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The Facts
and
The Fiction

[removed from "Speeches", Cabinet #7 DR]

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Federal Subsidies

☆THE FACTS AND THE FICTION☆

IN SELECTING a title for this paper, the Virginia Commission on Constitutional Government has purposely given preference to the term, *Federal Subsidies,* over the more commonly used term, *Federal Grants-in-Aid.* We believe that the commonly used term is misleading because the word *grant* implies a gift. The implication is erroneous in this instance. Furthermore, the word *aid* implies that the grantor is in a superior position, offering gratuitous assistance to some needy individual or institution. That implication also is erroneous in this instance. Thus we have selected the term *Federal Subsidies* as more accurately describing the subject to be discussed.

Reduced to its simplest terms, a federal subsidy originates and operates in the following manner. A member of Congress, or a member of the Administration, decides that a specified service is a desirable one, and that a law establishing a program to provide the service should be enacted. A case in point is the Vaccination Assistance Act of 1962, which is supposed to provide. immunization against polio, diptheria, whooping cough and tetanus. Congressman Oren Harris of Arkansas was of the opinion that such a program would be advantageous to the people of the United States. Presumably, he examined existing legislation in the fifty States, and concluded that it was inadequate. He therefore introduced a bill, H.R. 10541, that would authorize subsidies to States or localities planning immunization programs. The bill was debated briefly in the House of Representatives, with only sixty-odd members present, and passed July 26, 1962, on a voice vote. Several members of the House made the point that passage of the bill would inject the federal government into an area of activity that properly should be reserved to the States and the local governments, but their arguments were in vain.*

The bill went to the Senate where it was approved without a hearing by the Senate Committee on Labor and Public Welfare. It was passed by the Senate on a voice vote, without debate, on October 4, 1962. On October 23, 1962, the President signed the bill authorizing 36 million dollars to be distributed to States and localities by the U. S. Surgeon General during the next three years.

This is a fair example of how a federal subsidy comes into existence. A need is asserted (usually for a very worthwhile purpose), a law is passed, and the money becomes available from the federal treasury.

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*Representative Durno of Oregon, who is also a doctor, had this to say: "I think this is a continuing program, or it will be, and if the Congress proposes to adopt this kind of a program, it should be continuing. I think it is going to be an expansive program which is going to involve a lot more diseases. . . . I don't think that it is the dollars in this bill or the medicine in this bill that is the answer. I think the answer is a continuation and an acceleration and an extension of the program of public health, and those public programs should originate at the county level and at the State level more than at the Federal level." 108 *Congressional Record* 10912.

Representative Martin of Nebraska noted that he had sent a questionnaire on this matter to his constituents and that 73% of the replies were in opposition to an appropriation of "federal" money for this program. 108 *Congressional Record* 10911.

Representative Dominick of Colorado said, "For the life of me, I cannot understand why it is necessary for the Federal Government to get into this realm." He then entered in the *Congressional Record* an article from the *Denver Post* which related in detail the plan that had been developed and used successfully in that locality, without federal assistance. 108 *Congressional Record* 10904, 10905.

☆ Who Pays?

In the rush to accomplish this worthwhile objective, a number of important, and in some cases controlling, factors are overlooked. The most obvious error is the failure on the part of many legislators and administrators to observe that the money to finance the program must come from the people of the United States. Yet this is the most easily observable principle in all of government: if the federal government is to subsidize a program, the taxpayers of the nation must put the money in the federal treasury for that purpose. If the United States is to have a 36 million dollar federally subsidized vaccination program, the people of the United States must pay to Uncle Sam 36 million dollars in taxes, in addition to what they are now paying.

A related and similarly overlooked fact is that the people frequently have to pay additional State and local taxes in order to receive the federal subsidies for which they have already been taxed at the federal level. The reason is that two-thirds of all federal subsidies are available only on what is called a "matching basis." This means that State and local governments have to put up some specified percentage of their own funds in order to receive the subsidy from the federal government. But the taxpayer who provides funds for State and local governments is the same taxpayer who provides funds for the federal government, so the people actually have to pay increased State and local taxes in order to receive federal subsidies that they were taxed to provide.

These are matters affecting the pocketbook, and they are not trifling matters. In 1960 total expenses of these subsidy programs amounted to *12 billion dollars,* or *66 dollars for every man, woman and child in this nation.* For an average family of four, that means yearly taxes in the amount of 264 dollars to maintain federal subsidies and the "matching" funds required to receive these subsidies.

