



COLORADO CENTER
on LAW & POLICY

Justice and Economic Security for all Coloradans

Analysis of 2012 federal tax reform, part two: Sequestration and the Colorado budget

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This is the second in a series of issues briefs discussing federal budget changes and their implications.. This brief focuses on state budget cuts that will result from federal sequestration.

While this paper discusses the negative implications of sequestration, the passage of a rushed and one-sided federal budget would have far more dangerous and potentially devastating results. The final brief in this series will discuss budget options and the need for a balanced approach.

As a result Congress's failure to agree on deficit reduction, automatic sequestration cuts will strip billions of dollars from state budgets, costing jobs and hurting working families. Colorado stands to lose over a billion dollars in cuts to education, family support and job development programs while state lawmakers will face increased challenges in balancing the dwindling state budget.

What is sequestration?

The Budget Control Act of 2011 (BCA) allowed the United States to raise the debt limit in exchange for caps on discretionary program funding designed to reduce the deficit by more than \$1 trillion over 10 years. The BCA also established a Joint Select Committee on Deficit Reduction that was charged with reducing the deficit by another \$1.2 trillion over the same time. As a means of enforcement, the BCA further created "sequestration" – a procedure to automatically impose across-the-board cuts if the committee didn't come to an agreement on deficit reduction.

The BCA details the steps that must be taken as a result of sequestration. Sequestration cuts must reduce the deficit \$1.2 trillion over 10 years. The Congressional Budget Office estimates that this equates to \$984 billion in budget cuts, with the remainder of the deficit reduction coming from reduced interest payments of \$216 billion. The budget cuts will be divided equally over the 10 years amounting to roughly \$109.3 billion in cuts per year from 2013-2021.

The sequestration cuts must be divided equally between the national defense budget and all other budget functions. The non-defense reductions must come from discretionary spending (non-entitlement) and mandatory spending (entitlement). Discretionary spending includes spending on areas such as national parks, education, low-income housing and medical research.

Most mandatory spending has been exempted from sequestration. Areas exempt from spending cuts include:

- Medicaid
- Social Security
- the Children Health Insurance Program (CHIP)
- the Supplemental Nutrition Assistance Program (SNAP)

- veteran's benefits and retirement programs
- Temporary Assistance for Needy Families (TANF)
- refundable tax credits, such as the Earned Income Tax Credit and the Child Tax Credit
- certain federal highway programs

2013 sequestration

To date, the committee has not agreed on a debt reduction measure. Sequestration is scheduled to begin in January 2013.

Of the \$109.3 billion in scheduled cuts in 2013, \$54.7 billion will be made in defense spending and \$54.7 billion will be made in non-defense programs. Generally, this will result in an 8.4 percent reduction in most non-defense discretionary programs, an 8 percent cut in non-exempt, non-defense mandatory programs other than Medicare, and a 10 percent cut in defense programs.

The exact program reductions are still undecided. Policy analysts are making estimates based on past budget decisions and the precision of these estimates will vary based on political and congressional priorities.

Estimated federal cuts in 2013 with sequestration

Reductions in mandatory spending will likely include cuts in Medicare payments to providers and insurance plans, meaning that providers of Medicare will be reimbursed 98 cents on the dollar, instead of completely. This will amount to \$11 billion in cuts in 2013. Another \$5.2 billion will be cut from programs, such as student loans, vocational rehabilitations and social services block grants. This equates to \$16.2 billion of the total required \$54.7 billion in funding reductions. Therefore, the remaining \$38.5 billion will come from non-defense discretionary programs.

Defense cuts are more difficult to anticipate. The cuts will be proportionately distributed across all defense programs. Cuts would have been roughly 7.5 percent, however, the president chose to exempt military personnel funding from sequestration in 2013. Therefore, the cuts to other defense programs were increased to close to 10 percent.

