic intervention by the federal government in generations. Recovery Act investments slowed the economy's free fall, created between 1.1 and 1.5 million jobs by the end of September, and made economic recovery possible.

Matters would have been far worse if Congress had not passed the Recovery Act. The Recovery Act had already pumped \$175 billion into the economy by the end of September and generated about 170,000 to 235,000 jobs each month since April. The fact that the job situation remains so dismal reflects how deep a hole we were in.

The economic downturn has turned out to be far worse than what economists were predicting a year ago. At the

time of the presidential election, the consensus forecast among economists was that unemployment would hit 6.9% in early 2009. But it hit 8.1% in the first quarter and reached 8.5% in March, before the ink was even dry on the Recovery Act.

The economy was headed steeply downward last winter and in early 2009. The Recovery Act interrupted that decline and then started to create actual growth during the summer. In the second quarter of 2009, the economy's only area of growth was government consumption and investment, which increased by 11.4% over the previous quarter. Private consumption, investment, and net exports were all negative. Without the Recovery Act, total government expenditures would have fallen and gross domestic product would have dropped 3.7%. Instead, the economy declined by only 0.7%, and the smaller drop saved between 600,000 and 750,000 jobs in that quarter alone.

A note about the deficit

Critics argue that the Recovery Act and the rescue of the financial sector have exhausted our ability to pursue further fiscal solutions—government spending and tax cuts—to fight the recession.

But as a matter of economics, the government's anti-recession spending so far has been less than half as large as Keynesian analysis calls for. University of California, Berkeley Professor of Economics J. Bradford DeLong and Nobel Laureate Paul Krugman argue that we cannot afford *not* to make another large investment to create jobs and accelerate GDP growth. These economists maintain that failure to intervene further could result in a "lost decade" of economic stagnation similar to that which Japan experienced in the 1990s.

The long-term costs of an extended recession will far outweigh the additional interest payments on the national debt required to fund a major intervention. Some of those costs are set out in the report, *Economic Scarring: The Long-Term Impacts of the Recession*, by EPI Research and Policy Director John Irons. The primary reason we have a large fiscal deficit at this point is that we are in a major recession. The best way to tackle the deficit is to generate more jobs and get the nation firmly on a path to recovery.

Generating jobs through additional spending or a jobs tax credit will raise the fiscal deficit for the next year or two. But this result is entirely appropriate in the context of the recession, and will not damage the economy. In fact, it will reduce the damage to future growth that occurs as a result of the recession's impact on children's learning, lost innovation, and reduced investment.

The urgent need for bold, decisive action

The Economic Policy Institute has detailed some of the structural economic problems—including unprecedented income inequality, the disconnect between worker pay and productivity, and feverish financial sector growth—that helped precipitate this crisis. But it bears noting that the average American worker was not faring so well even before this recession began. We encourage stakeholders interested in long-term economic reforms to learn more by visiting www.AmericanJobsPlan.org for links to more resources. This report, however, focuses on the immediate jobs crisis and the need for a comprehensive plan to spur job creation.

The problem immediately confronting the economy is that resources are under-utilized. Too many people are unemployed and too many facilities are idle. The solution is to increase demand. People have lost vast amounts of wealth and income and cut back on spending. Businesses have lost customers. Exports fell as the world economy declined. That vicious cycle is continuing, though at a slower pace, and that is why government can provide an effective intervention. At this point, the greatest need is more jobs. As long as employers have only a single job opening for every six unemployed workers, the economy will continue to struggle.

The American people overwhelmingly support additional action to create jobs. The EPI/Hart Research survey found that more than three-quarters of respondents (81%) feel that more should be done to address the jobs crisis.

When asked about the largest economic problems facing the United States, respondents most commonly cited unemployment (53%); the deficit was a distant second, with only 27% rating it as one of the nation's most important economic problems. The poll showed that Americans believe the Recovery Act has helped, but they also want to see more direct action to create jobs. Large majorities support a public jobs program and job creation tax credits, and a majority supports more aid to the states.

The country's jobs crisis requires immediate attention. More should be done to generate robust job growth, restore incomes, create consumer demand, and drive sustained economic growth.

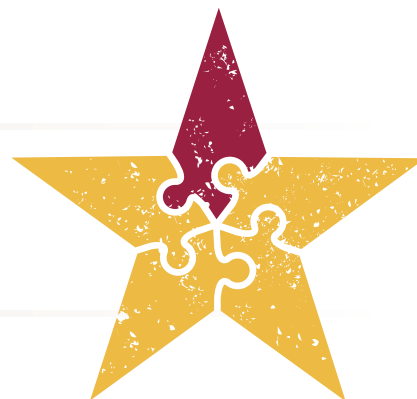
Large-scale job creation in the next two years will require bold, decisive action such as the American Jobs Plan. Implementing the American Jobs Plan would create or preserve at least 4.6 million jobs, bringing us a long way toward creating the 10.9 million jobs we need to return to pre-recession unemployment levels.

The American Jobs Plan has five components:

1. strengthening the safety net;
2. providing fiscal relief to the states and local governments;
3. increasing investments in transportation infrastructure and school repair and modernization;
4. creating public service jobs;
5. and enacting a new job creation tax credit.

This report discusses in detail each of the five components of the American Jobs Plan and describes how a modest financial transactions tax can recoup the entire cost of the plan within 10 years.

