Policy Report

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Throwing Money Away on Oil

By David Glasner

Ever since Mobil Oil began looking for a smaller oil company to take over — first Conoco and then Marathon — people have been asking why Mobil wasn't using its money to find new oil instead of trying to waste it on buying up another oil company that has oil that has already been found. At first, the big oil companies went after circuses and department stores, and now it seems that they are trying to devour their own. If Mobil persists, there are sure to be new congressional investigations of the oil industry and more charges that it is neither competitive nor interested in finding more oil; if anything, it is trying to limit the supply.

The oil companies will have no one but themselves to blame for the charges hurled at them, not because the charges are true, but because the oil companies' spurious arguments in their own defense are being turned against them. In their ineffectual attempts to argue against price controls and the windfall profits tax on crude oil, the oil companies could only claim that they needed higher profits to finance increased exploration and drilling for new reserves in their crusade to make America energy-independent — "America runs better on American oil" and all that.

The problem with the argument is simply this — it doesn't make sense. I should have thought this would be obvious to just about anyone, even oil industry executives. Yet both the oil industry and its critics seem determined to embrace the argument, if for their own very different purposes.

David Glasner, who teaches in the College of Business Administration at Marquette University, is on leave to write a book on energy regulation.

Whether one spends money on a particular investment project does not depend on his cash flow; it depends entirely on the anticipated costs of, and returns from, the project. If the project seems profitable — that is, anticipated returns exceed anticipated costs by a sufficiently great margin — financing can be obtained even without cash flow from those who have the cash but no comparably profitable project of their own. What, after all, is a capital market for if not to facilitate precisely such transfers of funds? And if the project is not expected to be profitable, all the cash flow in the world is not going to make the project any more attractive. Only a fool would invest in an unprofitable project just because he had a lot of cash stuffed in his pockets. And you can bet that oil industry executives are not fools — no matter what they sound like when they talk about economics.

"The oil companies will have no one but themselves to blame for the charges hurled at them because their spurious arguments in their own defense are being turned against them."

The problem with controlling crude oil prices, either with price ceilings or a windfall profits tax, was never that it deprived the oil industry of funds needed to finance further exploration and development of oil reserves. The problem is that controls have rendered exploration and development less profitable than other projects competing for scarce resources, which thereby reduced the amount of exploration and development. But by arguing as if cash flow were all that mattered, representatives of the oil industry have fostered the impression that only a shortage of ready cash was preventing them from undertaking more exploration and development.

Thus, whenever an oil company seeks to acquire some other concern, whether or not it is in an energy-related field, an immediate outcry is heard from those still trying to settle scores with the oil industry and by those actually taken in by the oil industry line. That's when we hear that Mobil should not be allowed to spend huge amounts of money to buy another oil company when that money could instead be used to find more oil. Before considering this objection, however, I want to discuss the antitrust implications of a merger between Mobil and another major oil company.

Concentration in the Industry

Even using the most simplistic measures of competition and concentration ratios, the oil industry does not appear to be notably concentrated or uncompetitive; nor would a merger between Mobil and Marathon have made a perceptible difference in the ratios. In the third quarter of 1981, according to the Lundberg Survey, Mobil, the sixth-largest gasoline marketer, had a 5.29% national share of the gasoline market. Marathon, the twelfth-largest gasoline marketer, had a 2.14% share of the market. Their combined share of 7.43%

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EDITORIAL

The Judiciary — Out of Order!

The American citizen has been beaten and abused by both the legislative and executive branches of the federal government. These abuses have been publicized and exposed for many years by concerned individualists. However, the judiciary has also contributed to the infringement of the natural rights of individuals. Far from protecting the rights of the citizens, the federal judicial system has been guilty of aggression in much the same way as the other two branches.

Rather than a system of checks and balances, the three branches of government seem to be in a winless race to spur the growth of government and subversion of individual rights. The proper function of a legal system in a free society is developing rules of just conduct that have universal applicability irrespective of their impact on particular individuals or groups. Instead, the judges have taken upon themselves the role of "social legislators," redistributing income by force of law — the equivalent of legalized theft.

The courts have continued to propagate positive economic policy despite their mandate to confine themselves to interpreting the law and guaranteeing constitutional protections. The courts have not limited themselves to striking down the illegitimate rules and regulations that the legislative and executive branches have established. Instead, the federal courts have established a dangerous trend of devising independent, detailed rules, standards, and formulae for prescribing government policy.

Federal district courts have laid down elaborate standards for food handling, hospital operations, recreation facilities, inmate employment and education, sanitation and laundry, painting, lighting, and plumbing. Courts have established formal procedures for administering discipline in public schools (Goss v. Lopez, 1975), designed the wording and extent of rights that police officers must relate to persons accused of committing crimes (Miranda v. Arizona, 1966, and its progeny), and mandated the extent of citizen participation in model cities programs (North City Area Wide Council v. Romney, 1971).

Judges have even ordered government agencies to implement policies regardless of costs, conflicts, or ensuing impact. A federal district court judge ordered that the State of Texas significantly upgrade the health and sanitation in its prisons and secure for every prisoner a judicially specified amount of living space in every penitentiary (Ruiz v. Estelle, 1980). Other judges mandated that bilingual education be offered in school (Serna v. Portales Municipal Schools, 1974) and ordered that such programs be extended through the twelfth grade in each school district in the state and required, regardless of the cost, that additional teachers be hired (U.S. v. Texas, 1981).

Federal district courts have struck down laws requiring a period of in-state residence as a condition of eligibility for welfare, suspended performance requirements for automobile airbags, forced the Farmers Home Administration to restore a disaster loan program, and told the Corps of Engineers to maintain the nation's non-navigable waterways.