Estimated Colorado cuts in 2013 with sequestration

Federal budget cuts will have a major impact Colorado's budget. Colorado receives about 25 percent of its state funding from the federal government. When the federal government cuts funding for programs, the result is reduced funding for state services and a greater strain on state and local budgets. Colorado will lose more than \$60 million in non-defense cuts. These cuts will be spread throughout the state, with the biggest hits coming to education, health and human services and job development programs. Job losses are eminent as budgets shrink and policymakers are forced to provide more with considerably less.

Colorado is home to a large number of defense contractors and military facilities. As such, a large percentage of federal defense funding comes into Colorado in the form of procurement contracts, employee wages and defense grants. If sequestration occurs, Colorado can expect a 10 percent across the board cut in federal defense funding, which equates to \$1.1 billion.

Colorado job loss estimates

Colorado Center on Law and Policy estimates show Colorado will lose more than 1,600 jobs from the \$60 million in non-defense federal cuts. For every million dollars in cuts, approximately 27 non-defense jobs are estimated to be lost. On top of that, every million dollars lost from defense means 11 fewer jobsⁱ.

The 1,600 jobs that will be lost from non-defense cuts include 1,215 direct jobs and an additional 416 indirect jobs spread among a variety of industry sectors, with the highest number of jobs lost in education.

Top 10 areas of job losses from \$60 million Non-Defense Spending Cuts	Estimated Jobs Lost
Other private educational services	517
Community food, housing, and other relief services	247
Child day care services	203
Individual and family services	104
Employment services	74
Food services and drinking places	44
Nursing and residential care facilities	43
Real estate establishments	30
Legal services	24
Environmental and other technical consulting services	21

The chart below shows federal aid provided to fund Colorado programs for 2012 and the estimated funding for 2013 after sequestration.

