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Corporate Welfare in the Federal Budget

by Tad DeHaven

Executive Summary

Rising federal spending and huge deficits are pushing the nation toward a financial and economic crisis. Policymakers should find and eliminate wasteful, damaging, and unneeded programs in the federal budget. One good way to save money would be to cut subsidies to businesses. Corporate welfare in the federal budget costs taxpayers almost $100 billion a year.

Policymakers claim that business subsidies are needed to fix alleged market failures or to help American companies better compete in the global economy. However, corporate welfare often subsidizes failing and mismanaged businesses and induces firms to spend more time on lobbying rather than on making better products. Instead of correcting market failures, federal subsidies misallocate resources and introduce government failures into the marketplace.

While corporate welfare may be popular with policymakers who want to aid home-state businesses, it undermines the broader economy and transfers wealth from average taxpaying households to favored firms. Corporate welfare also creates strong ties between politicians and business leaders, and these ties are often the source of corruption scandals in Washington. Americans are sick and tired of "crony capitalism," and the way to solve the problem is to eliminate business subsidy programs.

Corporate welfare doesn't aid economic growth and it is an affront to America's constitutional principles of limited government and equality under the law. Policymakers should therefore scour the budget for business subsidies to eliminate. Budget experts and policymakers may differ on exactly which programs represent unjustified corporate welfare, but this study provides a menu of about $100 billion in programs to terminate.

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Recent subsidy scandals—such as the failure of solar manufacturer Solyndra—have heightened public awareness of the waste and injustice of corporate welfare.

Introduction

The federal government will spend almost $100 billion on corporate welfare in fiscal 2012. That includes direct and indirect subsidies to small businesses, large corporations, and industry organizations. These subsidies are handed out from programs in many departments, including the departments of Agriculture, Commerce, Energy, and Housing and Urban Development.

There have been some efforts to cut corporate welfare in the past, but recent events make the need for subsidy cuts even more acute. For one thing, the federal government will run its fourth consecutive deficit in excess of a trillion dollars this year. Federal debt is approaching levels that most economic experts believe is dangerous. If the nation is to avert a debt crisis, federal policymakers need to dramatically cut spending. Whole programs need to be terminated, and handouts to businesses are a good place to start.

The problems created by corporate welfare spending include violating limited government, distorting the economy, picking winners and losers, and generating corruption. Some of the other ways that the government confers narrow benefits on favored businesses are through tax preferences, regulations, and trade barriers.

Recent subsidy scandals—such as the failure of solar manufacturer Solyndra—have heightened public awareness of the waste and injustice of corporate welfare. But wasteful corporate welfare has a long bipartisan history. Now is the time for policymakers to scour the budget and end similar programs that abuse taxpayer interests on an ongoing basis.

Almost $100 Billion in Corporate Welfare

This study is based on a line-by-line review of the federal budget looking for business subsidies. There have been numerous efforts by the Cato Institute and other groups over the years to define and calculate federal corporate welfare spending, which is not an exact science.[1] Nonetheless, included here are programs that provide payments or unique benefits and advantages to specific companies or industries.

Table 1 presents a list of corporate welfare programs in the budget, totaling $98 billion in spending in fiscal 2012.[2] These programs should be targeted for elimination as one step to getting federal spending and deficits under control. The following sections discuss the reasons why these programs are damaging, unneeded, and unfair.

Violating Limited Government and Equal Treatment

Under the Constitution, the federal government has specific, limited powers, and most government functions are left to the states. Federal powers enumerated in the Constitution include those designed to ensure an open national economy. But nowhere in the document is an open-ended power for Congress or the executive branch to choose favored businesses and appropriate funds to aid their private profit-seeking.

The enumerated powers granted to the federal government under Article 1, Section 8 were intended to limit the scope of federal authority. However, over time the courts have adopted an excessively broad interpretation of these powers. As a result, federal power in many areas has become largely unlimited, and many policymakers feel free to tax citizens to pay for all kinds of subsidy programs.

While many policymakers ignore constitutional limits when creating new programs, others sometimes justify business subsidies by adopting an expansive view of the General Welfare Clause. Article I, Section 8 says that Congress shall have the power to "lay and collect Taxes, Duties, Imposts and Excises, to pay the Debts and provide for the common Defence and general Welfare of the United States." That provision authorized the federal government to collect and spend money on the activities specified. It does not authorize

Table 1
Corporate Welfare Programs in the Federal Budget (millions of dollars)