One of the most egregious abuses of judicial power in recent history took place in New Jersey in 1976. The New Jersey Supreme Court ruled that heavy reliance on local property taxes to finance education discriminated against poorer school districts (Robinson v. Cahill). The Court based its ruling on a vague phrase in the state constitution mandating a "thorough and efficient" education for every child. Seizing on that phrase, the Court ruled that differences in tax revenues in different districts violated that provision of the constitution. The Court gave the New Jersey legislature three months to vote more money for local school districts, to be raised by a broad-based state tax. In effect, the Court required the legislature to pass a state income tax. The Court said that if the legislature failed to act within three months, it would consider setting state school-budget priorities itself. When the legislature failed to act by the mandated deadline, the Court threatened to order "appropriate and necessary" steps and then shut down the New Jersey public schools for 10 days until the legislature caved in and passed an income tax.

In 1970, Alexander Bickel, in his book, *The Supreme Court and the Idea of Progress*, warned that "all too many federal judges have been induced to view themselves as holding roving commissions as problem solvers, and as charged with a duty to act when majoritarian institutions do not." This dangerous trend, if allowed to continue, will increase the fundamental violations of human rights and the destruction of private property.

A return of the judiciary to its proper role of isolating the citizenry from government abuses and protecting human rights would do much to revitalize America. First, it would generate a tremendous decrease in the demand for court services by groups seeking to benefit at the expense of others by court actions that generate significant wealth transfers. Second, it would help diminish the over 80% increase in the production of American lawyers in the last decade, while we have had less than a 20% increase in engineers and physicists. (Japan and West Germany have increased their engineers and physicists by over 50%.) Third, and most important, it will help get the courts back on their historical mission of developing rules of just conduct that restrict human and property rights violations rather than propagating them.

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would have been barely larger than the 7.28% share of the current market leader, Amoco. And when one observes that a Mobil-Marathon merger would have raised the four-firm concentration ratio from 26.83 to 28.56% and the eight-firm concentration ratio from 46.64% to 48.78%, based on market shares in the third quarter of 1981, one is impressed with how negligible the effect of the merger would have been.

Of course, in certain local markets a combination of Mobil and Marathon dealers arguably could have reduced competition. In such markets there might have been grounds for requiring Mobil to divest itself of Marathon's marketing facilities. But from the outset, Mobil made it plain that it was primarily interested in acquiring Marathon's reserves of crude oil and that it would be quite willing to spin off all or part of Marathon's marketing and refining assets.

Concentration ratios for crude oil production and refining capacity are no different. A merger between Mobil and Marathon would have had only a slight effect on four-and-eight firm concentration ratios, and would not have made Mobil either the largest domestic crude producer or refiner.

I should not wish to claim too much for concentration ratios as indicators of actual or potential monopoly power within the oil industry or anywhere else. Those alleging that the oil industry is, or could easily become, monopolized, however, have no more convincing evidence to offer.

Critics maintain that the oil industry engages in collusive practices that belie the industry's relatively innocuous concentration ratios. Charges of collusion are, by their nature, extraordinarily difficult to prove or disprove, which is one reason such charges are made so freely. But it happens that we do have indisputable evidence of oil industry collusion which, despite open government approval and support, failed. In the middle and late '50s there were two attempts made, under the auspices of the federal government, at voluntary oil import restrictions. In both cases the oil companies agreed to limit the amount of cheap foreign crude oil they imported into the United States in order not to undercut the domestic price level. But despite their interest in maintaining domestic prices and despite the government's encouragement, the voluntary programs could not suppress the incentive of individual firms to "cheat" on the collusive agreement and to import additional cheap oil into the United States. It was only because of the failure of collusion that the voluntary programs had to be replaced by the mandatory import quota program. It transferred responsibility for enforcing the imports restriction from the industry, which was not capable of doing so, to the government, which was.

Moreover, the high domestic prices the import restrictions were designed to preserve were the result of so-called demand prorationing carried out by the leading oil-producing states. Were it not for demand prorationing enforced by the states, the oil industry would have been incapable of restricting domestic output and raising domestic prices in the first place. Indeed, demand prorationing itself would have been ineffective had it not been for the Connoly "hot oil" act, which made it a federal offense to sell oil produced in excess of state prorationing quotas across state lines. Any collusive or restrictive practices that the industry has engaged in have only been possible when the federal government enforced them.

A similar charge against the oil industry is that extensive vertical integration somehow increases the market power that can be exercised with what is apparently only moderate concentration. The charge is wholly disreputable and has neither theoretical foundation or empirical support. If a product must go through several stages of a process before it reaches consumers, effective monopoly control over it does not require control over each stage of the process. Control over any one of the stages

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Throwing Money Away (Cont. from p. 3)

is sufficient, and extending control through the entire process cannot increase the extent of monopoly control. Whatever monopoly power OPEC has been able to exercise was made possible by its control of supplies at the well-head. Indeed, as a monopolist, OPEC's interest would be for downstream operations to be as competitive and efficient as possible. Similarly, a monopolistic refiner or a monopolistic marketer could extract a monopoly profit by regulating the flow of the product through its own stage. There would be no reason to integrate either forward or backward. On the other hand, if no monopoly is exercised at any single stage, operating at more than one stage cannot create monopoly power that does not already exist. In relation to the degree of competition in the oil industry, the question of vertical integration is simply a red herring.

