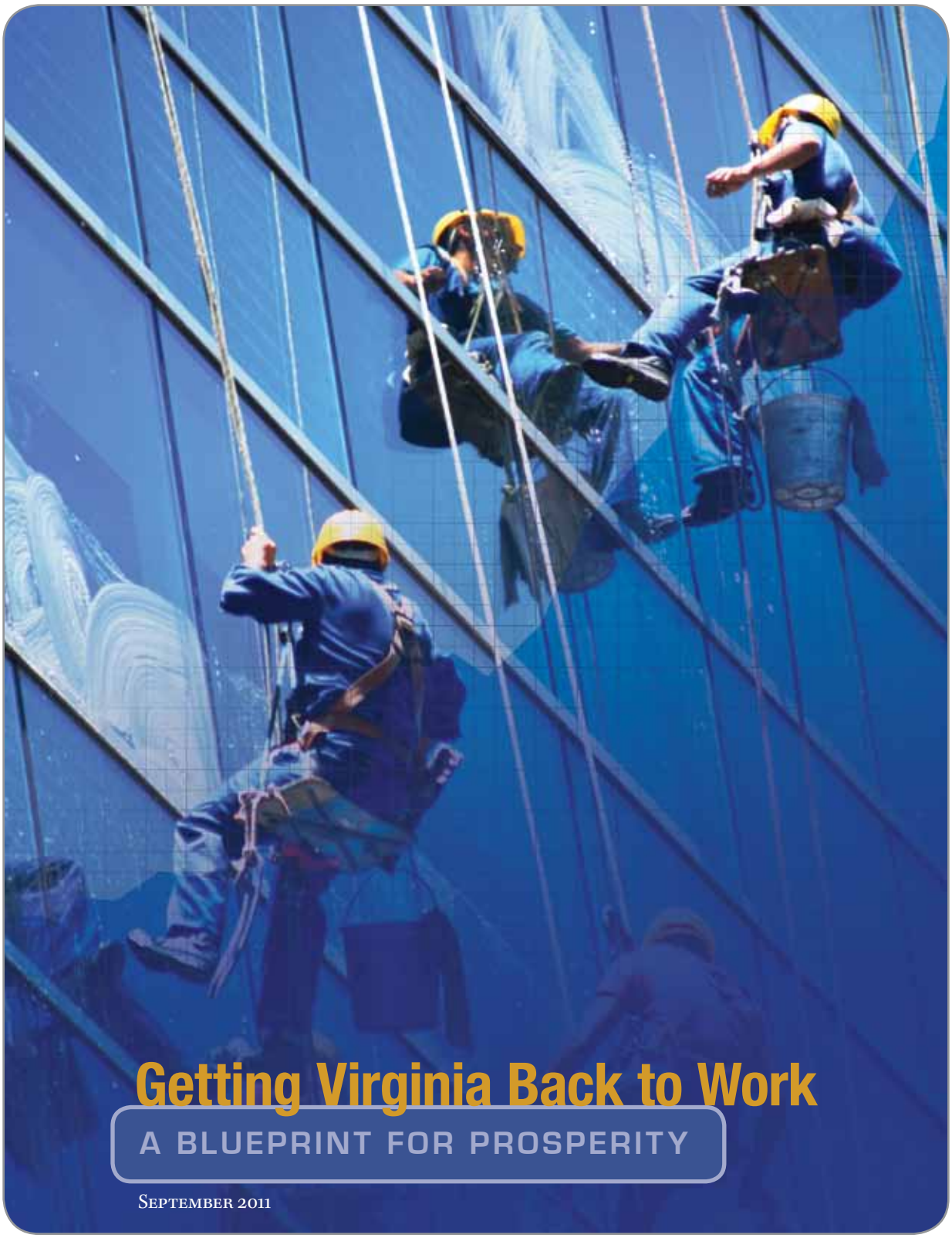

Getting Virginia Back to Work

A BLUEPRINT FOR PROSPERITY

September 2011

The Commonwealth Institute

Introduction: Virginia at a Crossroads

In the middle of the toughest economy we've faced in generations, too many hard-working Virginians have lost jobs, seen their hours or pay reduced, or been forced to clean out their savings just to make ends meet.

Yet, just when we need them most, state services have been cut. Crumbling roads, growing school class sizes, fraying support for families, and other challenges jeopardize our ability to create good jobs and ensure a better future for the next generation.

We don't have to accept this. We can get Virginians back on the job. And not just any job, but jobs that pay enough for families to thrive. Creating jobs in the Commonwealth — and keeping them here — will require that we make Virginia the best place to live, learn, work, and do business. To do that, we must:

- Pave the way for an economy that works (Chapter 1, page 5)
- Educate tomorrow's workers today (Chapter 2, page 11)
- Ensure a healthy and productive workforce (Chapter 3, page 15)
- Create a 21st century revenue system for a 21st century economy (Chapter 4, page 19)

Right now, Virginia's ability to provide the resources to uphold our legacy and invest in a strong economy is in doubt. The recession has been hard on Virginia's finances. Revenues are down significantly since the recession began, while demand for essential public services has increased. As Virginians struggle in a bad economy, they need more help with health care, job training, even putting food on the table. And many of the tools Virginia used to weather the fiscal storm of the recession won't be available anymore. The federal Recovery Act is coming to an end. The state's rainy day fund is mostly tapped out. Virginia is bumping up against its debt limit. Yet, we know we must address the needs of our residents.

We will need to work hard to equip our state with what we need to be good stewards of what we have inherited from previous generations of responsible Virginians, so that those who come after us will have the best possible chance for success.

Pave the Way for an Economy that Works

We need Virginians to be able to work their way into the middle class, not fall out of it. Without a strong middle class we can't have a strong Virginia. We got where we are today because the people who came before us made the right decisions to build schools and roads, make college affordable, and create strong, safe communities – the very things that support a strong middle class. Now, more than ever we need the kind of investments that help to create the jobs that support economic security and stability.

When Virginians hold jobs that provide enough income to live comfortably, they spend more on goods and services, pumping dollars back into our economy. In turn, businesses not only have the capital they need to grow more jobs, but they also have the need for more workers.

The only way to return robust job creation to Virginia is to have an economy that works for everyone. This means we need to protect the rights of our workers and level the playing field for our businesses. To do that, we must ensure that Virginia's workers are paid a fair wage; are given access to reasonable leave time for illness and other family emergencies; are not classified as independent contractors when they aren't; and are supported by an economic structure with responsible economic incentives and a tax code that encourages and supports business investment.

We have seen massive job losses, declining incomes, and evaporating benefits since the recession began. And despite the official end of the recession more than two years ago, Virginia's economy is still sluggish.

Making an already tough situation worse, the recession disproportionately hit those Virginians who were already struggling. Wage growth collapsed for a large share of Virginia workers. Progress in closing key racial and gender gaps in areas such as wages and unemployment has been destroyed. Many Virginians have been pushed out of the labor force altogether. Families feel squeezed by the rising costs of such necessities as fuel, food, higher education, and health care.

