

The Thomas A. Roe Institute for Economic Policy Studies

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A BUDGET STRATEGY TO REINVENT THE FEDERAL GOVERNMENT

INTRODUCTION

President Bill Clinton soon will submit his fiscal 1996 budget to a Congress committed to changing Washington's spending and taxing priorities. In apparent response to the election results, and to the House Republicans' "Contract With America," Clinton last month announced a plan for a modest \$60 billion tax cut to be financed by reforms in five agencies such as the Departments of Energy, Housing and Urban Development, and Transportation.

But while the White House and congressional Republicans seem broadly to agree that taxes on families, savings, and investment should be reduced and that government should be made smaller, there has been little discussion about what the federal government ultimately should look like. What government functions, for instance, are carried out most appropriately at the federal level and which at the state or local level? What functions should government shed completely? Meeting congressional demands for reduced taxes and a balanced federal budget will require a radical overhaul of the federal government. The President's budget thus should propose a genuine "reinvention" of government, and so must the Budget Resolution which the House and Senate Budget committees are responsible for drafting.

The budget for fiscal year 1996 also must be constructed in a way that recognizes the crucial political linkage between tax cuts and spending reductions. Tax cuts should be an integral part of any comprehensive strategy to reduce the size of government, not just because tax cuts are needed to return resources—as well as responsibilities—to the American people, but also to build constituencies for change. The Republicans' \$500-per-child tax credit, for instance, gives 35 million American families, raising 51 million children, a financial stake in cutting government spending. Cutting taxes for these families creates an instant, 35-million-strong grass-roots constituency who will benefit materially from smaller government and thus will be motivated to confront the pro-government lobbies whose programs face the ax. Members of Congress who want to downsize and reorder

government must employ tactics, such as tax relief, that create constituencies for reform. Cutting spending is impossible without mobilizing interest groups to lobby as strenuously for reform as those who will lobby against reform.

A budget strategy to cut the federal government and reassign functions also must deal with the many legal obstacles to a proper reordering of government. A host of budget rules, typically the result of interest group lobbying or the tactics of supporters of a larger federal government, waste taxpayers' money and make it literally illegal for agency officials to save money in certain ways.

Conservatives and other reformers on Capitol Hill therefore should move quickly on a budget strategy that will lead to a permanent reordering and downsizing of the federal government. There are three essential steps to such a strategy:

① Establish clear themes for the FY 1996 budget based on principles for the proper role of the federal government.

Among the principles for such an overhaul of federal functions:

- ✓ The federal government should not engage in any activity that is more appropriately within the purview of state and local government.
- ✓ The federal government should cease activities that are properly the responsibility of private sector institutions, or of the American people directly, and avoid those that stifle the marketplace.
- ✓ The federal government should discontinue programs that do not work, that have become outmoded or obsolete, or that duplicate other programs.

② Create constituencies for smaller government.

Among the techniques that can build constituencies for reforming government:

- ✓ **Link** blocks of spending cuts directly to specific tax cuts in order to show taxpayers that a cut in particular government programs is needed to put cash back in their wallets.
- ✓ **Use** privatization to create groups with an interest in transferring certain functions out of government control and keeping them in the private sector.
- ✓ **Ease** the concerns of state and local officials by using flexible block grants, removing mandates, and shifting to local governments both the taxing and spending authority for many federal functions.

③ End congressional practices that waste taxpayers' money and thwart reform.

Congress should:

- ✓ **End** the practice of "current services" budgeting.
- ✓ **Amend** the "pay-go" rule, which prevents using cuts in discretionary programs to finance tax cuts.

- ✓ **End** all prohibitions on privatization.
- ✓ **Abolish** all employment floors forced on federal agencies.
- ✓ **Repeal** the Davis-Bacon Act and the Service Contract Act.

The White House and congressional leaders soon will have an opportunity to show taxpayers how committed they are to “reinventing” government and returning resources to ordinary Americans when the serious work of crafting the fiscal 1996 budget begins next month. The test of this commitment is how aggressively the President’s budget and the Budget Resolution challenge the federal government’s relationship with local governments and the private sector, and how swiftly outmoded and inefficient programs are eliminated.

THREE STEPS TO REINVENTING GOVERNMENT

The budget debate will begin in earnest in early February, when President Clinton submits his fiscal 1996 budget to Congress. Given the vast differences between the modest reforms being discussed at the White House and the bolder vision of House Republicans, the Clinton budget most likely will be termed “dead on arrival.” The House Budget Committee will begin drafting its own budget in the form of a Budget Resolution, a non-binding blueprint (meaning it is not signed by the President) outlining the government’s spending and revenue priorities for the next fiscal year. Typically voted on in March, the Budget Resolution tells the Appropriations Committees how much money they can spend and, if necessary, tells the Ways and Means Committee and the authorizing committees whether changes need to be made in tax or entitlement laws. Such changes are voted on later in what is known as a reconciliation bill.