It may also be worth mentioning that the discriminatory taxation of dividends creates an artificial incentive for mergers and takeovers. After having paid its corporate tax liability, management must decide how much of the remainder is to be distributed to shareholders and how much to retain within the corporation to finance internal growth and, it is hoped, stock appreciation. Since for most shareholders capital gains are taxed at a lower rate than dividends, there will be a clear bias in favor of retaining earnings rather than distributing them as dividends. Thus, any corporation with a temporary abundance of cash will be inclined to acquire other firms and increase its stock price rather than distribute the cash to stockholders. Although it is unlikely that it was discriminatory taxation of dividends that caused Mobil to attempt to take over other oil companies, it may well have been a factor in previous oil company takeovers in non-energy fields.

Will Less Oil Be Found

So the real question is whether any less oil will be found if Mobil spends its money in a takeover of another oil company rather than use the money to search for more oil. There is no valid reason to suppose that the answer to this question is yes. A decision by Mobil to acquire another company's already-discovered reserves reflects a judgment on Mobil's part that such an acquisition is profitable. That does not render exploration projects, by Mobil or anyone else, less profitable. Nor does it render an oil company less capable of devoting resources to finding new reserves.

One might say that the money that Mobil uses to pay for the stock it would acquire is no longer available to pay for searching for oil. But that presumes that those who receive the money from Mobil are going to allow those funds to sit idle. They will not. They will either reinvest that money themselves or they will entrust it to those who they can expect to profitably invest it for them. In either case, anyone who can profitably search for oil will still be able to obtain financing to do so. Indeed, the increase in the value of oil stocks caused by a takeover by Mobil would make the search for new oil reserves appear even more profitable and hence encourage more, not less, exploration and development.

> "Controls have rendered exploration and development less profitable than other projects competing with them for scarce resources."

An assumption that a takeover reduces the funds available for energy development confuses a real transaction that uses up real resources with a financial transaction that merely transfers title to existing assets. A real transaction occurs when a firm, such as Mobil, employs labor and capital to search for oil or to perform some other task. That reduces the amount of resources available to the rest of the economy to undertake other real transactions, such as searching for gas. But a financial transaction, such as Mobil's acquisition of another firm, uses up relatively few real resources — certainly none that could be used for oil exploration — and thus does not reduce the amount of oil that is going to be discovered. At worst, it might reflect a decision by Mobil to specialize in the management of oil reserves and in the refining and distribution of oil products rather than in exploring for oil. This would mean that Mobil had decided to let others specialize in exploration and to acquire their reserves following discovery. If so, Mobil would become less integrated — a result that one would have thought would be welcomed, not deplored, by oil industry critics who have long regarded the integration of oil exploration, development, production, refining, and distribution with such suspicion.

How much more oil is going to be found in the United States, then, has virtually nothing to do with whether or not Mobil buys up Marathon or any other oil company. It depends purely on the amount of oil underground waiting to be found, on the resources available to find the oil, and the incentives for using those resources to find oil, rather than using them for other purposes.

The existence of bottlenecks (for example, shortages of drilling rigs) are sometimes cited by those who believe that incentives do not matter or that they are already sufficient to encourage as much exploration as the available resources can undertake. Hence, these individuals conclude, allowing the oil companies to recover higher prices on oil and gas will not lead to the discovery of more oil but will only increase the amount of cash available to the oil companies with which to buy up other oil companies.

The whole point of a price system that communicates the market values of products and resources emerging from the interaction of countless buyers and sellers, however, is to alert people to the existence of bottlenecks and to provide incentives to overcome them. Socialist and centrally planned economies are overwhelmed with bottlenecks not because of absolute physical limitations on the availability of resources, but because no one stands to gain (that is, make a profit) by eliminating the bottlenecks. The real obstacle that must be overcome in the effort to discover new reserves of oil and gas is that the value of new reserves is not fully reflected in the prices that the finders of the reserves may recover (nor can the value of the reserves be fully capitalized in the value of the stock of the firms that discover them) because of the windfall profits tax on oil and the ceilings on natural gas prices. It is these controls, not the takeover attempts by Mobil, that should concern those who think too little effort is devoted to the discovery of more oil. ■

PR Reviews

Discrimination, Affirmative Action, and Equal Opportunity, edited by Walter E. Block and Michael A. Walker. Fraser Institute, Vancouver, Canada, 1981. 271 pp. $9.95.

This collection of essays, offering a free-market perspective on discrimination, is one of the most important sources of information and argument to have been published on this topic. Contributors include such noteworthy economists as Thomas Sowell, Walter Williams, Gary Becker, and Walter Block. In addition, the volume closes with a delightful short story by Kurt Vonnegut, Jr. on the problem of egalitarianism. Nearly all of the articles convincingly demonstrate how the competitive market process tends to minimize racial discrimination by forcing the would-be discriminator to bear the costs of his prejudices. Heavily regulated and centrally planned economies, on the other hand, tend to generate discrimination because individual merit becomes further and fur-

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Briefs

☐ A recent report by the General Accounting Office has estimated that tax cheating now saves the American taxpayer more than $80 billion a year, nearly three times as much as the 1976 figure of $27.6 billion. Most of the $80 billion was attributed to unreported income estimated at between $150 and $400 billion.

☐ Thirty-one of American's state legislatures have already called for a constitutional convention to approve a balanced budget amendment — only three less than the two-thirds percentage required to call such a convention. In addition, there are 10 states where one legislative house has already approved a convention call. This situation is expected to bring pressure upon Congress to pass a balanced budget amendment in order to forestall a convention that could adopt all sorts of other amendments. Under the current amendment being considered by Congress, only a vote of three-fifths of the House and the Senate would allow a deficit in any fiscal year.