Program	2012 Outlays
Department of Agriculture	
Agricultural Marketing Service	1,289
Applied R&D	1,143
Farm Security and Rural Investment programs	3,175
Farm Service Agency	11,863
Foreign Agricultural Service	2,164
Risk Management Agency	3,829
Rural Business-Cooperative Service	372
Rural Utilities Service	1,330
Total, Department of Agriculture	25,165
Department of Commerce	
Applied R&D	785
Economic Development Administration	531
International Trade Administration	379
Minority Business Development Agency	24
National Institute of Standards and Technology	
Technology Innovation Program	8
Manufacturing Extension Partnership	131
National Oceanic and Atmospheric Administration	
Fisheries Finance Program	6
Fishery promotion and development subsidies	4
National Telecommunications and Information Administration	
Broadband Technology Opportunities Program	2,227
Total, Department of Commerce	4,095
Department of Defense	
Applied R&D	4,737
Total, Department of Defense	4,737
Department of Energy	
Energy supply and conservation	9,834
Fossil energy research and development	1,402
Advanced Technology Vehicles Manufacturing Loan Program	4,834

Program	2012 Outlays
Innovative Technology Loan Guarantee Program	1,260
Total, Department of Energy	17,330
Department of Housing and Urban Development	
Federal Housing Administration mortgage subsidies	15,739
Community Development Block Grants (to businesses)	285
Community Development Loan Guarantees	17
Total, Department of Housing and Urban Development	16,041
Department of the Interior	
Bureau of Reclamation	1,254
Bureau of Land Management	1,354
Total, Department of the Interior	2,608
Department of State	
Foreign Military Financing	5,201
Total, Department of State	5,201
Department of Transportation	
Federal Aviation Administration	
Commercial Space Transportation	16
Essential Air Service/Payments to Air Carriers	203
Federal Railroad Administration	
High-Speed Rail	1,251
Railroad Rehabilitation & Improvement	17
Railroad research and development	33
Maritime Administration	
Assistance to Small Shipyards	37
Title IX Guaranteed loan program	99
Ocean freight differential subsidies	175
Maritime Security Program	193
Total, Department of Transportation	2,024
Other Programs and Independent Agencies	
Appalachian Regional Commission	53
Export-Import Bank	*
International Trade Commission	91

Program	2012 Outlays
National Institutes of Health: Applied R&D	13,845
NASA: Applied R&D	2,799
National Science Foundation: Applied R&D	450
Overseas Private Investment Corporation	*
Small Business Administration	3,157
Trade and Development Agency	46
Total, Other Programs and Independent Agencies	20,441
Grand Total	**97,642**

Source: *Budget of the United States Government, Fiscal Year 2013* (Washington: Government Printing Office, 2012).
* Program did not have net outlays in FY2012.

the federal government to use its taxing power to bestow widespread benefits on favored commercial interests.

Other times, policymakers look to the Commerce Clause as a reason to intervene in the economy and subsidize businesses. The Constitution gave Congress the power to "regulate Commerce . . . among the several States." However, that provided the authority to remove barriers to interstate trade, not to actively hand out cash to favored businesses. The idea was to limit state government power, not to give discretionary power to the federal government to manipulate businesses and industries.

The Tenth Amendment was supposed to erect a further barrier to the broad discretionary power that today's politicians claim when they hand out subsidies such as corporate welfare. It reserved to the states, or to the people, those powers not specifically delegated to the federal government. Our federal system of government allows the states to subsidize businesses if they choose to do so, subject to their own legal restrictions, although that would still represent bad economic policy.

Federal business subsidies are not just bad economic policy; they also violate the bedrock American principle of equality under the law. Subsidies give advantage to selected interests at the expense of other businesses and taxpayers. The federal government's proper role in the economy should be that of a neutral referee, with intervention limited to facilitating the free exchange of goods and services.

The following are examples of the expansiveness of corporate welfare in the federal budget today. These programs violate equal treatment under the law and have no place under the framework of limited government and federalism established by the Constitution.

Community Development Block Grants. The Department of Housing and Urban Development's Community Development Block Grant program funds efforts to develop local communities. A large portion of the funding is channeled to businesses. For example, a craft brewery in Michigan recently received $220,000 to help it expand its brewing capacity.[3] That subsidy might be good for the brewery, but it was paid for by raiding the wallets of federal taxpayers, who will have less money to buy their own favored beverages and other products. This handout is also unfair to the hundreds of craft breweries that do not receive federal handouts, and instead rely on the voluntary sale of their products to consumers.

Rural Subsidies. The Department of Agriculture's Rural Business-Cooperative Service provides subsidies to businesses in rural areas of the country. One of its programs, the

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Value-Added Marketing Grant program, will hand out about $56 million this year to "producers of agricultural commodities" to help them make and market their products. Wineries across the country have recently been receiving these grants.[4] Once again, the grants are good for the particular wineries, but they come at a cost to both taxpayers and to wineries that don't receive federal aid. In addition, it is unfair for the federal government to run aid programs that favor rural areas of the country over urban areas, and vice versa. Americans are free to move wherever they want, and they can balance the costs and benefits of living or working in each location.

