

# **What Does Homeland Security Spending Buy?**

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International terrorism is probably the greatest security challenge America faces today. Policy makers have responded in two ways – going after terrorists abroad and improving security against terrorism at home by boosting homeland security funding. Regarding the latter, Congress and the administration moved swiftly to create a Department of Homeland Security and increased total funding for homeland security activities by 180 percent between FY2001 and FY2005.<sup>1</sup> (All FY2004 and FY2005 figures in this paper are official estimates) Total spending directed to homeland security activities will be at least \$47 billion for FY 2005, roughly \$435 per American household.<sup>2</sup>

This increase in security spending is part of a significant boost in the overall size of government. Between FY2001 and FY2005, the administration expects total outlays to rise from \$1,864 billion to \$2,442 billion—a 31 percent increase.<sup>3</sup> Clearly, no trade-offs are being made in the budget, as evinced by non-defense spending increases of 42 percent during the same four years that defense and homeland security spending have skyrocketed.<sup>4</sup>

On the issue of homeland security, the important question is whether America is getting the maximum level of benefit in exchange for this increase in spending.

This paper performs a detailed review of homeland security's spending practice. First, it takes a look at the economics of homeland security spending and contrasts that with the politics of decision making in this area. Second, it examines the state of homeland security spending. Finally, the paper analyzes how homeland security funds are being allocated and asks whether this is conducive to achieving improved security in the United States.

This paper will show that a substantial portion of new homeland security spending is being used for grants to state and local governments, many of which appear to be applied to questionable purchases. Second, the large increase in spending appears to have occurred without risk and cost benefit analysis, leading to a large amount of wasteful spending. For instance, a significant amount of spending is directed to addressing risks that are possibly obsolete, or fighting yesterday's battle, which is likely not the most efficient use of limited federal resources.

To conclude, the absolute amount of money spent on homeland security is not necessarily the issue in this work, but the political process leading to the way the money is spent is. Homeland security is a legitimate function of the federal government, and it is hard to say *a priori* what the optimal level of spending should be. However, economics suggests that if homeland security spending decisions are made on a political basis rather than on a sound cost benefit analysis, it will lead to the traditional public choice failures that plague government spending more generally. As a result, homeland security funding is likely to be misallocated, resulting in a less than optimal level of security in America.

## **II. The Economics of Homeland Security**

The terrorist attacks in 2001 stimulated a concerted effort to adopt security measures that would reduce the risks of similar events in the future. This was and is a logical response, as security, by definition, is about prevention of adverse consequences from the intentional actions of others. Economists think about security policies in terms of tradeoffs, formally comparing the costs and the benefits, both pecuniary and non pecuniary.<sup>5</sup>

We all make security tradeoffs. For example, when we lock the door to our house in the morning, we assess the small inconvenience of carrying a key in exchange for a modicum of security against a burglary. People make security decision trade-offs all the time, choosing more or less security as situations change. Optimal security decisions and policies require a good understanding of the risks and tradeoffs we face.

The scale of terrorism risk might seem to be small relative to the attention they command. For instance, 3,029 people died in the U.S. from terrorist attacks in 2001. During that same year, 156,005 people died from lung cancer, and 44,091 from automobile accidents.<sup>6</sup> While 3,000 deaths is clearly tragic, it is considerably smaller than other mortality risks, at least empirically. Of course, terrorists may hope that their future actions could significantly increase casualties, so the empirical probabilities may be a poor guide to the true risk.

But what makes deaths resulting from terrorist attacks different from the deaths from either automobile accidents or cigarette smoking is that these risks contain a voluntary element. Consumers of these products get some benefit from them, which compensates for the associated risks. There is no voluntary market transaction involving terrorism and no form of compensatory benefit. This has important policy implications. Consider what the federal government spends per year to increase automobile safety—\$38 million in FY2004—and compare it with the \$47 billion spent government wide on homeland security.<sup>7</sup> Terrorism is analogous to a flood that might occur, and government spending on terrorism is analogous to flood control.

Even presuming that politicians have chosen the level of spending on Homeland Security desired by voters, it is natural to ask whether that level is optimal. It is difficult both for scientists and for citizens to assess risks of events with low probability – such as acts of terrorism.<sup>8</sup> Through evolution and learning, people learn to handle many of the common risks they face in life. But Americans – fortunately – do not have extensive experience with terrorism. Even sophisticated assessors of risk—such as insurance companies—have a difficult time, though they do learn from experiences of other low probability risk events such as major natural disasters.<sup>9</sup>

The economics literature suggests that the media coverage of terrorism risks and the accompanying losses may create circumstances wherein people are likely to severely overestimate risks.<sup>10</sup> Viscusi *et al* (2003) show that the occurrence of such an event creates much uncertainty. More importantly it brings the realization that the future may contain many other severely adverse events than are currently unanticipated.<sup>11</sup>

This uncertainty is what could greatly magnify the terrorist threat, far beyond the actual damage that any single terrorist strike has historically caused. According to Trajtenberg (2003), it is precisely because of the uncertainty that accompanies the terrorist threat, and the associated costs (e.g. the provision of security at a myriad potential targets, reduced investments because of generalized uncertainty, disruption of travel, tourism, and perhaps also trade), that few terrorists, armed with relatively primitive means, can effectively threaten even a powerful nation.<sup>12</sup>

Thus, while the risks are difficult to quantify, there is reason to suspect that individuals may irrationally ratchet up their assessments of terrorist risk, and hence, may ratchet up their demand for homeland security spending. This may induce Congress to invest in projects that would not pass a cost benefit test. Whether that occurs or not is an empirical question.

### **What to invest in?**

While terrorism is only recently the dominant security issue in the U.S., economists have long studied the optimal provision of security more generally. In Gary Becker's seminal paper on

the economics of crime, he uses the tools of economics to think about the incentives of criminals and how to influence their behavior.<sup>13</sup> He explains that we can decrease unwanted behaviors by increasing their expected costs or decreasing their expected benefits. This approach applies to terrorism as well.

The primary method of discouraging terrorists is to make it more difficult to attack our assets. In effect, this reduces the “benefit” of a terrorist attack—since there presumably will be less damage—and forces terrorists to incur higher “cost” as they seek alternate targets. We install Jersey barriers to keep trucks away from important buildings, screen airline passengers, and employ internet firewalls. But it is important to make sure that the resources used to fight terrorism are being used effectively. This is not always the case. If a certain strategy reduces the threat of terrorism but has very high costs, it may not be the best use of resources if there is another approach that generates similar benefits but has lower costs to society.

For traditional criminals, potential incarceration is an important “cost” consideration and an efficient tool in deterring crime. And it is an effective use of resources since imposing stiff jail sentences is cheaper than guarding every house. Unfortunately, this approach is generally not effective against terrorists because they tend to be ideological extremists who give little weight to the personal costs of their actions. Suicide bombers, for example, will not be deterred by jail time. The most serious implication is that the possibility of deterrence is greatly reduced.<sup>14</sup>

Second, we can combat terrorism by decreasing the expected benefits to terrorists, either by increasing the probability of thwarting an attack or by decreasing the damage from a non-thwarted attack. To thwart attacks, we spend money on the CIA, FBI, and law enforcement to try to detect terrorist plots in advance. To decrease the damage from attack, we spend money on first responders, build fewer skyscrapers, and buy gas masks. One important implication of Becker (1968) is that there are tradeoffs between thwarting attacks and decreasing their damage: the more effective we are at thwarting attacks, the less we presumably should spend on decreasing their damage, and vice versa.

Taking the analysis a step further, the most efficient options to combat terrorism tend to be efforts to detect terrorists themselves or to respond effectively to minimize the damage after an attack has occurred. Spending to defend particular targets is generally less efficient. Both results stem from the fact that there are an almost unlimited number of targets, and the terrorist gets to choose where to attack. For example, suppose there are 100 potential targets, that we could perfectly defend for \$20,000 a piece, that the damage from un-defended attack would be \$500,000, and that we could mitigate one-tenth the damage from attack by spending \$50,000 on first responders.

If we knew where the terrorists would attack, we could spend \$20,000 to save \$500,000, which would be a prudent investment. But if don’t know the target, we would have to spend \$2,000,000 to defend all 100 targets, which outweighs the \$500,000 in damage. On the other hand, even if we did not know the target, we could spend \$50,000 on first responders to reduce the damage by \$250,000, which is an efficient tradeoff.

Of course, if we could track down terrorists in advance successfully, that would to prevent attacks on *all* possible targets, that approach would have similar efficiency properties as spending on first responders. In fact, it is possible that spending more money on intelligence and investigation might be far more cost effective than spending a little on every possible target or even waiting to be attacked and then cleaning up efficiently.

This raises again the notion of tradeoffs. Since the number of possible attacks is effectively unlimited and the resources we can devote to the fight against terror are limited, it

means that spending should not occur without a careful cost-benefit analysis. It is perfectly reasonable to decide not to implement an antiterrorism measure, not because it has no benefit, but because the tradeoffs are too high. For instance, locking up every Arab-looking person would reduce the potential for terrorism perpetrated by Islamic fundamentalists, but no reasonable person would suggest this approach because the costs (both pecuniary and moral) are too high. In the US, there are laws that prohibit police from profiling by characteristics like race, because we believe that such measures are unacceptable, but not because we believe them to be ineffective.

In the same way, some antiterrorist countermeasures might yield very high returns and reduce exposure to attacks tremendously, but the costs of implementing them are extremely high. If we install Jersey barriers around all major buildings and critical assets in the country, our exposure to attacks will be substantially lower, but the costs involved would be astronomically high.

Table 1. Cost Effectiveness of Selected Antiterrorism Expenditures

Cost to Prevent Terrorist Attack	High Cost	<i>Wasteful Outlays</i> Screen every airline passenger	<i>Major Sacrifices</i> Surround all critical infrastructure with concrete Jersey barriers
	Low Cost	<i>Simple Steps</i> Store fewer chemicals at water-treatment plants	<i>Efficient Outlays</i> Allow pilots to carry guns Place barricades on airplane cockpit doors
		Low Benefit	High Benefit
Benefit From Reduced Exposure to Attack			

Efficient expenditures concentrate limited resources on the most cost-effective expenditure rather than simply on the effective ones. For example, a cost effective security measure is to let pilot carry guns. Lott (2004) notes that “Terrorists can only enter the cockpit through one narrow entrance, and armed pilots have some time to prepare themselves as hijackers penetrate the strengthened cockpit doors.”<sup>15</sup> He adds that “the boredom and high attrition rates afflicting air marshals (who fly back and forth on long flight waiting for something to happen) does not apply to pilots.” And no extra pay is needed since pilots are volunteering to take time off and travel to the training at their own expense. In addition, 70 percent of the pilots at major American airlines have military backgrounds.<sup>16</sup> It reduces the cost of training them and increases the effectiveness of this simple measure. Besides, the fears of bullets damaging planes are greatly exaggerated. Lott (2004) reports that “As Ron Hinderberger, director of aviation safety at boeing testified before Congress: Commercial airplanes structure is designed with sufficient strength, redundancy, and damage tolerance that a single or even multiple handgun holes would not result in loss of an aircraft.”<sup>17</sup>

Also, attacks of the style of 9/11 could be prevented with simple cockpit barricades, which the airline industry has now installed at relatively low costs.<sup>18</sup> According to the Federal

Aviation Administration (FAA), the purchase and installation cost of an enhanced cockpit door is estimated at between \$30,000 and \$50,000. The total cost to airlines is estimated between \$300 million and \$500 million over a 10-year period, including increased fuel consumption costs resulting from heavier doors.<sup>19</sup> Congress originally appropriated \$100 million to the FAA to distribute to U.S. airlines for aircraft security enhancements, \$97 million of which were given to the airlines to help defray the costs of cockpit doors (approximately \$13,000 per door). It means that the total government cost was estimated between \$92.3 million and \$120.7 million over a 10-year period.<sup>20</sup>

In contrast, the burgeoning U.S. system for screening every bag of every airline passenger has already cost taxpayers \$10 billion in the last three years.<sup>21</sup> This system does little to prevent 9/11-style hijacking, which is the largest empirical airline-related risk.<sup>22</sup> Furthermore, this checked-bag screening does not necessarily reduce the probability of the destruction of airplanes, since neither carry-on bags nor airfreight are systematically checked for explosives, and terrorists have revealed a propensity to engage in suicidal behavior. Whether this \$10 billion is an efficient allocation of resources depends on whether alternative less costly measures have been crowded out by this spending.