The Budget Resolution thus is the first opportunity reform-minded Members have in the first weeks of the new Congress to show taxpayers what the government will look like once they have redefined Washington’s relationship with state governments and the private sector and have eliminated programs that are outmoded, inefficient, or wasteful. The final product should outline a government that is lean, focused only on national issues, and concerned with putting money and responsibility back in the hands of hard-working Americans.

There are three important steps that need to be taken in drafting a budget that truly redefines the federal government.

STEP # 1: SET BOLD PRINCIPLES FOR “REINVENTING GOVERNMENT”

A conservative Budget Resolution should set out bold themes that truly would “reinvent government” with spending decisions that reflect the proper functions of the federal government. This means doing three things, clearly and unambiguously:

- ✓ **Defining** the role of the federal government, compared to that of state and local governments;
- ✓ **Distinguishing** between public, or government, functions and those which should be the exclusive responsibility of the private sector;

- ✓ **Determining** which federal programs are outmoded, do not work, have completed their missions and are no longer needed, or duplicate the efforts of other programs.

Every spending change in the Budget Resolution should flow directly from three basic principles.

PRINCIPLE #1: The federal government should not engage in any activity that is more appropriately carried out by state and local government.

Since World War II, Washington has assumed hundreds of functions that were once exclusively within the jurisdiction of state and local governments. Many others must be undertaken by state and local officials in ways prescribed by Washington as a condition for receiving federal funds. According to Vice President Al Gore's National Performance Review, "much of Washington's domestic agenda, \$226 billion, to be precise," is allocated to state and local governments "through an array of more than 600 different grant programs."¹

A conservative Budget Resolution should be, among other things, a "Federalism Budget." Congress should declare in the Budget Resolution that the first responsibility of the federal government is national defense. It then should examine every other program to determine whether it is truly national in scope and can be carried out on a national scale only by the federal government. Funding for all agencies and programs that fail to meet this test, such as many education, welfare, health, transportation, and other programs, should be transferred to the states or returned to the people as federal tax reductions—leaving the states to decide whether and how to raise appropriate funds from their own citizens.

For example, the Budget Resolution should call on Congress to:

- ✓ **Devolve** all Department of Education functions to the states and close down the Department.
- ✓ **Transfer** the federal gas tax to the states along with full authority for highway and local transit spending. Eliminate any federal prohibitions against the privatization of these assets once they are in local hands.
- ✓ **Consolidate over 70** federally funded, means-tested anti-poverty programs into a single block grant and then limit the overall growth in spending for this new grant to 3 percent annually. Grant state and local governments broad authority to experiment with their own approaches to assisting the poor and ending dependency. This authority should be subject to general principles to require work and reduce illegitimacy.
- ✓ **Fold** the acute care portion of Medicaid into the welfare system and transfer it to the states, with state flexibility, in statute, to integrate health programs and other services. As a first step toward this reform of Medicaid, give states fixed,

1 *The National Performance Review: Creating a Government that Works Better and Costs Less* (Washington, D.C.: U.S. Government Printing Office, September 7, 1993), p. 51.

or capitated, payments. Also, remove most federal mandates and replace them with a simple requirement to provide a basic level of care.

- ✓ **Perform** a comprehensive inventory of all federal lands held by the U.S. Forest Service, the Bureau of Land Management, the Bureau of Reclamation, the U.S. Fish and Wildlife Service, and the U.S. Park Service. Transfer all land to the states other than those parks and wilderness areas deemed to be of national significance.
- ✓ **Eliminate** all federally funded infrastructure, community, and economic development programs. Use a portion of the savings to finance federal tax cuts in Enterprise Zones.
- ✓ **Institute** a blanket prohibition on the congressional practice of “earmarking” funds for specific local projects in appropriations bills. Last year, Congress earmarked spending for hundreds of such purely local projects, including:
 - ◆ \$1 million for an airport access road in Jacksonville, Florida;
 - ◆ \$1 million to upgrade 96th Street in Indianapolis, Indiana;
 - ◆ \$2 million for the Farmer’s Market in Toledo, Ohio; and,
 - ◆ \$750,000 for the SciTrek Science Museum in downtown Atlanta.

PRINCIPLE #2: The federal government should cease activities that are properly the responsibility of the private sector.

A conservative Budget Resolution should distinguish clearly between those activities that are the exclusive responsibility of the public, or government, sector and those that should be the exclusive responsibility of the private sector. In addition, it should describe areas where there is a public purpose but the activity still should be carried out by private institutions, either directly or under contract to government.