☐ One of the latest federal services to be privatized is the Census Bureau's program for tabulating census data for all of the nation's zip codes. The National Planning Data Corporation of Ithaca, N.Y. is spending over $250,000 to develop these statistics and expects to make a profit by selling them to retailers, direct mailers, private data firms, and other interested corporations.

☐ A study by the House Post Office and Civil Service subcommittee has estimated that President Reagan's one-day shutdown of the federal government last November cost over $85 million. However, this conclusion is established by a rather curious use of reasoning — the bulk of this cost was attributed to the fact that federal workers were still being paid despite their not working that day.

☐ An air quality test in the Environmental Protection Agency's new Superfund Office — located in a converted garage — revealed that the office's air quality was unacceptable due to carbon monoxide levels of up to 50 parts per million. Such a level of pollution would be unable to pass the Occupational Safety and Health Administration's safety limit for factories.

☐ The Reagans' visit to their California ranch last August cost taxpayers an estimated $300,000. This figure includes $5,220 an hour for the use of Air Force One as well as expenses for government employees, hotel rooms, phone calls, and so forth. Not included in this figure is the $750,000 spent to equip the ranch with a Secret Service command post and communications center.

☐ In order to comply with GAO requirements that they make their contract procuring process more competitive, the Department of Defense changed its definition of the word "competitive." The DOD recently announced that 69% of its contracts last June were awarded on a competitive basis. If the old definition of "competitive" is used, however, this figure falls to 41%.

☐ Rep. Ron Paul (R.-Tex.) wants federal agencies to stop referring to government products and services as "free of charge." He's introduced a bill that would require agencies to say "This product or publication has been paid for with United States tax dollars; therefore, it is available at no cost in addition to the tax expenditures already made for its production." ■

Trade Adjustment Assistance: A Bad Program Whose Time Has Come

By Marc B. Goodman

"As guides to practice, the moral principles of harmony and conflict were strained to their utmost into a pattern of all but complete contradiction." That is how Karl Polanyi described the functioning of the Speenhamland policy, aid-in-wages given to cushion dislocations during the industrial revolution in Britain. The same paternalistic and schizophrenic approach to economic change has characterized U.S. government policies 200 years later.

Traditionally, most economists have taken a dispassionate view of change, assuming that workers who suffer from changes in global production patterns would inevitably adapt to newer and more productive fields of endeavor. Indeed, the very hardships imposed by change would be the most powerful force in bringing about their redeployment into more fulfilling opportunities.

American legislators, in their greater wisdom, saw fit to cushion the adversities facing American workers. Economists' assumption that labor, as a factor of production, was both perfectly mobile and "fungible" (suitable to various employments) was, it seems, little consolation to the men, women, and children caught up in the trade winds of the times.

The Origin of TAA

There has long been concern for the impact of import competition on U.S. firms and employment, particularly on the micro level — individual firms, industries, and communities — rather than for the economy as a whole. Since 1947 U.S. trade legislation has made tariff concessions conditional, rather than absolute. Such concessions are subject to "escape clauses," which reverse the concessions or enact other restrictions if the original liberalization has an adverse impact on U.S. industry. With the Trade Expansion Act of 1962, a new approach was included, which was intended to forestall resort to the escape clause. In addition to the traditional gradualism and relief mechanisms built into the process of negotiated trade liberalization, the new program was devised to compensate those workers and firms that might be considered the victims of policies that would benefit the nation as a whole.

The original TAA legislation had three related objectives. Politically, it was designed to diffuse the overt and latent protectionist pressure and opposition to liberal trade policies.[1] Economically, it was meant to facilitate the process by which the displaced workers and affected firms adapted and were absorbed into new industries and new avocations. Socially, it was intended to ease the hardships associated with that displacement and the interim period of joblessness. While it was with the first objective that the program achieved its most notable success, no one seemed to mind that the other two purposes were inevitably contradictory.

> **"Subsidies to existing structures or income maintenance may serve only to frustrate any form of adjustment."**

The program envisaged, in addition to a host of other measures geared to ailing firms and industries (aid to communities was later incorporated into the program in the 1974 legislation), three forms of worker benefits: Retraining allowances, job relocation allowances, and cash benefits as supplements to unemployment insurance. Such an approach, being directed at conflicting goals, was bound to fail. Measures that subsidize worker mobility or plant relocation conflict with the government's goal of "preserving communities." Even more important, subsidies to existing structures or income maintenance may only frustrate any form of adjustment.

Many of these problems never fully surfaced simply because most parts of the program were never very effective. The workers program, however, ultimately began to burgeon out of control. These problems became evident when the Reagan administration ranked the program high on its "expendable" list. This prompted a subsequent reexamination of the program, which showed that in the 19 years of its operation it has failed to provide a single example of fulfilling its purposes, while countless cases have been cited of directly converse effects.

From the time of the enactment of the Trade Expansion Act in 1962 until 1969, no empirical evidence of the program's functioning was available. While the Trade Expansion Act's mandate was realized only through years of tedious and deliberate tariff-reducing negotiations, the U.S. economy was experiencing a boom of unprecedented duration, largely obviating the need for TAA programs. The few petitions that were received by the U.S. Tariff Commission were all denied, many in accordance with the criterion of the Act that only workers displaced due to import competition that could be directly traced to previous trade concessions were eligible.