Minority Business Subsidies. The Department of Commerce's Minority Business Development Agency is supposed to provide management and technical services to minority-owned businesses. However, much of its $24 million budget is spent on bureaucratic overhead costs.[5] More importantly, federal programs should be race-neutral, and not favor some ethnic groups over others. Some of the largest obstacles to the success of minority and nonminority entrepreneurs alike are excessive taxes and regulations. The government would aid all businesses, including minority businesses, if it focused on removing burdensome costs from productive entrepreneurs.

Farm Subsidies. Federal farm programs redistribute wealth from taxpayers to a small group of relatively well-off farm businesses and landowners. The United States Department of Agriculture figures show that the average income of farm households has been consistently higher than the average of all U.S. households. In 2010, the average income of farm households was $84,400—or 25 percent higher than the $67,530 average of all U.S. households.[6] Moreover, the majority of farm subsidies go to the largest farms. For example, the largest 10 percent of recipients received 68 percent of all commodity subsidies in 2010.[7] Numerous large corporations, and even some wealthy celebrities, receive farm subsidies because they are the owners of farmland. In fact, owners of land that is no longer used for farming have received billions in subsidies over the years.[8]

Distorting Economic Activity

Policymakers justify business subsidies by saying they are needed to fix alleged imperfections in the marketplace. The theory is that policymakers can design optimal subsidies in the national interest to remedy easily identified "market failures." The reality is that policymakers usually have parochial interests in mind when they create subsidy programs. And instead of making markets more efficient, subsidies distort economic activity and create even larger failures than might have existed in the marketplace.

By aiding some businesses, subsidies put other businesses at a disadvantage. For example, businesses that don't receive a loan backed by the government are disadvantaged when they compete against businesses that do receive government backing. Diverting resources from businesses preferred by the market to those preferred by policymakers leads to losses for the overall economy.

The following are examples of federal subsidy programs that distort economic activity and, thus, represent government failure:

Housing Subsidies. Policymakers have long argued that the government should intervene in housing markets to make the "American dream" available to more people. One government intervention is to guarantee mortgage loans issued by private lenders—an effective subsidy—through the Federal Housing Administration (FHA). The FHA insures lenders for 100 percent of the principal and interest on mortgages issued with small down payments. However, data shows that the smaller the down payment, the higher the possibility of a loan default.[9] To cover these losses, the FHA charges lenders fees on the mortgages it insures. Private mortgage insurers provide the same service, but they face bankruptcy if they insure risky loans without sufficient fees to recoup losses. The FHA, on the other hand, can tap taxpayers if it doesn't take in sufficient fee revenues to cover mortgage defaults. This year, the budgetary cost of paying bad loans that would otherwise be borne by lenders will be around $16 billion.

These losses to taxpayers from housing subsidies are only part of the problem. Housing subsidies also inflict damage on the broader economy, as is clear in the aftermath of the housing meltdown and financial crisis of recent years. The housing bubble was generated, in part, by government efforts to increase homeownership, which in turn fostered distortions in the housing market. However, instead of learning their lesson after the bubble burst and allowing the housing market to self-correct, policymakers have continued to intervene and subsidize. In recent years, policymakers have been using the FHA to try to help prop up the housing market and the agency's lending portfolio has soared to over $1 trillion.[10]

Small Business Subsidies. Policymakers argue that under market-driven lending, some worthy small businesses would be denied credit. And so Congress has tasked the Small Business Administration (SBA) with correcting this alleged market failure. The SBA tries to increase lending to small businesses by guaranteeing loans issued by private lenders for up to 85 percent of losses in the event that loan recipients default. As a result of the guarantee, lenders are more willing to lend money to riskier applicants because the taxpayer-backed SBA is ultimately responsible for the bulk of any losses.

However, the notion that the government needs to subsidize credit to small businesses is mistaken. Capital markets have developed effective private solutions, such as credit scoring, that enable lenders to make more prudent lending decisions. Second, small businesses with sound business plans and solid prospects should be able to raise debt and equity capital through private means. If a small business has shaky finances and questionable prospects, it should be denied private capital as a bad business risk. Indeed, the large failure rates on loans backed by the SBA illustrate that the government's credit market interventions do a poor job of allocating capital.[11]

Water Subsidies. For more than a century, the Interior Department's Bureau of Reclamation has subsidized irrigation in 17 western states. It builds and operates dams, canals, and hydroelectric plants. About four-fifths of water supplied by Reclamation goes to farm businesses, and the agency under-prices water to those users the most. These subsidies encourage farmers to grow crops in areas where it is inefficient or unsuitable to do so. Because farmers receive federal water at a small fraction of the market price, they overconsume it, which is leading to increasing battles over water supplies in many regions. Another result of subsidized Western irrigation is the environmental damage to rivers and wetlands—damage that the federal government, in turn, spends more taxpayer money trying to fix.[12]

High-Speed Rail. The Obama administration has poured billions of dollars into trying to develop a high-speed rail network. But if high-speed rail made economic sense, the private sector would build it without government subsidies. For example, freight rail makes economic sense, and private rail businesses heavily invest in building and maintaining their rail systems and rolling stock.

