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FOR IMMEDIATE RELEASE

Deep Budget Cuts Will Add to Unemployment Rolls at Wrong Time

HARRISBURG (July 9, 2009) – A state budget based entirely on cuts will accelerate Pennsylvania’s job losses and delay any economic recovery in the state when the recession is over, according to a labor economist with the Keystone Research Center.

State House leaders recently announced their intention to produce a no tax-increase budget that will make \$1.7 billion in additional cuts to Senate Bill 850, a bare-bones budget passed by the Senate in May. At a minimum this budget would result in 6,000 state employee layoffs, hospital closures, a more than a billion dollar cut in education funding, and higher local property taxes. The Hospital and HealthSystem Association of Pennsylvania estimates that Medicaid cuts contained in Senate Bill 850 would put 13,000 hospital employees across the state out of a job.

Still, some lawmakers want to resolve the current budget crisis with deep cuts to essential services, including education, health care, and public safety. Governor Rendell and other legislators favor a modest increase in the personal income tax, along with other targeted revenue measures, the use of budget reserves, and cuts to discretionary programs.

Keystone Research Center labor economist Mark Price explained that both tax increases and state spending cuts have an impact on the economy, but budget cuts do more harm than raising taxes during a severe recession. Price has a full analysis online: <http://66.147.242.158/~papolicy/?p=1267>.

Nobel Prize-winning economist Joseph Stiglitz and others have found that tax increases, especially on higher-income earners, are less damaging to the economy than spending cuts.

Price said that is because every dollar in state budget cuts reduces a full dollar of economic activity. Individuals, especially higher-income earners, save a portion of their income, so tax increases remove less than a full dollar of economic activity. As a result, tax increases do not hit the economy dollar-for-dollar like budget cuts do.

“Basic economic principles underlie Governor Ed Rendell's proposal to balance the state's budget in part through an increase in the state's personal income tax,” Price said. “The alternative course of significant cuts in state spending would increase the unemployment rolls at exactly the wrong time.”

“Pennsylvania’s unemployment rate remains about a percentage point lower than the national rate — an advantage that translates into 60,000 jobs,” Price added. “A budget agreement that relies solely on spending cuts would jeopardize that Pennsylvania advantage.”

Additionally, because state income taxes can be subtracted from federal taxable income, taxpayers who itemize deductions can receive as much as a 35 cent reduction in federal taxes for each dollar increase in state income taxes. This would make a tax increase even less harmful to employment than deep spending cuts.

Pennsylvania could target its income tax increase to higher-income earners, through a differentially higher tax on investment income (such as dividends, capital gains, and net profits), Price noted. This can be done in Pennsylvania without a constitutional change because each component of investment income is a separate “class” of income and thus may be subject to a different tax rate under the state’s constitutional uniformity clause.

Price also noted that state spending financed through bonds – in effect, through future state revenues – can be especially stimulating to the state economy in the short run, one reason that bond-financed water and sewer infrastructure and the state’s \$650 million Alternative Energy Investment Fund are so well timed.

*Read a full analysis online: <http://66.147.242.158/~papolicy/?p=1267>. This analysis is provided to Pennsylvania reporters as part of the **Keystone Research Center’s** ongoing tracking of the health of the Pennsylvania economy. The **Keystone Research Center** is a nonprofit, nonpartisan research organization that promotes a more prosperous and equitable Pennsylvania economy*

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