☆ "A Broader Tax Base"

A second obvious error is the belief that the federal government is better situated financially to initiate and maintain these programs than are the States and localities. One frequently hears proponents of federal subsidies maintain that the federal government has a broader taxing base than State and local governments. This argument is at best misleading. The States have basically the same tax resources that are available to the federal government. As a matter of fact, the States had power to levy direct taxes on income, the primary source of government revenue, long before the federal government was given that power. The sales tax, real estate tax, personal property tax and other taxes of less general use and acceptance are all available to State and local governments. There are some taxes used by the federal government that are not employed by State and local governments, and vice versa, but this does not justify the statement that the federal government has a broader taxing power than the States and local governments.

It quite possibly would be accurate to say that the federal government can more easily increase taxes than can State and local governments. This appears to be true, since the federal government now collects income taxes ranging from 20% to 91% of net income, while State governments, with the same taxing capability, have limited their income taxes generally to the 1% to 10% range. The reason for this would seem to be that the State governments are close to the people and are more sensitive to the popular demand for economy, while the federal government with its gigantic bureaus is separated from the people by long distances and by massive tangles of "red tape."

Accordingly, it may be suggested that the "superior taxing power" of the federal government rests not upon a broader tax base, but upon the federal government's ability to increase taxes with relative impunity.* Phrased in another manner, the Congress is less subject to control of the people than are State and local governments. Do the proponents of federal subsidies really mean that such spending programs should be passed upon by the legislative body that is least responsible to the people? Such a proposition would have found little support among the founders of this country, and should find little support among our people today.

☆ "Superior Borrowing Position"

A related argument in favor of federal subsidies is that the federal government occupies a borrowing position superior to that of the States and local governments. On close analysis, this argument falls of its own weight. The federal indebtedness as of June 30, 1961, amounted to 289.0 billion dollars. This sum is equivalent to 67.2% of national income. State debt is only 4.7%, and local debt is only 12.8%, of national income. Since 1932, the federal debt has increased about four times as rapidly as State and local debt combined. In the decade from 1952 through 1961, the States as a whole showed surpluses of revenue over expenditure in six of the ten years, with an over-all deficit of only 300 million dollars for the period. The federal government showed surpluses in only three of the ten years, with an over-all deficit of more

*In 1961, 67% of all taxes collected in the United States went into the federal treasury. The States received only 16 cents and the local governments only 17 cents of each tax dollar.

than *35 billion dollars*. As a rule State and local governments make provision for the systematic repayment of their debt obligations. The failure of the Federal government to make such provisions may go far in explaining our huge federal debt.

As of June 30, 1961, States and local governments had made loans to the federal government totalling 18.7 billion dollars. Far from being in a superior borrowing position, it is apparent that the federal government actually is in a borrowing position inferior to that of the States and the local governments.*

☆ Inequitable Distribution

Proponents of the many federal subsidy programs have promoted the idea that these subsidies result in an equitable distribution of tax funds. Nothing could be further from the truth. For example, federal subsidies returned to the State of Delaware during 1959 amounted to only 40 cents per dollar of taxes paid by Delaware citizens in support of the subsidy programs. The taxpayer in Mississippi received $4.18 for the dollar that he paid for the same purpose. The taxpayer in Connecticut received only 43 cents for his dollar, while the taxpayer in Arkansas received $3.35. A comparable situation exists in other States: The citizen of New Jersey receives 44 cents for his dollar; in New Mexico, the citizen receives $2.97 for each dollar. The *New Jersey Taxpayer* reports that in 1960 that State lost 143.1 million dollars through federal taxes that were spent for subsidies to other States. Pennsylvania lost 125.6 million dollars; New York lost 206.5 million dollars. Virginia lost 6.3 million dollars. Some States, of course, showed a profit at the expense of the others. All things considered, it would be rather difficult to devise a more inequitable system of tax distribution.

*See the appendix at the end of this paper for the figures upon which the comparisons of this section are based.

☆ Federal Control

One of the greatest illusions perpetrated by proponents of federal subsidies is that control over the expenditure of funds is left in the hands of the States and localities concerned. While it would appear practical for control of the subsidy programs to be vested in those governments closest to the people and most closely connected with the operation of the programs, this is not the case at all. To the contrary, it is a fact that regulation by Congress and by federal administrative agencies is a normal incident of each subsidy program. This regulation extends to policy and operations questions, as well as to financial considerations.

The result is that both the States and the local governments are rapidly becoming subordinate units of the federal government. Programs of a purely local nature, financed by taxes collected from the people in the locality, are in effect operated and controlled by the federal government in Washington.