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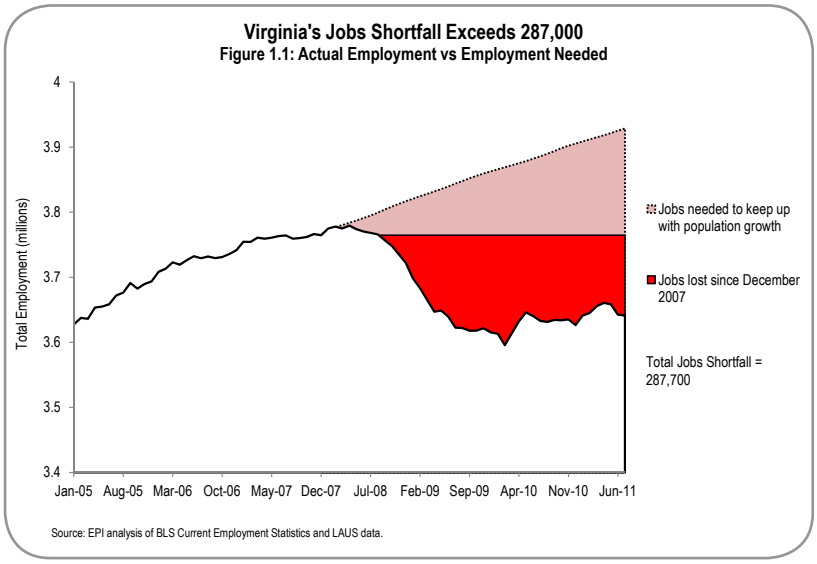
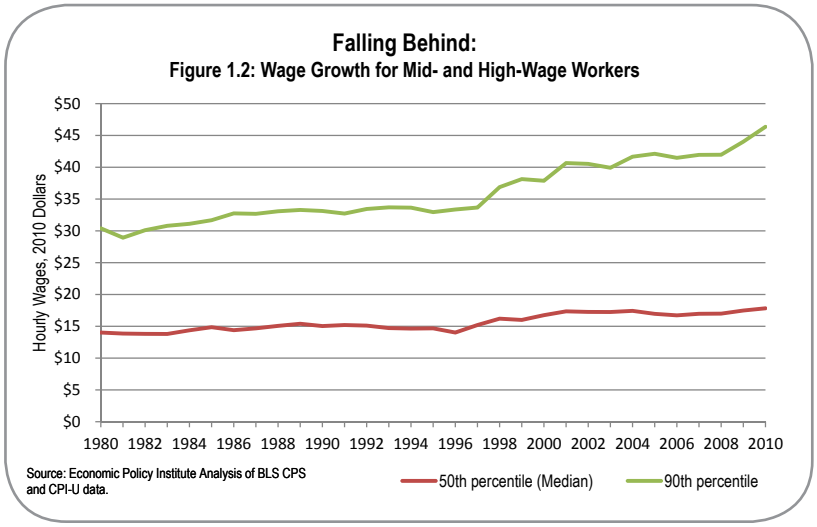
Virginia has resources to tackle these problems, yet we have consistently underinvested in solutions that would support our working families and economy.

With policies that invest in our working men and women, Virginia can rebuild, repair, and revitalize the Commonwealth's economy and create a path to long-term, sustainable growth.

Rebuild Virginia's Middle Class and Increase Financial Stability for Families

The American Dream — working your way into the middle class — is elusive for too many Virginia families today. For those laid off during the recession, finding new employment remains difficult. As of this June, there were still 4.6 unemployed workers for every job opening in the South, according to the Bureau of Labor Statistics. The small number of jobs added in recent months is a drop in the bucket compared to the massive number of jobs lost during the recession. Between December 2007 and June 2009, 125,200 jobs were lost in Virginia; yet only 1,800 were added between June 2009 and July 2011.





This anemic job growth during the economic recovery, combined with Virginia's growing population, means Virginia is short 287,700 jobs compared with before the recession (Figure 1.1). Many young Virginians have been discouraged from even joining the labor market. In 2009, for the first time in generations, fewer than half of Virginians between the ages of 16 and 24 were employed, and it got worse in 2010. While unemployment continues to plague too many Virginians, thousands who still have jobs are hanging by a thread. Many have exhausted their savings and are living paycheck to paycheck. Worries about job security and income have led families to cut back on spending, further threatening the economic recovery.

While many of the problems we face today are linked to the recession, others are part of a long-term trend toward inequality and insecurity that predates the immediate crisis. In reality, the recession exacerbated Virginia's already large disparities in wages and income (Figure 1.2). In 2010, the ratio between the wages paid to Virginia's highest- and lowest-paid workers was the highest ever and the second highest nationally. Despite robust gains by Virginia's highest paid workers, its lowest paid workers have lost ground in recent years.

We have the opportunity to restore Virginia's middle class and improve the financial stability of Virginia's families.

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Invest in middle-class jobs, not corporate giveaways. Virginia's economic development funds provide a powerful tool to create good jobs and set standards for employers. Subsidizing jobs that pay poverty wages, do not offer health benefits, or employ few Virginians makes no sense. Corporate tax credits, economic development deals, and state contracts must include strong, transparent and accountable job creation and job quality goals. Further, there should also be provisions that require companies to repay the state if they fail to create the jobs they promised.

Establish a Virginia development bank. The financial crisis precipitating the Great Recession proved America's financial system is not meeting the needs of the nation's working families, communities, and small businesses. However, Virginia can tilt the playing field back in the favor of average Virginians by establishing a state bank. Serving as a successful model, North Dakota has been operating its own state bank for the past 90 years to the exclusive benefit of North Dakota citizens, farmers, and small businesses. A Virginia state bank would be run as any profitable business. But unlike private corporations, the profits of a Virginia state bank would belong to the citizens of the Commonwealth, not to shareholders and CEOs located elsewhere. In 2009, a year when banks all over the country were struggling, the Bank of North Dakota brought in record profits and asset growth, while continuing to invest in local communities. A Virginia state bank would support state economic development goals by increasing access to capital for Virginia businesses and farms, in partnership with local financial institutions. A Virginia state bank would not compete with local banks, but would partner with them to ensure that Virginia's money is put to work in Virginia.

Help workers find and qualify for jobs. As the economy starts to rebound, Virginia's employers need resources for easily finding local, qualified workers. It's also important for Virginia's workers to have a centralized place to find information on available jobs, opportunities to advance their skills, and access to worker protections. Virginia should invest in a network of strong workforce development centers to facilitate such matches.

Strengthen Virginia's Earned Income Credit (EIC) to make work pay. Virginia allows families who receive the federal Earned Income Tax Credit to take 20 percent of the value of that credit and apply it against the state income taxes they owe. Earned income credits have a proven track record of providing incentives to work, reducing poverty, helping struggling families, and stimulating local economies. To ensure that the program reaches its full potential, Virginia should continue to conform to the enhanced version of the federal EITC adopted in 2009. The state should also make the state's Earned Income Credit refundable, so low-pay workers who owe no state income tax can use the credit to offset other taxes — such as sales, excise, and property taxes — that disproportionately hit low-income Virginians. With more cash to spend, low- and moderate-income workers are able to put money back into the local economy.