An intensive privatization, or denationalization, effort to reassign essentially private functions to the private sector is long overdue in this country. Governments throughout the world, from Russia to Mexico and from Japan to Great Britain, have been redefining the role of government in a private economy. These governments are aggressively denationalizing state-owned enterprises, cutting subsidies to inefficient industries, removing barriers to private investment, and restoring property rights. Yet the U.S. government continues to control hundreds of private activities and functions such as public utility management, railroad services, small business loans, printing and publishing, agriculture subsidization, and oil extraction and storage.

Privatizing commercial functions can yield considerable short-term revenues while greatly improving the efficiency of services. Candidates for sale to the private sector include the \$200 billion direct loan portfolio, Amtrak, the Power Marketing Administrations, part of the Postal Service, many federal buildings and real estate holdings, and some public lands. In some cases, such as transferring the ownership of public housing to residents, the aim is not to raise revenue, but to change the social environment of communities.

In some cases, privatization provides the only hope for many inefficient and unreformed programs starved of capital due to federal budget constraints. But in the private sector, investment flows to enterprises that can produce valuable goods and services. Consider the problems in five programs documented by the U.S. General Accounting Office (GAO):

- ◆ Many of the 337 dams built by the Bureau of Reclamation are over a half-century old and in desperate need of repair.²
- ◆ The Forest Service now needs \$644 million to maintain and reconstruct trails and recreation sites.³
- ◆ Within a few years, much of the Army Corps of Engineers' \$125 billion inventory of water resources projects will have reached the end of its design life.⁴
- ◆ Ongoing modernization projects at the Federal Aviation Administration are billions of dollars over budget and years behind schedule. "Of the more than 200 projects in FAA's modernization effort, only 36 are completed, accounting for just 3 percent of the \$32 billion" FAA will spend to upgrade the air traffic control system between 1982 and 2000.⁵ The best solution to this problem would be to transfer the air traffic control system to a corporation owned jointly by the airlines.⁶
- ◆ The National Weather Service modernization program "has exceeded its expected cost and is far behind schedule. The initial cost estimate of nearly \$2 billion has risen to \$4.6 billion," and the projected completion date has slipped from 1994 to 1998.⁷

"Reinventing" programs as broken as these will not save them from their eventual collapse. Privatization is the only remaining way to raise the capital necessary to rescue them.

The Budget Resolution can set out changes to restore the proper demarcation between public and private activity according to the following framework:

① Denationalize government-owned commercial activities.

Examples:

- ✓ **Dismantle** the Power Marketing Administrations and sell them through public stock offerings.

² U.S. General Accounting Office, Transition Series, *Natural Resource Management Issues* (GAO/OCG-93-17TR), December 1992.

³ *Ibid.*, p. 9.

⁴ *Ibid.*

⁵ U.S. General Accounting Office, Transition Series, *Transportation Issues* (GAO/OCG-93-14TR), December 1992, p. 13.

⁶ See Robert W. Poole, Jr., "Restructuring the Air Traffic Control System," in Edward L. Hudgins and Ronald D. Utt, eds., *How Privatization Can Solve America's Infrastructure Crisis* (Washington, D.C.: The Heritage Foundation, 1992).

⁷ U.S. General Accounting Office, Transition Series, *Commerce Issues* (GAO/OCG-93-12TR), December 1992, p. 14.

- ✓ **Dismantle** the Tennessee Valley Authority and sell it to the public and to investor-owned utilities.
- ✓ **Sell** Amtrak in the same manner as Conrail.
- ✓ **Sell** or give the air traffic control system to a consortium controlled by the major U.S. airlines.
- ✓ **Privatize** the National Weather Service and weather-related satellites.

② **Sell commercial assets and use the proceeds to finance tax cuts or to buy down the federal debt.**

Examples:

- ✓ **Sell** the \$200 billion direct loan portfolio to the secondary loan market.
- ✓ **Sell** the Naval Petroleum Reserves.
- ✓ **Sell** commercial public lands.
- ✓ **Sell** most of the nearly 1,200 government-owned non-defense aircraft.
- ✓ **Sell** the Federal Helium Reserves.
- ✓ **Sell** the Defense Stockpile.
- ✓ **Sell** federally owned buildings and real estate, including the real estate holdings of the Postal Service.

③ **Make government business-neutral by funding no program, project, or research initiative that benefits private industry directly.**

Examples:

- ✓ **Eliminate** agriculture research programs.
- ✓ **Eliminate** energy research programs.
- ✓ **Halt** funding for the Magnetic Levitation (MagLev) high-speed rail research program.
- ✓ **Close** the U.S. Travel and Tourism Administration.
- ✓ **Eliminate** the Market Promotion Program.
- ✓ **Close** the Export-Import Bank.
- ✓ **Terminate** maritime programs such as Operating-Differential Subsidies and the Ocean Freight Differential program.
- ✓ **Abolish** the Small Business Administration.
- ✓ **End** export subsidy programs such as the Export Enhancement Program and the Foreign Agriculture Service.
- ✓ **Eliminate** below-cost timber sales.