Even in more densely populated areas, such as Europe and Japan, where high-speed rail might make sense, rail operators are dependent on government subsidies.[13] In the United States, passenger rail might make economic sense in certain corridors, such as the Northeast, but we should let the market decide whether passengers are willing to pay for high-speed service.

Interestingly, a Florida company recently announced plans to build and operate a completely privately financed rail line that would connect Miami to Orlando.[14] If it fails, at least taxpayers won't be on the hook. If it succeeds, it could provide a model to other entrepreneurs. Contrast that with a Nevada company with ties to Sen. Harry Reid (D-NV) that is seeking a $4.9 billion loan from the Federal Railroad Administration (FRA) to build a rail line between Las Vegas and Victorville, a city 81 miles east of Los Angeles. The project makes little economic sense, and prompted the *Washington Post* to call for the FRA to "derail this gravy train."[15]

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Undermining Markets by Picking Winners—and Many Losers

Policymakers do not possess special knowledge that enables them to allocate capital more efficiently than markets.

Policymakers do not possess special knowledge that enables them to allocate capital more efficiently than markets. They are no more clairvoyant about market trends and scientific breakthroughs than anyone else. Thus, when the government starts choosing industries and technologies to subsidize, it often makes bad decisions at taxpayer expense. Businesses and venture capital firms make many mistakes as well, but their losses are private and not foisted involuntarily on taxpayers.

In addition to the money that's often wasted when policymakers try to steer the market in certain directions, government meddling can also delay the development of superior alternatives by entrepreneurs who don't receive subsidies. That's because private investors usually prefer to provide capital to projects that are subsidized over ones that are not. Private investors, such as venture capitalists, make investments based on the perceived risk and expected returns. Thus, when the government gives a company a financial leg-up over its competitors, a private investor's upside potential is enhanced, while the downside risk remains limited to the amount it invested.

The following are examples of federal programs that subsidize businesses in an attempt to pick winners:

Energy Subsidies. The U.S. Department of Energy (DOE) has been subsidizing the development and commercialization of "alternative" fuels for decades. Successive administrations have attempted to plan for the country's future energy needs by effectively throwing taxpayer money against a wall and hoping that something will stick. For example, the DOE has been funding "clean coal" research for decades, but it has little to show for the effort.[16] Every president from Ronald Reagan to Barack Obama has supported clean coal subsidies. Unfortunately, clean coal has been a costly and unproductive exercise from the taxpayers' point of view, and it remains unpopular with environmentalists. The Government Accountability Office found that many clean-coal projects have "experienced delays, cost overruns, bankruptcies, and performance problems."[17] More recently, the Obama administration's costly campaign to increase subsidies for alternative energy sources, including solar and wind, has been marked by high-profile failures and scandal, which is discussed below.

Automaker Subsidies. The Department of Energy's Advanced Technology Vehicles Manufacturing (ATVM) Loan Program provides subsidies to companies to develop "greener" automobiles. Companies that have received assistance from the ATVM program include Ford and Nissan.[18] In a 2009 article in *Wired* magazine, Darryl Siry, a former executive with Tesla Motors, which received an ATVM loan, wrote that startup companies applying for energy subsidies "have admitted that private fundraising is complicated by investor expectations of government support."[19] Siry notes that the government trying to pick winners distorts the market for private capital, which "will have a stifling effect on innovation, as private capital chases fewer deals and companies that do not have government backing have a harder time attracting private capital."[20]

The ATVM program is just the latest attempt by policymakers to create greener cars. In 1993, the Clinton administration launched its Partnership for a New Generation of Vehicles. This program handed out $1.2 billion over eight years to U.S. automakers for the development of hybrid cars. The program was widely panned, but instead of eliminating such subsidies altogether, the George W. Bush administration replaced it with a new initiative called FreedomCar. This program focused on developing automobiles that would run on hydrogen fuel cells, and it cost taxpayers about $2 billion.[21] The Obama administration announced in 2009 that the government was "moving away from funding vehicular hydrogen fuel cells to technologies with more immediate promise."[22]

Rural Broadband Subsidies. The 2009 federal stimulus law contained $7.2 billion to subsidize rural broadband service through the

Department Agriculture's Rural Utility Service and the Department of Commerce's National Telecommunications and Information Administration. A recent study found that the subsidies provide coverage in areas where the majority of households already have access to service.[23] As a result, the benefit of providing broadband services to the relatively small number of unserved households is dramatically outweighed by the exorbitant cost to taxpayers. The authors note that subsidizing the construction of duplicative broadband networks creates "strong disincentives to private broadband investment in the long run, as potential future investors will discount expected returns for the possibility that the government may step in, *ex post*, to subsidize a competitor."[24]

Information technologies have rapidly evolved and will continue to do so as long as the regulatory climate remains friendly. A Cato analysis on broadband subsidies explained, "what attracts new competitors is the ability to make a profit by offering lower prices or better service to the existing providers' current customers, or by serving customers whom those providers have yet to serve."[25] However, the government's subsidization of existing technologies reduces the incentive to develop even more advanced technologies.

