Tufts University | Jonathan M. Tisch College of Civic Life

THE CENTER FOR STATE POLICY ANALYSIS

TESTIMONY

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cSPA Testimony, American Rescue Plan and US Treasury's Interim Rule on Guidance

I want to thank you for inviting me to testify today. It's always a privilege to be able to help the Commonwealth address difficult policy questions.

My name is Evan Horowitz and I'm the Executive Director of the Center for State Policy Analysis at Tisch College, Tufts University, abbreviated as cSPA and pronounced "sea-spa."

cSPA provides timely, relevant research on live legislative topics — in a strictly non-partisan way. Since launching last year, we've done work on state tax revenues, creative approaches to economic aid, police reform, the digital divide, both ballot questions, and most recently on key principles for maximizing the impact of the American Rescue Plan (ARP) in Massachusetts.

ARP counts as a seismic fiscal event — a one-time infusion of federal dollars that is far bigger than the CARES Act and far more flexible than what we got after the Great Recession. Spending this money will be easy; spending it effectively will not.

Today, I want to make 4 main points, which I'll summarize now and then discuss one by one.

> 1) Because ARP provides one-time money, it is best used for one-time investments in things like broadband networks, school building upgrades, state capacity, and public health infrastructure.
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> 2) There may be creative ways to use one-time ARP funding to support longer-term needs, for instance by covering large startup costs or establishing endowments and loan programs.
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> 3) A deliberate, transparent process is vital for keeping track of the many different ARP funding streams and ensuring effective coordination between state and local decision-makers.
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> 4) When spending ARP money, the state will have to navigate some challenging economic feedback loops, including escalating costs for infrastructure projects and the declining utility of Covid-focused public health interventions.

I'm now going to expand on these four points, starting with: *Point 1: One-time dollars are best suited for one-time spending.*

As you know, ARP contains a number of different funding streams, for areas like education, housing, and transit. Here I'm focused on the roughly $5 billion in direct aid to the state of Massachusetts.

Unlike tax revenue, which we collect year after year, this is a one-time gift from the federal government, which we can spend in various ways over a small number of years but which will eventually run out.

Any spending decisions need to reflect the one-time nature of ARP dollars. And the most straightforward approach is to use ARP money for short-term projects that won't require ongoing support.

Fortunately, the options are legion, even after accounting for ARP spending guidelines around public health needs and pandemic-related economic damage. I'll note just a few:

a) Improvements in the air-quality and ventilation systems of public buildings — like schools and libraries — would seem well-positioned to meet ARP's twin focus on Covid recovery and local investment.

b) A surge approach around mental health and substance abuse issues, including hazard pay for health workers and conversion of facilities, could help address the likely scar tissue of the past year.

c) Paying down some of the state's unemployment insurance debt would help businesses who are currently being asked to cover costs clearly attributable to the pandemic (and this use is expressly permitted under ARP spending rules.)

d) A push for universal, affordable broadband would enhance state competitiveness and boost the economic prospects for countless workers and families around the state.

In general, when considering how ARP money can be used, the state should take a flexible approach to federal guidelines, particularly when it comes to investments in racial equity and lower-income communities. Good faith efforts to respond to real Covid-wrought needs in qualified census tracts are likely to be deemed acceptable, which opens up a lot of room for state action and assistance.

Beyond that, there may also be opportunities to exploit budgetary fungibility, where ARP funds free up tax dollars for broader use. This would have to be done carefully, and in coordination with the annual budget process, but the opportunity may justify the effort.

Point 2: Using one-time ARP funding to support longer-term needs

With a careful approach, it is sometimes possible to build durable programs with one-time dollars.

One possibility is for ARP money to backstop endowments and loan programs, setting aside a block of funds today so that you can spend the interest over time or support future lending. Any such effort would need to be targeted to a particular ARP focus, like affordable housing in qualified census tracts, but that could plausibly be done through existing loan programs, like the Mass Housing Partnership or MassDevelopment.

Another way to support long-term state needs with one-time ARP funds is to stand up new initiatives, or introduce pilot programs, with the expectation that their future viability would require regular appropriations and future tax dollars — potentially including money from the proposed millionaires tax.

Expanding early education and childcare opportunities in areas hit hard by Covid would be one option, well within the acceptable bounds of ARP spending rules. And, if successful, those programs could later be extended, or expanded.

Note, however, that this approach creates a potential fiscal cliff when ARP-funded programs suddenly run out of money. And while it may be tempting to think of the millionaires tax as a long-term substitute, its fate is uncertain. However, as the millionaires tax is expected to appear on the 2022 ballot, and ARP funds don't have to be committed until the end of 2024, one way to square this circle is to hold some decisions in abeyance and await the voters' verdict.

Point number 3: the need for a clear, novel, deliberate process

ARP money is substantial enough, and the spending restrictions unique enough, that a separate para-budget process will be required, with different deadlines and a multiyear purview extending through the culmination of ARP spending.

In this regard, the fact that ARP money doesn't need to be fully committed until the end of 2024 has some advantages but also some drawbacks.

On the plus side, it means there will be time for robust debate around spending decisions. Just because federal dollars are expected to reach state hands in the coming months doesn't mean they must be immediately spent; better to make room for careful planning and real deliberation.

However, the multi-year time frame is also long enough to allow for a lot of temporization and can-kicking. Absent a near-term deadline or other forcing mechanism, it could be hard to reach timely agreement among groups with different goals and priorities.

To ensure a better mix of debate and timeliness, it might make sense to put ARP spending decisions on an annual or semi-annual cycle, with interim spending targets.

In addition, coordination and transparency will pose real challenges. Direct aid to the state is just one of a number of ARP funding streams, alongside aid to towns and targeted spending in areas like education. Maximizing impact across these funding streams — and making sure towns and the state are driving in the same direction — will require a new system for information-sharing.

A portal for tracking ARP spending across all levels of government — with corresponding reporting mandates — would be extremely valuable. Alternatively, an oversight panel could be set up, with an ambit to collect information, share data, and issue regular reports.

Point number 4: ARP spending will take place in a volatile economic landscape

The irony of ARP is that while the program gives states large amounts of money to spend on Covid-related public health issues, the need for Covid-related spending is diminishing by the day, as cases recede and the labor market improves. The new normal may well be different from the old, but the urgent challenges of 2023 and 2024 are unlikely to look anything like those of our recent plague year.

What's more, the US economy promises to be extremely robust in the months and years ahead, which creates serious trade-offs for state spending.

We are entering a totally different dynamic from the New Deal or Great Recession scenarios people tend to envision, where government spending helps unemployed workers and stokes dormant economic activity. Jobs are already coming back; travel and restaurants too; consumer spending is at record levels; and one of the main problems with the economy right now is a shortage of essential materials like lumber and microchips.

If, today, the state dedicated a chunk of ARP money to school building upgrades and affordable housing in low-income communities, it would face searing costs for labor and materials, dramatically reducing the social return on ARP investment.

Worse, so long as the economy remains supply-constrained — whether because of supply problems or because we achieve full employment —any large-scale use of ARP dollars will create a bidding war between private businesses and the public sector over scarce resources.

In this scenario, the most effective uses of ARP money may involve efforts to spread out spending via long-term loan programs or debt repayment, as can be done for unemployment insurance. Also valuable would be programs to expand the state's economic capacity through broadband subsidies, targeted workforce training, or incentives to drive opportunity in qualified census tracts.

I'm going to stop here, though I'm happy to answer any questions or share further thoughts. I'm glad to be able to represent cSPA and share some of our findings with you. We're always ready to provide research on topics or issues that you think useful.