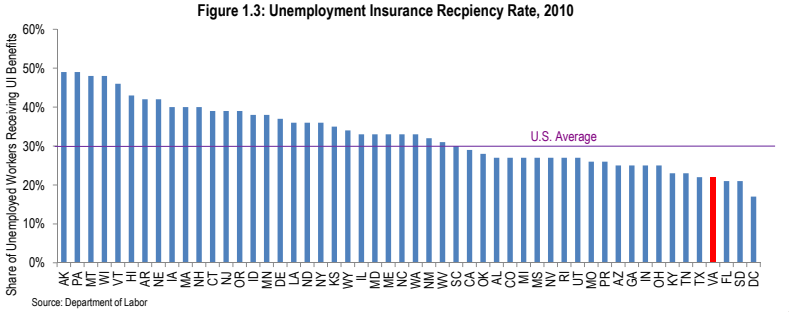
Create portable retirement accounts for workers at Virginia's small businesses. Most Virginians would like to save more money for retirement, but many lack the easiest, most reliable means to do so: automatic deductions from their paycheck that get placed into a 401(k), IRA, or the equivalent. For many small businesses, the time and effort needed to set up such accounts for their workers keeps them from providing this option. Additionally, most workers will have a number of different employers during their lifetimes, meaning they may have to keep track of a variety of accounts. Creating a publicly managed system of portable retirement accounts would make saving a much more realistic option for many workers. This will enable more Virginians to support themselves after they retire, reducing the long-term demand on state services such as Medicaid and housing for low-income seniors.

Protect Virginia Families During Tough Times

During tough times, Virginia needs targeted, responsive ways to quickly get struggling families back on their feet. This makes good economic sense as well as being the right thing to do. Putting money into the hands of families is one of the fastest, most efficient ways to stimulate job growth. Families spend in their local communities and provide a much-needed boost to local businesses. Small businesses can't grow and hire unless their customers have money in their pockets.

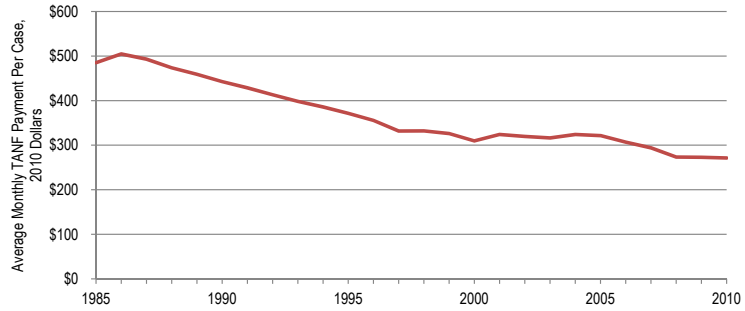
Policies that help keep Virginia's working families afloat when they fall on hard times are a key component of a vital and sustainable long-term economy.

Bottom of the Barrel:
Figure 1.3: Unemployment Insurance Recpiency Rate, 2010



Source: Department of Labor

Helping Less:
Figure 1.4: Average Monthly TANF Payments (2010 dollars)



Source: TCI analysis based on data from BLS and Virginia DSS.

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Remove barriers to obtaining food.
The Supplemental Nutrition Assistance Program (formerly called food stamps) helps many working, retired, and unemployed families put food on the table. While the federal government pays for the cost, states manage the system for enrolling eligible families. Virginia should do all it can so that everyone who is eligible gets this key support during tough times. This includes

- Improving public awareness of the availability of SNAP
- Allowing low-income families to receive SNAP even if they have some savings, thereby encouraging families to save more
- Accounting for the recent spike in heating costs through raising the gross income test

Remove unreasonable barriers to unemployment compensation. Out-of-work Virginians are less likely to receive unemployment insurance than the unemployed in almost any other state (Figure 1.3). Fewer than 22 percent qualified for Virginia unemployment insurance in 2010, compared to 30 percent of unemployed workers in the country as a whole, according to the federal Department of Labor. The small share of Virginia workers receiving unemployment compensation is caused by a number of factors including overly stringent eligibility standards. For example, Virginia is one of just four states that does not allow job searches using the telephone to count toward the weekly work search requirement.

Create a voluntary work-sharing program. A "work-sharing" program provides employers with an alternative to layoffs during a temporary decline in business. In such an arrangement, the wages and hours of some or all employees may be reduced, and affected employees may qualify for partial unemployment benefits to help make up for lost wages. Layoffs create economic and emotional hardship. By providing a layoff alternative, both employers and employees benefit. Employers are able to retain their trained employees, positively positioning them for recovery, and employees are able to maintain a level of financial stability while also keeping any health insurance and retirement benefits. At least 18 states already operate these special unemployment insurance programs.

Reverse the erosion of TANF support for low-income children. The purchasing power of Temporary Assistance to Needy Families (once known as welfare) payments has not increased since 2000, despite a nearly 25-percent increase in the cost of food, housing, clothing, and other necessities in the past 11 years (Figure 1.4). Virginia should restore its commitment to low-income children by increasing the value of TANF payments to 2000 levels. For a family of three in the Richmond area, this change would mean a maximum payment of about $400 per month, with some families getting less. And Virginia should require that TANF payments rise automatically with inflation every year.

Protect the Rights of Virginia Workers and Level the Playing Field for Virginia's Businesses

To have an economy that works for Virginia's employers and employees alike, the state must help make sure that everyone plays by the rules of the game. However, abusive practices by some undermine the good faith efforts of employers and employees whose hard work contributes to the schools, roads, and public safety system that lay the foundation for a strong economy and prosperous future.

Historic advances in workers' rights were a major factor in the country's recovery from the Great Depression. A renewal of these protections will provide economic security for working families and uphold the hope that everyone who is willing to work has the means to support his or her family.

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Crack down on misclassification of workers as independent contractors. When workers are misclassified as independent contractors, they lose the benefits of regular employment such as employer-sponsored health care and access to unemployment compensation in case of layoff. Studies have shown that 10 to 30 percent of employers misclassify employees as independent contractors, costing state and federal governments billions in unemployment insurance payments, workers compensation payments, and income taxes. This misclassification hurts workers by denying them access to core protections during tough times. Misclassification of workers tends to be clustered in certain industries, making targeted audits highly cost effective.

Make sure workers are paid the wages they earned. When labor standards are not enforced effectively, unscrupulous employers can get away with practices such as wage theft and hiring workers under the table, which can give them an unfair advantage at the expense of their workers. Cracking down on employers who cheat their employees by not paying for overtime, requiring workers to attend meetings or trainings without pay, or reneging after-the-fact on wage agreements would help the majority of Virginia's employers who play by the rules and protect Virginia's most vulnerable workers. Due to fear of retaliation, lack of knowledge of their legal rights, or lack of access to a lawyer, many workers today are unable to protect their basic rights.

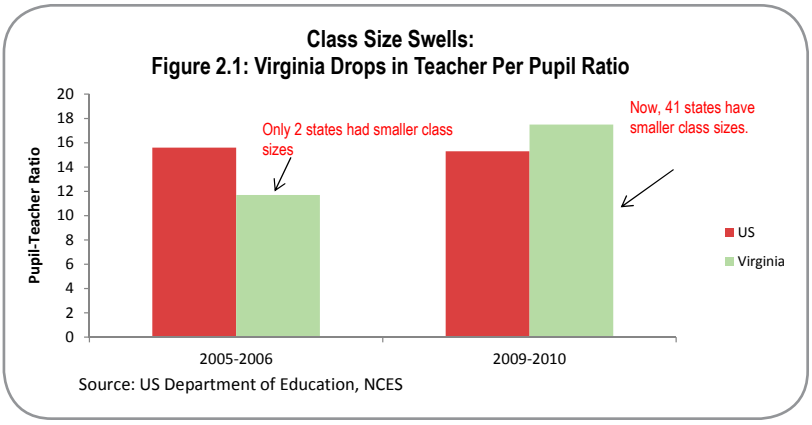
End poverty wages and restore the minimum wage. Although wages for the median worker in Virginia grew 27 percent in the past 30 years, adjusted for inflation, the value of the minimum wage fell by 12 percent. Today's $7.25 an hour minimum wage sets such a low floor that Virginia fails to protect both low-wage workers and decent employers who are undercut by their competitors who pay poverty wages. Virginia should restore the minimum wage to its 1968 purchasing power of about $10 — $5 for workers whose income is substantially from tips. And the minimum wage should automatically go up every year to reflect changes in prices so the lowest paid workers do not constantly fall further behind.