Last but not least, it is worth noting that federal expenditures are not the only costs associated with homeland security. First, even though successful terrorist attacks can impose significant economic costs, defense and homeland security spending displaces resources from the private sector toward the production of security measures that, while necessary, are not terribly productive in terms of economic growth.<sup>23</sup> The Joint Economic Committee (JEC) for instance observe that “increased spending on security will likely be associated with lower economic growth since more capital and labor are diverted toward security production and away from the production of final demand.”<sup>24</sup>

In other words, because security always involves a tradeoff, more security spending does not always mean more security and more security does not always make us better off. Given these factors, then, how can an outside observer evaluate whether spending is excessive and poorly focused? Clearly, two logical possibilities exist. First, one could examine spending that occurs and evaluate whether significant waste exists. Second, one could identify possible additional programs that could accomplish heightened security in a more cost effective manner. For the most part, this study will focus on the former approach, but the latter is an important topic for future research.

### **Who should pay for Homeland Security?**

Before turning to an evaluation of existing programs, one should also evaluate the economic reasoning behind federal provision of homeland security. National defense is often cited as the archetypal public good, i.e., one person’s consumption of the good does not prevent another person from consuming the same good.<sup>25</sup> Another characteristic of public goods is that they are non-excludable, i.e., it is hard or impossible to prevent anybody that desires from getting access to and enjoying the public good once it is produced. Private goods have opposite characteristics: they are rival and excludable.

Economic theory suggests that it is efficient to have governments provide public goods, but to resort to private markets for the provision of non-public goods, e.g., governments should provide national defense, but markets should produce washing machines. Indeed, national defense is the strongest justification for government, since as Trajtenberg (2003) notes, markets

might fail to provide it, whereas other traditional public goods, such as “maintaining law and order,” can theoretically be provided by private markets in a decentralized fashion.<sup>26</sup>

As already mentioned, a key feature of terrorism is that the threat is generalized (it can happen anywhere, at any time) and yet any particular attack is “local.” By implication, homeland security is a mix of public and private goods. Accordingly, governments should provide some types of homeland security, while other types are best left to private markets. For example, governments should invest in intelligence gathering to track down terrorists, since this is a public good that benefits all citizens. But the protection of private property, such as personal residences, should be left to individuals because it is not a public good.<sup>27</sup>

A similar logic applies to which aspects of homeland security are public goods at the national versus state level. (See Table 2.) Espionage, intelligence, and immigration control benefit all the states, so the *federal* government should make these investments. But the benefits of protection of public infrastructure like bridges and water treatment plants are enjoyed by the residents of a particular state, rather than many states, so these investments should be made at the *state* level. This is not to say that the entire economy might not suffer were a specific bridge to be destroyed, but rather, that the principle economic impact of such an unfortunate event would be felt locally.<sup>28</sup>

Table 2: Who should be responsible for Homeland Security?

Federal Government	State and Local Government	Private Sector
Espionage Intelligence Immigration Protection of Electric Grid	Protection of Infrastructure such as: Bridges and Water reservoirs First Responders	Protections of Infrastructures such as: Stadiums, Skyscrapers and individual houses

### A Public Choice Approach to Homeland Security Spending

Public choice theory also can be applied to homeland security spending. Many decisions on homeland security come through the political process. According to public choice economics, each participant has an incentive to maximize the political benefits of any particular action. This means that decisions are not always based on an assessment of the common good.

Schneier (2003) asks an interesting question to illustrate that point.<sup>29</sup> Imagine that after September 11<sup>th</sup>, all the players involved in airline security were in a room trying to figure out what to do. Some members of the public are scared to fly, others aren't. The airlines are desperate to get more people flying but are wary of security systems that are expensive. They are also worried that increased security might impose great organizational costs on them. The elected officials in the room are concerned about reelection and are concerned that they might be blamed for the attacks. And they need to be seen by voters as doing something to improve security. The FAA is left torn between its friends in the airline industry and its other friends in government.

Because everyone in this example is hypothetically looking at the security problem from his own perspective, no one is really trying to figure out what the right security tradeoffs are. As a consequence, the airline industry is happy to let the government take over the job of airport

screening because it won't cost them as much and it won't be their fault if there is another attack in the future. The politicians want to be perceived as actively addressing the concerns of the voters. The FAA enjoys its increased powers in a context that pleases the government and the airlines, and the public likes the feeling that something is being done. Yet it does not mean that the measures adopted will end up increasing security.

Public Choice theory underlines the different incentives and processes that operate when goods are sought through political means rather than through economic means.<sup>30</sup> For instance, if you have to use your own money to buy the lock on the door to protect your house, you will make sure that the increased security from the lock is worth the price of the lock. In the words of Buchanan (1969), an individual spending his own money makes sure that anticipated benefits exceed the costs.<sup>31</sup> In the political process though, the people buying the lock are rarely the ones paying for the lock. As such, they have less reason to balance costs and benefits.

The political appropriation and distribution of goods concentrates its benefits and disperses its costs. Many people can be taxed at a low rate so a small number of people can be given large sums. Special interests groups have an incentive to lobby the government to see that wealth is transferred to them. The term economists use to describe such lobbying is "rent-seeking."<sup>32</sup> These pressure groups have a clear advantage in a political process where politicians are frequently accused of hearing nothing from the many and a lot from the few.<sup>33</sup>

But policymakers represent an interest group too. In seeking reelection, they have an incentive to please those who might have money or votes to contribute to them. For instance, being elected by state voters rather than federal ones, a Congressman has an incentive to try to bring back to his state as much federal money as possible rather than to fight to cut down federal spending.<sup>34</sup> A good example of this phenomenon is the increasing number of low priority and wasteful spending items—also called pork barrel spending—introduced by Congress at the last moment into federal spending bills and directed at a specific state locality or at a specific facility. In the same way, politicians are likely to favor and transfer wealth to targeted industries—like the farm or the automobile industry.<sup>35</sup>

Thus, constituencies and interest groups are created for each particular political benefit program, and it may become, if this theory is correct, nearly impossible to develop policy initiatives without their input. This of course has major implications for the way politicians will make decisions about homeland security spending. First, because policymakers who are ultimately making homeland security decisions are often not the ones making the tradeoffs, it is possible that they will throw money at the problem rather than finding the most cost-effective antiterrorist measure to adopt. Also, lawmakers are likely to use homeland security funds to achieve non-homeland security agendas through the use of pork barrel spending and corporate welfare.

Finally, "homeland security" pressure groups—e.g. first responders, state officials and/or specific industries like the airline industry—may have an incentive to lobby lawmakers to try to grab a bigger share of the funding allocated to homeland security programs and /or to transfer their responsibilities to the federal government. In a recent paper, Besley et al. (1999) look at the tradeoffs between centralized and decentralized provision of local public and private goods.<sup>36</sup> They emphasize the importance of the politics of decision making for the move toward more centralization of local responsibilities and the inefficient allocation of resources resulting from this process.<sup>37</sup> Federalization of airline screeners and the trend toward the federalization of law enforcement and first responder programs are recent examples that may be consistent with this evidence.

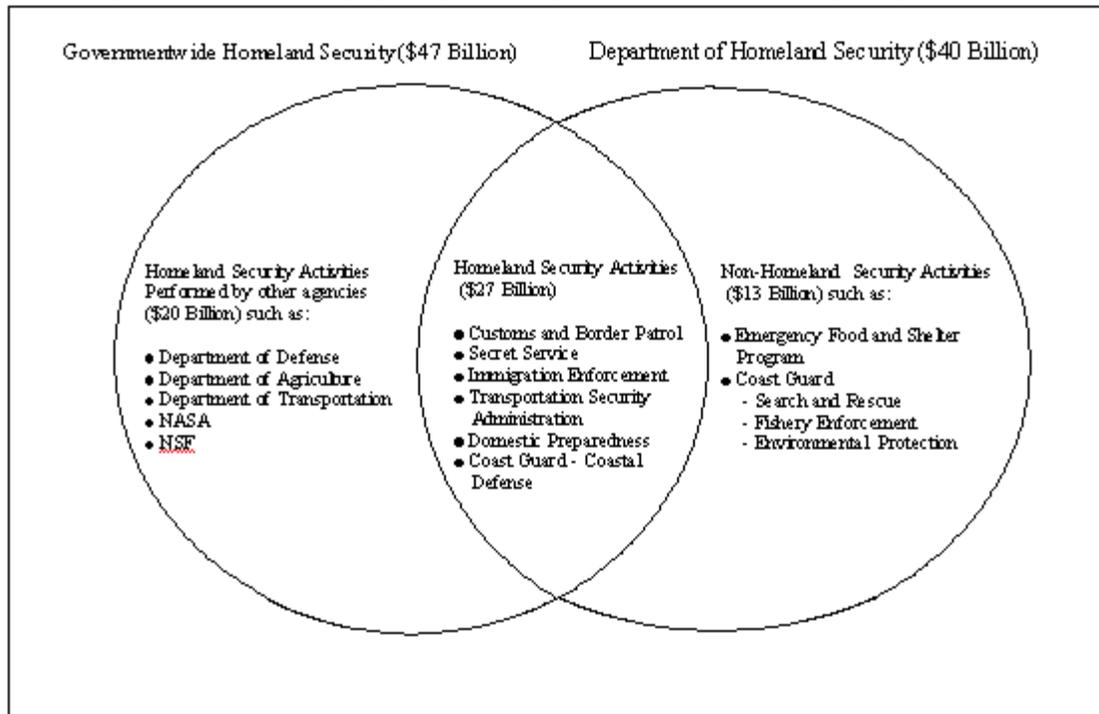
### **III. The State of Homeland Security Spending**

According to the Congressional Budget Office, “tracking and analyzing [homeland security] spending has proven to be difficult.” The funding is split into 200 different appropriation accounts within the federal budget and involves many different functional areas of government. Furthermore, most of the funding resides within accounts that primarily finance activities not directed at homeland security.