A recent case from Ohio will serve to illustrate the point. In that State, employers had paid to the federal government 30 million dollars in taxes for the administration of an unemployment compensation program. Of this amount, 17 million dollars was to be returned to the State for the purpose of making unemployment compensation payments to qualified persons in Ohio. The federal Department of Labor threatened to withhold the 17 million dollars from the State of Ohio pending that State's adoption of two procedural rules. The money in question had been collected from Ohio. It was to be spent in Ohio by an administrative agency of that State. The program under which the money was to be distributed had been approved by the Ohio courts. Ohio's unemployment compensation administration had been in operation for over twenty-two years and in the last five years alone had handled 95,684 cases without a complaint. Yet, the federal Department of Labor proposed to penalize the State of Ohio 17 million dollars for failure to comply with federally established regulations for the distribution of this money. It is quite apparent that State and local governments are not left free to establish programs they believe proper with federal subsidies. To the contrary, it appears that federal regulation of an essential function touches upon its most minute detail and in at least some cases operates to the detriment of the people affected.

It is common knowledge, of course, that in urban renewal programs, federal regulations touch upon virtually all areas of activity, including wages, hours of work, public housing, and a great many other items.

The area of farm subsidies is now so tangled and chaotic that it is difficult even for members of Congress to understand what is taking place, but one thing is certain: The farmer is subjected to more federal regulation in practically every area of his enterprise than he has ever been subjected to before.

In public welfare programs, where federal subsidies play an all-important role, a summary and analysis of federal-state regulations covers over 250 pages. A summary of federal laws regulating urban renewal covers 62 pages.

In speaking against a proposed program of federal subsidies for colleges and universities, John A. Howard, President of Rockford College, Illinois, is quoted as saying, "Any legislation which gives money away must have some restrictions to insure that the money is spent for the intended purpose." Furthermore, if the program is adopted, "the federal government, which proposes to underwrite a third of the cost of construction and provide substantial scholarships to students, will become in one congressional vote the largest single customer of all private colleges and a substantial customer of all public ones."

☆ "The Federal Government Must Act . . ."

Surely the most harmful and the most deceptive argument used in favor of federal subsidies is typified in the statement, "the federal government must perform those functions that the State and local governments will not perform." This statement and its several variations are directly contrary to the United States Constitution, for they mean that any State power not used, or, in the opinion of the federal government, improperly used by a State, is conferred upon the federal government. The Tenth Amendment to the Constitution provides to the contrary, that "The powers not delegated to the United States by the Constitution, nor prohibited by it to the States, are reserved to the States respectively, or to the people." If a State legislature considers, for example, a State Vaccination Act, and passes such an act, this is perfectly proper. On the other hand, if a State legislature rejects such an act or fails to consider such an act, this does not confer on the federal government power to consider a Vaccination Act for all the States. As a matter of fact, the Constitution implicitly denies such a power in the federal government, though the Supreme Court has in recent years held to the contrary.

One of the basic purposes of the fathers of this nation in establishing a union that left the States free to handle their internal problems was to permit a diversity of experiment on the proper solution of complex problems. Thus in the prevention of contagious diseases, New York might decide that a State-wide voluntary public vaccination program offers the best chance for success. Oregon might decide that each town, city, or county should be left free to establish its own program. Arizona might determine that people uncoerced by State pressure, and free of taxes to support such State programs, could best care for their own needs. If one plan proved better than the others, and equally suitable to most areas of the country, presumably that plan would be adopted by most States. Perhaps different plans would have varying appeal to different areas of the country. And if one plan proved detrimental to the interests of the people, that plan would be avoided, and its ill effects confined to the State that had attempted it. But with federally subsidized programs covering the entire nation, the opportunity for experiment is curtailed, and we are reduced to an "all-or-nothing" situation. This is a far cry from Supreme Court Justice Harlan's observation that one of the great strengths of our federal system of government is that we have in the fifty States fifty separate laboratories for social experiment.

Another basic purpose accomplished by reserving to the States the power to deal with their internal problems was the keeping of government as close to the people as possible. It was believed by the authors of our Constitution that the creation of an all-powerful central government would lead to restrictions on the liberty of the people. With this in mind, the central government was given power to act only in those cases when it was necessary or extraordinarily desirable for

all the States to act as a single unit. With extreme caution, the powers to be exercised by the central government were expressly set forth in the Constitution, and the Congress was given power to do those things necessary and proper to give effect to the expressly enumerated powers. Those powers not given the central government were reserved to the States, and the authors of our Constitution went so far as to have this basic principle explicitly stated in the Tenth Amendment. In this manner they guaranteed, or thought they guaranteed, for all time that all functions of government except those specifically delegated in the Constitution should be performed by those bodies of government closest to the people, the States. Jefferson, Madison, and those other authors of liberty as we have known it understood that government kept close under the watchful eyes of the people is good government; they knew that an all-powerful central government far from the watchful eyes of the people could become careless, incautious in the expenditure of public money, and unjust.