1. STRENGTHENING THE SAFETY NET



The first component of the American Jobs Plan is to strengthen the safety net—including unemployment compensation, COBRA health coverage, and nutrition assistance. The Recovery Act signed into law last February contained two important supports for unemployed workers and their families. First, it provided for Emergency Unemployment Compensation for people who had been unable to find work before their benefits expired. It also provided a 65% federal subsidy of COBRA health care benefits for up to nine months to help make health insurance more affordable to the unemployed. These supports are critical to helping families make ends meet while they search for new work. But they are also highly effective at increasing overall demand in the economy, and therefore at creating new jobs.

Unemployment insurance

With long-term unemployment at record levels, 600,000 workers exhausted their unemployment benefits this fall before Congress approved an additional extension of benefits for 14 weeks in every state, and 20 weeks in states with unemployment higher than 8.5%. Unemployed workers can now collect a maximum of 99 weeks of unemployment compensation, including 26 weeks of regular state benefits and up to 73 weeks under the three federal extensions.

But when the Emergency Unemployment Compensation program expires on December 26, 2009, unemployment benefits will once again be exhausted after 26 weeks. This reversion back to normal pre-recession coverage will occur at a time of the highest unemployment rate in a generation and the highest spell of long-term unemployment on record. With unemployment expected to average above 10% for the next year, the number of job seekers will continue to far exceed the number of job openings, and long-term unemployment will remain high.

While unemployment benefits, which generally replace about 30-50% of pre-layoff income, are rarely sufficient to cover a family's total costs, they can help pay for basic necessities such as food and some housing costs.

Two other Recovery Act provisions relating to unemployment insurance must also be renewed to maximize the assistance they provide. First, the Act increased every weekly benefit check by \$25, an amount that provides real help to struggling families. And second, the first \$2,400 of unemployment compensation was excluded from federal income taxation, saving the average unemployed person hundreds of dollars in taxes.

COBRA subsidies

The Consolidated Omnibus Budget Reconciliation Act (COBRA), passed in 1986, allows workers who are laid off from their jobs to keep their employer-sponsored insurance at their own expense for up to 18 months. The COBRA take-up rate by unemployed workers, however, has traditionally been low, largely because health care premiums are so exorbitant. Workers whose income has been cut by half or more can't afford to purchase health insurance. The Recovery Act helped make insurance more affordable by subsidizing 65% of the cost.

However, even with that subsidy, only a relatively small portion of unemployed workers are electing to keep their employer-sponsored health insurance through COBRA. A recent report by Ceridian, which is the largest provider of COBRA administrative services in the nation, found that the COBRA take-up rate had increased from 12.4% before the Recovery Act subsidy's implementation to about 17.7% between March and June of this year. "The historically low COBRA usage rates were not greatly improved even with a 65% subsidy, primarily due to the high premium cost," the Ceridian report found.

An analysis of health care costs relative to unemployment benefits helps show how COBRA can be out of reach for a family, even with a seemingly generous 65% subsidy. In September, unemployed workers received an average weekly unemployment benefit of \$333.62, which equates to a total monthly benefit of \$1,446. The average monthly health care premium for a family in 2009 is \$1,115, or 77% of the unemployment benefit without the subsidy, \$390 or 27% with it.

Considering that many of the unemployed have been out of work for months and have likely exhausted their savings, and that unemployment benefits typically barely cover basic necessities like food and housing, it's understandable that few could afford COBRA before the subsidy and may still not be able to afford it at 35% of the total cost. While an extension of the COBRA subsidy, currently set to expire December 31, 2009, is essential to help keep the unemployed from losing their health care, it is not sufficient. An 80% subsidy would bring the average monthly premium cost down to \$223, more within reach of most families. In addition, the current nine-month duration of the subsidy should also be extended so that unemployed workers can have access to affordable health care for as long as they are eligible for COBRA.

Congress has already recognized that COBRA is widely unaffordable, even with a 65% subsidy. When it renewed and expanded the Trade Adjustment Assistance Act as part of the Recovery Act, Congress increased the COBRA subsidy for workers who have lost their jobs as a result of increased imports or production outside of the United States to 80%. All unemployed workers should receive the same benefit.

Nutrition assistance

In November the U.S. Department of Agriculture (USDA) reported that 17 million households had difficulty putting enough food on the table at times during 2008—a significant increase from 13 million households in 2007. The level of food insecurity that the USDA found in 2008 is the highest it has been since the nationally representative food security surveys were initiated in 1995. Increases in food stamp benefits are a

particularly effective way to encourage consumer spending, because every dollar increase in food stamps is likely to be spent quickly and locally, and—according to chief economist Mark Zandi of Economy.com—will boost GDP by \$1.73. Congress should examine options for increasing nutrition assistance.

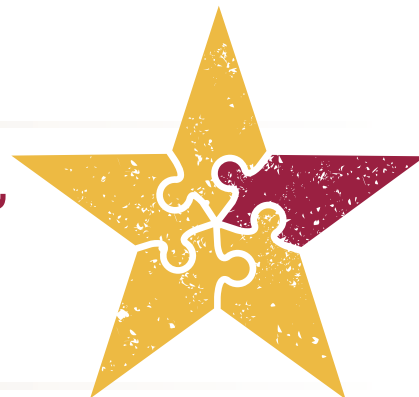
Benefits of safety net spending

In addition to sustaining some of the neediest families, safety net spending in the form of unemployment insurance and health insurance subsidies helps the economy as a whole by circulating cash into local communities and helping businesses avert further job cuts. Each \$1 billion of unemployment compensation generates an estimated \$1.63 billion to \$2.15 billion of additional GDP. If the unemployed did not receive insurance benefits, then their reduced consumption would be a serious drag on the economy, reducing demand for businesses' goods and services, leading them to reduce investments and lay off additional workers. Rather than stabilizing the economy, limiting unemployment benefits would set off another round of disastrous payroll losses and imperil the recovery.