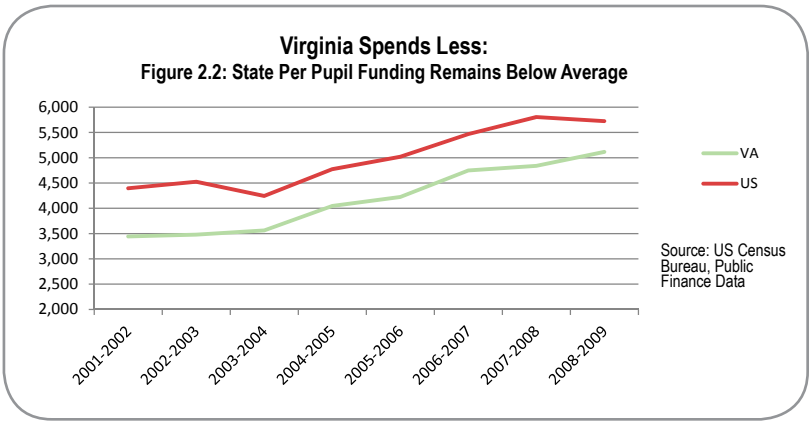
Give all workers access to paid sick time and family leave insurance. When workers are not guaranteed paid sick time or family leave insurance, they endanger the public health by incentivizing employees to show up for work while ill. No one should lose their job because they get sick, and no parent should have to choose between caring for a child and keeping a roof over their heads. For many families, a few days of lost wages or unexpected expenses due to a child's illness or a broken-down car can spell disaster. Recent analyses of the effects of mandatory paid sick leave laws show no negative impact on job growth or business growth, consistent with a large body of literature showing paid sick leave to be beneficial to workers and employers through increased productivity and reduced spread of illness. In addition to the public health benefits associated with paid sick leave, family caregiving has an economic value of $9.9 billion a year in Virginia, according to a 2007 study by the Family Caregiver Alliance, and helps reduce Medicaid and long-term care costs.

Educate Tomorrow's Workers Today

The state's changing economy places a premium on preparing Virginians for tomorrow's jobs. In fact, attracting businesses to the state depends on it. Companies invest in a location if the schools there will produce the skilled workforce they need, so we owe it to our children and ourselves to invest in world-class public education.

The economic downturn of the past few years has taken a serious toll on education. Virginia's level of investment in K-12 education has fallen significantly below where it was before the recession. In recent years the state has slashed basic support for important services such as early reading intervention, school buses and reduced class sizes in the lower elementary school grades. These reductions have diminished the quality of education throughout the Commonwealth. Just a few years ago, Virginia had a great atmosphere for learning – the third smallest class size in the nation. Today, it's 41st (Figure 2.1). Class size reduction programs are essential — children need smaller class sizes so they can pass standardized tests and continue to achieve academic success. While the cuts in spending have jeopardized all of Virginia's public school students, children of low-income families are especially vulnerable, as they may be underfed and unprepared for success in school.





By cutting state support, the Commonwealth shifts more costs to local communities at a time when they, too, face reduced revenue from dramatically reduced property values. Because K-12 education is financed primarily by local property taxes, some communities can afford to raise more money for public schools than others. Communities with high property values and high tax rates can generate more money for the school system, while less affluent communities struggle to provide basic facilities and pay competitive wages to teachers.

Soon, another source of funding will be cut, when federal stimulus money expires before the end of the academic school year. The Federal Recovery Act pumped billions of dollars into the public school system helping to stave off even more teacher layoffs and severe cuts. Without increased funding to make up for the loss, the school systems are in danger of seeing even more cuts.

By embracing reforms in key policy areas, Virginia can make sure that every child has the opportunity to succeed in school today and to be productive tomorrow.

Restore State Funding for K-12 Education

Giving every Virginia child a chance at the best possible education is the best way to ensure that tomorrow's innovators and entrepreneurs are Virginians. But, Virginia's public school funding system is among the least fair in the United States, according to a recent national study by the Education Law Center. Not only did the state score a low grade for the amount of money it spends on public education but it also scored poorly in how that money is distributed. Virginia spent only $5,115 per student in 2008-2009. Our rank for state per-pupil funding dropped to 35th in 2008-2009 from 33rd in 2006-2007 (Figure 2.2). The state spends much less compared to our surrounding states and the nation. Maryland invests 32 percent more than Virginia in K-12 education, spending $6,752 per student; West Virginia spends $6,636 per student. The national average is $5,729.

Virginia has the capacity to adequately fund the public school system and provide a high quality education to all.

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Fund Schools to Provide a Skilled Workforce. By increasing the amount of state revenue invested in its schools, Virginia can get its spending per-pupil amount where it needs to be. When the state does not fulfill its share, larger total budget reductions occur. Less affluent school divisions depend primarily on state aid to fund their budgets. Raising the state share will provide a more equitable funding stream, lessen the financial burdens on schools, and control for funding disparities across localities. Today, the state picks up about 42 percent of what it costs to run schools — leaving 52 percent to localities (the federal government contributes 6 percent). Nationally, the average state contribution is 47 percent, leaving 44 percent to the localities and 9 percent to the federal government. This heavily unbalanced mix of funding shortchanges local schools in less affluent areas and limits the opportunity of students across the Commonwealth. Because of state budget cuts to K-12 education, localities have spent an extra $3.2 billion a year in education expenses just to keep schools open and provide basic services to students. The state must close the gap between state funding and the amount local school divisions are required to spend to be sure the quality of education is the same throughout the Commonwealth.

Decrease class sizes. Teacher layoffs, school closings, and reductions to programs have caused class sizes to balloon across the Commonwealth. A few years ago Virginia was ranked third in the nation for having 11 students per teacher in each classroom. Now, each classroom has 17 students per class compared to the national average of 15 students per classroom. According to a 2009 report to the Virginia Department of Education, smaller class sizes are especially beneficial for reading and math achievement and for low-income and minority students.[1] Virginia has a program in place that can produce results. Virginia's K-3 Class Size Reduction program was created in 1994 to help schools with high concentrations of at-risk students reduce class sizes below 24:1, but funding cuts have limited progress in making substantial reductions. A similar program in Tennessee (Project STAR) found that smaller class sizes in K-3 created 11 new graduates per 100 students. Virginia must continue to invest in class size reduction programs because they are essential and pay for themselves in the lifetime of a student.

Keep our teachers. A quality education, begins with the teacher. With school enrollment on the rise, it is important for the state to hire and keep high quality teachers. However, since 2007, there have been 1,200 fewer teachers in public schools across the Commonwealth. Investing more state funds in K-12 education will provide resources to hire highly qualified teachers and pay competitive wages. According to the National Education Association (NEA), in 2009-10, the average salary for teachers in Virginia was $50,015. This is $5,187 less than the national average and $4,722 less than the average of the Mid-Atlantic states.[2] Paying decent wages to teachers is critical to the success of our public schools. Better salaries would allow the state to recruit and retain the best teachers. Low teacher pay comes at a high cost for schools and children, who lose good teachers to better paying jobs. Education research shows that teacher quality is the most important schooling factor influencing student achievement.