Congress and the administration also created a new Department of Homeland Security (DHS) to consolidate in one agency activities that had previously been spread throughout the federal government. Many—including at first President Bush—opposed the idea that creating additional layers of bureaucracy would make America more secure. In spite of this early opposition, DHS Secretary Tom Ridge today oversees nearly 190,000 employees and including funding for Project Bioshield, mandatory spending and fee-funded programs, DHS received a total of \$40.7 billion for FY2005 through the Homeland Security Appropriation Act of 2005 which President Bush just signed into law.<sup>38</sup> This is \$896 million more than the president had requested in its February budget.<sup>39</sup>

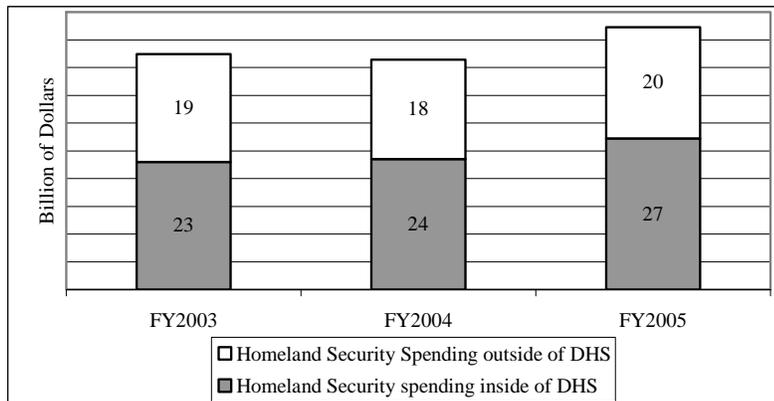
Despite the creation of the DHS, homeland security spending continues to be an elusive figure to quantify because a large portion of homeland security spending takes place outside of the Department of Homeland Security. In addition, its name notwithstanding, the Department of Homeland Security’s activities are not strictly directed to the protection of the homeland.

Figure 1: Homeland security spending versus Department of Homeland Security Budget, FY 2005



Sources: Budget of the United States, FY 2005, and Department of Homeland Security Budget in Brief, FY 2005

Figure 1 illustrates that point. In February, President Bush proposed the FY2005 budget for the Department of Homeland Security to be roughly \$40.2 billion (this amount does not include the 2004 Iraq supplemental of \$25 billion).<sup>40</sup> Only \$27 billion of DHS's budget is directed toward activities that meet the executive branch's definition of Homeland security.<sup>41</sup> The remaining \$13 billion—a significant portion of DHS's budget—finances non-homeland security activities like the Coast Guard's role in maritime rescue and FEMA's Emergency Food and Shelter Program. Figure 1 also shows that the President's proposed budget authority for homeland security activities government-wide represents about \$47 billion for FY2005.<sup>42</sup> It means that \$20 billion out of \$47 billion is spent and labeled homeland security spending outside of DHS. Figure 2. Homeland Security Spending: Outside vs. Inside of DHS



Source: Budget of the United States, FY2005 Table S-6.

Note: Includes all supplemental for 2003 and 2004

Figure 2 shows that during the last three years, a large amount of homeland security spending has taken place outside of the Department of Homeland Security. This is explained by the way legislators decided which programs should or not be transferred to the newly created DHS. It appears that the only real question asked then was “in” or “out.” As it happened, large homeland security items were left out of DHS, while some small items not related to homeland security were incorporated into DHS, perhaps because this made the programs less likely targets for future cuts.

Table 3 shows which agencies and departments are supposedly performing homeland security activities outside of the Department of Homeland Security. It also shows how much money the President requested for each agency and department for homeland security activities in FY2005.

Table 3. Homeland Security Funding By Department and Agency  
(Budget Authority in Millions of Dollars \$)

Departments	FY2005	Department's Share of Total HS funding outside of DHS
Agriculture	651	3.2%
Commerce	150	0.7%
Defense-Military	8023	39.8%
Energy	1497	7.4%
HHS	4276	21.2%
Justice	2581	12.8%
State	955	4.7%
Treasury	87	0.4%
Transportation	243	1.2%
Veterans Affairs	297	1.5%
Corps of Engineers	84	0.4%
EPA	97	0.5%
Social Security Administration	155	0.8%
NASA	207	1.0%
NSF	344	1.7%
Other Agencies	525	2.6%
<b>Total HS Funding</b>	<b>20172</b>	<b>100.0%</b>

Source: Budget of The United States, FY2005, Table S-6.

Note: FY2003 and FY2004 Supplementals are included

Note 2: FY2004 and FY2005 are estimates

Of those, four agencies—the Department of Defense (DOD), Health and Human Services (HHS), Justice (DOJ), and Energy (DOE)—account for approximately 81 percent of total government-wide homeland security funding outside of DHS. Not surprisingly, a large portion of the homeland security money will be spent by the Department of Defense—\$8 billion in FY2005—and by the Department of Justice—\$2.5 billion.<sup>43</sup>

Other funding decisions are more curious. The Environmental Protection Agency (EPA), for example, receives significant funding. The funding supports programs to develop technology to “help decision-makers prepare for, detect, contain, and decontaminate chemical and biological attacks directed against buildings and water treatment systems.”<sup>44</sup> NASA also receives funding. The NASA funding supports the development of microscopic sensors for the detection of biological, chemical, and nuclear weapons and the monitoring the nation’s air and water resources.<sup>45</sup> Veteran Affairs, which has the primary mission of caring for veterans, receives homeland security spending “to ensure that our facilities are sufficiently hardened to protect our own staff and patients and ability to serve veterans.”<sup>46</sup>

The U.S. Department of Agriculture (USDA) receives funding “to focus upon three key areas: agricultural production and the food supply, USDA facilities, and USDA staff.”<sup>47</sup> The Department of Commerce (DOC) also receives funding to develop a formal working relationship with the DHS Science and Technology Directorate and the DOC Technology Administration’s National Institute of Standards and Technology (NIST). NIST research includes programs for the detection of chemical, biological and other explosive threats.<sup>48</sup>

Why all these agencies with new homeland security accounts are getting homeland security funds is not a trivial question since many of these agencies have suffered from documented mismanagement.<sup>49</sup> Official reports about various shuttle disasters and the General Accounting Office (GAO) have repeatedly declared NASA mismanaged.<sup>50</sup> Reports also show that in the last 20 years the Department of Energy has consistently terminated projects prior to completion, causing billions of dollars of losses, while most of its other projects were either over budget or behind schedule.<sup>51</sup> The Army Corps of Engineers, which now receives homeland security funds as well, has been found to falsify data to justify large construction projects.<sup>52</sup> And the agency is frequently criticized for wasting billions on environmentally damaging projects in the districts of important Members of Congress.<sup>53</sup>

The GAO reported that the Pentagon’s financial management problems are “pervasive, complex, long-standing, and deeply rooted in virtually all business operations throughout the department.”<sup>54</sup> And DOC is found to need improvement in its financial management and control over its internal weakness while USDA is often declared to “lack financial accountability over billions of dollars of assets.”<sup>55</sup>

One might think that the creation of the DHS would have allowed the government to move spending away from agencies with troubling track records. With so much funding spent on homeland security outside of DHS, the promise that the creation of DHS would result in an entity with sole responsibility for the government’s efforts against terrorism is called into question. Moreover, with the money split between so many departments and programs, the ability of DHS or Congress to conduct effective oversight decreases. The new department has authority over the parts of agencies subsumed under it but not over the many more that remain outside of its control.

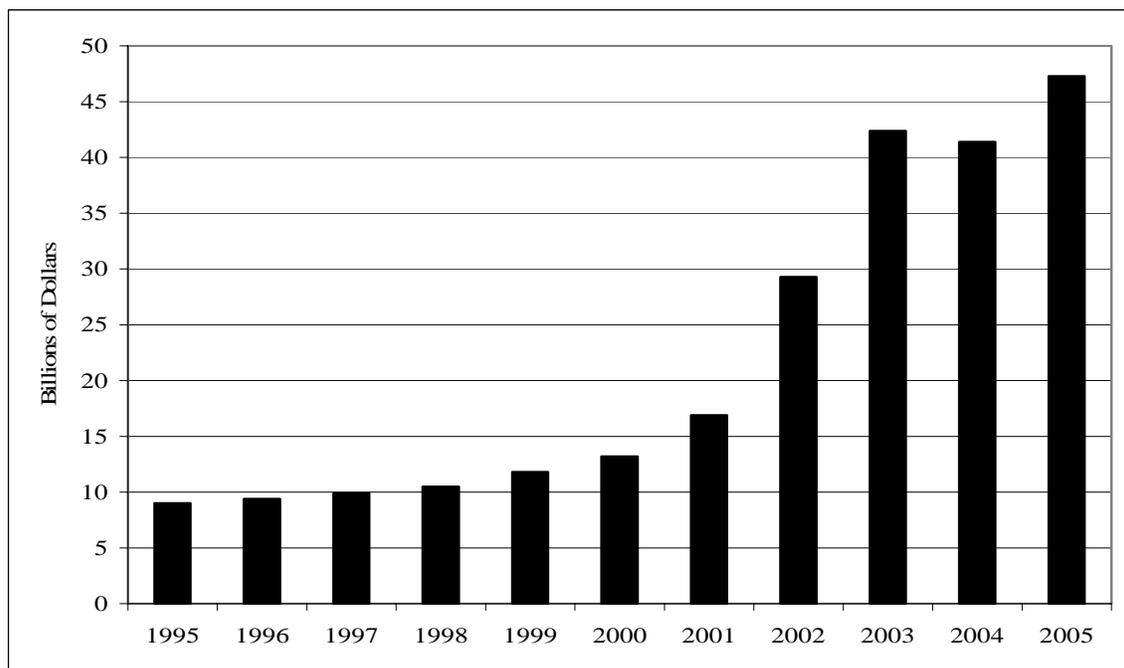
There is also a great risk that the political effect of the words “homeland security” will increase the necessity of effective oversight. Agencies, including DHS, are often aggressive advocates of the expansion of their own budgets and protect vigorously their own statutory mandates. With so much of the spending already diffused, the current structure invites future disputes. Conversely, because so much money unrelated to homeland security activities is spent inside DHS, the risk of funding increasing for these activities under the assumption that it serves some homeland security purpose may also be high. Last Christmas, for instance the DHS handed out about \$153 million for programs offering food and shelter for the poor to be spent thorough

2004. This is a significant increase from this program's previous year budget.<sup>56</sup> And in September the Senate attached \$2.9 billion in disaster aid for farm states plagued by droughts, floods and freezes in the past year to the FY2005 Homeland Security bill. Another \$700 million in hurricane aid for Florida farmers may be added in conference.<sup>57</sup> Also, Homeland Security Secretary Tom Ridge is now campaigning aggressively about the idea that hurricane disaster relief and others are a legitimate part of homeland security since the Federal Emergency Management Agency (FEMA) can respond to a wider variety of emergencies than just terrorism relief. This is likely the first step toward the slippery slope of the increased involvement of the Department of Homeland Security in non-homeland security activities.