Policy recommendation

As the first components of the American Jobs Plan, EPI recommends continued extension of unemployment insurance and subsidized COBRA, as well as an increase in the COBRA subsidy to 80% from the current 65%. Congress should also examine ways to strengthen nutrition assistance.

2. FISCAL RELIEF FOR STATE AND LOCAL GOVERNMENTS



The second component of the American Jobs Plan is to provide additional fiscal relief to state and local governments. The recession has led to much lower tax revenues at the state and local levels and to higher spending for state safety net programs, but unlike the federal government, state and local governments are legally required to balance their budgets.

As a result, while federal policy makers are enacting expansionary fiscal policy, state and local policy makers are cutting spending and raising taxes, moves that will lead to lower consumer demand and more unemployment. And these contractionary fiscal efforts have just begun: state and local budget gaps are likely to be as large or larger this fiscal year and next.

If not offset through federal policy, state and local budget cuts will result in the loss of millions of jobs—most of them in the private sector—and create a drag on the economy.

Benefits of state and local budget relief

One of the most effective pieces of the Recovery Act has been the \$144 billion in state budget relief, provided mainly in the form of Medicaid and education funds. EPI economist Josh Bivens estimates that the \$52 billion in state and local budget relief expended so far boosted the economy by \$73 billion through the end of October and is responsible for an additional 360,000 to 500,000 jobs that would otherwise not exist. According to a recent report by Mark Zandi, chief economist at Moody's Economy.com, each dollar of budget relief has provided nearly twice the economic stimulus as temporary tax cuts.

Budget relief prevents tax hikes and spending cuts, the latter of which are particularly harmful to the economy for two reasons. First, laying off teachers, firefighters, police officers, and bus drivers deprives individuals of needed public services like education, safety, and transportation. Second, spending cuts disproportionately impact low-income households because they are highly sensitive to reductions in services: a decrease in Medicaid benefits, for example, reduces their disposable income, forcing them to cut back their consumer spending on a nearly one-to-one basis. Businesses' sales then fall, forcing firms to slash wages or lay off workers, who then cut their own spending. By rippling in this way across the entire economy, each dollar of spending reduction results in \$1.41 in lost economic activity.

State and local spending cuts mainly hurt the private sector. Of the \$1.41 in lost economic activity, 41 cents is spending taken right out of the private economy, while \$1 is taken out of direct government spending (e.g., education) and transfers (e.g., Medicaid). Of that dollar, 25 cents is in the form of reductions in transfers to private individuals, while 75 cents is reductions in direct government spending. But even 30% of that direct government spending—or 22 cents—is in reduced demand for private supplier industries (those industries supplying the firetrucks and textbooks, for example), leaving 53 cents in actual loss to the public sector. Taken together, a full 88 cents of the \$1.41, or 62% of the total economic impact of a dollar in budget cuts, falls on the private sector.

While the budget relief in the Recovery Act was beneficial to the economy, too little was provided. Between this current state fiscal year, which started July 2009, and the next, states face a \$357 billion budget shortfall after drawing down rainy day funds; local governments face an additional \$80 billion shortfall. Federal relief will shave off \$106 billion, or about 25%, of this \$437 billion two-year state and local budget shortfall, with the rest of the \$331 billion translating into spending cuts and tax increases.

More immediately, between the mid-year shortfalls in fiscal year 2010 (currently underway) and the full shortfalls in 2011, state and local governments will raise taxes and cut spending by \$204 billion.

Policy recommendation

We recommend that the federal government extend the state and local budget relief provided in the Recovery Act by \$150 billion over the next year and a half, through state fiscal year 2011. The additional relief will save between one million and 1.4 million jobs.

3. INVESTMENTS IN TRANSPORTATION AND SCHOOLS



The third component of the American Jobs Plan is increased investment in transportation infrastructure and the repair and modernization of the nation's school buildings and facilities.

Our public transit systems are for the most part inadequate. For example, even some major cities lack subways, adequate bus service and light rail, and inter-city passenger rail service is almost non-existent. The massive long-term investments to bring these systems into the 21st century would create hundreds of thousands of good jobs in a wide array of industries, including manufacturing, engineering, and construction. At the same time, our highway system has fallen into dangerous disrepair, with a staggering inventory of unsafe bridges and neglected repairs of road and highway surfaces. The Recovery Act provided about \$50 billion worth of transportation infrastructure funding, which—while badly needed—only addressed about 6% of the five-year transportation deficit. We should immediately begin to address this public investment deficit in order to increase productivity, expand economic opportunities, and generate jobs.

We want to draw special attention to a less visible but equally vital infrastructure need: maintaining and repairing the nation's schools. A bold plan to address the pervasive problem of deferred maintenance and repair could put nearly a quarter of a million people to work in 2010 while improving safety and education for millions of children. Investment in the repair and maintenance of the nation's 97,000 public school buildings would boost the recovery and deliver long-term benefits to the economy.

In 1995, an extensive survey and analysis by the Government Accountability Office (GAO) found that America needed \$113 billion (\$159 billion in today's dollars) to bring its school building inventory into good repair. Although the United States expended nearly \$550 billion for public school construction from 1995 to 2007 (\$770 billion in today's dollars), most of these funds were to build new schools and additions to meet the space needs of nearly 5 million additional public school students. The 86,000 already existing school buildings were neglected. Most school districts were unable to catch up or keep up with the maintenance, repair, or capital renewals needed to support the health, safety, or educational requirements of staff and students.