- ④ Cut regulatory spending in order to enhance competition, benefit consumers, and honor property rights.**
- ✓ **Phase out** agriculture subsidies.
 - ✓ **Eliminate** agriculture quota and marketing order programs.
 - ✓ **Terminate** the Conservation Reserve Program.
 - ✓ **Eliminate** the federal fuel tax subsidy for Ethanol.
 - ✓ **Impose** a moratorium on federal land purchases.
 - ✓ **Eliminate** the National Biological Survey.
 - ✓ **Reduce** overhead expenses for the Environmental Protection Agency.
 - ✓ **Privatize** the Consumer Product Safety Commission.
- ⑤ Eliminate the government's risk exposure.**
- ✓ **Sever** all federal ties and implicit taxpayer guarantees to Government-Sponsored Enterprises such as the Federal Home Loan Bank System (FHLBS), Federal National Mortgage Association (FNMA), Federal Home Loan Mortgage Corporation (FHLMC), and Government National Mortgage Association (GNMA).
 - ✓ **Close** the Farmers Home Administration (FmHA) and Farm Credit System (FCS).
 - ✓ **Terminate** the Federal Crop Insurance Corporation (FCIC).
 - ✓ **Allow** the Pension Benefit Guarantee Corporation greater flexibility in setting its premiums so that revenues cover losses and expenses on a sustained basis.
- ⑥ Require users of federal enterprises to cover program costs through user fees.**
- ✓ **Allow** National Parks to increase entrance fees to cover a greater share of maintenance and reconstruction costs.
 - ✓ **Allow** airports to establish market-based take-off and landing fees.
 - ✓ **Raise** Medicare Part B premiums to reflect the true cost of service.
 - ✓ **Turn over** all responsibility for harbor maintenance and dredging to local authorities and allow them establish market-based fees to cover the cost of this dredging.
 - ✓ **Increase** user fees to cover the cost of Coast Guard services to private boat owners.
- ⑦ Privatize social services.**
- ✓ **End** HUD low-income housing subsidies and use a portion of the savings to finance portable vouchers.
 - ✓ **Sell** or give public housing to tenants.

- ✓ End federal funding for ACTION.
- ✓ End federal funding for ACTION's VISTA program.
- ✓ Terminate the new AmeriCorps volunteer program.

PRINCIPLE #3: The federal government should terminate programs that do not work, that have become outmoded or obsolete, that duplicate other programs, or that do not involve legitimate government functions.

Most would be stunned to learn how old many federal programs and agencies really are. Large segments of the federal bureaucracy were created decades ago for purposes long since forgotten. It is time, for instance, to strip out of the budget such pre-World War II programs as the Rural Electrification Administration, the National Helium Reserves, Impact Aid, and the Interstate Commerce Commission.

Many relatively new programs also have seen their missions made obsolete by technological and social changes. The Corporation for Public Broadcasting, international broadcasting programs such as the Voice of America, Low-Income Home Energy Assistance, and the Department of Energy, for example, are all outmoded or irrelevant because of technological and market changes.

Because outmoded, obsolete, or inefficient programs almost never die, bureaus, agencies, and programs that duplicate each other's functions have sprung up all over the government. Last year, the National Performance Review identified a staggering degree of duplication throughout the federal bureaucracy. For example:

- ◆ Some 14 separate government departments and agencies spend \$24 billion a year on 150 employment and training programs.⁸

FEDERAL BUDGET DINOSAURS

- X The Army Corps of Engineers, created 1824.
- X U.S. Department of the Interior, created 1849.
- X U.S. Department of Agriculture, created 1862.
- X The Mining Act of 1872.
- X The Cooperative State Research Service, created 1888.
- X The Bureau of Reclamation, created 1902.
- X The U.S. Forest Service, created 1905.
- X The Bureau of Mines, created 1910.
- X The Naval Petroleum Reserves, created 1912.
- X The Agriculture Extension Service, created 1914.
- X The National Park Service, created 1916.
- X The National Helium Reserves, created 1925.
- X The Davis-Bacon Act, enacted 1931.
- X The Tennessee Valley Authority, created 1933.
- X The Export-Import Bank, created 1934.
- X The Soil Conservation Service, created 1935.
- X The Power Marketing Administrations, created 1937.

- ◆ Washington spends “about \$60 billion a year on the well-being of children. But we have created at least 340 separate programs for families and children administered by 11 different federal agencies and departments.”⁹

The U.S. General Accounting Office also has documented massive duplication throughout the federal government. Entire Cabinet agencies are duplicated by other federal departments. Among the GAO’s findings:

- ◆ “The Department of Commerce shares its mission with at least 71 federal departments, agencies, and offices.”¹⁰
- ◆ “Export promotion programs are fragmented among 10 agencies. The U.S. Department of Agriculture, not Commerce, receives about 74 percent of total funding for these programs, although it accounts for only about 10 percent of U.S. exports.”¹¹

A conservative Budget Resolution should expose these outmoded, inefficient, or duplicative programs and excise them from the budget. As Members of Congress draw up the Budget Resolution, they should:

① Question the need for any program that is more than 50 years old and eliminate any which is outmoded or obsolete.

