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Corporate Welfare

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Welfare bums and welfare queens are by no means limited to the public housing projects. They are also to be found in the corporate boardrooms of some of the most prestigious business firms in the nation, but wherever found, this system is corrupting and inefficient. Government efforts to direct capital to its most productive uses have been a dismal failure, compared to private money managers and entrepreneurs. This is because the latter, but not the former, face a "cruel" market test every day, which weeds out inefficiency.

The phrase *corporate welfare* has been coined to portray the idea that government involvement in the economy is innately corrupting; it also imparts the information that there are welfare bums and welfare queens to be found in the boardroom and not just in the public-housing projects. This particular intervention comes in every conceivable shape and size: grants, sweetheart business deals arranged by the commerce department, cut-rate insurance, low-interest loans, a protective wall against foreign competition, exclusive contracts, and a mind-boggling maze of other special interest privileges (Moore 1997, 3).[1] The phrase conveys the debilitating effects that government subsidies impose on corporations, which parallel the dependent and self-destructive behavior bred by social programs for the poor. Instead of being subsidized with millions of taxpayers' dollars, the fate of ailing corporations should be left up to the cruel market test wherein only the efficient survive the competition.

For most Americans, the term *welfare* is associated with any number of negative images: laziness, illegitimacy, family breakup, irresponsibility, and wasted tax dollars. As welfare brings to mind the image of a "young unwed

mother of two or three infants, huddled in front of a TV set in a public housing tenement and living at taxpayer expense on monthly Aid to Families with Dependent Children (AFDC) checks and food stamps" (Moore 1997, 3), it is striking that America's most costly welfare recipients today are actually Fortune 500 companies—recording best-ever earnings of $24 billion dollars in 1997—costing taxpayers $87 billion per year (Moore 1997, 3).[2]

Upholding his promise to "end welfare as we know it," and urged by the American people to do so, President Clinton signed the Personal Responsibility and Work Opportunity Act (PRWOA) in August of 1996. The Temporary Assistance of Needy Families (TANF) program, which arose from this welfare reform, established a time limit on welfare benefits as well as work, training, or education requirements in exchange for benefits (policyalmanac.org).[3] The result is that the number of people on welfare has declined roughly 50 percent from a 1994 peak, with "record levels of former recipients now working and paying taxes, not collecting them" (Moore 1997).

Unfortunately, none of this reform ethic has taken root in the realm of corporate welfare.[4] In fact, the business community has come to regard subsidy payments as "de facto entitlements." There is no five-years-and-off time limit when it comes to corporate handouts. With the exception of a few "anticorporate welfare warriors"—Republicans, Senator John McCain[5] and Representative John Kasich;[6] Democrats, Senator Russ Feingold and Representative Tom Andrews; and of course Libertarians across the board—almost no one wants to make an enemy of big business. Even though there is bipartisan support for eliminating many major corporate welfare programs, little has been done to reduce the funding for them. While "Congress typically rails indignantly against corporate handouts," it "flinches when it comes time to make the cuts" (Moore 1999, 1). Congress will not even cut the most egregious corporate welfare programs, such as the Department of Commerce's high-tech grants to Silicon Valley, the advertising subsidies for Ralston Purina cat food, and California's dancing raisins (Moore 1999, 4). The Bush Administration has, however, hinted at its "intent to reappraise the federal government's role in subsidizing private businesses" (Slivinski 2001, 2) and included a recommendation of $12 billion in total corporate welfare cuts in its first proposed budget.[7] Though meager, these are the largest proposed cuts in many of these programs' budgets since Ronald Reagan was in the Oval Office (Slivinski 2001, 8).

If corporate welfare is an unproductive end game, why does it keep growing, even in a period of ostensible intensive government cost cutting? For starters, it has good public relations and an army of bureaucrats are working to expand it. A corporate-welfare bureaucracy of an estimated eleven thousand

organizers and agencies has grown up with access to city halls, state houses, the Capitol, and the White House. They offer attractive and well-financed seminars, conferences, and training sessions. They have their own trade associations. They publish their own journals and newsletters. They create attractive Web sites on the Internet; they never call it welfare. Instead they characterize it as "economic incentives," or "empowerment zones," or "enterprise zones" ("Corporate Welfare" 1998, 38).[8]

Whatever the name, the results are the same; corporate welfare is intrinsically unfair. Some companies receive public services at reduced rates, while others pay the full cost. Some companies are excused from paying all or a portion of their taxes due,[9] while others pay the full amount imposed by law. Some companies receive grants, low-interest loans, and other subsidies, while others must fend for themselves ("Corporate Welfare" 1998, 38).