Make Sure Students' Nutrition Needs are Met

Hungry children focus on their need for food rather than their studies. Ensuring that our children get the nutrition they need can help us meet our educational and economic goals. This is too big a problem to leave only to parents, especially with more than 750,000 Virginians living in poverty. Even more disturbing, 47 percent of the state's children are more likely than adults to live in poverty. Unfortunately, based on recovery models from prior recessions, poverty rates will continue rising through 2011. Facing anemic job growth and battered wages, many families are still living on tight budgets and can't afford to provide a nutritious breakfast at home or buy lunch at school.

Virginia should implement a Food Action Plan to make school meals more widely available. This makes sense for a number of reasons. Properly nourished children more actively participate in the classroom and perform better on standardized tests. Studies show students who eat breakfast have higher math and reading scores. A Food Action Plan will not only reduce hunger, but also has the potential to improve other outcomes, like increasing school achievement, boosting family income, and supporting child development.

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Expand participation in school breakfast. Breakfast is essential to waking up your brain and body, especially for school-aged children. Research has linked eating school breakfast to better academic performance. There are more than 1.2 million students enrolled in Virginia's public schools but only 196,000 participate in the federal School Breakfast Program (SBP) every day.[3] Since the federal SBP is an entitlement, the program has room to grow when the economy is weak. More children have become eligible to receive free or reduced breakfast during the economic recovery, giving Virginia even more incentive to maximize participation rates across the state.

The state can do this in several ways. Being sure each child has access to breakfast is the first step. Several states have explored the option of providing universal breakfast in all public schools as well as serving breakfast in first period classrooms. A recent report by the Food Research and Action Center, found that school districts that offer breakfast in the classroom free to all students have the highest participation rates.[4] Not only will hungry children reap the benefits of free breakfast but also families with battered incomes will receive some relief by not having to purchase school meals.

Expand access to summer meals. School ends in the summer, but of course young peoples' nutrition needs continue. Many are at a higher risk for both hunger and obesity because they lose access to regular, nutritious school meals. The Virginia Summer Meals for Kids Program, funded by the U.S. Department of Agriculture, provides children free summer meals at hundreds of sites across the Commonwealth. However, more than 80 percent of the 466,000 eligible for free and reduced school meals don't participate.[5] The state should improve outreach and expand the number of locations serving food to school-aged children.

Make use of available after-school meal dollars. A new federal nutrition law expands the ability of states to receive federal reimbursements for feeding low-income children after-school meals. These meals require no state or local matching funds. The amount available could reach nearly $133 per child each school year.[6] Virginia could boost participation in this program by assuring that all publicly funded after-school programs serving meals receive the federal reimbursements.

Strengthen the Virginia Preschool Initiative

When children start school behind, they stay behind. Education reform begins with high-quality preschool. Investing in early childhood education can bring huge cost savings and increased economic benefits to the state. The Virginia Preschool Initiative (VPI) serves at-risk 4-year-olds by providing comprehensive early education, health and social services, transportation and ways to stimulate parental involvement. Research on the effectiveness of this state-funded program demonstrates high returns. A recent study conducted by the University of Virginia found students who attend VPI programs show improved performance in kindergarten and first grade compared to students who did not attend preschool at all.[7] Also, in 2007 the Joint Legislative Audit and Review Commission (JLARC) documented higher literacy scores in kindergarten and higher 3rd grade Standards of Learning pass rates for at-risk children participating in VPI. They also outperformed other kindergartners on the Phonological Awareness Literacy Screening (PALS) kindergarten test. Teachers report that VPI students are more prepared academically and socially to enter kindergarten.

Without providing high-quality preschool to all at-risk 4-year-olds, many at-risk 5-year-old children will continue to enter kindergarten without adequate skills. The primary goal of Virginia's targeted pre-K system is to improve schooling for disadvantaged children, which clearly is in the state's best interest. The state should continue to invest in this program to allow disadvantaged students the same opportunities. VPI deserves support for all the returns on investment it brings. There are options the state could use to strengthen VPI and give a greater number of at-risk 4-year-olds access to preschool.

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Help school divisions find solutions for funding. One sure way to close the achievement gap is to give more children access to preschool. VPI has experienced a 21 percent uptick in enrollment since 2008, with more than 15,700 children having access to the program. As impressive as that is, the number of at-risk 4-year-olds in Virginia continues to be a concern because for every low-income 4-year-old attending VPI, there is at least one who could participate and is not. VPI funding is split between the locality and the state. Children are often turned away because local school divisions can't afford to pay their share. The state must work with local school divisions to remove funding barriers to give a greater number of disadvantaged children access to quality preschool. The state can work to lower the local match requirement to encourage participation and provide funding incentives to enroll more children. Early childhood education is important if we want to remain a leading state in providing a quality education to all.

Encourage school divisions to create partnerships with private providers. With recent upticks in enrollment and a growing population of school-aged children, schools simply have run out of space. The state should work to encourage school divisions to establish private partnerships to be sure each VPI slot is filled. More local school divisions have reached out to private providers to host students who could not be accommodated by public schools. During 2010-2011 school year, about 1,600 children attended VPI in a private classroom and the list is growing. The state should encourage this practice until all students in need are served. Virginia can promote collaboration with private pre-K programs by providing incentives for school divisions that fill all unused VPI slots through private partnerships.

Ensure a Healthy and Productive Workforce

Healthy men and women are more productive workers. Yet Virginia faces significant challenges in making sure that everyone has access to the quality care they need. About one million Virginians, including more than 130,000 children, remain without health insurance coverage according to Census Bureau data (Figure 3.1). Many more struggle to afford insurance, a situation compounded by the fact that many employers are paying a smaller share of premium costs than in the past and that overall costs are rising.

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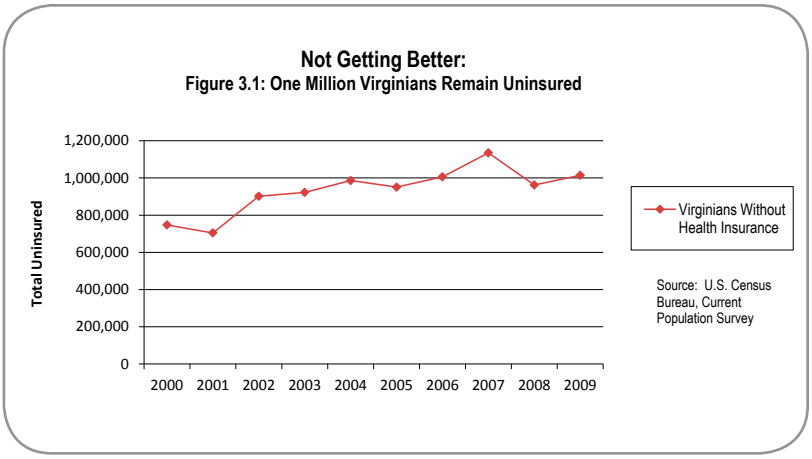
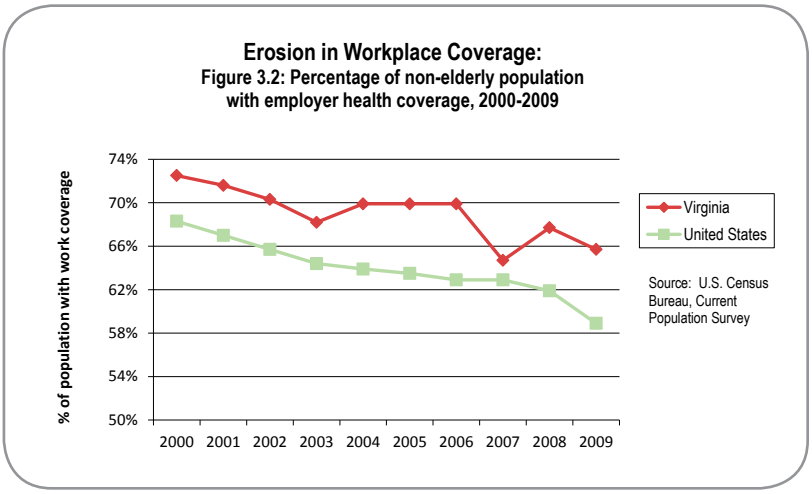
p16 Design and Implement a Health Insurance Marketplace that Works for Small Business and Consumers