Examples:

- ✓ **Reduce** the scope and activities of the 170-year-old Army Corps of Engineers.
- ✓ **Close** the 85-year-old Bureau of Mines.
- ✓ **Abolish** the 81-year-old Agricultural Extension Service.
- ✓ **Terminate** the 60-year-old Soil Conservation Service.
- ✓ **Terminate** the 60-year-old Rural Electrification Administration.
- ✓ **Close** the 70-year-old National Fertilizer Development Center.
- ✓ **Abolish** the 108-year-old Interstate Commerce Commission.

② Terminate newer programs that are outmoded or obsolete.

Examples:

- ✓ **Close** down the Department of Energy, moving nuclear defense functions to the Department of Defense and abolishing all research programs.
- ✓ **Stop** funding the Corporation for Public Broadcasting and allow it to become a self-supporting grant-making foundation much like the United Way.
- ✓ **End** Impact Aid.

9 *Ibid.*, p. 51.

10 GAO, Transition Series, *Commerce Issues*, p. 9.

11 *Ibid.*

- ✓ **End** Low-Income Home Energy Assistance.
- ✓ **Terminate** P.L. 480 foreign aid grants.
- ✓ **Terminate** the Targeted Export Assistance Program.
- ✓ **End** Trade Adjustment Assistance.
- ✓ **Phase out** the Federal Communications Commission while deregulating the industry.

③ **Eliminate programs that duplicate or overlap other programs.**

Examples:

- ✓ **Close** down the Department of Commerce, moving trade programs to the U.S. Trade Representative's Office and the National Oceanic and Atmospheric Administration to the Department of Interior.
- ✓ **Close** most, if not all, of the government's 1,200 independent commissions, councils, and boards.
- ✓ **Consolidate** the 150 federal job-training programs and either block grant them to the states or use the savings to finance a "training credit."

④ **Cancel programs with a long history of failure or irrelevance.**

Examples:

- ✓ **Terminate** the Appalachian Regional Commission.
- ✓ **Abolish** the Small Business Administration.
- ✓ **Close** down the Minority Business Development Administration.
- ✓ **Abolish** the Economic Development Administration.

⑤ **Terminate programs that should not be undertaken by the federal government.**

Examples:

- ✓ **Shut down** the Legal Services Corporation.
- ✓ **Abolish** the National Endowments for the Arts and Humanities and the Institute of Museum Services.
- ✓ **End** the College Work Study Program.
- ✓ **End** Law-Related Education Grants and Law School Clinical Experience Grants.
- ✓ **End** Health Professionals Education Subsidies.

STEP #2:

BUILD CONSTITUENCIES FOR SMALLER GOVERNMENT

Reinventing government is no easy task politically. As government has exploded over the past forty years, so also have the number of interest groups—in and out of government—whose livelihoods depend upon government largess. When reductions in or eliminations of programs are announced, groups which stand to lose benefits can be expected to launch campaigns to keep them in the budget. However, this can be offset by creating or identifying other interest groups which stand to benefit materially from less government and will be highly motivated to campaign on behalf of spending cuts. Indeed, it is even possible in some cases to turn opponent groups, such as public employees, into advocates for reform by designing reforms that appeal to their particular interests.

Three strategies should be employed to counter the pro-spending lobbies and to build constituencies for smaller government:

① Directly link tax cuts to spending cuts.

The House Republican “Contract With America” contains a five-year, \$200 billion tax cut package for families with children, seniors, businesses, and entrepreneurs. Linking these tax cuts directly to spending cuts has two positive effects. First, it creates an instant grass-roots lobby in favor of lower government spending. Second, it “sugar-coats” the political “pain” of deep cuts in spending, allowing politicians to “bring home the tax cuts” in the same manner they traditionally have “brought home the bacon.”

The proposed \$500-per-child tax credit creates a spending-cut constituency. Some 35 million families, caring for 51 million children, are eligible for this tax credit. This represents a powerful grass-roots force which will benefit materially from reduced federal spending and thus can be motivated to press for the elimination of programs—yielding the savings needed to cover the revenue cost of tax relief. Conservatives should bundle programs into an “omnibus” spending cut and tax relief package. Then let the defenders of arts subsidies or the Rural Electrification Administration argue that families with children should not get tax relief because their programs are too important.