Programs that Congress might not approve if they were outside of DHS may likely sail through because of their DHS affiliation. Indeed, a significant volume of legislation since 9/11 has been rushed through in a tone of urgency with reference to the tragedy and its relationship to homeland security, with the \$190 billion farm bill serving as a recent example

#### IV. The Rapid Growth in Homeland Security Spending

Figure 3. Trend in Homeland Security Spending between FY 1995 and 2005



Sources: Budget of the United States, Fiscal Year 2005, Table S-6 and Office of Management and Budget, "Securing the homeland, Strengthening the Nation" [http://www.whitehouse.gov/homeland/homeland\\_security\\_book.pdf](http://www.whitehouse.gov/homeland/homeland_security_book.pdf)

Funding for homeland security activities has risen substantially since 2001. Figure 3 shows the government-wide trend in homeland security spending since FY1995. Levels for FY 1995 through 1997 are estimated, as OMB did not collect data on these activities prior to FY1998.<sup>58</sup> Not surprisingly, the estimate shows that homeland security spending was relatively small prior to 2001 and increased drastically between FY2001 and FY2005, from \$16.9 billion to

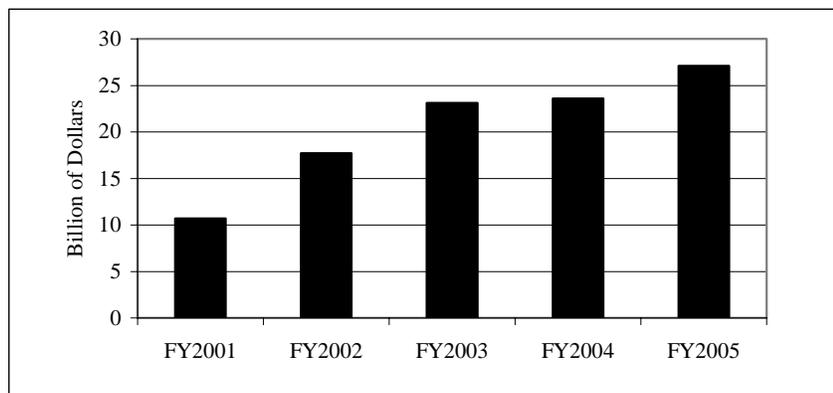
at least \$47.7 billion—a 180 percent increase over that period. Nor has the growth slowed in recent years. The figures show a \$6.1 billion (15 percent) increase since FY2004.

Also since FY 2001, Congress and the President increased nondefense discretionary appropriations for homeland security from \$10 billion in 2001 to the president's request of \$30 billion for FY2005—a 200 percent increase in 4 years.<sup>59</sup>

The largest part of this increase comes from an increase in the total Department of Homeland Security's budget, which grew from \$31.2 billion in FY2003 to a requested \$40.2 billion in FY2005 (this figure does not include the Iraq supplemental). This represents a 29 percent increase since the department was created in November 2002 and a 10 percent increase since FY2004.<sup>60</sup>

Figure 4 shows the increase in homeland security activity spending in the Department of Homeland Security.

Figure 4. Evolution of Homeland Security Activity Spending Within DHS Since FY20



Source: Budget of the United States, FY2005, Table S-6.

The Department of Homeland Security was established in 2003 so the figures for 2001 and 2002 represent the spending of the agencies that eventually composed the new department. These agencies that are now part of DHS include the Coast Guard, the Federal Emergency Management Agency (FEMA), the Secret Service, the Transportation Security Administration, and offices that were formerly part of the Immigration and Naturalization Service (INS) and the Customs Service.

The portion of the DHS budget devoted to homeland security has increased from an estimated \$10.7 billion in FY2001 to a proposed \$27.1 billion in FY2005.

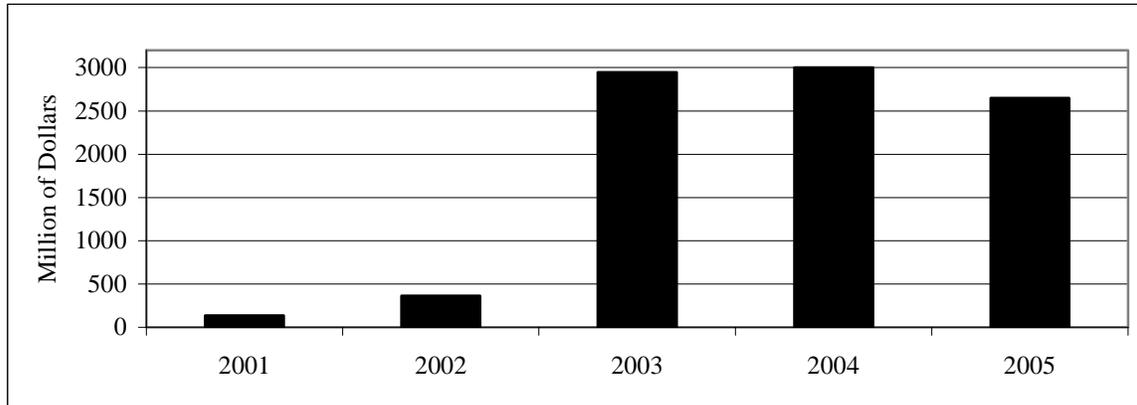
## V. Risk And Cost Benefit Analysis in Homeland Security Spending

Are homeland security funds within DHS well spent? How much security does \$27 billion buy? On this score, information gleaned from the budget documents range from mixed to vague. A review of homeland security spending by DHS raises considerable doubt.

The September 11<sup>th</sup> attacks revealed some gaps in the ability of local officials to respond to terrorist attacks on major urban cities. In response, Congress moved swiftly to appropriate homeland security funds to state and local governments. Total federal homeland security spending to state and local governments increased from \$2.7 billion in FY2001 to \$5.5 billion in FY2005 (a 100 percent increase).

A significant portion of that effort was directed to “first responder” programs – essentially federal funds for state and local police and fire departments. Homeland Security funding to state and local governments for first responder programs increased from \$616 million in FY2001 to \$3.6 billion in FY2005 (a 500 percent increase). But the biggest share of this first responder program explosion took place in the form of grants to lower level governments. Figure 5 shows the increase in terrorism preparedness grant programs to the states for first responders. Between FY2001 and FY2005, the money appropriated for these grants increased by roughly 2000 percent from \$135 million to \$2.6 billion.

Figure 5. DHS Grants to States to Enhance the Ability of First Responders



Source: Office of Domestic Preparedness, " State Homeland Security Grant Program I and II."

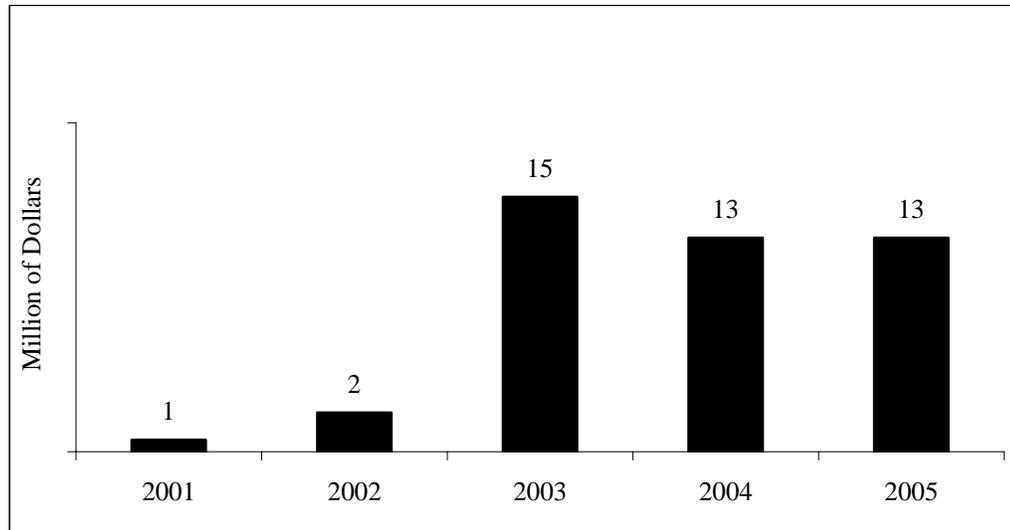
This first responder grant money—which is channeled through the Department of Homeland Security—is intended to help so-called first responders to buy chemical and radiological detectors, improve their emergency communication systems, expand training and take a series of other steps to help deter and respond to terrorist attacks.

While the quantity of funds is significant, the funds are not being allocated according to a plan that was devised by security experts. According to a report released in April 2004 by Chairman of the House Select Committee on Homeland Security Chris Cox (R-Calif) “An Analysis of First Responder Grant Funding,” the formula that drives the process is mainly to blame for that evolution.<sup>61</sup> In keeping with the way Washington spreads federal taxpayer’s money to the states—whether for highways, education or emergency preparedness—DHS follows in part a formula set by Congress that provides every state with a guaranteed minimum amount of state grants regardless of risk or need. Specifically, the formula written into law by Congress into the Patriot Act after September 11<sup>th</sup> guaranteed each state 0.75% of the total amount appropriated to DHS for state terrorism preparedness grants, with smaller shares going to territories like Puerto Rico. It amounts to 40 percent of the total pot of money being divided up equally among the states, regardless of size, risk, or need.

Prior to September 11<sup>th</sup>, total funding covered by the formula—i.e the State Homeland Security Grant Programs (SHSGP), which is the sum of a series of separate grants, plus Critical Infrastructure Protection Grants—amounted to \$97 million.<sup>62</sup> It means that in 2001 the guaranteed minimum each state would receive was less than \$1 million. However, due to the 20-fold increase in this program between FY2001 and FY2003 from \$97 million to \$2,066 million the minimum guaranteed amount each state was receiving went from \$1 million to \$15.5 million

regardless of risk or need.<sup>63</sup> In FY2004, this minimum guaranteed sum is estimated to be at least \$13 million (see Figure 6).

Figure 6. Trend in Minimum Guaranteed to States by DHS



Source: Author's calculation based on Office of Domestic Preparedness Figures, FY2005

After this 40 percent of SHSGP is allocated to states, the 60 percent left over is apportioned among states based on population, not risk. For the smallest states, this formula means an additional \$2 million on top of the guaranteed minimum. In FY2003, the two combined allocation formulas resulted in Wyoming, the least populous state, receiving \$17.5 million and California, the most populous state, receiving \$164 million regardless of risk or need.<sup>64</sup> And according to the same calculation, in FY2004 Wyoming is guaranteed to receive a minimum of \$15 million and California, the most populated state, at least \$133 million.

The underlying theory behind this all-state-minimum formula is that terrorists could strike anywhere and that heads of homeland security agencies in rural and small states throughout the country have now become convinced that their turf is just as threatened as Washington, New York or Chicago. The journalist Amanda Ripley adds in the *New York Times Magazine* “when asked about relative risks, these officials talk about relative worth and the right of their citizens to get the same kind of protection that they are afforded in other places in the country.”<sup>65</sup>

The theory that money should be spent smoothly across states has not been supported by reasoned analysis during the public policy debate. And experts in the field have reached different conclusions. The Insurance Services Office (ISO)—a private company—serves the insurance industry by maintaining data on risks of all kinds and helping insurance companies underwrite policies at prices commensurate with those risks. In 2003 ISO did a research project to set objective prices for terrorism insurance. They surveyed five former FBI, CIA and Pentagon intelligence experts and applied their opinions to a database of 300,000 potential targets. They then used this information to set baseline rates for terrorism insurance. Their conclusion is the following: The highest risk cities in the U.S. are New York, Washington, DC, Chicago, San

Francisco and those at high risk of attack are Los Angeles, Philadelphia, Houston, Seattle and Boston.<sup>66</sup>

Many other glitches in the homeland security grant distribution are the result of those two government formulas. For instance, among the top 10 states and districts receiving grants only the District of Columbia also appeared on a list of the top 10 most at risk places.<sup>67</sup> Currently, states in rural, less populated areas, or populated areas – but less likely to be targeted by terrorist acts – often receive a disproportionate amount of grant money.

Table 4 shows how much in dollars per capita each state received from State Homeland Security Grants Programs for FY2003. New York State received 4.68 percent of general grant money while its population accounts for 6.55 percent of the nation’s population. California received 7.95 percent of general grant money while its population accounts for 12 percent of the nation’s population. And Wyoming, which has a population that accounts for 0.17 percent of the nation’s population, receives 0.85 percent of all the grant monies. This translates to \$5.05 per capita in New York State, \$4.69 per capita in California and \$35.30 per capita in Wyoming. And spending on U.S. territories is equally variable. In FY2003, the US Virgin Islands received \$97.15 per capita, Guam \$84.11, and Northern Mariana Islands \$50.26.