One supposed role of government is to help ensure a level playing field for people and businesses. This so-called level playing field intrinsically calls for minimal interference in the marketplace and substantially reduced tax rates and regulatory burdens. Business subsidies, which are often said to be justified because they correct distortions in the marketplace, actually create huge distortions of their own. Business subsidies divert credit and capital to politically well-connected firms (which are not necessarily the most efficient producers) at the expense of their less politically influential rivals, tilting the playing field in favor of the largest, most politically influential, or most aggressive businesses (Slivinski 2001, 10).

Bureaucrats have a disappointing record of picking winners and losers. The basic premise of federal business subsidies is that the government can direct the limited pool of capital funds just as effectively as, if not better than, venture capitalists and money managers. The core function of private capital markets is to direct investment to industries and firms that offer the highest potential rate of return (Hazlitt 1979, 90). Natural selection occurs independent of any intervention into the free-market system. The truth is that capital markets rely on more sophisticated knowledge, and in much larger quantities, than a government could ever collect, use effectively, or even fathom (Hayek 1948). This fact dooms most capital allocation decisions by bureaucrats to failure (Slivinski 2001, 9). Capital markets require that the President and Congress cut those programs and tax provisions that artificially raise the rate of return for particular corporations,[10] which interfere with market signals for no overriding social or economic purpose (Hazlitt 1979, 90).

Corporate welfare fosters an incestuous relationship between businesses and government. In Washington today, industry trade associations and lobbying

firms continually pressure lawmakers to give out new business subsidies or to protect longstanding handouts. This is a natural byproduct of an administration that uses its power to give taxpayer money to favored interests. If there were no possibility that subsidies might be offered, demands for them would naturally diminish if not disappear altogether. The reality, however, is that the federal government has been redistributing wealth virtually since its inception (Slivinski 2001, 10).

This system is sustained by a budget process that stacks the deck in favor of new spending. It is also nurtured by the problem of diffuse costs and concentrated benefits, as seen when subsidies are given to a few at the expense of many (Moore 1999, 12; Friedman 1962). Because there is such a large number of taxpayers—any given corporate welfare subsidy may cost each taxpayer only a few cents—most individual citizens do not have an interest in lobbying against subsidies; the cost of doing so far outweighs simply paying the taxes. However, the recipients of those subsidies have a substantial interest in making sure they maintain this flow of money. Thus, there is a great deal of lobbying by special interests with very little counteraction on behalf of the longsuffering taxpayer. In addition, subsidies create a perverse incentive for businesses; if their competitors are receiving help from the government, it is in their best interest to try to avail themselves of it too. That incentive serves only to turn many businesspeople into lobbyists, not entrepreneurs (Slivinski 2001, 10).

Some argue that condemning corporate welfare eliminates public policy's influence on the direction of private investment and other resource allocation—thereby hobbling government (Laird and Reich 1998, 74). However, corporate subsidy programs lie outside Congress' strictly limited and enumerated spending authority under the Constitution and thus should be eliminated if only for that reason. Nowhere in the Constitution is Congress granted the authority to spend funds to subsidize the computer industry or to enter into joint ventures with automobile companies or to guarantee loans to favored business owners. The main effects of such corporate welfare programs are to undermine free enterprise and corrupt the political system as well (Moore 1999, 15). Yet, particularly since the New Deal, by applying very expansive readings of the "general welfare" clause, the Supreme Court has allowed Congress to redistribute wealth from taxpayers to favored business interests (Slivinski 2001, 11).

Advocates of corporate welfare often maintain that federal support of business is in the national interest—"Can't afford to subsidize? … can't afford not to subsidize!" (Wipond 1996, 47). However, the arguments in support of corporate welfare do not stand up under scrutiny.

Corporate welfare is said to preserve high-paying American jobs. Subsidies have grown in recent years, without any indication that the benefits they confer on the public exceed the costs. The justification for much of the welfare is that the U.S. government is creating jobs. While James A. Harmon, president and chairman of the Export-Import Bank of the United States (which has received billions in subsidies)[11] contends that “American workers … have higher-quality, better-paying jobs, thanks to Eximbank’s financing” (“Corporate Welfare” 1998, 37) at the companies that have accounted for about forty of all Eximbank’s loans, grants, and long-term guarantees in the 1990s, overall employment has fallen, as more than a third of a million jobs have disappeared (“Corporate Welfare” 1998, 37).

In 1991, prohibitive duties were placed on low-cost Japanese computer parts. The motivation was to save jobs in the U.S. factories that made computer circuit boards. The decision to keep out foreign parts inflated (by almost $1,100) the cost of a personal computer manufactured by U.S. companies, such as IBM, Apple, Microsoft, and Compaq. That gave a huge advantage to Japanese computer companies; it significantly reduced sales of the domestic computer firms; and, worst of all, thousands of Americans were thrown into unemployment (Moore 1999, 8).