Family tax cuts linked to spending cuts also address the political concerns of uneasy Members of Congress. Using U.S. Census data, Heritage Foundation analysts have calculated the number of eligible children in every state and congressional district. The typical congressional district has some 117,000 children in families eligible for the \$500-per-child credit. Thus it would receive nearly \$59 million per year in family tax relief under this plan. These statistics allow Members of Congress to balance the political interests of constituents who may be “hurt” by spending cuts with those of the thousands of families whose finances will be improved through tax cuts. This calculus could be used with other tax cuts as well.

Example. Bundled cuts in business-oriented programs (such as the Small Business Administration, Export-Import Bank, and Market Promotion Program) could be used to finance a reduction in the capital gains tax and improvements in the deductibility of capital investments. While these spending cuts take government programs away from a

few politically connected industries, the tax cuts will benefit a strong grass-roots constituency of entrepreneurs and small businesses.

② Create constituencies through privatization.

Countries all over the world have used various privatization techniques to overcome opposition to reform from vested interests, including public employees. Britain, for example, used gifts of stock to managers and workers in nationalized industries to build strong support for the privatization of firms. The Netherlands generated broad-based public support for privatizing its postal service by selling the public a minority interest in the operation. This is merely a first step toward full private ownership. Other countries such as Chile, Colombia, and Peru have successfully privatized their Social Security systems by giving individuals greater control over funds.¹²

Example. Cutting or eliminating HUD public housing subsidies certainly will raise opposition from local bureaucrats and private landlords who benefit directly from those subsidies. But using some of these savings to finance portable vouchers for tenants, or offering to sell housing at deep discounts to residents, creates a new constituency of residents who benefit directly from this spending cut. The experience of the huge program of public housing sales in Britain, and of more limited sales in this country, also indicates that when residents own or control their own homes they have a far greater interest in caring for housing than bureaucrats ever can have.

Example. The White House has proposed turning the Federal Aviation Administration's air traffic control functions into a government-owned corporation like Amtrak. This is not the best way to privatize or improve this operation. Making this a fully private corporation, owned wholly or in part by the private airline industry, would put control of this underfunded service directly into the hands of those with the most to gain from tertiary steps to invest in new technology and improve the level of service.

Example. There is considerable political opposition to selling or denationalizing the government-owned dams and utilities known as the Power Marketing Administrations. However, based upon the success achieved by other countries in selling state-owned utilities, this opposition can be neutralized by offering favorable stock options in the new utility to employees, residential customers, environmentalists, fishing and agricultural interests, or others who may feel that they stand to lose by the elimination of bureaucratic control over these subsidized utilities. Several countries have found that it is even worthwhile to sell stock options at below-market prices in order to encourage broad public support for denationalization.

③ Build state and local cooperation through federalism.

Understandably, many governors and local officials fear that reduced federal spending will mean a rise in federal mandates. Other officials fear that when current federal functions are transferred to local levels, they will be left with the painful task of raising local taxes to finance these new responsibilities. These fears can be eased. Conserva-

¹² James K. Glassman, "How Much Would Be Offered for the 14th Street Bridge?" *The Washington Post*, December 21, 1994.

tives should develop plans to make state and local officials both partners in the effort to shrink the federal budget and beneficiaries of that process.

Five measures would reduce the concerns of most local officials:¹³

- ✓ Require full federal funding of any program mandated by the federal government.
- ✓ Whenever possible, transfer full control and financing of federally funded programs currently operated by states to the respective state governments.
- ✓ Reform the requirements on the states to compensate the federal government for any assets they privatize that are held jointly or that once received federal funds.
- ✓ In keeping with Ronald Reagan's Executive Order 12612, monitor all federal rules and regulations for their impact on the states and minimize this impact.
- ✓ Extend "regulatory waivers" to allow states more effectively to manage environmental and housing programs.

Example. There are sound public policy reasons for cutting federal highway spending and federal grants to inefficient local public transit systems. There also are potentially large budget savings. However, these programs are financed through the federal gasoline tax, so cutting the federal grants would unfairly burden local governments while allowing Washington to pocket gas tax revenues. A more reasonable solution would be to eliminate both the federal gas tax and the spending programs, transferring to state governments the responsibility for highway and transit spending along with the financing mechanism. State governments then could decide for themselves whether higher state gas taxes are needed to finance local projects. Some might choose to use tolls or other privatization methods to operate local highways or transit systems.

STEP #3: REMOVE OBSTACLES TO SAVING TAXPAYERS' MONEY AND REORGANIZING GOVERNMENT

No owner of a private firm would knowingly institute rules that force company managers to waste money. But Congress routinely enacts rules and mandates that force agency managers to waste billions of taxpayers' dollars. Some legislative requirements stop agencies from even studying ways to save money. Most of these rules have been instituted under pressure from agency officials or program beneficiaries. Others are the byproduct of ill-conceived budget process "reforms" in the past. A conservative Budget Resolution should propose legislation to eliminate these rules as part of a general reform of the budget process.