Table 4: Dollar Per Capita Received by States From Homeland Security First Responders Grant Programs for FY2003

State	\$ Per Capita Grants	State	\$ Per Capita Grants
Virgin Islands	97.1	Oregon	8.6
Guam	84.1	Puerto Rico	8.3
Northern Mariana Islands	50.3	Kentucky	8.0
Wyoming	35.3	South Carolina	8.0
American Samoa	34.9	Louisiana	7.7
District of Columbia	31.5	Alabama	7.7
Vermont	29.4	Colorado	7.7
North Dakota	28.7	Minnesota	7.3
Alaska	28.4	Arizona	7.1
South Dakota	24.6	Wisconsin	7.1
Delaware	23.5	Maryland	7.1
Montana	21.3	Missouri	7.0
Rhode Island	18.7	Tennessee	6.9
Hawaii	16.7	Washington	6.8
New Hampshire	16.4	Indiana	6.8
Maine	16.2	Massachusetts	6.7
Idaho	15.8	Virginia	6.4
Nebraska	13.2	North Carolina	6.1
West Virginia	12.8	Georgia	6.1
New Mexico	12.6	New Jersey	6.1
Nevada	11.4	Michigan	5.8
Utah	10.9	Ohio	5.6
Arkansas	10.0	Pennsylvania	5.5
Kansas	10.0	Illinois	5.5
Mississippi	9.7	Florida	5.2
Iowa	9.5	New York	5.1
Connecticut	8.7	Texas	5.0
Oklahoma	8.7	California	4.7

Source: Author's calculation based on Office of Domestic Preparedness, "Fiscal Year 2003 State Homeland Security Grant Program," and "Fiscal Year 2003 State Homeland Security Grant Program - II" And the U.S. Census.

One should not conclude that more money should be handed to states with a lower dollar grant per capita or with a large population like California or that money should be taken away from small states with high dollar per capita. Cox (2004) points out “It is not the case that American Samoa should receive proportionately less or should, in the nature of things, receive more or less than anywhere else, except in my view, if security needs require it.”<sup>68</sup> In other words, grant money should only be distributed based on an evaluation of risk and security need and nothing else. The political formulas used now to allocate the money disconnect the funding from the risk of being attacked.

The same lack of assessment of risk and need exists in the way states allocate or pass through the funding from DHS to their localities (they are obligated to pass through 80 percent of the money received).<sup>69</sup> For instance, Carafano (2004) reports “California distributes its federal grants in base-amounts of \$5,000 to each county, an amount so small and arbitrary it seems that it is difficult to imagine how it could be used productively.”<sup>70</sup>

## **VI. Use Of Homeland Security Grants**

The lack of risk-based funding coupled with the absence of federal terrorism preparedness standards or goals to guide expenditure of funds at the state and local levels has resulted already in some questionable uses of terrorism preparedness grants.<sup>71</sup> Expressing his concern, Chairman Nickles from the Senate Budget Committee notes, “Congress is creating programs under the banner of homeland security, which in some cases, some cities and some states are using as more or less revenue sharing.”<sup>72</sup> And Chairman Chris Cox notes that “there have been numerous reports suggesting that the first responder monies that have been received and spent to date have not necessarily gone to the first responders who need it most, or for projects that materially enhance our homeland security.”<sup>73</sup>

The data support their fears. Some of the misused of federal funds per states and local governments include:

\$63,000 decontamination unit bought with federal funds and now stored in a warehouse in rural Washington State because the state does not have a HAZMAT team to use it.<sup>74</sup>

\$22,800 spent by an unnamed state to buy six radios that are incompatible with county radios<sup>75</sup>

\$58,000 used by rural Colchester, Vermont (population 18,000) to buy a search and rescue vehicle capable of boring through concrete to search for victims in collapsed buildings.<sup>76</sup>

\$30,000 used by officials in Lake County, Tenn., to help a high school buy a defibrillator to have on hand for a basketball tournament.<sup>77</sup>

\$350,000 spent by a small volunteer’s fire department in Virginia on a custom-made fireboat.<sup>78</sup>

\$1.5 million spent by the County of Grand Forks, N.D. (pop. 70,000), to buy more bio-chemical suits than police officers, two trailers equipped with gear to respond to weapons of mass destruction, decontamination tents and a semi-armored van.<sup>79</sup>

\$500,000 spent by Outagamie County, Wis. (pop. 165,000) to buy chemical suits, generators, rescue saws, disaster-response trailers, emergency lighting, escape hood and a bomb disposal vehicle.<sup>80</sup>

\$98,000 spent on training courses in incident management by the Tecumseh fire department in Lenawee County Michigan that no one attended.<sup>81</sup>

\$900,000 awarded to the Steamship Authority, which runs ferries to the resort island of Martha’s Vineyard, and Vineyard harbor to upgrade their facilities.<sup>82</sup>

\$557,400 to North Pole, a town in Alaska (1,570 people) for homeland security rescue and communications equipment.<sup>83</sup>

These are not isolated cases of unfortunate uses of homeland security funds. Meanwhile, as Senator Nickles points out “[large and high risk cities] are as likely to waste homeland funds as low risk areas.”<sup>84</sup> Senator Conrad notes “I have heard from individual departments that spending initiatives that were pending previously that were not approved once they were given the label of homeland security, whether or not they fit the description, sailed through.”<sup>85</sup> For instance, Washington DC—incontestably one of the high threat areas in the country—used the region’s first wave of Homeland Security aid to fund leather jackets for its police force.<sup>86</sup> It also used \$300,000 for a computerized car towing system that the mayor had promised for three years to help combat fraud by private towing companies and \$100,000 to fund the mayor’s popular summer jobs program.<sup>87</sup>

While many inefficient allocations of funding have occurred, almost three years after the State Homeland Security Grant Program was launched, first responders across the Nation have not received the vast majority of the \$6.3 billion that congress and the Administration have allocated in terrorism preparedness grants since September 11 (FY2002 to FY2004).<sup>88</sup> In fact \$5.2 billion in the Department of Homeland Security grant money remains in the administration pipeline, waiting to be used. At the end of the year, the money requested by the President for FY2005 will be added to the funding pipeline (\$2.6 billion).<sup>89</sup>

## **VII. Are Federal Grants to States Efficient?**

The real question is whether these problems with homeland security grants to the states are not simply symptomatic of any federal grant system. If that is the case, it means there are more productive ways to protect America than federal grant programs to state and local governments.

In theory, the United States is a federal system, meaning that the federal government was designed to have specific limited powers with most basic functions left to the States. But in the last fifty years, the federal government has undertaken a large number of activities that were traditionally and constitutionally reserved to the states. To extend its power into state affairs the federal government has developed a vast and complex system of grants to states and local government.<sup>90</sup>

In FY2004, the total amount of federal grants paid out to the states and local government is scheduled to reach well over \$418.1 billion. President Bush requested \$416.5 billion for grants for FY2005.<sup>91</sup> According to the GAO, over the past 20 years the number of federal grant programs to states and local government has proliferated from less than 450 in 1980 to roughly 700 in 2001.<sup>92</sup> These grants are directed towards a huge range of activities such as education, healthcare, transportation, housing and more.

To be sure, these grants are an imposition of federal priorities on state and local government.<sup>93</sup> But are they an economically efficient way to manage homeland security spending?<sup>94</sup>

Numerous reports have pointed at the complexity and redundancy in the federal grant industry as well as at the mismanagement, fraud and abuse of federal funds. The GAO notes “GAO’s work has been pointing out the chronic problems of federal grants since at least 1975.”<sup>95</sup>

And in spite of GAO recommendations and occasional reforms, the same problems remain. So although the initial goal of grant programs might be a high-minded purpose—such as help for poorer regions or homeland security—they frequently have turned out to be an extremely ineffective way to achieve a policy goal.

The unsatisfactory performance of federal grant programs has been repeatedly reported. Indeed, the Office of Management and Budget regularly points out that grant programs have poorer performance, on average, than other federal programs.<sup>96</sup> These grants often come within the frame of one-size-fits all federal regulation, which reduces States' incentive to be innovative.

This abundant literature serves as evidence that federal grants and funds to states are a wasteful way of providing government services to Americans. There is no reason to believe that it will suddenly become an effective way to enhance America's homeland security. In addition to the problems underlined in the previous section, GAO reports that homeland security grants are already following the same troubling pattern of other federal grants.<sup>97</sup> First, the amount of homeland security funds transferred to lower level governments is growing at an impressive rate. Homeland security funds—which included grants from DHS, DOJ and HHS—handed down to the states increased from \$2.7 billion in FY2001 to a proposed \$5.5 billion in FY2005.<sup>98</sup> In FY2003, a total of \$8 billion was paid to state and local governments to finance homeland security activities.

Second, excessive complexity and duplication in the federal homeland security grant industry is already quite evident. For instance, GAO describes the extreme complexity and fragmentation of the major federal homeland security assistance programs targeted to first responders.<sup>99</sup> Some grants go to state emergency management agencies, some go to state fire marshals, some go directly to local first responders and some go to the cities. Some grants are paid by DHS through the Office of Domestic Preparedness and/or through FEMA, some are paid by the Department of Justice through the Office of Justice Programs and/or through the Office of Community Policing Services and others are paid by the Department of Health and Human Services through the CDC and/or through the health Resources and Service Administration. Finally, there at least 16 overlapping grant programs for local first responders such as firefighters and local law enforcement – highlighting the problem of duplication in the federal grant program.<sup>100</sup>

And like other grant programs, homeland security grants have spurred much wasteful lobbying activity.<sup>101</sup> Edwards (2004) reports “On March 4<sup>th</sup> 2004, 3,000 officials flew into Washington to lobby Congress for larger first responder grants; they were followed on March 16 by firefighters from across the country coming to lobby Congress.”<sup>102</sup> Other officials are coming to complain about the level of grants they are getting compared to others and asking for a level playing field.

And yet, when Senator Nickles asked Homeland Secretary Ridge in February this year, “these [first responder] funds, correct me if I am wrong, these funds really aren't supposed to be a subsidy for local police and fire, is that correct?” Secretary Ridge replied without blinking “That's correct.”<sup>103</sup>

According to security expert Bruce Schneier “critical to any security decision is this notion of trade-offs, meaning the cost—in terms of money, convenience, comfort, freedoms and so on—that inevitably attached themselves to any security system.” He adds “better understanding of trade-offs leads to a better understanding of security decisions.”<sup>104</sup> A recurring recommendation from the GAO over the years has been the need to use risk management as an important element in developing a national strategy to fight terrorism.<sup>105</sup>

Risk management is about playing the odds. It is figuring out which attacks are worth worrying about and spending money on and which are better left ignored. It is spending more resources on the serious attacks—defined as being very likely or if successful having devastating effects—and spending less on the trivial ones. It is taking a finite security budget and making the best use of it. In other words, homeland security should be about wise choices, not just increased spending.

Risk management is also about figuring out who is the best player suited to address a given risk. At the federal level, homeland security should be about preventing adverse consequences from the intentional and unwarranted actions of others. In that sense, federal homeland security grants are not making us more secure. The grant programs—especially the first responder grants—are predicated on the notion of cleaning up after terrorists successfully attack. This is a huge waste of our scarce federal resources. Cox (2003) notes, “The mission of the Department of Homeland Security must be first and foremost to prevent another deadly attack on the United States.”<sup>106</sup> And he adds “A dollar spent on preventing the next terror attack is vastly superior to spending dollars on cleaning up the mess when we fail to do job one, which is preventing terrorism.”<sup>107</sup>

Homeland security should be based on the investigation, interdiction and elimination of terrorist threats. The \$5.5 billion going to states and local governments would be best spent on bolstering the ability of federal law enforcement and intelligence services to achieve these goals instead of subsidizing local fire stations throughout the country.