Research Subsidies. The Constitution allows the federal government to "promote the Progress of Science and useful Arts, by securing for limited Times to Authors and Inventors the exclusive Right to their respective Writings and Discoveries." The securing of patents has long provided a stimulus to private research, discovery, and product development. America's great technological advancements have mainly come from private-sector efforts aimed at creating better products and earning profits.

There is a theoretical argument for the government doing some "basic" scientific research, but there is less support for the government meddling in applied and development-oriented research. And even the government's basic research can be unproductive and pork-barrel in nature. Government research proponents often argue that federal funds are necessary to support high-risk investments that the private sector would not undertake. However, the private sector undertakes risky projects all the time. Consider the growing interest in private space travel spurred by the 2004 launch of SpaceShipOne, the world's first private manned space flight. That flight was funded by Microsoft co-founder Paul Allen. Other wealthy entrepreneurs have launched their own space projects. A new company backed by billionaire investors, including Google's Larry Page and Eric Schmidt, recently announced that it is developing plans to mine asteroids for precious metals.[26]

Policymakers often claim that they want to invest in "high reward" areas, but with fast-changing markets, no one knows whether risky ventures will end up being lucrative or flops. Even the smartest venture capitalists invest in duds, but at least the costs of those failures are borne by private investors. With government-funded research, the costs of failed investments are borne involuntarily by taxpayers.

Funding new businesses should be left to the experts in the venture capital and angel investment industries. These types of investors pump about $50 billion annually into innovative companies.[27] There would be even more funding of private innovation if policymakers freed U.S. capital markets from excessive tax and regulatory burdens.

A Corrupting Relationship

Business subsidies create an unhealthy —and sometimes corrupt—relationship between businesses and the government. The more that the government intervenes in the economy, the more lobbying activity is generated. The more subsidies that it hands out to businesses, the more pressure lawmakers face to hand out new and larger subsidies. As the ranks of lobbyists grow, more economic decisions are made on the basis of politics, more resources are misallocated, and the nation's standard of living is harmed.

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The unhealthy relationship between government and business is not just a modern phenomenon. Since the dawn of the Republic, federal policies have often been driven by business interests at the expense of taxpayers and consumers. In the 1790s, the Whiskey Rebellion stemmed from Congress—at the behest of Alexander Hamilton—passing an excise tax on whiskey that fell unevenly on small-scale distillers in the frontier lands west of the Appalachians. The large distillers in the more economically developed east recognized the competitive advantage it gave them over the small producers and supported the tax.

In the 1870s, the Credit Mobilier scandal stemmed from subsidies for the transcontinental railroads, and the tight connection of those subsidized businesses with some members of Congress.[28] In the 1920s, the Teapot Dome scandal stemmed from the Secretary of the Interior secretly handing out oil leases to certain favored businesses and receiving a $400,000 payoff.[29]

In his book *The Big Rip-Off: How Big Business and Big Government Steal Your Money*, reporter Timothy Carney describes Hamilton as "the first big champion of big government in the United States" based partly on his support of business subsidies.[30] Unfortunately, we are living today with all the problems created by Hamilton's flawed vision of the government "helping" the private sector. As Carney explains, big businesses have been helping big government grow for more than a century:

> Federal regulation of meatpacking was the desire of large meat packers. U.S. Steel turned to Teddy Roosevelt for salvation from laissez-faire. Woodrow Wilson seized control of the U.S. economy to the elation of big business. Herbert Hoover laid the groundwork for the New Deal, with the support of Henry Ford and Pierre DuPont. Franklin D. Roosevelt's New Deal found its greatest champions among top business leaders. Big business guided the drafting of the Marshall Plan. Dwight Eisenhower deflated conservative hopes of cutting government, thus elating corporate America. Lyndon Johnson, the icon of big government, was the favorite of big business.[31]

The story has continued in recent years, as the following examples illustrate:

HUD Subsidies. In the 1980s, President Ronald Reagan's Department of Housing and Urban Development (HUD) overflowed with corruption under Secretary Sam Pierce.[32] Pierce routinely dished out grants, loans, and other sorts of subsidies to friends and private business associates. And HUD created programs that involved large subsidies to mortgage lenders, developers, and other businesses, with Republican Party contributors as frequent beneficiaries.

Trade Subsidies. In the 1990s, the Clinton administration used the Department of Commerce to raise money for the Democratic Party by giving top business executives access to export promotion trips abroad in exchange for donations. The scheme was orchestrated by Commerce secretary Ron Brown, formerly head of the Democratic National Committee and a top Clinton campaign fundraiser. Business leaders who played the game and made campaign contributions not only got taken on trade missions, but were also rewarded with loans from the federal Overseas Private Investment Corporation, which subsidizes American exports. The *Boston Globe* found a "massive amount of OPIC support given to companies that traveled with Brown and donated to the Democrats."[33] Conveniently, one of Brown's top lieutenants at Commerce also served on the board of directors of OPIC.