A detailed analysis by the 21st Century School Fund of school district spending on maintenance, repair, and capital renewals revealed that the nation's deferred maintenance deficit has worsened considerably since 1995. Nearly \$300 billion of required maintenance in pre-kindergarten through 12th grade public school buildings has been neglected. This amount works out to an average of about \$41 per square foot and \$5,400 per student.

Chronic deferred maintenance, repair, and capital renewals can result in unsafe drinking water, unsafe food storage and kitchen equipment, inoperable building door locks, infection risk and asthma from exposures to mold under carpets, alarm systems beyond repair, and danger from structural problems. Gyms, pools, and libraries are closed because of leaky roofs and other maintenance problems.

Without adequate funds, school buildings are maintained as part of a “run to fail” system that neglects preventive and routine maintenance and performs upgrades and replacements of major building systems, components, and finishes only in response to crises.

Maintenance and repair work are labor intensive. Making progress on the most critical needs with an investment of \$30 billion—just 10% of the most urgent deferred maintenance—could provide important, productive employment to nearly 240,000 workers in the private and public sectors. Currently, 1.5 million construction workers are unemployed, and the market for new construction remains severely depressed. Both small businesses and their employees will welcome the work.

Policy recommendation

In addition to increased investments in transportation infrastructure, we recommend the allocation of \$30 billion to school districts for school modernization according to the Elementary and Secondary Education Act’s Title I formula to ensure that the money reaches every school district quickly and efficiently.

4. PUBLIC SERVICE JOBS



The fourth component of the American Jobs Plan is to create jobs directly by putting unemployed people to work in jobs that will benefit their communities. If the private sector can't put people back to work, then the public sector must. Twice in the past during times of high unemployment, the United States successfully turned to large-scale programs of direct job creation. We can build on those successes to increase employment and household income in the communities most severely affected by the economic downturn. In doing so, we can reduce the need for unemployment compensation and health coverage for the unemployed while improving health, housing, education, job readiness, transportation, and public infrastructure.

With a goal of putting one million people back to work, the program should be funded at \$40 billion per year for three years, with funding allocated to local governments and states according to the Community Development Block Grant (CDBG) formula. The CDBG formula targets communities based on levels of short-term and long-term economic distress, as reflected in measures such as poverty, population decline, and age of housing stock. The formula could be improved with measures of unemployment and long-term unemployment, but to speed startup the first year could use the existing formula.

The U.S. Department of Labor should allocate funds and oversee the program at the federal level. Projects would be selected for funding by the highest local elected official based on the ability of the project to provide immediate employment to community residents, its benefit to the community, and the management capacity of the applicant.

Local governments would design public sector programs or select projects proposed by nonprofit organizations and public-private partnerships that can quickly employ residents of the targeted communities while delivering a needed service.

During the first six to nine months, the program would fund fast-track jobs. Projects would be limited to a discrete list of activities in order to allow for quick implementation and large-scale employment. This fast-track authority should be carefully defined to prevent abuses. It should be limited to four areas that reflect national priorities and demonstrate a high potential impact for aggregate job creation: neighborhood/community improvement, child health and development, access to public services, and public safety.

Fast-track jobs might include, for example:

- cleaning up of abandoned and vacant properties to alleviate blight in distressed and foreclosure-affected neighborhoods;
- staffing emergency food programs to reduce hunger and promote family stability;
- working in Head Start, child care, and other early childhood education programs to promote school readiness and early literacy;
- renovating and maintaining parks, playgrounds, and other public spaces.

After nine months, the program would move into the full implementation phase, and projects would be identified based on a planning process that would involve community input. Priority for funding under the longer-term phase would be given to employment projects that:

- integrate education and job skills training, including basic skills instruction and secondary education services;
- coordinate to the maximum extent feasible with pre-apprenticeship and apprenticeship programs;
- provide jobs in sectors where job growth is most likely and in which career ladders exist to maximize opportunities for long-term, sustainable employment for individuals after program participation.

Jobs would be made available broadly to the unemployed, but local governments would be permitted to target the program to those most in need, such as those unemployed for more than six months or people residing in a high-poverty community.

It is critically important that the jobs created be new jobs that add to total employment and not substitutes for jobs currently held by public employees. Experience shows that local governments will be tempted to replace employees paid by local taxpayers with employees paid with federal funds. To prevent this, there must be strict rules against substitution, coupled with strong enforcement of the rules; and federal funds for these jobs should be accompanied by the state and local fiscal relief proposed as part of this plan.

To ensure the maximum job creation, 80% of funding for each project must be spent on wages, benefits, and support services (such as child care) for individuals employed. To ensure that the jobs do not undermine local labor standards, the projects must pay prevailing wages and benefits.

During the Great Depression, public job programs employed millions of people and left a legacy of improvements in the national parks and forests, more than 100,000 miles of new roads, 35,000 public buildings, urban art and murals, soil conservation, and many other valuable contributions to national life and prosperity. A smaller program in the 1970s employed 750,000 people at its peak, gave on-the-job training that boosted the long-term income of hundreds of thousands of young people and urban residents, and performed valuable services in thousands of communities.

We know from those experiences that a large-scale jobs program can be geared up quickly and help put a million of our citizens back to work in jobs that will improve their communities and contribute to shared prosperity.

Policy recommendation

We recommend that the federal government spend \$40 billion per year over the next three years to directly create jobs that put unemployed Americans back to work serving their communities.