It does not mean that investing money on first responders is not important. However, states and local communities should be in charge of most of their preparedness efforts. If police officers feel they need more equipment to do their job, or firefighters need training they are not getting right now, they should turn to their state and local officials for funding.

More importantly, leaving the responsibility for developing proper first responder policies to the states makes much sense. Federalizing first responder programs accentuates the public choice problem that already plagues the political process. When first responder programs are funded at the federal level, a Congressman from Wyoming has no incentive admitting that his state is not a likely target or that if it ever were a target, the level of damages would be limited. This same Congressman has no incentive to turn down federal money, and even less incentive to volunteer sending his state taxpayer’s dollars to benefit other states. By contrast, when first responder programs are states’ responsibility, then this same Wyoming Congressman in theory should have a stronger incentive to assess risk and potential damages to his state accurately. He should have an incentive to decide whether to spend more on homeland security or on other accounts.

It does not mean that local communities would never have any claim to federal funds. But these funds should be accessed only when needed in case of an emergency, in the same way that FEMA funds can be accessed following a natural disaster.<sup>108</sup> But implementing this system should not be an excuse to federalize the cost of state and local responsibilities.

Economics and public choice theory suggest a natural organization that appears to have eluded lawmakers so far. Not every jurisdiction needs a bomb squad. What every jurisdiction needs is to know where they can get a bomb squad if they need one, and/or where to ask if they need to find a bomb squad. Today, it is incredibly easy and fast for a team of specialized responders to fly from one state to another and to help the state in distress. After September 11<sup>th</sup>, individuals, firefighters, police officers and many others all over the country mobilized to help New York and Washington. And that would happen again.

## VIII. Homeland Security and Special Interests

The evidence suggests that homeland security grants to state and local governments are at times wasted. Accordingly, reform of this system is a worthy priority. A first step in that direction would be to eschew the requirement that every state get part of the homeland security money. Congress, however, appears to be moving in the opposite direction. For example, instead of reforming the way money is distributed to states, a new program called the Urban Area Security Initiative Grants has just been created.

In theory the Urban Area Security Initiative Grant program is designed to allocate the money based on an evaluation of risks.<sup>109</sup> The three principle criteria used are population density (half of the weight), presence of critical infrastructure (one third), and presence of a credible threat (about 1/6 of the weight). Early 2003, Congress announced that it would pay a total \$100 million grant to seven cities—New York, Washington, Los Angeles, Seattle, Chicago, San Francisco, and Houston—that had made the “high threat list.”

Secretary Ridge and Members of Congress, however, immediately started receiving calls from city officials who felt they had been unfairly left out. As a result, the list of qualifying cities started to expand considerably. In May of 2003, the number of most-at-risk cities had grown from 7 to 30.<sup>110</sup> In a few months, the pool of money had increased from \$100 million to \$700 million.<sup>111</sup> Then in 2004, the Department of Homeland Security announced an even longer list of 50 cities, including Indianapolis, Louisville, Columbus, and Fresno and a budget of \$625 million.<sup>112</sup> In FY2004, each of these cities will receive respectively \$10 million, \$9 million, \$8.7 million, and \$7 million on top on the minimum guaranteed from the grants to first responders.<sup>113</sup>

Aware of this issue, House Homeland Security Committee Chairman Cox is currently promoting legislation, HR3266, the "Faster and Smarter Funding for First Responders Act of 2004" that would authorize the Secretary of the Department of Homeland Security (DHS) to change the criteria used to distribute funding to DHS' major programs in order to base grants to state and local governments primarily based on the risk of terrorist attacks and the magnitude of potential damages—not population.<sup>114</sup> However, the strong oppositions in the Senate may impede this reform. Senator Leahy (D-VT), member of the powerful Homeland Security Appropriations Subcommittee, for instance, has argued that dropping the all-state minimum formula would “shortchange rural states.”<sup>115</sup> And according to some Senate aides, because of the attractiveness of spending discretion, “the Cox bill is going no where.”<sup>116</sup>

The good news is that the House version of intelligence reform legislation (HR10) includes language, which originated in the House Selected Committee on Homeland Security, changing the funding formula to base homeland security grants on risk assessment. If that language survives a House-Senate conference, it will be an important step in the right direction and a serious improvement of how we are spending homeland security funds to protect our nation. However, it probably won't go through without serious resistances since the Senate version of the intelligence reform legislation does include such strong provisions and it is unlikely that Congress will meet to straighten their differences after the elections.

A surprising endorsement of the intelligence bill's risk or threat based model however just came from seventeen fire and police organizations. In a letter to Rep. Peter Hoekstra (R-Mich), chairman of the congressional conference committee, they wrote “We believe that the funds should be distributed based on a risk or threat-based model.”<sup>117</sup> They even went further

than the House version of the intelligence bill (HR10) under which each state would receive at least 0.25 percent of the total grant pool (versus 0.75 percent with the current formula). They note that “To the extent that state minimums are included, we urge that the minimums be kept low, in order to provide maximum funding to areas of greatest need.”<sup>118</sup> Yet, again the victory logic over state dependency seems rather unlikely due to the extreme resistance the idea is receiving.

Finally, even if the concept of allocating homeland security funds based on risk assessment is finally endorsed and adopted, many state officials believe that the process of assessing these terrorist threats and risks, even with ongoing guidance from DHS, will remain a very flawed procedure due to the subjective interpretations. Based on previous experiences, DHS officials already acknowledge that the 50 states ‘terrorists risk assessments usually fall short of being objective.’<sup>119</sup> Moreover, the economic incentive does not seem to favor a proper evaluation of those risks. Financial stakes are high for state officials who might feel that if their state is seen as a non-risk state, no money would be coming their way.

Confirming this intuition is the fact that shortly after the creation of DHS in March 2003, the 50 state governments were asked to initiate terrorist threat risk assessments by identifying critical assets and people or groups within their states that posed a terrorist threat. The assessments were due in early 2004. According to David Miller, Iowa’s homeland security administrator, because of the amount of money at stake “some leaders felt they ought to list at least one threat for their region, even if it was just a risk of terrorist passing through the area.”<sup>120</sup>

To be sure, all levels of government contain some amount of inefficient or wasteful spending. The criteria used to identify such wasteful appropriations are the following ones: 1. the appropriation is not properly authorized by the House and/or the Senate and was not requested by the administration, 2. the appropriation is unauthorized and unrequested, has locality-specific or has facility-specific earmarks including those funds above the administration request, 3. the appropriation involves the transfer or disposal of federal property or items under terms that circumvent existing law and 4. new items added in conference that were never considered in either bill in either the House or the Senate.<sup>121</sup>

According to Citizens Against Government Waste (2004), in FY 2003 Congress added a record level of \$22.5 billion in wasteful spending.<sup>122</sup> The Republican leadership this year is no different, with 8,000 pork items attached to the February Omnibus bill.<sup>123</sup>

And it is now obvious that rather than curbing lawmakers’ appetite for home state earmarks, the surge in emergency spending to strengthen “homeland security” and bolster the Pentagon budget provides ample opportunities for lawmakers to direct such funds to their districts and states. Federal coffers are wide open to fight terrorism, and lawmakers can hardly be faulted for pushing projects aimed at protecting their constituents. As a result, in spite of promises by appropriators to pass a pork-free homeland security bill, the fiscal 2004 Homeland Security bill is laden with earmark projects.<sup>124</sup>

Some of the pork items in the FY2004 Homeland Security bill are:

\$2,000,000 to the Great Lakes Region to purchase an Icebreaker so that commercial ships can go through during the winter time.

\$200,000 to project Alert, a school-based drug prevention program for middle grade youth.

\$7,100,000 for forensic support and grants to the National Center for Missing and Exploited Children.

\$100,000 to the Child Pornography Tipline

\$3,000,000 to Child Labor Enforcement

\$10,000,000 to Intercity Bus Security to improve security for operators and passengers by providing bus security enhancements and training to bus companies and others.

\$22,000,000 to trucking industry security program to promote security awareness among all segments of the commercial motor carriers and transportation community.

\$19,250,000 to be split between Mobile Alabama, Burlington Iowa, LaCrosse Wisconsin, Chelsea Massachusetts, New Orleans Louisiana, Morris Illinois and Charleston, South Carolina for alteration of bridges.

\$2.5 billion for “highway security,” which consists of building and improving roads.

\$70,000,000 for the Homeland Security Fellowship Program for students and universities.

\$50,000,000 to the National Exercise Program to provide an exercise program that meets the intent of the Oil Pollution Act of 1990.

\$38 million to fully cover all remaining fire claims from the Cerro Grande Fire in New Mexico

\$20,000,000 added by the Senate for the renovation of Nebraska Avenue Headquarters of the Department of Homeland Security.

\$6,400,000 for the Intellectual Property Rights Center. The center’s focus is to combat intellectual property right crime—a long time FBI project.

\$500,000 to Kentucky Morehead State University Institute for regional Analysis and Public Policy for a homeland security program

\$60,000,000 to the Urban Search and Rescue Team to structure local emergency services personnel into integrated disaster response task forces.

CAGW (2004) counted 18 wasteful items amounting to \$423 million in the 2004 Department of Homeland Security bill.<sup>125</sup> And this year is no different than last year. In fact, it is even more pronounced as \$896 million were added over the President’s request to the FY2005 homeland security funding bill.<sup>126</sup>

During the debate that preceded Congress and the Senate’s adoption of fiscal 2005 Homeland Security appropriations bill, lawmakers showed an extremely high level of regional concern reflecting a change from last year, when they vowed to keep the bill clean of earmarks. First, countless attempts were made to use the bill as a vehicle for large packages of emergency hurricane and drought aid. Senator Leahy (D-Vt) championed an outsourcing ban saying that “it would save the jobs of a 100 Vermonters.”<sup>127</sup> Thankfully, Republicans managed to block Senator Lautenberg (D-NJ) from adding another \$100 million for fishing enforcement and Coast Guard rescue operations. In the end, Senate leaders stopped Senate Democrats from adding more than \$20 billion to the \$33 billion FY2005 Homeland Security spending bill.

Sadly, Senators Max Baucus (D-Mont.) and Conrad Burns (R-Mont.) managed to attach \$2.9 billion—accounting for nearly 10 percent of the bill’s total cost—to the FY2005 Homeland Security bill in so-called disaster aid for farm states. Another \$700 million in hurricane aid for Florida farmers was added and then later removed. Drought relief or hurricane relief have nothing to do with homeland security and should not be presented as having anything to do with the essential task of defending the homeland from terrorists.

Finally, Senator Pete V. Domenici (R-NM) obtained an increased spending of \$20 million for the National Infrastructure Simulation and Analysis Center, collaboration between Sandia and Los Alamos national laboratories in his own state.<sup>128</sup>

To conclude, if we add to that figure the reported \$1.8 billion spent wastefully by state and local government, it means that billions, which could have been spent on worthy security, were not.<sup>129</sup>

## **VIII. The Transportation Security Administration: Fighting Yesterday's Battles**

One of the major shortcomings that led to the 9/11 tragedies was that the responsibility for protecting commercial airlines was left to the government, the FAA, the FBI, the CIA, and the INS. They failed. By contrast, reinforcing cockpit doors would have most likely prevented most of the deaths that occurred on that fateful day.