Five specific budget reforms are needed to permit a restructuring of the federal government:

¹³ For a full description of these recommendations, see Scott A. Hodge and Adam D. Thierer, "The National Performance Review: Falling Short of Real Government Reform," Heritage Foundation *Backgrounder* No. 962, October 7, 1993.

① Eliminate “baseline” budgeting.

On the first day of the 104th Congress, House Republicans fulfilled one of the provisions of the “Contract With America” by voting to eliminate the practice of “baseline” or “current services” budgeting. The Senate should act quickly on this House initiative. Under “current services” budgeting, program costs are projected into the future based upon such criteria as the requirements of current law, estimated inflation rates, and the expected growth in demand for the good or service provided.

Using current services budgeting, a program that costs \$100 million this year might be projected to cost \$110 million next year. But if the program is budgeted at \$105 million instead of at the projected \$110 million, it is said the program has been “cut” by \$5 million—even though it received \$5 million more than in the previous year. If the program actually is cut in the way understood by Americans outside of Washington—say by \$5 million, to \$95 million—Washington registers this as a \$15 million cut.

Baseline budgeting is not just a deception at taxpayers’ expense. According to budget scholar Allen Schick, it also weakens lawmakers’ control over the budget by strengthening the claims on funds by interest groups before any allocation decisions have been made.¹⁴ These groups effectively become entitled to the projected increases in a program and are permitted to claim that their funding has been cut merely because the current year’s increase falls below the baseline increase.

These interest groups can be held in check, at least to a degree, if spending levels are discussed in layman’s terms that indicate just how much spending is to rise or fall compared with the previous year. If current services budgeting is eliminated, the fiscal 1996 budget could become the first “honest budget” since that practice was introduced in 1974.

② Allow cuts in discretionary, or appropriated, programs to finance tax cuts.

Current budget rules mean that tax cuts (which can cause permanent reductions in revenues to the Treasury) may be financed only by cuts in entitlement programs or by increases in other taxes. Under this “pay-go” (for pay-as-you-go) rule, only changes in programs which operate under permanent law can offset each other. While this rule correctly requires that legislated increases in entitlement spending be balanced by cuts in other entitlements, it does not allow tax cuts to be financed by cuts in discretionary, or annually appropriated, programs. Thus, for example, cuts in pork barrel and other wasteful spending may not be used to fund tax relief for needy families. This provision within the pay-go rule should be repealed and the requirement to balance increases in entitlements with cuts in other programs should be retained.

The White House opened the door to elimination of this anti-taxpayer budget rule when it announced its \$60 billion tax cut package for middle-class families. Clinton proposed financing these tax cuts by cutting discretionary spending programs such as energy, transportation, and housing. The new Congress should join the White House in repealing this rule.

14 Allen Schick, *The Capacity to Budget* (Washington, D.C.: The Urban Institute Press, 1990), p. 210.

③ End all prohibitions on, and micromanagement of, the privatization process.

Since 1981, Congress has enacted over 40 separate laws expressly prohibiting the privatization of government services. In some cases these laws prohibit agencies from even studying privatization options. Such bans cost taxpayers billions each year.

Example. The Farmers Home Administration (FmHA) wrote off some \$8.5 billion in loan losses during the early 1990s, partly because Congress prohibits it from cracking down on bad debtors or from hiring private collection firms to collect on delinquent loans. In many cases, new loans must be given to known poor credit risks.

For a comprehensive listing of these congressional roadblocks, see the appendix to this study.

④ End the practice of setting agency employment floors.

Congress regularly sets minimum staffing levels for certain agencies, even if the work could be done with a fraction of the staff. These “employment floors” are designed to protect jobs in agencies or field offices and prevent managers from making the most effective use of the employees they supervise, such as by shifting workers from one department to another.

While the National Performance Review has worked to lessen this practice and give managers greater flexibility, employment floors still exist. The practice should be stopped, and work should begin on allowing even greater agency flexibility.

⑤ Repeal the Davis-Bacon Act and the Service Contract Act.

The Davis-Bacon Act of 1931 increases the costs of government construction contracts by over \$1 billion annually by forcing contractors to pay union scale wages on all federally funded construction contracts, even though less expensive labor often is available. This legislation was enacted to keep black workers off federal construction sites, and that is precisely what it has done for 60 years. A similar law, the Service Contract Act of 1965, has the same impact on federally funded service contracts. The extra costs imposed by these two laws: \$2 billion per year.

CONCLUSION

Now that the White House and congressional reformers seem to agree on the need to shrink the size of the federal government and return to taxpayers their hard-earned money, it is time to outline what the federal government should look like after its “reinvention” has been completed. Once the Clinton plan has been submitted to Congress in early February, the House Budget Committee will begin work on its own version of the fiscal 1996 budget. Each of these documents should describe what government functions, for instance, are carried out most appropriately at the federal level and which at the state or local level as well as which ones government should shed completely because they conflict with the private sector or have become obsolete.