5. JOB CREATION TAX CREDIT



The fifth and final component of the American Jobs Plan is a tax credit for new job creation deployed over the next two years. According to our estimates, a tax credit for firms equal to 15% of expanded payroll costs would lead them to hire an additional 2.8 million employees next year. Such a credit would have to be:

1. **Wide-ranging.** The tax credit should be designed to stimulate a wide range of jobs across economic sectors and across all kinds of firms, regardless of size or current profitability.
2. **Temporary.** It should be of limited duration to encourage job creation when the labor market is weakest and to limit the cost to the treasury.
3. **Large.** It should be large enough so that it will lead firms to hire new employees and cause a significant number of jobs to be created economy-wide.
4. **Efficient.** The tax credit should target new job creation as much as possible and not simply be a handout to businesses.

In line with these principles, we suggest a broad-based refundable tax credit for employers that expand their workforce in 2010 and 2011. In the first year the credit would be equal to 15% of the net increase in that portion of a firm's payroll subject to Social Security taxes. In the second year the credit would drop to 10%. The reduction in the second year would encourage firms to hire sooner rather than later and would provide a significant incentive for expanded employment.

To ensure that the credit is most effective at stimulating new hiring and to ease implementation, the credit would be calculated as a percentage of the increment to firms' Social Security payroll tax expenses over a base amount. We suggest using firms' payrolls in the four quarters prior to enactment (adjusted for inflation) and calculating the tax credit based on the incremental increase in the expenses for payroll taxes paid. Employers already report Social Security and Medicare payroll taxes each quarter on IRS Form 941; adding a few lines to the form would allow a wage credit to be implemented relatively simply. The credit would be refundable, so even firms that are not profitable (and thus have no tax liability) would benefit. It would also be provided quarterly so it would help firms' cash flow immediately after hiring.

The credit should be broad-based, extended to all private firms, nonprofit organizations, and state and local governments.

By basing the credit on total Social Security payroll taxes, it would also reward expansion of work hours as well as employment. And basing it on that portion of wages subject to Social Security payroll taxes ensures that the credit does not apply to wages increases for very high wage earners.

Impact

The job creation tax credit as outlined above would have a significant impact on job creation. Using estimates of how wage costs influence employer hiring, we find that the credit would lead to the creation of 1.4 to 2.8 million new jobs in the first year and slightly less in the following year as the tax credit is reduced.

The cost of the program is relatively modest. The initial revenue loss would immediately be limited due to offsetting increases in revenue from corporate tax receipts and individual tax payments. We estimate the gross revenue cost to be between \$71 billion and \$80 billion in the first year and between \$62 billion and \$67 billion in the second. However, the total cost to the government would be significantly less, since greater employment also means less spending on social safety net programs like unemployment insurance, health care, and nutrition assistance, and because some revenue would be recouped through higher corporate receipts. When these savings are included, we estimate a total cost of between \$13 billion and \$37 billion in the first year and between \$14 billion and \$36 billion in the second.

All told, the job creation tax credit would be a cost-effective way to create jobs. Factoring in the revenue loss from jobs that would have been created anyway, the cost would be between \$4,700 and \$26,300 per net new job created in the first year. This compares favorably to other means of generating jobs and is certainly more favorable than other business tax breaks, which typically have a low “bang-for-the buck” in terms of job creation.

Policy recommendation

To encourage employers to expand their workforces, we recommend a refundable tax credit, worth 15% of expanded payroll in the first year and 10% in the second, for businesses, nonprofits, and state and local governments that enlarge their payrolls through hiring, adding hours, or increasing wages.

PAYING FOR THE AMERICAN JOBS PLAN WITH A FINANCIAL TRANSACTIONS TAX

Enactment of the American Jobs Plan would have immediate benefits for employment, but as long as the impact of the recession continues to weigh on the job market next year and through 2011, government economic policy must remain expansionary. When unemployment moderates and the economy has rebounded, it will be appropriate to address the federal budget deficit. The spending required by the American Jobs Plan would occur within the first two years after its enactment; in years three through 10, all of this spending could be recouped through a *financial transactions tax*.

Proposals for a financial transactions tax (FTT), such as one by Congressman Peter DeFazio (D-Ore.), have been met with strong opposition, especially from Wall Street. This opposition is misplaced. An intelligently designed financial transactions tax should be a key item on the policy menu. Those concerned about the state of the job market today and the state of the deficit tomorrow should embrace a proposal that calls for increased action to boost employment in the next two years that is paid for with the implementation of an FTT. The economic bottom line is that a financial transactions tax is a progressive revenue-raiser that is likely to be either efficiency-neutral or even efficiency-enhancing. Few other revenue-raisers can make this claim.

What would a well-designed financial transactions tax look like?

A financial transactions tax would levy a small “sales tax” on the transfer of ownership of a financial asset. For stock transfers, a rate of 0.5% (possibly split between buyer and seller) would raise significant revenue while not causing harmful economic effects. The rate would apply to and vary for other asset classes to provide disincentives for investors to arbitrage away the tax by moving out of stocks and into other instruments.

To put a 0.5% transaction tax in perspective, a typical state sales tax on goods and services is about 5.0%, or 10 times our proposed tax.

Taxing the simple transaction, rather than calculated proceeds, reduces the scope for disguising proceeds to avoid the tax. Also, taxing each transaction at a fixed rate implicitly imposes a higher tax on short “roundtrips,” that is, rapid (hourly or daily) turnovers of asset ownership. These short roundtrips generally do not provide large profits for investors, so the fixed transactions costs will impose a comparatively heavy fee. Conversely, if an asset is bought and held for an extended period, the transactions fee will likely constitute a small percentage of the total proceeds. This structure usefully biases the incidence of the tax toward speculators and away from long-term investors.