Corporate welfare is said to subsidize research activities that private industries would not finance themselves. Many Fortune 500 companies have received millions of dollars of funding to undertake research they could easily finance on their own. Government funding of research often ends up simply underwriting other aspects of corporate operations. Created in 1982, the Small Business Innovation Research (SBIR) program’s goal is to “stimulate technological innovation” (Wallsten 2000, 13). Rather than stimulate technological progress, SBIR subsidies effectively crowd out private research and development. Subsidies are apparently going to “better” firms whose projects would likely be funded even without federal support. The SBIR program provides an incentive for companies to cut their research budgets and pass research and development costs on to the government (Wallsten 2000, 15).

Arguably, let us ignore this crowding-out effect and assume that government subsidies to research and development actually succeed in increasing funds devoted to this purpose. Would that imply a benefit to the economy? Not at all. There is, contrary to the advocates of subsidies for this purpose, such a thing as overinvestment in research (Kinsella 2001). In the absence of any reason to believe that the market does not optimally allocate resources between innovation and all other purposes, the presumption must be that government

support for these expenditures, to the extent they succeed, have the effect of promoting malinvestments in the economy.

Corporate welfare is said to counteract the business subsidies of foreign governments to ensure a level playing field. In fact, when it comes to subsidies and trade barriers, often instituted to maintain competitiveness, they actually hinder proper economic development. There are currently thousands of tariffs levied on thousands of goods and import quotas imposed on numerous others. All of these barriers have the effect of protecting domestic industries from foreign competition in goods and services. They also restrict the free flow of goods in the economy, leading to decreased supply, foregone economic production, and higher prices for consumers (Slivinski 2001, 25). No one knows precisely the total cost to American consumers of barriers to free trade, but several authoritative sources place the figure at $80 billion a year. “There is virtually no specific U.S. trade restriction the economy wide costs of which do not exceed the industry-specific benefits” (Moore 1999, 8). Therefore, Congress should immediately lift all barriers to free trade.

Lower prices of products for consumers would be one immediate and tangible benefit of abolishing trade barriers that support and protect favored domestic industries. If subsidy cuts were accompanied by tax cuts, the lowering of the tax burden would be another clear benefit to consumers, workers, and the U.S. economy.[12] That factor alone would make the United States even more competitive with the high-tax, high-subsidy nations of the European community and Japan.

Protectionism produces no substantial gains. Industrial policies and the politics of “crony capitalism,” for instance, have begun to collapse and cause economic problems in Japan[13] and elsewhere in Asia. Japan is beginning to abandon the very policies that proponents of U.S. corporate welfare support (Slivinski 2001, 9).

Domestic subsidies cost the United States jobs, business formation, and overall growth. Not only do they reduce normal competitive pressures to innovate, they also place industries not receiving favored treatment at a disadvantage by effectively raising their costs of capital and labor relative to subsidized sectors (Moore 1999, 13).

There is a second argument against U.S. government subsidies to U.S. businesses as a response to similar practices abroad: There is nothing wrong, from our perspective, with the latter practice. That is, suppose that Japan subsidizes its automobile manufacturers to the extent that Honda, Toyota, and so forth can afford to sell their products to the U.S. consumer for half price. This, naturally, would tend to drive out of business all U.S. auto producers.[14]

If this program is expected to last indefinitely, it is in effect a subsidy from the Japanese government to U.S. consumers. Why should we look such a gift horse in the mouth? In the face of such Japanese largesse, we no more need U.S. car production than we now need horse and buggy manufacture, thanks to the largesse of improved technology that has long ago vitiated a previous need for the products of that industry. Similarly, if the French were to give us free or heavily subsidized wine, it would no longer be rational for us to invest resources in this product. Under these stipulations, the reasonable course of action is for people in the U.S. automobile and wine industries to shift to the production of goods and services that are not being given to us for free, or at artificially low prices. What is the point of doing those things for ourselves, at great cost, if others will do them for us for free?

However, suppose these gifts are really Trojan horses. They are not really gifts made to us out of the goodness of the hearts of the Japanese and French governments. Instead, posit that this beneficence is only a ruse, an attempt to get us to transfer factors of production out of the wine and auto industries, and when this nefarious predatory pricing scheme has unfolded, they will jack up prices to astronomical levels, after having made us dupes, dependent upon their only temporary largesse.

If true, then we can foil their evil machinations by leaving skeleton crews in the wine and auto industries (McGee 1958), ready to spring immediately back into action when and if these wicked plans are put into action. Further, there will be every incentive for U.S. firms to do precisely this if they suspect that the foreign subsidies are merely a gambit in an attempt to ruin our domestic industries. In the meantime, while the getting is still good, it would be folly for the U.S. government to subsidize the manufacture of these products so that they may be fully operational, during the phase of the diabolical foreign plan to hook us on their wares.