Funding Levels for federal programs Comparison of FY2012 funding and FY2013 funding with sequestration	Colorado (dollars in thousands, federal fiscal year)		
	Enacted in 2012	2013 Estimates with Sequester	Change from 2012 to 2013
Department of Agriculture			
Women, Infants and Children (WIC) Supplement Feeding Program	\$ 69,672	\$ 64,238	\$ (5,434)
Department of Education			
Title I - Grants to Local Education Agencies	\$ 148,316	\$ 136,747	\$ (11,569)
Vocational Rehabilitation - State Grants	\$ 40,548	\$ 37,386	\$ (3,163)
Special Education - Basic State Grant	\$ 154,235	\$ 142,204	\$ (12,030)
Improving Teacher Quality	\$ 27,122	\$ 25,007	\$ (2,116)
Career and Technical Education State Grants	\$ 15,766	\$ 14,536	\$ (1,230)
Department of Energy			
Weatherization Assistance Program	\$ -	\$ -	\$ -
Department of Health and Human Services			
Adoption Assistance	\$ 20,739	\$ 21,786	\$ 1,047
Centers for Disease Control and Prevention (CDC): State and Local Capacity	\$ 9,531	\$ 8,788	\$ (743)
Child Care and Development Block Grant	\$ 28,442	\$ 26,224	\$ (2,219)
Child Care Entitlement - Mandatory and Matching	\$ 38,444	\$ 38,444	\$ -
Child Support Enforcement	\$ 59,656	\$ 57,010	\$ (2,646)
Community Services Block Grant	\$ 5,856	\$ 5,399	\$ (457)
Consolidated Health Centers	\$ 65,306	\$ 70,939	\$ 5,633
Foster Care	\$ 54,297	\$ 54,563	\$ 266
Head Start	\$ 81,055	\$ 74,733	\$ (6,322)
Low-Income Home Energy Assistance Program (LIHEAP)	\$ 47,308	\$ 43,618	\$ (3,690)
Medicaid - Administration	\$ 114,443	\$ 118,606	\$ 4,163
Medicaid - Vendor Payments	\$ 2,394,150	\$ 2,540,058	\$ 145,908
Medicaid Part D Clawback	\$ (91,725)	\$ (91,679)	\$ 46
Promoting Safe and Stable Families	\$ 3,490	\$ 3,218	\$ (272)
Social Services Block Grant	\$ 27,537	\$ 25,389	\$ (2,148)
Children's Health Insurance Program	\$ 130,420	\$ 136,071	\$ 5,651
Substance Abuse and Prevention Block Grant	\$ 26,103	\$ 24,067	\$ (2,036)
Temporary Assistance to Needy Families (TANF)	\$ 136,057	\$ 136,057	\$ -
Department of Homeland Security			
State Homeland Security Grant Program	\$ 2,801	\$ 2,583	\$ (219)
HUD and Independent Agencies			
Community Development Block Grants (CDBG) - Entitlement	\$ 24,966	\$ 23,019	\$ (1,947)
CDBG - Non-entitlement	\$ 7,967	\$ 7,346	\$ (621)
EPA - Clean Water State Revolving Fund (SRF)	\$ 11,496	\$ 10,599	\$ (897)
EPA - Drinking Water State Revolving Fund (SRF)	\$ 15,919	\$ 14,677	\$ (1,242)
Department of Justice			
State Criminal Alien Assistance Program	\$ 4,743	\$ 4,373	\$ (370)
Justice Assistance Grants	\$ 2,782	\$ 2,565	\$ (217)
Department of Labor			
Workforce Investment Act (WIA) - Adult Employment and Training	\$ 10,860	\$ 10,013	\$ (847)
Dislocated Workers	\$ 16,138	\$ 14,879	\$ (1,259)
Employment Service State Grants	\$ 11,124	\$ 10,256	\$ (868)
Unemployment Insurance - State Administration	\$ 47,809	\$ 44,080	\$ (3,729)
Workforce Investment Act (WIA) - Youth Activities	\$ 11,883	\$ 10,956	\$ (927)
Department of Transportation			
Federal Aid Highways - Bridge Replacement & Rehabilitation (R&R)	\$ 34,900	\$ 34,900	\$ -
Federal Aid Highways - Interstate Maintenance	\$ 88,360	\$ 88,360	\$ -
Federal Aid Highways - National Highway System	\$ 118,692	\$ 118,692	\$ -
Federal Aid Highways - Equity Bonus	\$ 100,282	\$ 100,282	\$ -
Federal Aid Highways - Surface Transportation Program	\$ 111,596	\$ 111,596	\$ -
Program Totals			
Covered Programs	\$ 918,776	\$ 857,838	\$ (60,938)
Exempt Programs	\$ 3,310,311	\$ 3,464,746	\$ 154,435
Grand Total	\$ 4,229,087	\$ 4,322,584	\$ 93,498

** Numbers in red show estimated program cuts resulting from sequestration

ⁱ To estimate the economic fallout to the Colorado economy due to sequestration cuts, our simulation model calculates economic spending that would have occurred if federal funds were not cut. We use IMPLAN economic modeling software, which utilizes Colorado-specific data, to estimate the lost economic activity and its effect on other sectors of the economy. IMPLAN modeling employs a mathematical economic technique called input-output modeling. IMPLAN uses data on how industries transact with other industries, precisely, it models how the output of one industry becomes an input to other industries, which contributes to final demand. IMPLAN calculates gross outputs of various industries that are required to supplement the final demand of another sector.

The spending titles in the Colorado budget do not correspond precisely to the industry categories within the model. To match the IMPLAN codes many cuts were assigned as child care services, individual and family services, community food and housing services, or employment services. Unemployment insurance was modeled as a loss in household income.

The cuts to the defense budget take the form of procurement, grants, and wages. We added the procurement and grant money together and coded the spending as scientific research, engineering, communications manufacturing, or construction of nonresidential structures. Wage cuts were coded as federal government military payroll and employment.

To calculate the jobs created for every million in spending, total job loss figures were calculated by IMPLAN separately for the \$1.1 billion in defense cuts and the \$60 million in non-defense. Those job totals were then divided by the initial cut in spending the multiplied by 1 million.

Additional information regarding IMPLAN software is available at: <http://implan.com/V4/Index.php>.