p17 Protect Medicaid and Children's Health

In fact, in the past decade, the share of Virginians who receive health coverage through employers has fallen by nearly 10 percent, according to the U.S. Census Bureau (Figure 3.2). For Virginians who don't have the option of coverage through an employer, buying insurance is even harder. Less than 5 percent of Virginians purchase their insurance in the non-employer market because it costs far more than what working families can afford.



In addition, Medicaid in Virginia — which serves those unable to afford coverage on their own — ranks 48th in the nation in per capita spending. Children face similar difficulties, as income eligibility for the state's health insurance program for children (called FAMIS in Virginia) is more restrictive than in 42 other states.[8] And parents of low-income children generally cannot gain access to Medicaid for themselves if they make more than $7,000 a year.



Despite these challenges, Virginia is well positioned to make the changes necessary to meet everyone's health care needs. By embracing reform efforts in several policy areas, Virginia can significantly improve the quality of life for all Virginians. We must protect our health care community – one of the fastest growing sectors of our economy – from provider payment cuts that often result in fewer doctors and nurses willing to see patients with public health insurance coverage. We have to honor our commitment to families who have fallen on tough times. By protecting public health care programs, all our children can grow up to be productive, and workers who have fallen on hard times can focus on getting back to work.

Design and Implement a Health Insurance Marketplace That Works for Small Business and Consumers

The new national health care law (the Affordable Care Act) presents the Commonwealth with new challenges, but, more importantly, significant opportunities. One of the key features of the new law helps make sure everyone can access affordable health coverage. The Virginia health benefit exchange, scheduled to begin in 2014, will be designed as a Web-based health insurance marketplace where Virginia consumers and small businesses can shop for health insurance.

Virginia's current non-employer marketplace does an inadequate job of providing affordable health coverage options. The new exchange will provide premium assistance for those with low and moderate incomes looking for coverage. Businesses with up to 50 employees will be able to access the exchange to provide health insurance for their workers. According to a federal survey, only 37 percent of businesses in Virginia with fewer than 50 employees now provide insurance to their workers. So this will be an important step forward.

For the exchange to be successful, however, it must be accessible to Virginia consumers.

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Develop a Web-based enrollment system allowing easy access to affordable health insurance options, with detailed information on price and quality. Most small businesses will access the health benefit exchange through the Internet. It is critical that Virginia's exchange be user-friendly and displays health insurance options transparently. Each health insurance option should contain basic and easily presented information on price and quality, so people have enough information to make informed choices. Additionally, many consumers accessing the exchange will be eligible for Medicaid or FAMIS and the exchange should seamlessly direct them to the coverage for which they are eligible.

Make consumer representatives part of the governance of the exchange and prevent anyone with a direct financial conflict of interest from serving on a governance board. Consumer representatives, especially those with expertise in working with low- and moderate-income Virginians and those who work with diverse communities, can help the exchange work for Virginians who need health insurance. It will be important to prevent those with direct conflicts of interest from making decisions regarding the health benefit exchange. For instance, insurance company employees will have a direct conflict because the decisions of the board might have an impact on their financial situation. Of course, their expertise can be used in an advisory capacity, but they should not be making direct decisions on the how the new marketplace will run.

Provide a level playing field by requiring all health insurance plans in Virginia to follow the same rules. Health insurance will not be affordable for many consumers in the exchange if insurers operating outside of the new marketplace target younger, healthier Virginians with bare-bones health plans. This would create a situation where the exchange is populated heavily by less healthy persons who need assistance in paying for premiums and other cost-sharing, driving up premiums and making the insurance options less attractive. Virginia should create an equitable system that requires all health insurance plans, regardless of where they are sold — inside or outside the exchange — to operate under the same rules.

Protect Medicaid and Children's Health

More Virginians can play their part in the state's economy if they have the resources to maintain good health. But Medicaid in Virginia provides those resources to fewer residents than most other states.

While many states have expanded eligibility to make their Medicaid program more responsive to the needs of their citizens, Virginia has mostly chosen to follow only the minimum federal requirements in program eligibility.

The result is:

- More than half of the state's Medicaid enrollees are children with family incomes at the federal minimum of up to 133 percent of the federal poverty level.
- Our FAMIS program only covers children up to 200 percent of the federal poverty level.
- For the elderly, blind and disabled populations, Virginia generally covers individuals up to only 80 percent of the federal poverty level, only slightly higher than the minimum requirement of 74 percent.
- For non-disabled or elderly adults, where there is no federally imposed minimum, Virginia still falls well below most other states.
- A non-disabled adult parent (with two children) with an annual family income more than $7,000 is unlikely to be able to access Medicaid in Virginia.

During the economic downturn and recession, Virginia made significant cuts in Medicaid payment rates to hospitals, nursing homes, and other providers, and also limited access to Medicaid for developmentally and intellectually disabled Virginians. Further cuts to Virginia Medicaid could limit coverage even more, especially for children, the elderly and disabled in the state.

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Actively speak-out against proposals to convert Medicaid into a block grant. Recent estimates suggest that Virginia would have received 25 percent less in federal Medicaid money in the past decade under a block grant program similar to what some members of Congress have proposed. Under a block grant system, states would be allowed to reduce eligibility for low-income children, seniors and others who have previously had secure insurance coverage.

In addition, Congress is considering whether to rescind the maintenance-of-effort (MOE) requirement that has prevented states from reducing Medicaid eligibility in recent years. In the past two years, the MOE has prevented Virginia from making deep cuts to Medicaid eligibility for the elderly and disabled, as well as a reduction in eligibility for FAMIS that would have resulted in 30,000 children losing health insurance coverage. Medicaid in Virginia is a lean program not characterized by excess. Cost increases have been driven almost entirely by increased enrollment and rising health care costs, not poor management or ill-advised state decisions. A federal block grant, especially in an economic downturn when enrollment naturally increases because fewer people can afford their own coverage or to get it through employers, would likely result in the state further limiting eligibility and enrollment for children and others who need access to basic health care.