Perhaps for different reasons, both the Left and the Right in America should recognize the damaging effects of the expansion of the modern corporate welfare state. Democrats should understand that corporate welfare is the essence of corrupt government (Bartlett 1997). We have basically put Uncle Sam up for sale to the highest bidder—"that is seldom the poor, the disabled, or the working-class family with two wage earners struggling to pay the electric bills each month" (Moore 1999, 4). Meanwhile, Republicans on the Right should see that business handouts make big business a mere ward of the state—an advocate of government expansionism and a well-financed enemy of Adam Smith's invisible-hand capitalism. Corporate welfare, in sum, is "the antithesis of good government and the antithesis of a free-market economic system" (Moore 1999, 4).

On the one hand, there is an insidious effect of special privileges[15] for corporations that ought to be keenly appreciated by those with an interest in markets and morality: Such goings-on undermine the morality of the business community. Suppose you are the CEO of a corporation. As a moral businessman, the last thing you would do would be to seek a special subsidy from the government. However, you know that your competitors are likely, more than likely, to tread down this morally dangerous path. If you do not, you will to that extent risk the economic viability of your firm. On the other hand, you have an obligation to the stockholders of your company to maximize their return by all legal methods. Unhappily, the law is such that you will not be imprisoned for seeking just such unfair advantages. The result is a moral quandary.

Nor is this difficulty by any means limited to the business community. It affects all of us, in our role as consumers, citizens, members of society, and so forth. For example, is it not to take advantage of government subsidies to use such government institutions as the Post Office, public roads, and Bureau of Motor Vehicles. Virtually all of us will accept Social Security, police and fire protection, and so forth. Are we all not, therefore, welfare bums of a sort?

One defense of this practice is that we are all "just getting our own money back," and, it cannot be denied that this is true in at least many cases, but not all. The scope of the present article does not allow for a solution to this predicament (Block 2004; Block, forthcoming). Here, we must content ourselves with pointing out that government subsidies create highly complex moral quandaries.

Notes

1. Note, we do not mention tax loopholes. Strictly speaking, to say that a failure to tax is a subsidy is to imply that government is the legitimate owner of the entire gross domestic product (GDP): What the state fails to take from the citizen it is really "giving" to him. This notion, of course, must be rejected as irrational and out of keeping with the doctrine of private property rights.
2. Similarly, *welfare bum* and *corporate welfare bum* depict the pejorative manner in which both groups are helped by many segments of the populace.
3. To address long-term welfare dependency, TANF placed a five-year lifetime limit on assistance, and also stipulated that by 2002, 50 percent of families on assistance in every state must be engaged in work-related activities (policyalmanac.org).
4. President Clinton also proclaimed his intent to reinvent government and end irresponsible business subsidies; however, he proposed aggregate increases of 10 percent for major corporate welfare programs almost every year he was in office (Slivinski 2001, 2).

5. In 1997, Senator John McCain (R-AZ) and a bipartisan group of senators and outside interest groups announced their support for legislation to curb business subsidies (Bartlett 1997).
6. In the House, Budget Committee Chairman John Kasich formed a one-man crusade against welfare for the well off. In 1997, he formed the Stop Corporate Welfare Coalition, an eclectic group that runs across the political spectrum, from Grover Norquist on the Right to Ralph Nader on the Left (Moore 1997, 28).
7. These proposed bills still have to go through conference committee to have their differences worked out, but the original bills can give a preliminary indication of where the budgets of individual programs might end up (Slivinski 2001, 8). Spending bills working their way through the House and Senate Appropriations Committees have, however, reversed or diluted most of Bush's proposed cuts (Slivinski 2001, 1).
8. To the extent that enterprise zones are limited to tax reductions, they do not constitute corporate welfare. Typically, however, they include much more, such as explicit government subsidies to business.
9. See endnote 1, supra, for a critique of the concept of tax subsidies.
10. By these restrictive policies, wages and capital returns might indeed be kept higher than otherwise for the particular company, but wages and capital returns for other corporations would be forced down, lower than otherwise. That company would benefit only at the expense of the other corporations (Hazlitt 1979, 101).
11. The House bill advocates a cut of $125 million, or 15 percent, as opposed to Bush's proposed cut of 25 percent (Slivinski 2001, 8).
12. If corporate welfare were eliminated tomorrow, the federal government could provide taxpayers with an annual tax cut more than twice as large as the tax rebate checks mailed out in 2001 (Slivinski 2001, 2).
13. In Japan, the myth of industrial policy as a competitiveness strategy has led to a 60 percent reduction in the value of the Japanese stock market since 1990 (Moore 1999).
14. Nowadays, it is not so easy to distinguish between U.S. and foreign producers of road vehicles, as many of the latter have opened up plants in this country.
15. Some writers use the word *privilege* as a synonym for wealth. He is privileged means he is rich. We abjure such word usage. Instead, in our view, *privilege* in this context means an unwarranted advantage given to some companies but not others.

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