Changes in the Law

In 1969 the interpretation of the TAA statute was loosened (along with that of the escape clause), eliminating the requirement that imports be traced to past concessions. Subsequently, the Tariff Commission was able to certify some groups of workers in the 1969-74 period, but the programs were still largely unutilized. This changed dramatically with the Trade Act of 1974. With this legislation, the eligibility criteria were loosened to require only that imports be adjudged to have "contributed importantly" rather than to have been the major cause of injury. Other definitions and delineations in the scope of the program were similarly revised that effectively expanded TAA assistance.

Most significantly, responsibility for administering the programs was taken from the Tariff Commission and divided between the Departments of Labor and Commerce, which began to aggressively promote the programs. These changes, along with increasing U.S. unemployment and mounting import competition, soon enabled the TAA Workers Program to become one of the fastest growing in the federal government. From 1962 to 1975 the program covered a total of 54,000 workers. Yet in fiscal 1980 it certified half a million workers in one year alone.

According to the new TAA charter, there were three criteria for eligibility once it had been determined that (three or more) workers had been separated from employment at a firm. The firm's production or sales must have declined prior to the date of the petition. Imports of similar or competitive products must have increased (either absolutely or as market share). Finally, the increase in imports must have contributed importantly to the decline in sales or production.

Determination of the three criteria was not as simple and straightforward as the drafters of the legislation expected. In addition to the normal problems associated with data bases for imports (many imports are recorded only in "basket" categories that include numerous products) and differing interpretations of what might define products as "like or competitive," industry-wide production statistics were often aggregated much too broadly to provide any guide to trends or causality. Production and sales data gathered from individual firms were not only of questionable validity, but were open to almost infinite interpretations according to choice of base periods used and concomitant seasonal and cyclical fluctuations. Perhaps the thorniest determination would be the causal link between the sales or production declines and the increase in imports.

Undaunted, the TAA administrators established a customer survey office, which was to require the firm under investigation to submit lists of customers who had at one time reduced their orders. Questionnaires would ask these customers why they cut back their purchases. Of course, not only is this information extremely unreliable, but lengthy delays and the uncertainty of receiving responses made the questionnaires a farce. TAA bureaucrats also did not consider the proprietary and confidential nature of the customer lists and their motivations. Another problem was the possible effects of the confusing forms; many customers of often already-distressed suppliers must have concluded either that the supplier was under investigation for some possible wrongdoing or that its failure was imminent.

The difficulties of interpretation and verification made the disposition of many cases seem arbitrary not only to would-be recipients but also to the Labor Department's own TAA investigators. The investigators were exhorted to deemphasize concerns with consistency and conformity with legislative intent and to concentrate on the goal of maximizing "production" (of reports). Obviously frivolous petitions, many filed in all but name by overzealous state Unemployment Insurance officials, were investigated with the normal thoroughness and expense, even when initial telephone conversations confirmed that neither the separated workers nor the company's management placed any credence in the role of imports. Not only was no attempt made to screen or terminate such petitions with abbreviated investigations, but no effort was made to discourage the practice through the state agencies. On the con-

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TOTAL NUMBER OF WORKERS CERTIFIED 1975-1980 Main Industries (thousands)

Industry	Workers
Automobiles	408.9
Apparel	117.6
Steel	107.3
Footwear	63.2
Electronics	49.9
Fabricated metal products	25.7
Textiles	23.5

TRADE READJUSTMENT ALLOWANCE

Fiscal Year	Total Outlays (millions)
1976[1]	$ 70
1977	151
1978	258
1979	259
1980	1,624
1981 estimated	2,743*

*Actual outlays for 1981 were $1.3-$1.4 billion according to DOL and OMB.
SOURCE: U.S. Department of Labor, provided to House Committee on Ways and Means, Subcommittee on Trade, hearings held March 30-31, 1981.
[1]TRA supplement to UI only

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✓ Washington Update

The chairmen of both the House and Senate immigration subcommittees have introduced an immigration reform bill that rejects much of what President Reagan requested last fall. The bill would give permanent resident status to most current illegal aliens, set up stiffer penalties for employers who hire illegal aliens, and require a national form of identification for all employers. Although Reagan's proposal contains a significantly different series of enforcement measures and penalties, administration sources have announced that they would be willing to strike a compromise on most of these issues.

To conform to the administration position, Commerce Secretary Malcolm Baldrige has dropped his longstanding support for uniform federal standards for product liability law at the state level. Baldrige testified in front of a Senate subcommittee that except for "pressing national needs," the states should be "free to adopt their own standards, enforced by state officials in state courts." This shift has been interpreted as a definite sign that the White House intends to apply its "new federalism" to state and local law.

The Reagan administration has decided to exempt the government's largest student aid program (Guaranteed Student Loan) from federal laws that forbid institutions receiving federal funds from discriminating on the basis of race, sex, or handicap. This move will allow a few hundred schools of business and other proprietary schools to continue their current policies without danger of federal interference. Several civil rights and legal authorities predicted the decision would be struck down by the courts.

The Environmental Protection Agency, acting under court order, has recently issued a 90-page document outlining proposed national guidelines for cleaning up hazardous waste dumps. The plan details methods for identifying and investigating abandoned dumps and establishing clean-up priorities, a procedure that will be financed by the $1.6 billion created by the 1980 "Superfund" law. The plan will not become final until after the EPA reviews public comments.

In an attempt to increase government revenue, Sens. Robert Dole (R-Kan.) and Charles Grassley (R-Iowa) have proposed a bill that would require more complete reporting of income sources not subject to withholding taxes, such as interest and dividends. It is estimated that this plan could raise $20 billion. The bill's income reporting requirements would be exempted from the Paperwork Reduction Act due to their cumbersome nature.