Financial transactions taxes exist today

Several countries have implemented examples of well-functioning financial transactions taxes. In the United States, the Securities and Exchange Commission currently levies a 0.00257% fee on stock transactions to fund its operating expenses. Japan had a 0.3% sales tax on stock transactions that raised substantial revenues (up to 4% of GDP during the stock market bubble of the late 1980s) before it was repealed in 1999. The United Kingdom currently imposes a 0.5% stock “stamp tax” on each trade on the London stock exchange.

The existence of the U.K. stamp tax belies an important argument often made against the tax in the United States—that it will harm the international competitiveness of U.S. stock exchanges and send companies fleeing to foreign ones. The fact that the London stock exchange is one of the largest in the world (in the top five in value of domestic market capitalization and total value of share trading, according to the World Federation of Exchanges Database) suggests that it has not been hurt unduly by the stamp tax. Furthermore, the U.K. tax means that the United States has more room to impose its own tax without losing competitive ground.

Lessons on designing a tax

The United States can learn from the rest of the world’s experience with financial transaction taxes. In the U.K., payment of the stamp tax is necessary to prove that ownership of the asset has legitimately changed hands. This feature gives it a built-in enforcement device: those who try to evade the tax will have trouble enforcing their claim to asset ownership.

On the other hand, the U.K. stamp tax is often criticized for taxing only stock transfers and thereby leaving a wide range of other asset markets unaffected. Those looking to evade the tax can engineer financial substitutes for stock transactions in these other asset markets. A well-designed tax would tax other asset classes as well as emerging asset classes at rates in line with the stock rate.

How much money could a financial transactions tax raise?

The U.K. stamp tax raised an amount equal to 0.2% of U.K. gross domestic product in the latest year analyzed; a similar share in the United States would equate to \$30 billion. A 2004 Congressional Research Service study found that a 0.5% tax based on stock transactions could raise \$79 billion annually. A review for the Canadian government in 1996 found that six of the nine countries surveyed collected revenue greater than 0.6% of their total GDP, equivalent to \$85 billion in the United States in 2009.

A financial transactions tax could raise considerably more than these estimates—0.8% to 1.6% of GDP according to a 2002 study—by taxing a wider range of assets than stocks. In 2009 that range would amount to \$113-226 billion. In short, the tax can be a significant revenue-raiser.

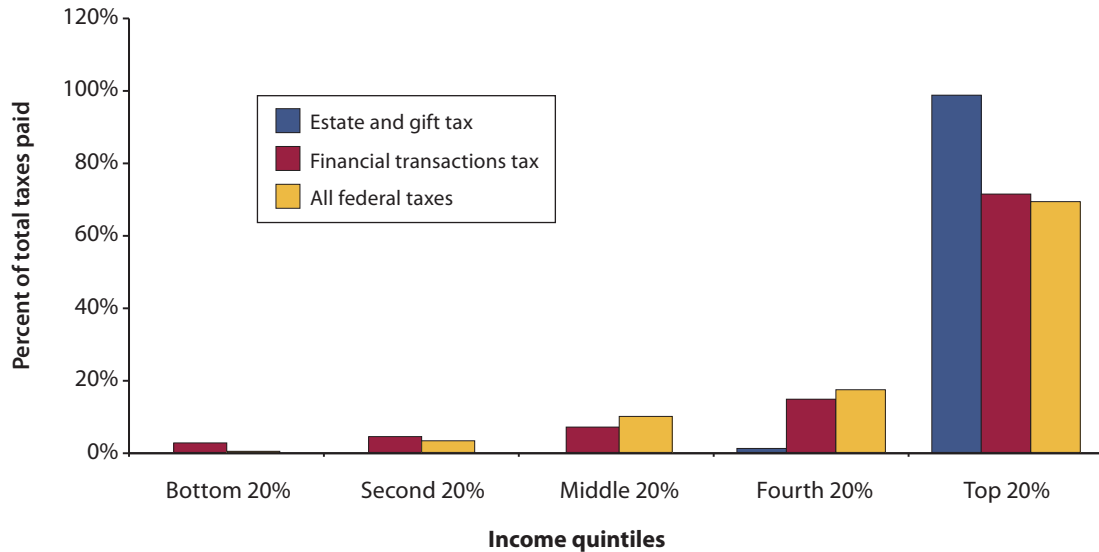
Who would pay the financial transactions taxes?

Probably the best guess as to who will be subject to the tax is to look at who owns financial assets now. A 2009 analysis of data from the Survey of Consumer Finance shows that the mean holdings of financial assets by the wealthiest 10% of households is *45 times* greater than the mean holdings of the bottom 75% of households. In terms of wealth classes, the effect of the tax would therefore be extremely progressive and would help to reverse somewhat the decline in the progressivity of the federal income tax code that occurred between 2000 and 2006.

To make the incidence of an FTT more comparable to other taxes, one can look at the distribution of financial assets across income, not wealth, classes. By this measure, an FTT scores very well on progressivity even when stacked against overall federal taxes and even what is commonly regarded as the most progressive element of the current tax code – the federal estate and gift tax (see **Figure A** on the next page).

FIGURE A

Distribution of all federal taxes, the financial transactions tax, and the estate and gift tax



SOURCE: Tax Policy Center and authors' analysis of Survey of Consumer Finance data.

What would be the economic impact of an FTT?