Scheiner (2003) explains how government involvement in airplane safety and treaties to limit the amount of damages airlines would have to pay to families of international airplane crash victims artificially changed the economics of airplane safety.<sup>130</sup> A direct consequence was that it made sense for airlines to resist improvements in airplane safety since the cost of safety failures was reduced drastically.

Yet, in spite of past failures, the government's response to 9/11 was to federalize the security screeners and authorize the military to shoot down airliners if they are hijacked. After the terrorist attacks in 2001, Congress rushed into existence a new antiterrorism agency to protect America's planes, trains and trucks. The legislation (The Aviation and Transportation Security Act) was meant to enable the federal government to take over screening of passengers and baggage at all but 5 of the 429 U.S. commercial airports. The five airports are San Francisco, Kansas City, Rochester, N.Y., Jackson Hole, Wyo., and Tupelo, Miss. The Transportation Security Administration was born and it is now part of the Department of Homeland Security.

Three years after the federal takeover of airport passenger screening, the 45,000-employee bureaucracy has been inundated with complaints about its performance. According to GAO, the federalized system has proven to be very ineffective at providing quality airport screening. Their diagnosis is that TSA is unresponsive and bureaucratic. And DHS just released the results of a four-month audit that showed that passenger screening by the TSA needs to be improved to keep explosives and weapons off commercial aircraft.<sup>131</sup> According to the Congressional Quarterly, the report published Wednesday September 22<sup>nd</sup> is a sanitized version of the full report, which details the nature and number of the screening failures. The full report remains classified.

This is no trivial matter considering the amount of money allocated to TSA. TSA's budget increased from \$1.35 billion in FY2002 to \$5.3 billion requested in FY2005.<sup>132</sup> Its budget now exceeds that of the FBI. And although Congress originally charged the agency with protecting all modes of transportation, it has done little beyond aviation. In fact, over 95 percent of TSA's budget requested for FY2005 is devoted to air transport.<sup>133</sup> Also, in effect TSA is only responsible for passenger and baggage screening. The airports are still responsible for securing the other crucial parts of the airport. It appears therefore, that TSA provides only a small portion of air transport security, yet still complains of under funding.<sup>134</sup>

However, the true cost of TSA to taxpayers goes way beyond the expected \$5.3 billion it will cost in FY2005. Sound homeland security requires investing in activities to make America more secure without hindering economic growth. The lack of staffing flexibility in TSA, for instance, imposes a tremendous and unjustified cost to airports. The airline business is an

extremely competitive industry, with airlines adding and dropping airports on short notice. Since passenger and baggage screening workforces affect all passengers, the impact on passenger processing of improperly sized screening workforces is incredibly costly and constitutes a significant drag on the economy.<sup>135</sup> A quick back of the envelop calculation suggests that if 624 million passengers spend 2 hours waiting in line—which is the estimate given by the ATA—the aggregate opportunity cost incurred is roughly \$4 billion per year. This number is to be added to the actual cost of TSA itself.

In addition, many security experts have argued that TSA’s mandate is not pointed at the right target. Schneiner (2002) explains that “The federal government and the airlines are spending millions of dollars on systems that screen every passenger to keep knives and weapons out of planes, but what matters most is keeping dangerous passengers out of airline cockpits which can be accomplished by reinforcing the doors.”<sup>136</sup>

House Aviation Subcommittee Chairman Mica (R-FL), who was never comfortable with creating this new bureaucracy, has been a strong voice pointing to the poor performance by TSA.<sup>137</sup> Mica (2004) notes, “They look nice. They have a patch and a uniform, but my question is: how well do they detect threats?”<sup>138</sup> Now he has advocated the return of all airport security screener jobs to the private sector.<sup>139</sup> According to the law that created TSA, after three years with the new system, airport managers will be allowed to ask for private screeners who ultimately would be overseen by TSA. The airport industry has predicted that between 20 and 100 of the nation’s 445 commercial airports will ask to revert to using private screener companies when they have the chance this November.<sup>140</sup>

In spite of the evidence of TSA’s low performance, Democrats have already expressed their opposition to this idea and House Democrats say “they will stop even one from booting TSA’s workers.”<sup>141</sup> On July 22, Rep. Maloney of New York, who heads the House Democratic Task Force on Homeland Security and three Democratic co-sponsors introduced a bill (HR 4970) to repeal the opt-out provision.<sup>142</sup>

A GAO report comparing the performances of private screeners and public screeners explains that “TSA provided the screening contractors with little opportunity to demonstrate innovations, achieve efficiencies, and implement initiatives that go beyond the minimum requirements of the Aviation and Transportation Act [...] TSA has allowed them to implement some airport specific practices.”<sup>143</sup> As a result, GAO concludes, “These practices have enabled the screening contractors to achieve efficiencies that are not available at airports with federal screeners.”<sup>144</sup>

By contrast, in April 2004, Homeland Security Inspector General Ervin testified to the House Transportation and Infrastructure aviation subcommittee that U.S. airports with federal screeners and the few ones with private screeners do an equally poor job.<sup>145</sup> This observation however, does not serve as an endorsement of public screeners. Indeed, when private security screeners do a poor job, they can be fired and the system can be reformed or terminated. Besides, according to a new report by the department of Homeland Security inspector general, poor oversight by TSA in the four pilot programs is probably to blame for the poor performances of the private contractors.<sup>146</sup> The report notes that TSA’s involvement limits contractors’ ability to improve their program.

According to Robert Poole, Director of Transportation Studies at the Reason Public Policy Institute, “Global experience in combating terrorism, particularly in Europe and Israel, has clearly demonstrated that the best approach to aviation security relies on private-sector security companies that are held to the highest performance standards but have the flexibility to

innovate.”<sup>147</sup> He adds, “International experience has also demonstrated the superiority of a system that directs resources, technology and scrutiny to individuals that represent the greatest risks.”<sup>148</sup> Yet Congress put in place a system that does exactly the opposite.

This is more troubling, when considering that some homeland security programs appear to be properly designed to assess and concentrate on high-risk elements. For instance, the U.S. government has contracted—after a truly competitive process—with the defense contractor TRW to devise methodologies for best-practice vulnerability assessments in ports.<sup>149</sup> Part of the Maritime Transportation Security Act (MTSA) of 2002 requires ports to perform their own risk assessments.<sup>150</sup> Almost all the \$200M the federal government spent on port security in 2002 and 2003 was to finance these individual risk assessments. Of course, the results were spotty and some of the assessments were questionable. Yet as a whole, the dollar amounts is small and constitutes a step in the right direction since it set the stage for more-thoughtful assessments to come.

But the most impressive program in homeland security activities seems to be the highly leveraged government initiative called Trusted Shipper. Here, the onus is on the private sector to verify the bona fides of the shippers in advance of their cargo arriving in U.S. ports. This program relies on the common-sense fact that most terrorists would find it very difficult to impersonate a well-established company. Of course, the most likely reason the government turned to Trusted Shipper was because it was going to be physically impossible to screen all cargo—they will end up screening 2 percent of boats that were identified as high-risk vessels—so they were forced to be reasonable.

To conclude, unlike these programs—which remain imperfect—TSA is poorly leveraged. And TSA does not make us safer. Moreover, the obvious lack of trade-offs between spending and efficiency would actually make us less secure. Congress should follow Chairman Mica’s advice and return all screener jobs to the private sector. The federal screeners could get the first opportunity to apply to the private jobs. There is no doubt that the \$5.3 billion would be better spent on tracking down and wiping out the terrorists than on TSA.

## **IX. Lack of Trade-Offs in the Budget Compromises Security**

Between FY2001 and FY2005, the administration expects total outlays to rise from \$1,864 billion to \$2,423 billion—a 30 percent increase.<sup>151</sup> The Bush administration has followed a remarkably irresponsible course by requesting many spending increases often in the name of security but rarely asking for cuts to programs or agencies. As for Congress, most members are blaming the overall spending increases on post-9/11 national security costs and few talk about eliminating unneeded government programs to fund this added protection money. No trade-offs are being made in the budget, as evinced by the fact that non-defense spending has increased by 42 percent in four years.<sup>152</sup>

While the Pentagon’s budget grew by 46 percent in the last four years (that figure does not include the \$25 billion requested by the White House in May this year for Operations in Iraq), nondefense related department budgets have also ballooned. The Department of Education budget has grown rapidly under President Bush. Education outlays increased from \$36 billion in FY2001 to an estimated \$64 billion in FY2005, an 80 percent increase.<sup>153</sup> This is remarkable considering that the GOP presidential platform in 1996 stated: “The federal government has no constitutional authority to be involved in school curricula . . . this is why we will abolish the

Department of Education.”<sup>154</sup> The Bush administration has argued that new spending was a necessary price to get education reforms through Congress. The final No Child Left Behind legislation of 2002 boosted spending but was stripped of most real reforms.

Farm programs are also ballooning under a Republican White House and Congress—some of them under the homeland security label. In the last four years, funding for the Department of Agriculture will grow at least 20 percent.<sup>155</sup> The farm bill signed into law by President Bush in 2002 represented a reversal of the Republican 1996 Freedom to Farm Act, which aimed to wean farmers off federal price supports and subsidies.<sup>156</sup> Republicans have turned their back on their own farm reforms with the embrace of price supports and higher farm subsidies.

In theory, the tragic events of September 11<sup>th</sup> should have made security the U.S.’s budgetary priority, but the more spent on non-security activities, the less there is available for productive homeland security spending.

The record of almost continual growth in most departments over the years raises concerns about the newly created Department of Homeland Security. In FY2004, the department’s budget was \$36.1 billion.<sup>157</sup> The White House had claimed that the department would not cost any additional money because it was to consolidate activities already carried out in nine other departments.<sup>158</sup> However, spending for DHS keeps rising with no indications of actual cost savings.

According to the 9/11 commission’s recently released 600-page report, our government bureaucracy failed us. It seems legitimate to ask why not get rid of some of it instead of adding to it? At the very least, if the White House and Congress want more security spending, they should find serious savings elsewhere in the budget.

## **X. Conclusion**

In the largest open society in the world, improving homeland security is a challenging task. Among other vulnerable targets, the United States has thousands of miles of borders, thousands of bridges, sports stadiums and shopping malls, hundreds of skyscrapers and power plants. Certainly, the attacks on Washington DC and New York have put immense pressure on the Administration and Congress to show that security against future attacks is being enhanced.

A common path to bad security is knee jerk reaction to the news of the day. Sadly, too much of the U.S. government’s response post 9/11 seems to be exactly that. We have been told that we are in graver danger than ever and that in order to be secure, homeland security spending needed to increase drastically. And it was increased: by roughly 200 percent since FY2001. Yet, because most of the money is allocated on a political basis rather than a sound cost benefit analysis, much of the new spending will not result in sound security. In other words, the security we are getting against terrorism is likely to be ineffective, yet comes at an enormous expense.

By definition, the purpose of homeland security is to make America safer. As such, wasteful spending and grants to state and local governments do not achieve that goal. In the same way, the federalization of law enforcement and airport security screeners appear to be ineffective ways to address our homeland security problem. In some cases, they might increase our feeling of security but in reality they might even make us less safe.

Economics suggests the following: spending decisions should be based on a true cost benefit analyses. It also underlines the need to more formally deliberate what level of

government is the best suited to make homeland security investments taking under considerations the public choice ramifications of the alternatives. And finally, it requires paying particular attentions to pork barrel spending and sanctioning it.