☆ A Powerful Hand

Today the federal government, by managing more than 90 federal subsidy programs accounting for the expenditure of 12 billion dollars, is extending a powerful hand into the affairs of all the States, all the local governments, and every citizen in this country. Power feeds upon power, and the staggering growth of the subsidy programs in the last few decades attests to the increased power of the federal government over our day-to-day lives. *"A power over a man's subsistence amounts to a power over his will."**

*THE FEDERALIST No. 79, at 497 (Wright ed. 1961) (Hamilton) (italics in original).

The Commission does not maintain that all federal subsidies are unnecessary and without constitutional justification. Some of these programs clearly fall within a proper interpretation of the power of Congress to maintain armies and navies, or within other powers delegated to the federal government by the Constitution. But a great number of the subsidy programs, costing billions of dollars in tax funds each year, do not fall within any power granted to the federal government, and many improper programs are proposed each year. The inevitable result of continued expansion of federal power in this field is the creation of an all-powerful central government that substantially controls the life of each citizen.

The waste, inefficiency and corruption found in many of the subsidy programs only emphasize the need for change. Practically every day brings a new report of wasted welfare payments, scandal in agricultural subsidies, or questionable dealings in urban renewal projects. As we surrender more of our freedom to high federal taxes, we receive in return more waste, inefficiency and corruption. The situation is not improved by the fact that our government officials may be making their best effort—if the program itself is faulty, honest administration cannot cure the defect.

☆ A First Step

As a first step toward solution of this difficult problem, the Commission recommends that all citizens and their representatives in government calmly consider on its merits each new proposal for a federal subsidy. Any proposed federal subsidy concerning a matter that can be solved within the framework of city, county, or State government should be rejected. Furthermore, any proposed program that does not

reasonably fall within one of the powers delegated by the Constitution to the federal government should be rejected. If this is done and done faithfully, the normal course of events will bring about a re-examination of the more unnecessary existing subsidy programs. The industrial States of the North and Midwest will begin to understand that by a balanced program for reducing federal subsidies they can actually improve their State programs and at the same time reduce the tax burden on their citizens. And perhaps it is not too much to expect that the federal government, as it is partially relieved of the expensive subsidy burden, may relieve the taxpayer of a portion of his burden.

March 1963

APPENDIX

Figures relating to comparison of the relative debt positions of federal, state and local governments. Latest comparisons are for the year 1961.

National income for 1961	\$430.2 billion[1]
Federal debt in 1932	19.5 billion[2]
Federal debt in 1961	289.0 billion[2]
State debt in 1932	2.8 billion[3]
State debt in 1961	20.0 billion[4]
Local debt in 1932	16.4 billion[3]
Local debt in 1961	55.0 billion[4]

State surpluses (+) and deficits (—) of general revenue over expenditure, 1952-1961:[5]

1952	+	\$1.0 billion	1957	+	\$0.4 billion
1953	+	1.1 billion	1958	—	1.9 billion
1954	+	0.1 billion	1959	—	1.9 billion
1955	—	0.7 billion	1960	+	1.2 billion
1956	+	0.5 billion	1961	—	0.1 billion

Federal surpluses (+) and deficits (—), 1952-1961:[6] (excluding trust funds)

1952	—	\$4.0 billion	1957	+	\$1.6 billion
1953	—	9.4 billion	1958	—	2.8 billion
1954	—	3.1 billion	1959	—	12.4 billion
1955	—	4.2 billion	1960	+	1.2 billion
1956	+	1.6 billion	1961	—	3.9 billion

State and local governments held \$18.7 billion in securities issued by the federal government as of June 30, 1961.[7]

1. *Statistical Abstract of the United States for 1962,* page 312.

2. *Annual Report of the Secretary of the Treasury for the Fiscal Year ended June 30, 1962,* page 380.

3. *Historical Statistics of the United States,* U. S. Bureau of the Census, pages 728-730.

4. *Summary of Governmental Finances for 1961,* U. S. Bureau of the Census, page 24.

5. *Compendium of State Government Finances in 1961,* U. S. Bureau of the Census, page 1.

6. *Annual Report of the Secretary of the Treasury for the Fiscal Year Ended June 30, 1961,* page 415.

7. *Id.* at page 98.

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