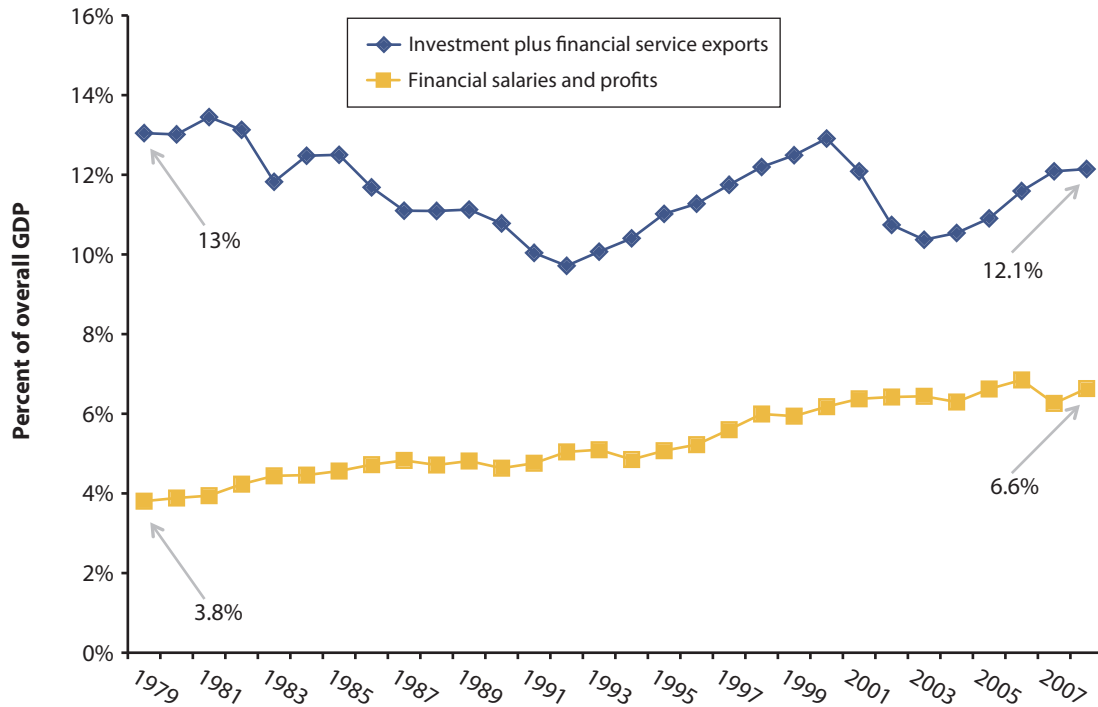
Any newly introduced tax will change behavior and affect economic efficiency. The impact of an FTT depends greatly on how one views the current structure of U.S. financial markets. If one assumes that financial markets are efficient and allocate capital optimally, then the tax will reduce this efficiency by curbing financial activity at the margin. But the current upheaval in global financial markets has undermined this “efficient markets” view of finance and given credence to the “noise trader” approach, which argues that financial markets are prone to speculation, herd behavior, and excess volatility. If this is true, then marginal transactions in financial markets may have zero or even negative social utility.

This noise trader view is bolstered by examining two trends of the past three decades (see **Figure B** on the next page). While the financial sector takes up a larger and larger share of the U.S. economy over that time, increasing by almost 3 full percentage points of GDP (its share was 75% larger in 2009 than in the late 1970s), real investment in plants and equipment (plus financial services exports) is actually less. Given that one of the core functions of the financial sector is allocating capital efficiently, it seems odd that more and more resources are demanded by this sector to do the same amount of capital allocation.

The academic research to-date shows mixed results of raising transactions costs (including FTTs) on asset trading and overall volatility. While there is little in this evidence to argue strongly that a first-order benefit of an FTT would be to rationalize financial markets dominated by noise traders, there is also nothing in this evidence to suggest that an FTT would cause any economic harm.

FIGURE B

High finance: a growing sector does less with more



SOURCE: Bureau of Economic Analysis.

Policy recommendation

We recommend a modest 0.5% tax on financial transactions to pay for the American Jobs Plan. The tax would take effect three years after the implementation of the plan, and at year 10 it would cover the plan's entire cost, making it deficit-neutral.

JOBS CREATED BY THE AMERICAN JOBS PLAN

Each of the five points of the American Jobs Plan would have a significant impact on job creation. **Table 1** shows the estimated first-year impact of each element of the plan.

1. **Safety net spending.** The investments in safety net programs (unemployment insurance and COBRA) would create jobs indirectly because those receiving assistance will have greater disposable income to spend on goods and services. An additional \$110 billion in these programs would increase nationwide employment by 931,000 jobs.
2. **Relief to state and local governments.** Fiscal relief to state and local governments would prevent many public sector layoffs and create jobs in the private sector. States are currently facing several budget crises. For fiscal year 2011 (which starts in July 2010),

state and local governments are facing a \$182 billion shortfall, even after including \$38 billion in Recovery Act assistance for that year. Without assistance, they will be forced to fire public sector employees (such as teachers and first responders), cut programs, raise taxes, or some combination of the three. All of these adjustments would also harm private sector employment, since the reduction in disposable income for those laid off would lead to less consumption of goods and services. Private sector employment would be further harmed as private firms that directly deliver services based on state funding—organizations such as hospitals, nursing homes, and construction contractors—are forced to cut back as well. Additional assistance of \$150 billion to state and local governments would increase employment by about one million jobs. About half of this employment impact would be in the private sector.

TABLE 1

Cost and jobs created under the American Jobs Plan

| Policy | Cost (\$billions) | Multiplier | GDP impact | Job impact (thousands) |
|---------------------------------------|-----------------------|------------|------------|------------------------|
| Strengthened the safety net | \$110 | 1.7 | 1.3% | 931 |
| Relief to state and local governments | \$150 | 1.4 | 1.5% | 1,046 |
| School modernization | \$30 | 1.6 | 0.3% | 239 |
| Public service Jobs | \$40 | | | 1,000 |
| | \$330 | | | 3,216 |
| Job creation tax credit* | \$71 to \$80 | | | 1,420 to 2,840 |
| Total | \$401 to \$410 | | | 4,636 to 6,056 |

* The range is due to different assumptions about the responsiveness of hiring to labor costs. See *The Job Creation Tax Credit* at <http://www.epi.org/publications/entry/bp248/>

SOURCE: Authors' analysis.