The Interstate Commerce Commission recently announced an important change in its merger policy that will allow newly merged railroad systems to offer lower prices and better service than their competitors. Previously, all merged systems — even those dating from the 1920s — were barred from lowering their fares and increasing the speed of their trains for fear that this would hurt the other companies not included in the merger. All of the changes will be fully implemented by 1 July 1982.

The Reagan administration has shrugged off objections from conservatives and tobacco-state legislators and endorsed legislation which would require stronger health warning labels on cigarette packages. In a series of letters addressed to Health and Human Services Secretary Richard Schweiker, Sen. Jesse Helms (R-N.C.) complained about "what is perceived as incipient 'Califanoism' in your department." Another congressman, Rep. L.H. Fountain (D-N.C.), warned that the new label would "injure the revenue bonanza which government receives from this honorable crop."

Federal Trade Commission Chairman James Miller is currently seeking the authority to limit his agency's powers to regulate unfair and deceptive advertising and other trade practices such as high-pressure sales tactics. Under Miller's proposed changes, the FTC could bring cases only when the action in question caused substantial consumer injury without creating significant consumer benefits. Miller is also considering another proposal that would permit the FTC to file suits against deceptive advertising practices only when fraudulent intent could be demonstrated.

In light of intense protests from environmental advocates, EPA reversed its position and reimposed a ban on the disposing of hazardous liquids in landfills. Under the new rules, landfills cannot accept barrels containing "free-standing" hazardous liquid. The liquid must either be siphoned off, padded with absorbent material, or solidified — each alternative allowing only 5% of the barrel's contents to be liquid.

The Federal Communications Commission approved the construction of 79 low-power television stations, out of 6,000 applications. A low-power station is limited in coverage to a 12- or 15-mile radius, but it is inexpensive to operate and free to originate programming. Low-power TV is the first new broadcast service considered by the FCC in 20 years.

The FCC decided to allow AM radio stations to broadcast in stereo but also decided not to choose among five different and incompatible transmission systems. Despite pleas from such companies as Magnavox and Motorola, the FCC said the marketplace could do a better job selecting the right system. Only Republican Commissioner Abbott Washburn voted against leaving the matter to the market. ■

Trade Adjustment Assistance (Cont. from p. 7)

trary, the program's objective of maximizing production was fulfilled, and evidence was given to the success of this "outreach" project. (Massachusetts, in particular, was cited, the source of a greatly disproportionate share of petitions, where Unemployment Insurance officials admitted to me to having "twisted some arms" to get workers to sign petitions.)

When the workers who had filed for the benefits had been reemployed after a short layoff period, investigations had to go forward because those workers may have been entitled to some cash payments for that period during which they had been jobless. In fact, studies by the General Accounting Office and by the Brookings Institution showed that most benefits were received only retroactively, in the form of a lump-sum payment, after the workers had been re-employed, often at the same position.[2]

Reasons for the Failure

Almost certainly, the greatest inadequacy of the TAA for Workers Program results not from administrative failure but from a fundamental design flaw, a result of the lack of clearly defined objectives and priorities. While the concept behind TAA was the promotion of dynamic responses to changing competitive conditions, only the retraining and relocation facets of the program for workers served any such purpose. According to Labor Department statistics, less than 3% of the 1.7 million TAA recipients since 1975 have participated in training programs. The aspect that has come to predominate, the cash benefits designed to relieve the hardships of job displacement, is inconsistent with the aim of promoting adjustment. TAA case investigations showed that the income maintenance part of the program not only acted as a disincentive to retraining and relocation but even resulted in refusals by laid-off workers to accept reemployment at their former positions. The retroactive delivery of benefits, while making a mockery of any notion of actually serving adjustment, is perhaps to be appreciated for at least

(Cont. on p. 10)

Regulatory Watch

DEPARTMENT OF COMMERCE

An investigation by the International Trade Administration has concluded that at least one known exporter from Taiwan has been "dumping" clear sheet glass in American markets. As a result, all Taiwanese firms selling clear sheet class in America will be required to put down cash deposits equal to the margin for the last shipments by those firms for which data are available. Another review of this matter will be conducted in August 1981.

The North Pacific Fishery Management Council, a branch of the National Marine Fisheries Service, which is in turn a branch of the Commerce Department's National Oceanic and Atmospheric Administration, has recently established a new branch — the Scientific and Statistical Committee and its advisory panel. This new committee will hold separate meetings and will have primarily an advisory and informational role.

The ITA has recently finished its administrative review of the countervailing duty order on vitamin K from Spain. A preliminary determination was issued which instructs the Customs Service to assess countervailing duties equal to the calculated value of the net subsidy, 4.8% of the f.o.b. invoice price of the merchandise. This investigation originated from a Department of Treasury mandate issued in 1976.

NOAA has proposed regulations to implement section 101(a)(5) of the Marine Mammal Protection Act of 1972. This section calls for a legal mechanism that would allow the incidental, but not intentional, taking of small numbers of nondepleted marine mammals for specified purposes other than commercial fishing. In addition, this section will also contain specific regulations to govern the taking of ringed seals in the Beaufort Sea for the period from 1982 to 1986.

A recent ITA study has determined that motorcycle batteries from Taiwan are likely to be sold in the United States at less than "fair value." This study was in response to a complaint from the Yuasu-Reading General Battery Corporation of Reading, Pa. Within the next month, the ITA will determine whether these imports are threatening to substantially injure American industry.

The National Bureau of Standards has drawn up an "exclusion list" of various computers and information processing systems for which Federal Information Processing Standards do not apply. This exclusion list is used in conjunction with the applicability provisions of the Federal I/O channel level interface standards to determine which information systems should be used by federal agencies.