Just as important, however, these documents also must address the crucial linkage between tax cuts and spending reductions. They should recognize that “reinventing” government involves not just cutting spending, but also redefining which institution—the

American family or the central government—is best equipped to spend money on such important matters as housing, food, welfare, and raising children. The answer to this question will reveal whether the White House or Congress is more committed to changing Washington's spending and taxing priorities.

Scott A. Hodge
Grover M. Hermann Fellow in Federal Budgetary Affairs

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HOW CONGRESS HAS BLOCKED PRIVATIZATION

AGRICULTURE

- X Minimum employment levels exist at the Farmers Home Administration, Agricultural Stabilization and Conservation Service, and the Soil Conservation Service.
- X The Farmers Home Administration is prohibited from contracting with private debt collection firms to collect delinquent payments.
- X Agriculture is precluded from selling loans made by the Agricultural Credit Insurance Fund.

COMMERCE

- X NOAA is prohibited from commercializing meteorological satellites.
- X NOAA is required to use appropriated funds for certain projects.
- X The Department of Commerce is prohibited from selling its economic development loans.
- X The National Technical Information Service is prohibited from contracting out services.

DEFENSE

- X Minimum civilian employment levels exist at Army depots.
- X The Department of Defense is prohibited from contracting out security and fire-fighting services.
- X The Crane Army Ammunition Activity and McAlester Army Ammunition Plants are prohibited from contracting out services.
- X The Department of Defense is prohibited from contracting out core logistics maintenance functions.
- X The Philadelphia Defense Personnel Support Center is prohibited from contracting out services.
- X The Department of Defense is prohibited from contracting out any activity performed by 10 or more civilian employees.
- X The Department of Defense is prohibited from contracting out logistics activities to non-governmental personnel.
- X The Department of Defense is prohibited from contracting out entire medical facilities.

- X Officers at Fort Benjamin Harrison, Indiana are prohibited from A-76 procedures.¹⁵
- X A-76 implementation is impeded by complicated requirements for notice and reporting.
- X The Army Corps of Engineers is prohibited from contracting out reservoirs in Mississippi.
- X The Army Corps of Engineers is prohibited from contracting out the operations and maintenance of hydroelectric power facilities.
- X Only installation commanders have the authority to decide which commercial activities will be subject to A-76 review (Nichols amendment).

ENERGY

- X The Department of Energy is prohibited from studying alternative pricing structures.
- X The Department of Energy is prohibited from studying the sale of the Power Marketing Administrations, except Alaska.
- X The Department of Energy is prohibited from using appropriations for the privatization of the Naval Petroleum Reserves.
- X The Department of Energy is prohibited from studying or proposing the privatization of the uranium enrichment programs.

GENERAL SERVICES ADMINISTRATION

- X GSA is prohibited from contracting out certain intra-agency service positions.

HEALTH AND HUMAN SERVICES

- X The FDA is prohibited from adopting user fees.
- X The Social Security Administration is prohibited from contracting outside the United States for printing services.

HOUSING AND URBAN DEVELOPMENT

- X HUD is prevented from selling section 202 loans.
- X Minimum employment levels exist within the Public and Indian Housing Program.
- X HUD is prohibited from selling section 312 direct loans.

¹⁵ A-76 is the title of the OMB circular that outlines and regulates the process and procedures for federal contracting out of competition.

INTERIOR

- ✗ The National Park Service, Fish and Wildlife Service and Bureau of Land Management are prohibited from contracting out any services.

JUSTICE

- ✗ The Department of Justice is prohibited from contracting out any functions involving law enforcement, litigation or the administration of justice.
- ✗ The Department of Justice is prohibited from the sale of loans or guarantees held by the Federal Financial Bank.

LABOR

- ✗ The Job Corps is forbidden to contract out any Civilian Conservation Center.

TRANSPORTATION

- ✗ The FAA is prohibited from contracting out maintenance for national airways system facilities.
- ✗ The Coast Guard must delay the A-76 process for congressional review.
- ✗ Minimum employment levels exist within the FAA for air traffic controllers.
- ✗ The Department of Transportation is prohibited from funding changes in the current federal status of the Transportation Systems Center or the Turner-Fairbank Highway Research Center.

TREASURY

- ✗ Minimum employment levels exist at the Customs Service despite the fact that automation has reduced the need for large staffing levels.

VETERANS AFFAIRS

- ✗ Minimum employment levels exist within the VA medical care staff.
- ✗ The Department of Medicine and Surgery is prohibited from contracting out certain activities.

RAILROAD RETIREMENT BOARD

- ✗ Minimum employment levels exist within the Railroad Unemployment Insurance Trust Fund.

SMALL BUSINESS ADMINISTRATION

- ✗ The SBA is prohibited from selling loans held or guaranteed by SBA and held by FFB.