Ron Brown died in a plane crash in April 1996 in Bosnia while on a trade mission, but investigations into his dealings continued. In 1998, U.S. District Judge Royce Lamberth determined that Commerce officials systematically concealed and destroyed documents relating to the trade mission scandal.[34] He compared the behavior of Commerce officials to that of "con artists" and "scofflaws," pointing to the "flurry of document shredding in the Secretary's office" after Brown died.[35]

Enron Subsidies. Enron Corporation is a poster child for the harm of business subsidies, particularly with regard to its disastrous foreign investments. Enron lobbied government officials to expand export subsidy programs, and it received billions of dollars in aid for its projects from the Export-Import Bank, the Overseas Private Investment Corporation, the U.S. Trade and Development Agency, the U.S. Maritime Administration, and other agencies. Enron received about $3.7 billion in financing through federal government agencies.[36]

Business subsidies create damaging economic distortions. All those subsidies to Enron induced the firm to make exceptionally risky foreign investments. And the resulting losses were an important factor in the company's implosion.[37]

A 2010 *Bloomberg* investigation, which looked at the Ex-Im Bank, found that companies seeking financing aid from this agency had been paying the travel expenses of government employees on visits to projects under consideration.[38] For instance, Exxon Mobil spent almost $100,000 on Ex-Im Bank employees responsible for helping the agency decide whether it should aid Exxon on a major gas project in Papua New Guinea. Eleven months later, the Ex-Im Bank approved $3 billion in financing for the venture.

Early in the Bush administration, high-level officials went to considerable lengths to help Enron on an investment in India that had gone bad.[39] When the *Washington Post* reported this in 2002, the administration argued that it was simply trying to guard taxpayer interests in the more than $600 million in federal loans that had been given to Enron by Ex-Im and the Overseas Private Investment Corporation.[40] However, the government should not be putting taxpayer money into such risky private schemes in the first place.

Maritime Subsidies. The Federal Maritime Administration's Title XI program guarantees loans made to companies to purchase vessels constructed in U.S. shipyards. Previous administrations have tried to eliminate the program, but members of Congress with constituents that directly benefit from the program have kept it alive, despite losses to taxpayers. A Bloomberg report cites the example of former Sen. Trent Lott (R-MS) and Sen. Daniel Inouye (D-HI), prominent supporters of the loan guarantee program. One particular company, which was owned by a billionaire real estate developer, received a $1.1 billion Title XI loan guarantee for two cruise ships to be built in Senator Lott's hometown of Pascagoula, Mississippi. Senator Inouye sponsored a provision in a defense bill that give the company the exclusive rights to operate cruise ships in Hawaii. The company eventually went bankrupt, costing taxpayers $187 million.[41]

Green Subsidies. One of the Obama administration's chief policy initiatives has been to spur the development of a "green" economy by subsidizing alternative energy companies. However, as the *Washington Post* reported, "Obama's green-technology program was infused with politics at every level."[42] The Department of Energy $535 million loan guarantee awarded to the now-bankrupt solar company, Solyndra, is the prime example. Solyndra first applied for a federal loan in 2007, when President George W. Bush was in office. The Department of Energy finally approved a loan in September 2009, after receiving repeated pressure from Obama administration officials to make a decision on the loan so that Vice President Biden could announce the approval at a groundbreaking for the company's factory.[43] The following May, President Obama visited Solyndra and called it an "engine of economic growth."[44]

A little more than a year after Obama's visit, Solyndra filed for bankruptcy protection. Administration officials had received numerous warnings that Solyndra's financials were shaky; however, Obama's advisers remained preoccupied with political considerations.[45] The *Post* noted that the "main players in the Solyndra saga were interconnected in many ways, as investors enjoyed access to the White House and the Energy Department."[46] According to the *New York Times,* Solyndra "spent nearly $1.8 million on Washington lobbyists, employing six firms with ties to members of Congress and officials of the Obama White

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House" during the period of time that its loan request was under review by the Department of Energy.[47] The interconnected relationship between investors and the administration goes beyond Solyndra. The *Washington Post* found that "$3.9 billion in federal grants and financing [from the Department of Energy] flowed to 21 companies backed by firms with connections to five Obama administration staffers and advisers."[48]

Other Types of Corporate Welfare

Tax Preferences

The federal tax code contains many deductions, credits, and exemptions that distort investment and create unequal tax treatment of individuals and businesses. The government defines "tax expenditures" as "revenue losses attributable to provisions of the federal tax laws which allow a special exclusion, exemption, or deduction from gross income or which provide a special credit, a preferential rate of tax, or a deferral of tax liability."[49] Note that "tax expenditures" is a loaded term, since tax cuts are not the same as spending increases. Also, the official lists of tax expenditures are not carved in stone, and indeed they include a bias in favor of broad-based income taxation, which penalizes saving and investment.[50]