The Economic Development Administration has recently granted funds for administrative attempts to create economic development programs for Indian lands and reservations. Approximately $1,500,000 in assistance will be provided in the form of direct grants for projects

Trade Adjustment Assistance (Cont. from p. 9)

somewhat attenuating this effect.

With their characteristic foresight, the drafters of the Trade Act of 1974 mandated that a special fund be established from customs revenues (generated by imports made possible by TAA) out of which its funding would supposedly be drawn. Although the directive lacked any practical effect, no method of gauging the program's effect on tariff revenue being possible, new TAA employees, perhaps to preempt misgivings, are encouraged to believe in the mythical self-financing instrument.

The architects of the TAA program defined it as an open-ended system of entitlements, lacking any budgeting process. Estimated to cost approximately $250,000 per year, the program ballooned to over $1.3 billion in fiscal 1980 and was projected at $2.7 billion for 1981. (Actual outlays for 1981 were $1.3-$1.4 billion according to the Department of Labor and Office of Management and Budget).

At last, the Reagan administration tried to lower the axe with the Trade Act Amendments of 1981, incorporated into the Omnibus Budget Reconciliation Act. The criterion for imports to have "contributed importantly" to displacement was to be replaced by the more restrictive "substantial cause." Eligibility would be withheld until 60 days from termination and until regular unemployment benefits have been exhausted, eliminating the great majority of recipients. Ceilings of total income received from all sources (notably various government benefits plus private Supplemental Unemployment Benefits) would be put into effect. With these and other obvious and long overdue changes, outlays for 1982, projected at near $1.5 billion under the former program, would be slashed to $350 million and held to that level for subsequent years. Of this, $112 million would be reserved for retraining and job search, reducing to $235 million the regular allowances. Due to expire under its sunset provision at the end of 1983, the program may well be allowed to die.

Rep. Sam Gibbons (D-Fla.), chairman of the Trade Subcommittee of the House Ways and Means Committee, which oversees the TAA program, had long been sympathetic to the program and as recently as two years ago had favored extending its scope. In recent congressional hearings, the effects of the program having come to light, he characterized it as "a crude tool that blew up in our faces."

It can truly be said that the Trade Adjustment Assistance for Workers Program is one of the reasons the federal government enjoys the reputation it has today.

INFLATION MONITOR

A quarterly feature of *Policy Report*, the "Inflation Monitor" shows the distorting effects on relative prices throughout the economy of government fiscal and monetary measures. All figures are expressed as annual rates of change unless otherwise indicated.

	1981 4th Quarter	1981 3rd Quarter	1981 2nd Quarter	Average for Last Year
MONETARY SECTOR				
Monetary Base	3.9	5.8	6.0	5.3
MI*	5.7	0.3	9.2	4.9
M2	8.8	8.4	7.1	8.2
M3	9.2	10.1	9.8	10.3
Discount Rate (average)	13.4	14.0	14.0	13.6
Prime Rate (average)	15.8	20.3	18.9	18.6
PRICE CHANGES				
Consumer Price Index	5.3	13.5	7.4	8.9
All-Finished-Goods P.I.	5.4	2.8	6.0	7.1
Intermediate-Materials P.I.	3.5	4.3	10.0	7.6
Capital-Equipment P.I.	9.4	5.7	8.0	8.5
INDUSTRIAL PRODUCTION INDICES				
Consumer Goods	144.3	149.5	150.1	147.9
Producer Goods	150.2	154.7	153.9	153.1
Raw Materials	144.1	154.4	153.9	151.6
Ratio of Capital Goods Production to Consumer Goods Production (1967 = 1.00)	1.04	1.03	1.03	1.04

SOURCE: *Federal Reserve Bulletin.*

*As of January '82, M1-B has been redefined as M1.

TRADE ADJUSTMENT ASSISTANCE PAYMENTS (millions)

	1981	1982	1983	1984	1985	1986
Current base	2,743*	1,500	1,000	500	500	500
Proposed Reagan cut	—	–1,150	–760	–380	–380	–380
Reagan budget	2,743	350	240	120	120	120

*Actual outlays for 1981 were $1.3-$1.4 billion according to DOL and OMB.

[1]Organized labor's voice was one of the very few raised in opposition to the constriction of TAA, maintaining that the program was the result of an explicit compact between government and labor, in return for which labor would give its support to trade liberalization. In fact, not only had labor's support for open trade long since evaporated, but it had become one of the first critics of TAA, repeatedly denouncing it as "burial insurance."

[2]Charles R. Frank, Jr., *Foreign Trade and Domestic Aid* (Washington, D.C.: Brookings Institution, 1977); also see "Worker Adjustment Assistance Under the Trade Act of 1974 — Problems in Assisting Auto Workers," Report to Congress by the GAO Comptroller General, 11 January 1978.

PR Reviews (Cont. from p. 5)

ther separated from productivity. In several of the articles the very notion of discrimination is subject to searching analysis. It is shown to be a far slipperier concept than is often realized since discrimination is merely a form of human choice. *All* choice implies some kind of discrimination or a choice could not be made. It is further argued that the concepts of "equality" and "equality of opportunity" are even more questionable and that any attempt to enforce equality (other than equal rights before the law) will invariably hurt both the interests and the freedom of all parties concerned.

The book is highly recommended both as an introduction to the problem of discrimination and as a supplement to the previous work that such economists as Sowell, Williams, and Armen Alchian have done in this area.

Beating the System: The Underground Economy, by Carl P. Simon and Ann D. Witte. Auburn House Publishing Co., 1982. 296 pp. $21.95/$12.95.