Position Virginia to successfully implement the 2014 Medicaid expansion that will provide coverage to more low-income working Virginians. Virginia and all states will expand Medicaid to cover all non-elderly consumers with incomes up to 133 percent of the federal poverty level in 2014. The expansion will be entirely funded by the federal government until 2016. Then the federal share will decrease slightly, reaching a 90-10 federal/state split by 2020. Since Virginia's Medicaid has one of the lowest income eligibility requirements for adults in the country, the state will benefit more than most other states from the generous federal support.

This expansion presents a tremendous opportunity for Virginia to reduce the number of people who lack health insurance. As many as 425,000 Virginians are expected to gain coverage through Medicaid expansion. Additionally, policymakers should resist rescinding the MOE requirement, an action that could result in reduced federal support and tightened FAMIS eligibility, which would threaten coverage for tens of thousands of Virginia children who need health care.

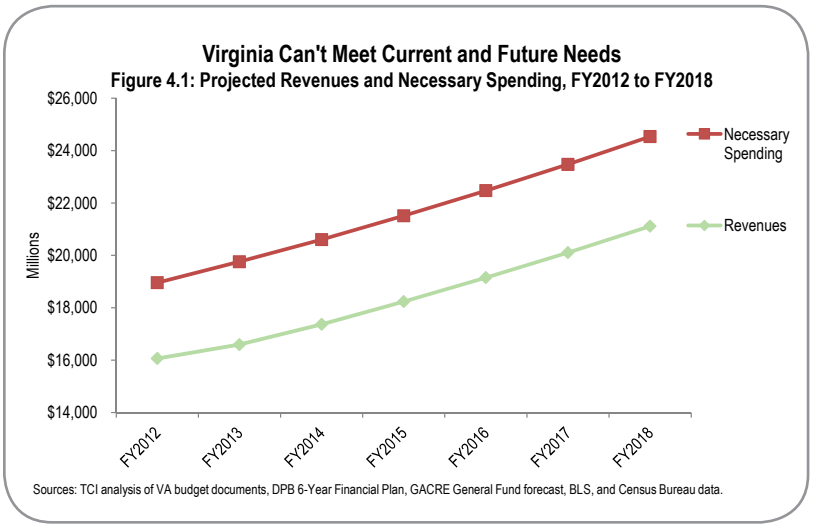
Chapter 4

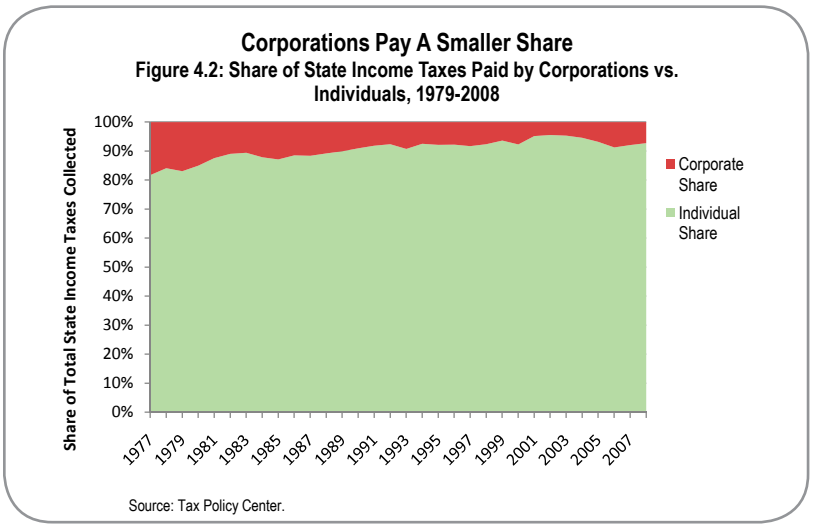
Create a 21st Century Revenue System for a 21st Century Economy

Virginia's system for raising the resources necessary to meet public needs was designed for yesterday's economy. By eliminating old and ineffective tax breaks we can avoid needlessly giving away millions of dollars a year to large corporations while raising tuition for our college students, placing children in more crowded classrooms, and risking public safety and quality of life. That's a bad deal. By reforming Virginia's corporate income tax, we can close loopholes that let big businesses avoid paying their fair share. And by modernizing our income and sales taxes we can make sure that we're funding our state in ways that better reflect the realities of the modern economy.

Virginia has ignored the reality of income distribution in failing to update state income tax brackets and rates for nearly 25 years. Additionally, the state sales tax has not kept pace with consumer spending trends that have shifted dramatically from goods to services in our economy. Compounding the problem, old and ineffective tax breaks and credits are not regularly evaluated for their effectiveness, despite a price tag estimated to be in the billions of dollars every year.

BLUEPRINT





While the recession is clearly to blame for much of the state's continuing fiscal shortfalls, the downturn also has revealed some serious problems with the state's revenue structure. Virginia faces a yawning gap between revenues and needs. Without action, even if economic conditions improve, we will not have the resources to maintain Virginia as one of the best states to live, learn, work, and do business.

For too long Virginia has responded to the problem of inadequate resources with cuts to the very services that help build a strong economy in the first place. By reducing the state's level of investment in public structures – slashing support for K-12 education, cutting payments to health care providers, putting off proper maintenance of our infrastructure, and borrowing from the state retirement plan — we have placed our immediate security and future prosperity at risk.

Virginia's cuts-heavy approach has reduced current investment far below pre-recession levels. And even this reduced level of support for public needs can't be maintained without changes to the tax system. As shown in Figure 4.1, new revenue is critical to keeping Virginia on the road to recovery and positioning it for a prosperous future.

There is another way. Through key reforms to Virginia's tax code, we can adopt a balanced approach that includes revenues instead of over-relying on service cuts.

Reform Virginia's Corporate Income Tax So Businesses Pay Their Fair Share

Virginia has struggled with inconsistent and declining corporate income tax revenues in recent years. More than 60 percent of corporations in the state pay no corporate tax at all, according to the state Department of Taxation. Many large, multi-state corporations use complicated accounting gimmicks to reduce their tax bills in Virginia. Closing loopholes in the corporate income tax and eliminating specific corporate tax giveaways could provide more than $100 million in new revenues to meet public needs each year.

Virginia's largest source of revenue is the state's income tax, typically accounting for about 70 percent of the general fund. Yet, in the past 30 years, corporations have paid less and less while individual workers and families have had to make up the difference (Figure 4.2 on page 19). Since the late 1970s, the share of the income tax paid by corporations has been cut roughly in half. Meanwhile, in 2008, individuals paid 92 percent of the total income taxes collected by the state.

Companies doing business in the Commonwealth benefit from Virginia providing a productive workforce, a means of transporting their products, and a legal system to protect their property rights. Through a few key technical reforms, Virginia can bring in significant new revenues, while also working to make sure that all who benefit from state services pay their fair share in funding them.

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Enact mandatory combined reporting. Today, many large, multi-state corporations can shift income earned in Virginia to subsidiaries in other states where tax rates are lower or businesses aren't taxed at all. To counter this practice, 24 states have passed laws that require companies to add up all of the income from all entities and apportion it to the states where the money was made. By enacting combined reporting, Virginia could gain more than $100 million a year and also end a tax advantage that local businesses don't share.

Eliminate "nowhere income." Another series of loopholes in the state's tax code allows big Virginia-based corporations to avoid taxation on profits made in states with no corporate taxes. One way for Virginia to have a claim on taxes from such companies is to reinstate the "throwback" rule adopted in 1960 and repealed in 1981. Under this provision, profits made in a state in which a Virginia corporation may not be subjected to an income tax get "thrown back" to Virginia and taxed here instead. This brings in new revenue and levels the playing field among all Virginia businesses.