Nonetheless, the enactment of special tax preferences is bad policy, and preferences for businesses are a form of corporate welfare. Some of the arguments made in this paper against corporate welfare spending also apply to business tax preferences:

- Tax preferences distort economy activity by redirecting investment toward businesses that are favored by policymakers. The quintessential example is the various tax credits offered to producers of alternative energies, such as wind and solar power.
- Tax preferences benefit particular businesses to the detriment of others. Businesses that don't produce a product favored by policymakers will face higher tax burdens on their investments than the favored firms.
- Tax preferences empower special interests. One of the biggest obstacles to comprehensive tax reform is the opposition of special-interest groups who enjoy advantages in the tax code. These groups will fight to maintain their special treatment and tend to block overall tax reform.
- Tax preferences help foster an unhealthy relationship between the government and businesses. As mentioned above, a large scandal during the Reagan administration involved the flow of tax credits and other housing subsidies to politically connected Republicans via the Department of Housing and Urban Development.[51]

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Regulations

Some people might assume that government regulations on businesses always serve the general public interest. In reality, regulations often serve the interests of the industry being regulated—a situation referred to as "regulatory capture." Nobel laureate economist George Stigler explained that "as a rule, regulation is acquired by the industry and is designed and operated primarily for its benefits."[52] Regulatory capture occurs because some businesses in an industry that is being regulated have an incentive to influence the drafting of regulations to give themselves an economic advantage over consumers or other businesses. Instead of benefiting the public, regulations often end up stifling competition, which causes reduced innovation, fewer choices for consumers, and higher prices.

Federal regulations, as a whole, are very expensive to the economy. Economists Nicole Crain and Mark Crain estimate the annual cost of regulations to be $1.75 trillion.[53] That amounts to a massive hidden tax on the economy. In addition, it cost taxpayers about $55 billion in 2011 for the federal government to develop and enforce federal regulations.[54]

Tim Carney examines corporate welfare issues, including regulations, in the *Washington Examiner*'s "Beltway Confidential" column. The following are some recent examples he found of businesses manipulating regulations to their own advantage:

- The Internal Revenue Service wants to require tax preparers to pass a test and pay a fee in order to continue doing business. The nation's two largest tax preparation companies, H&R Block and Jackson Hewitt, are supporting the IRS effort because the regulatory burden would make it harder for smaller tax preparation firms to compete with them. Carney notes that H&R Block hired lobbyists immediately after the IRS's announcement, and that the IRS official in charge of writing the rules is H&R Block's former CEO.[55]
- The Obama administration's controversial decision to mandate that health insurance companies provide contraceptive coverage is a boon to pharmaceutical companies. The contraceptives must be FDA-approved, and deductibles or co-pays are not allowed to be required for the benefit. That means consumers need not worry about the price of the contraceptive, which favors producers of name-brand contraceptives. Carney notes that shortly after he approved the mandate, the president "travelled up to New York City to collect $35,800 checks at a fundraiser hosted by the top lobbyist at the nation's largest drug company—Sally Susman, VP for government affairs at Pfizer."[56]
- The Environmental Protection Agency recently ordered large trucks to reduce their greenhouse-gas emissions. Truck operators will have to spend $50,000 or more per vehicle to upgrade their rigs or buy a new truck that meets the EPA's requirement. The powerful American Trucking Association supports the requirement, while smaller owner-operators are opposed. The reason is simple: the requirement will squeeze out the small operators to the benefit of the larger operators. Carney notes that the former Republican governor who heads the ATA, Bill Graves, "has a record of using big government to protect his industry."[57]

Trade Barriers

International trade plays a crucial role in the growth and prosperity of the United States. Trade generates competition, promotes transfers of technology, and allows consumers and businesses access to the best products worldwide. The result is innovation, higher productivity, and rising living standards. However, the federal government lessens the benefits of open trade when it restricts imports.

A prime example of the damage caused by trade restrictions comes from the federal government's sugar policies. The government guarantees a minimum price for sugar in the domestic market by maintaining a system of price supports, domestic marketing quotas, and import barriers. As a result of these policies, U.S. sugar prices have been more than twice world market prices, to the benefit of U.S. sugar producers. While these producers gain, the government's sugar policies cost American consumers about $1.9 billion annually.[58] In addition, the artificially high prices hurt American businesses that use sugar, and numerous U.S. companies have decided to move production to Canada and Mexico, where sugar prices are considerably lower.[59]

Another example of harmful trade barriers are the antidumping and countervailing duty laws. These rules allow duties to be imposed on foreign goods that are found to be "unfairly" priced by a complex and bureaucratic process involving the International Trade Administration (ITA) and International Trade Commission. The premise of these laws is that low-price imports are damaging to America. But low prices benefit both U.S. consumers

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and U.S. businesses that use imported products. Like regular business subsidies, the antidumping and countervailing duty machinery is politically driven, and U.S. industries can petition the ITA to conduct investigations on foreign goods that they object to, essentially using government power to attack their competitors. Not surprisingly, one study found strong correlations between political contributions made by firms seeking protection and antidumping outcomes in their favor.[60]

Hurdles to Reform

If federal business subsidies cause more problems than they solve, why do policymakers persist in supporting these interventions? It isn't because business subsidies are particularly popular with voters. Indeed, the federal government's recent bailout of the financial industry has galvanized the public's perception that the relationship between the government and business is often corrupt.