In one of the most extensive studies of the underground economy to date, Simon and Witte look at the size, scope, and causes of this important phenomenon. Instead of approaching the problem using an aggregative macroeconomic framework as many economists do, a microeconomic, sector-by-sector analysis is used. Nearly every major sector of the underground economy from tax evasion to prostitution to bartering services is examined and then summarized. Extrapolating from sketchy and unreliable data, Simon and Witte estimate that the underground economy is now approximately one-tenth of reported national income and is growing by over 10% a year. More than half is attributed to tax evasion.

Beating the System does a good job of illustrating many of the secondary consequences of government intervention into the market, although the authors do not always recognize them as such. They do note that there is the tendency for unrecorded activities to make economic indicators (such as GNP, productivity rates, inflation rates, etc.) almost meaningless.

Although *Beating the System* is recommended as a good survey of the underground economy, it is not without flaws. Perhaps its most serious error is its treatment of government revenue loss as a *cost* of illegal activities rather than a *benefit*. On questions of public policy, the authors are admirably openminded towards legalization of many underground activities but also disappointingly noncommittal.

The Economics and Politics of Oil Price Regulation, by Joseph P. Kalt. The MIT Press, Cambridge, Mass., 1981. $35.00.

Government regulation of domestic energy markets has grown tremendously since the 1973 Arab oil embargo and represents one of the most significant recent changes in the American economy. Kalt's study, subtitled *Federal Policy in the Post-Embargo Era,* focuses on one aspect of this regulation — petroleum prices. Using a neoclassical "cost-benefit" approach to economic efficiency, Kalt divides the consequences of petroleum price regulation into two categories, allocative and distributional, and attempts to measure the consequences of intervention for each category. Particular attention is given to the refined petroleum products markets. The book also provides an analytical explanation of the political factors that shaped American post-embargo oil policy by using modern "public choice" theory and then investigates such a theory with an econometric study of the recent voting behavior of the U.S. Senate. Kalt's conclusion is that ". . . within the domestic public-policy arena, the Energy Crisis is primarily a battle over the appropriate distribution of income within society, rather than the manifestation of some massive failure of markets and institutions to allocate the nation's resources efficiently . . . the energy policies actually yielded by the political process have seldom been responses to the possibility or actuality of such failures."

The free market perspective of this book earns it a strong recommendation, but not without a serious caveat. Although mathematical tools of exposition are often used, the text stands on its own. However, in many cases, the validity of Kalt's method of presenting his case depends upon econometric measurement or cost-benefit analysis — two procedures that are sometimes inappropriate for the often subjective and immeasurable kinds of phenomena that the economist must deal with.

"To be governed . . ."

Out of order?

It finally happened. A government agency is suing itself. Ten holdover directors on the board of the U.S. Legal Services Corporation, which provides lawyers for the poor, are suing 10 Reagan appointees named to replace them on the ground that they are serving illegally because they were named during a congressional recess and have never been confirmed by the Senate.

—*U.S. News & World Report,* March 15, 1982

Part of Reagan's new Caribbean aid package?

Embarrassed Agriculture Department officials are hustling to tighten identification procedures for people applying for food stamps. Reason: Mexicans have been discovered driving across the border to U.S. grocery stores, buying supplies with food stamps and returning to Mexico.

—*U.S. News & World Report,* March 15, 1982

Balancing the budget?

U.S. News & World Report examined the government travel records of nearly 1,000 persons in high positions in the Carter and Reagan administrations. Despite the Reagan team's determined budget cutting throughout most of the federal establishment, the study found that—

Cabinet secretaries and other first-echelon appointees routinely exempt themselves from rules requiring economy rather than first-class travel and, in a few instances, have even crossed the Atlantic on the supersonic Concorde.

Some officials charter $1,000-an-hour jets and use government-owned planes that permit a level of luxury and convenience unknown to the average traveler.

Government-paid jaunts for the select few sometimes include vacation stopovers or hometown visits.

When top officials reach their destinations, they sometimes run up limousine bills of hundreds of dollars a day and luxuriate in $350-a-day hotel suites, with the tab covered by the taxpayers.

Reagan appointees are no more tight-fisted in their use of travel privileges than Carter appointees were, and some of them are less so.

—*U.S. News & World Report,* March 15, 1982

The economic program is working!

The new living-cost tax deduction that members of Congress awarded themselves is working to perfection. After being in session only 27 days this year, they already have earned unchallengeable deductions exceeding the old $3,000 annual limit.

—*U.S. News & World Report,* March 29, 1982

Democracy?

In an election year the influence of special interest groups is magnified, particularly since many of them hold the keys to the treasuries of some 3,000 political action committees, which poured $53.3 million into congressional campaigns in 1980 and will be spending even more this year to support their friends and punish their enemies.

Six hundred and eight trade and professional group funds distribute campaign cash where it will do the most "good" for the contributors. There also are 1,327 corporate PACs, 313 Labor PACs, 41 sponsored by cooperatives, and 539 others not affiliated with any particular industry but mostly ideological in nature.

—*The Press,* April 1982

The republican form of government

To qualify for the [Michigan press corps' legislative] honor roll, the words must have been spoken in a public forum and heard by at least two reporters. Each statement was intoned by a different elected official. . . .

- "There comes a time to put principle aside and do what's right. . . ."
- "It's a step in the right direction, it's the answer, and it's constitutional, which is even better. . . ."
- "I don't think people appreciate how difficult it is to be a pawn of labor. . . ."
- "Let's violate the law one more year."

—*Wall Street Journal,* March 19, 1982

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