3. Investments in schools and transportation. The Recovery Act contained additional funding for the nation's infrastructure, including roads, bridges, and waterways. However, one element that was initially included but then stripped out of the final version was money for improvements to school buildings. Adding \$30 billion to restore school facility funding and adding to other infrastructure investments would boost employment by 239,000 jobs.

These three components of the American Jobs Plan—each of which is an extension or augmentation of the Recovery Act—would in total boost employment by 2.2 million jobs. However, given the severity of the downturn, we must also look to new policy to spur employment in the private sector and to employ people directly to provide public services.

4. Public service jobs. The United States has a long history of direct public service employment in times of economic crisis, and a new program today could be targeted at distressed, high-unemployment communities and provide services such as environmental clean up, community policing, before- and after-school care of children, demolition or boarding up of abandoned houses and buildings, and parks improvements. A \$40 billion investment in public service employment would employ an estimated 1 million people.

5. Job creation tax credit. The job creation tax credit would provide a temporary credit to firms that expand employment. The approach would give businesses a credit of 15% of expanded payroll costs in 2010 and 10% in 2011. The credit could spur an estimated 1.4 to 2.8 million new jobs in 2010 and 1.1 to 2.3 million in 2011.

Taken together, the gross cost of the five components of the American Jobs Plan is roughly \$400 billion in the first year. However, the *net* cost of the plan would be much lower; we estimate that roughly 40 cents of each dollar spent on the plan would be recouped through higher revenue induced by increased economic activity, as well as reduced spending on existing safety net programs.

In total, the extension and augmentation of the Recovery Act together with the public service employment proposal would add about 3.2 million jobs to the economy that would otherwise not exist. A final estimate of the American Jobs Plan is more difficult because of how the tax credit might interact with other aspects of the jobs proposals; however, a conservative estimate would suggest that the total package, using the lower bound estimate of the job creation tax credit, would lead to at least an additional 4.6 million jobs over the first year.

CONCLUSION

To help the tens of millions of Americans who are unemployed or underemployed, Congress and the Obama administration should take bold, decisive action to create jobs. The Recovery Act passed earlier this year helped pull the economy out of its sharp descent. But the American people, who see unemployment as one of the

most important economic problems facing the country, overwhelmingly favor additional action to create jobs. The American Jobs Plan would create at least 4.6 million jobs in the first year alone. Over a 10-year period, the entire cost of the plan would be paid for with a financial transactions tax.

ECONOMIC POLICY INSTITUTE'S Economy Track

Launched in October 2009, **Economy Track** provides the tools to track the recession and unemployment crisis, with the option of focusing specifically on trends by state, race/ethnic group, gender, occupation, and education level. Bringing together up-to-date and historic data, this site also provides important context by comparing the current economic downturn to past recessions. All of the data and methodology underlying Economy Track's graphs are downloadable and fully sourced, with some data available exclusively from this new Economic Policy Institute resource.

Some of the economic trends that can be examined and compared via Economy Track include:

JOBS & UNEMPLOYMENT

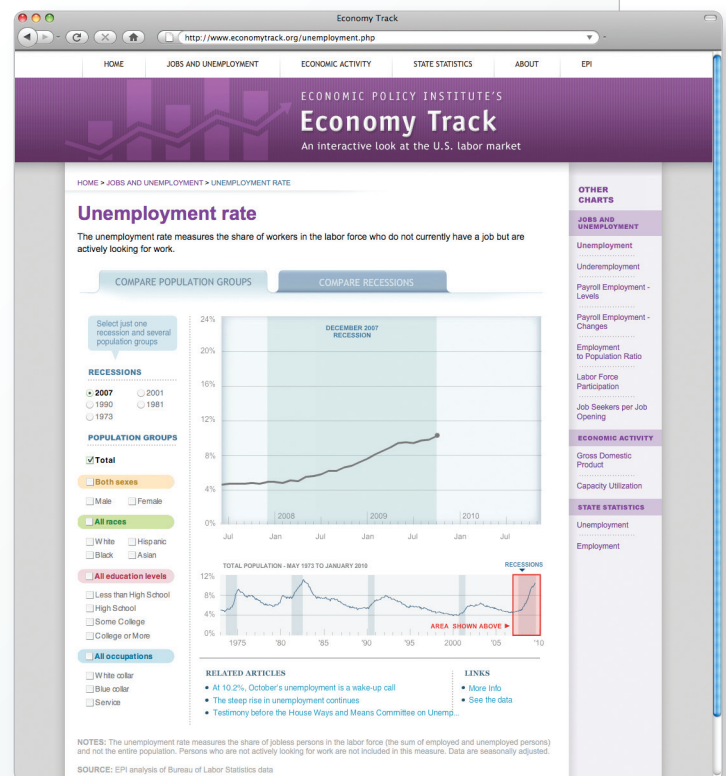
- Unemployment Rate
- Underemployment
- Payroll Employment
- Employment-to-Population Ratios
- Labor Force Participation
- Job Opening and Labor Turnover

ECONOMIC ACTIVITY

- Gross Domestic Product
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ECONOMIC POLICY INSTITUTE

1333 H Street, NW
Suite 300, East Tower
Washington, DC 20005-4707

phone: 202-775-8810

fax: 202-775-0819

www.epi.org

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