The financial bailout certainly appeared corrupt, given the many government officials who had strong ties to the financial industry. The government responded to the crisis by engineering a massive infusion of taxpayer money into banks and other companies that they deemed "too big to fail." The Congressional Budget Office estimates that the final cost to taxpayers for the Troubled Asset Relief Program (TARP), which was used to provide capital to troubled financial institutions and to bail out Chrysler and General Motors, will be $32 billion.[61] The Office of Management and Budget estimates that it will cost taxpayers $68 billion.[62] And the federal takeover of the failed government-sponsored mortgage giants, Fannie Mae and Freddie Mac, has cost taxpayers more than $180 billion.[63]

Two polls of likely voters by Rasmussen Reports in 2011 found little support for corporate welfare programs.[64] A majority said that the federal government shouldn't guarantee loans issued by private lenders to small businesses or finance the sale of military weapons from U.S. companies to foreign countries. Only 29 percent said the government should help finance export sales for large corporations. A plurality (46 percent) said farm subsidies should be abolished. Similarly, polls continue to show strong public opposition to the 2008 federal bailout of the financial industry. For example, a 2010 Pew Research Center/*National Journal* poll found that only 13 percent would be more likely to vote for a candidate who supported federal loans to banks, while 46 percent said they would be less likely.[65]

Nonetheless, most people aren't kicking down the doors of Congress to demand that particular corporate welfare programs be ended. That is because the cost of each particular subsidy represents just a tiny portion of the average household's total tax bill. By contrast, the businesses that receive subsidies have a strong incentive to spend time and money lobbying policymakers to protect their benefits. A major reason why policymakers continue to support business subsidies is the disproportionate influence of special interests.

It is tough for the average citizen to compete with the paid professionals who defend each program. Many policymakers champion the merits of special-interest causes after being sold on their virtues by listening to lobbyists' bullet points year after year. Policymakers in Washington are surrounded by doting staffers, political operatives, and persistent lobbyists representing countless special interests. The result is an endless stream of input encouraging them to spend more money. Many policymakers learn to enjoy the adulation of special-interest groups, and most fear the flak they would receive from other elected officials and interest groups if they actually tried to cut spending.

Congressional committee hearings tend to reinforce the pro-spending echo chamber in Washington. A study conducted by former Yale professor James Payne showed that committee hearings are dominated by witnesses in favor of more spending. Payne surveyed 14 congressional committee hearings and found that "in those 14 hearings, 1,014 witnesses appeared to argue in favor of programs and only 7 spoke against them, an imbalance of 145 to 1."[66] Witnesses, who typically include representatives from lobbying groups, federal agencies, and even members of Congress, rarely admit that any program is a failure or unnecessary. They don't admit failure because they are vested in the continued funding of programs: their careers, pride, and reputations are on the line.

Conclusions

Rising spending and huge deficits are pushing the nation toward an economic crisis. There is general agreement that policymakers need to find wasteful and damaging programs in the budget and terminate them. Corporate welfare is a perfect target. It misallocates resources and induces businesses to spend time on lobbying rather than on making better products. It is unfair to taxpayers and it generates corruption.

When the government subsidizes businesses, it weakens profit-and-loss signals in the economy and undermines market-based entrepreneurship. Most of America's technological and industrial advances have come from innovative private businesses in competitive markets. Indeed, it is likely that most of our long-term economic growth has come not from existing large corporations or governments, but from entrepreneurs creating new businesses and pioneering new industries. Such entrepreneurs have often had to overcome barriers put in place by governments and dominant businesses that are receiving special treatment.

Unfortunately, corporate welfare programs are fiercely protected by the recipients and their lobbyists. The voice of the average taxpaying citizen is drowned out by the pro-spending echo chamber in Washington. Many policymakers convince themselves of the merits of business subsidies after being inundated with the talking points in favor. Other policymakers don't want to offend their fellow legislators by targeting programs for cuts, and so they just "go along to get along."

Despite these hurdles to reform, Congress is entirely capable of cutting spending and will have to do so in coming years to avoid an economic calamity. Financial markets will simply not allow the government to run trillion dollar deficits endlessly. When Congress does start cutting, corporate welfare should be high on the list.

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