Another reform that would help limit "nowhere income" would require Virginia to refine its definition of non-business income. In other words, income that cannot be directly assigned to a particular state, and may escape taxation, would be assigned to the state in which the corporation is headquartered.

Eliminate net operating loss carrybacks. Virginia allows companies with an unprofitable year to apply losses to their prior year tax returns and generate refunds. This tax break, known as "the net operating loss (NOL) carryback" deduction creates budgetary challenges for Virginia, particularly in tough times, because it diverts scarce funding for public services to other purposes.

Enact a strong minimum corporate tax. In 2008, roughly 64 percent of Virginia corporations paid no corporate income tax. One solution to this problem is to enact a strong minimum corporate tax. Fourteen states have a flat rate minimum tax — varying between $20 and $800. Eight more have an alternative minimum tax that establishes a higher floor than a simple flat rate.

Bring Sunlight to Tax Breaks that Operate on Autopilot and Cost Billions of Dollars a Year

Each year, Virginia gives up about $2 billion in revenue in the form of various tax breaks. Unlike money appropriated through the budget – which is reviewed and subject to yearly approval — these credits, deductions, deferrals, exemptions, and preferential rates (called tax expenditures) rarely undergo any thorough evaluation to find out whether they are meeting their intended policy goals or that their cost is not growing out of control.

Virginians have a right to know if the money could be better spent in other ways that create jobs and invest in a strong economy.

By reforming the tax expenditure process, Virginia can bring in new revenue and also build public trust through heightened transparency and accountability.

BLUEPRINT

Issue a comprehensive report that examines all tax breaks and aids in meaningful evaluation. Some type of reporting is currently undertaken by 41 states, including Virginia. But Virginia's efforts fall short on a number of measures. In order to be useful, a tax expenditure report must include the intended purpose of each tax break, who benefits and how much they get, and an estimate of total cost. A solid tax expenditure report can shed light on underperforming programs or those that cost far more than was anticipated when the tax break was established. It can also highlight programs that are meeting or exceeding expectations and that yield a high return on investment.

Attach a "sunset" provision to tax break legislation. This means that every tax break voted in by the legislature would include a date on which it would expire unless it is renewed. Today, most tax expenditures are, in effect, permanent. Requiring an active process to renew tax breaks increases the likelihood that there will be an analysis of cost and effectiveness.

Target existing tax expenditures to make them more effective. Two examples of tax breaks that help people who arguably don't need it concern the age deduction and the sales tax limitation on yachts and other watercraft.

Age Deduction for Taxpayers Age 65 and Older: In 2004, the legislature changed the $12,000 age deduction so that instead of everyone 65 or older getting the same amount, now how much a person receives depends on their income. Those making more than $50,000 get less. But anyone already in the program was allowed to continue receiving the full deduction regardless of income. By means-testing those who started receiving the age deduction before 2004, the state would regain more than $40 million a year to use for general public needs.

Sales and Use Tax on Watercraft: Virginia taxes the sale of watercraft at a reduced rate of 2 percent (instead of the 5 percent applied to other goods) and limits the total amount collected on any vessel to $2,000 even if 2 percent of the selling price exceeds that amount. This means that a Virginian with a million dollar yacht gets a tax break, while working families pay the full sales tax on everything they buy.

Modernize Virginia's Individual Income Tax and Sales Tax to Reflect Today's Economy

Virginia's economy looks much different today than it did 25 years ago, but the Commonwealth has trouble making the investments needed in that economy because the two most important revenue streams — the income and sales taxes — have not been updated to reflect major changes in the way people earn and spend. As a result, these revenue sources do not support an environment in which businesses want to create jobs. To meet the needs and priorities of the state's residents, businesses, and communities now and going forward, Virginia needs a revenue system that matches up to key trends in people's incomes and spending habits. Trying to operate a competitive and prosperous 21st century state with a 1980s tax system is like trying to use a mule team to explore outer space — Virginia will continue to find itself falling short.

Reforms are needed to both the state's income and sales taxes.

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Modernize tax brackets and rates. The rate of state income tax and the levels of household income at which those rates take effect have not been touched since 1987. Under the current structure, rising incomes and outdated brackets have made it so that nearly 60 percent of Virginia taxpayers now pay the top marginal rate of 5.75 percent. This relatively flat income tax structure means that millionaires pay the same rate (on every dollar they make over $17,000) as middle-class Virginians. Modernizing the brackets and adding a new top rate for top-earners would mean Virginia's income tax would be more capable of growing with the economy and meeting rising needs — and it would reduce the share that middle- and low-income households pay.

Update the sales tax to include more services. When Virginia's sales tax was enacted, people spent more money on goods than services, so the tax accomplished its goal of raising money for public needs through a levy on purchases. But purchasing patterns have shifted dramatically over the years. Today, 45 percent of Americans' household spending is on services, up from just 31 percent roughly 30 years ago. Virginia is among the states that tax the fewest number of services.[9] If Virginia were to tax services comprehensively, sales tax revenues could increase by at least one third.[10]

Enact an "Amazon law." Nothing better reflects the change in what people buy and how they buy it than the Internet. Increasingly, purchases are made online from merchants in other states. Many of those merchants don't collect Virginia sales taxes, which causes the Commonwealth two major problems. First, it loses much-needed revenue. Second, it puts local "bricks and mortar" sellers at a disadvantage because the absence of sales tax (the law actually does require Virginians to pay the tax, but enforcement is nearly impossible) means it costs 5 percent (Virginia's sales tax rate) less to buy online. There are a number of ways Virginia could increase sales tax revenue from out-of-state Internet sales.

The most popular legislative approach, commonly referred to as an "Amazon law," requires retailers to collect sales tax if they have marketing deals with "affiliate" sellers who are physically present in the state. Affiliates place links on their websites to the retailer's site and receive a commission when someone follows the link and buys something from the retailer.

1 A Preliminary Review and Analysis of The Virginia Standards of Quality: Report to the Virginia Department of Education, Augenblick, Palaich and Associates, July 2009.

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3 Virginia Department of Education School Nutrition, http://www.doe.virginia.gov/support/nutrition/resources/faqs.shtml, accessed 6/14/2011

4 School Breakfast in America's Big Cities, http://frac.org/wp-content/uploads/2011/01/urbanbreakfast2009-2010.pdf, accessed 6/14/2011

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6 Center for American Progress, http://www.americanprogress.org/issues/2011/02/pdf/hunger_report.pdf/, accessed 6/14/2011

7 The University of Virginia study followed a cohort of students from approximately 1,000 public schools, representing more than 99 percent of the districts in Virginia from fall 2007 to spring 2009. Huang, F. L., et al. The differential effects of preschool: Evidence from Virginia. Early Childhood Research Quarterly (2011), doi:10.1016/j.ecresq.2011.03.006

8 Virginia's income limit is a firm limit, while several other states with the same published income limit disregard certain income, such as for child care expenses.

9 Federation of Tax Administrators, Sales Taxation of Services: 2007 Update, October 2008; www.taxadmin.org/fta/pub/services/services.html. See report for extensive footnotes that affect classification as taxable or exempt.

10 Mazerov, Michael. 2009. "Expanding Sales Taxation of Services: Options and Issues." The Center on Budget and Policy Priorities. July 2009.

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