That will be a good start. The challenge of determining what the best security investments are will remain and should be left to security experts rather than politicians. Governments, by nature, are very inefficient institutions. We must accept this as fact. So instead of thinking that the solution to 9/11 is more and more of the same approaches that failed us, policymakers should start doing the analysis needed and making the tradeoffs as to where we should focus our limited security resources.

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<sup>1</sup> Author's calculation based on Office of Management and Budget, Budget of the Government and Mid-Session review for FY2005, (Washington: Government printing Office, July 2004).

<sup>2</sup> Author's calculation based on *The Budget of the United States Government, Fiscal year 2005*, Table S-6, (Washington: Government printing Office, February 2004).

<sup>3</sup> Author's calculation based on *The Budget of the United States Government, Fiscal year 2005*, Historical Tables and Congressional Budget Office, *Budget and Economic Outlook: An Update*, Table 1-2, September 2004.

<sup>4</sup> Author's calculation based on Office of Management and Budget, Budget of the Government and Mid-Session review for FY2005. Also, see Veronique de Rugy, "The Republican Spending Explosion," Cato Institute Briefing Paper no. 87, March 3, 2004.

<sup>5</sup> For a good discussion about the concept of tradeoffs see James Buchanan, *Cost and Choice, An Inquiry in Economic Theory*, Collected Works of James Buchanan Volume 6, (Indianapolis: Liberty Fund).

<sup>6</sup> Center For Disease Control, <http://www.cdc.gov/nchs/datawh/statab/unpubd/mortabs.htm>

<sup>7</sup> Department of Transportation's Safe, Accountable, Flexible and Efficient Transportation Equity Act of 2003 (SAFETEA), authorizes funds for Federal-aid highways, including highway safety programs. The numbers are compiled from <http://www.fhwa.dot.gov/reauthorization/safetkeyinfo.htm#ast>. And *Budget of the United States, FY2005*, Table S-6.

<sup>8</sup> The difficulty of estimating low probability risks is stressed by Kunreuther et al. (1978).

<sup>9</sup> There is a recent but large literature on Insurance and terrorism risk in the wake of September 11<sup>th</sup>. See for instance, Jeffrey R. Brown, Randall S. Kroszner, Brian H. Jenn (2002), "Federal Terrorism Risk Insurance," NBER Working Paper No. w9271 Issued in October, Gordon Woo (2003), "Insuring Against Al Qaeda: Risk Management Solutions," NBER Meeting and Howard Kunreuther, Erwan Michael-Kerjan and Beverly Porter (2003), Assessing, Managing and Financing Extreme Events: Dealing with Terrorism," NBER Working Paper No. 10179.

<sup>10</sup> The role of media attention is discussed in Fischhoff et al. (1981).

<sup>11</sup> W. Kip Viscusi and Richard J. Zeckhauser, "Sacrificing Civil Liberty to Reduce Terrorism Risks," John F. Kennedy School of Government Harvard University, Faculty Research Working paper RWP03-017, January 2003.

<sup>12</sup> Manuel Trajtenberg, "Defense R&D in the Anti-Terrorist Era," NBER Working Paper No. 9725, May 2003.

<sup>13</sup> Becker, Gary. "Crime and punishment: An economic approach," *Journal of Political Economic*, 1968.

<sup>14</sup> See John R. Lott Jr. (2001), *The Bias Against Gun: Why Almost Everything You Have Heard About Gun Control is Wrong*, (Washington DC: Regnery Publishing, Inc), Chapter 6. Lott tests the economic model (that if you make something more difficult or increase the cost of being caught for doing something people do less of it) on perpetrators of multiple victim public killers. He finds that in this case, although legal sanctions such as higher death penalty execution rates should imply both fewer attacks and fewer people harmed, it is less of a significant factor in deterring multiple victim killings than it is in deterring normal murders. Also See Frey et al (2003)

<sup>15</sup> John R. Lott Jr. (2004), "Pilots Still Unarmed," *New York Post*, January 6, 2004.

<sup>16</sup> See Lott (2004).

<sup>17</sup> John R. Lott Jr. (2004), "Marshals are Good But Armed Pilots are Better," *Wall Street Journal Europe*, Friday January 2<sup>nd</sup>.

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<sup>18</sup> For a complete explanation of the cost effectiveness of reinforced cockpit doors in airplanes see Bruce Schneier, *Beyond Fear: Thinking Sensibly About Security in an Uncertain World*, (New York: Copernicus Books, 2003), p. 46. Other experts have raised the fact that some engineering constraints in the wall and the hinges where the doors are hanged might reduce the effectiveness of these doors. See Lott (2004), "Pilots Still Unarmed." Yet, it still seems that a very cost effective measure.

<sup>19</sup> Federal Aviation Administration, "Airlines Meet FAA's Hardened Cockpit Door Deadline," Press release, April 2003.

<sup>20</sup> Ibid.

<sup>21</sup> Department of Homeland Security, Budget in Brief, FY2005, p. 14.

<sup>22</sup> In Bruce Schneider (2003), makes this point using the data compiled by Wm. Robert Johnson and published in the "Worst Terrorist Strikes U.S. and Worldwide." 12 out of 25 of the deadliest terrorist strikes of the last 80 years are airline related. 10 out of these 12 involve crashing of an hijacked plane.

<sup>23</sup> For a good discussion on the economic costs of terrorism see S. Brock Blomberg, Gregory D. Hess and Athanasios Orphanides, "The Macroeconomic Consequences of Terrorism," CESifo Working Paper No. 1151, March 2004.

<sup>24</sup> Joint Economic Committee, "The Economic Cost of Terrorism," May 2002, p. 7.

<sup>25</sup> See for example Gold (1999) for a good review of the literature and a discussion of defense as a public good.

<sup>26</sup> There is however a strong case to be made that even defense could be better provided by the private sector.

<sup>27</sup> Of course, saying that some areas of homeland security have public features and should probably be provided by the government does not exclude the possibility of inefficient and wasteful provision of that good.

<sup>28</sup> An argument in favor of federalization of these investments is that because investing in protection is likely to displace a terror attack, the private sector or local and state governments might have an incentive to overspend on homeland security.

<sup>29</sup> Bruce Schneier, *Beyond Fear: Thinking Sensibly About Security in an Uncertain World*, (New York: Copernicus Books, 2003), p. 33.

<sup>30</sup> See James Buchanan and Gordon Tullock (1962), *The Calculus of Consent*, University of Michigan Press, Ann Harbor.

<sup>31</sup> James Buchanan, *Cost and Choice, An Inquiry in Economic Theory*, Collected Works of James Buchanan Volume 6, (Indianapolis: Liberty Fund).

<sup>32</sup> For a discussion about the economics of interest groups see Mancur Olson (1982), 'The logic', in *The Rise and Decline of Nations: Economic Growth, Stagflation, and Social Rigidities*, New Haven: Yale University Press, p. 17-35. Also see George J. Stigler (1974), 'Free Riders and Collective Action: An Appendix to Theories of Economic Regulation', *Bell Journal of Economics and Management Science*, 5 (2), p. 359-65. Gary S. Becker (1983), 'Theory of Competition Among Pressure Groups for Political Influence', *Quarterly Journal of Economics*, XCVIII (3), August, p. 371-400. For a good description of the theory of rent seeking see Gordon Tullock (1967), 'The Welfare Costs of Tariffs, Monopolies, and Theft', *Western Economics Journal*, V, p. 224-32 and Robert Tollison (1982), 'Rent Thinking: A Survey', *Kylos*, 35 (4), p. 575-601.

<sup>33</sup> For discussion about the dynamic of pressure groups see Becker, G. (1983), "A Theory of Competition among Interest Groups for Political Influence," *Quarterly Journal of Economics* 98, 371-400 and Becker, G. and C. Mulligan (1998), "Deadweight Costs and the Size of Government," NBER Working Paper 6789.

<sup>34</sup> For a discussion on pork Barrel Spending see for example Acemoglu, D. and J. Robinson (2001), "Inefficient Redistribution," *American Political Science Review* 95, 649-61 and Baron, D. (1991), "Majoritarian Incentives, Pork Barrel Programs, and Procedural Control," *American Journal of Political Science* 35, 57-90. See also Coate, S. and S. Morris (1995), "On the Form of transfers to Special Interests," *Journal of Political Economy* 103, 1210-35 and Shepsle, K. and B. Weingast, (1981), "Political Preferences for the Pork Barrel: A Generalization," *American Journal of Political Science* 25, 96-112.

<sup>35</sup> Grossman, G. M. and E. Helpman (1994), "Protection for Sale," *American Economic Review* 84, 833-50.

<sup>36</sup> Timothy Besley and Stephen Coate (1999), "Centralized Versus Decentralized Provision of Local Public Good: A Political Economy Analysis," NBER Working Paper No. 7084.

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<sup>37</sup> See also, Stephen Coate (1997), "Distributive Policy Making as a Source of Inefficiency in Representative Democracies," Institute of Economic Research, University of Pennsylvania, Working Paper No. 97-041.

<sup>38</sup> Mickey McCarter, "Bush Signs Homeland Security Appropriations Bill," Congressional Quarterly, October 18, 2005.

<sup>39</sup> Department of Homeland Security, Budget in Brief, FY2005, p. 3.

<sup>40</sup> Department of Homeland Security, Budget in Brief, FY2005, p. 3.

<sup>41</sup> Author's calculation based on *The Budget of the United States Government, FY2005*, Table S-6.

<sup>42</sup> Most funding for homeland security is classified as discretionary spending and provided through appropriations. Mandatory spending finances some additional homeland security activities but at a much lower level (\$2 billion in FY 2004 and roughly the same for FY2005).

<sup>43</sup> *The Budget of the United States Government, FY2005*, Table S-6.

<sup>44</sup> For details about these programs see Environmental Protection Agency's web site,

<http://www.epa.gov/ordnhsr/>

<sup>45</sup> For details about these programs see <http://www.azonano.com/details.asp?ArticleID=302> and

<http://earth.nasa.gov/eseapps/theme9.htm>

<sup>46</sup> For more details about this program see

<http://www.homelandsecurity.org/journal/Interviews/displayInterview.asp?interview=5>

<sup>47</sup> For more details about USDA's homeland security activities see

<http://www.usda.gov/news/speeches/st28.htm>

<sup>48</sup> For details see <http://www.dhs.gov/dhspublic/display?theme=27&content=775>

<sup>49</sup> For detailed examples of selected agencies' mismanagements see Chris Edwards, "Downsizing the Federal Government," Cato Institute Policy Analysis no. 515, June 2, 2004.

<sup>50</sup> NASA, *Columbia Accident Investigation Board, Vol. 1* (Washington: NASA, August 2003) and GAO, "Space Station: Actions Underway to Manage Costs but Significant Challenges Remain," GAO-02-735, July 17, 2002 and GAO, "Compliance With Cost Limits," GAO-04-648R, April 2, 2004.

<sup>51</sup> GAO report cited in a Senate Committee on Government Affairs, Vol. 1, pp. 37-47 and GAO, "Major Management Challenges and Program Risks: Department of Energy," GAO-03-100, January 2003

<sup>52</sup> Michael Grunwald and Mike Allen, "Corps of Engineers' Civilian Chief Ousted," Washington Post, March 7, 2002, p. A1.

<sup>53</sup> Chris Edwards, "Downsizing the Federal Government," 2004, p. 18.

<sup>54</sup> GAO, "Fiscal Year 2003 U.S. Government Financial Statement: Sustained Improvement in Federal Financial Management is Crucial to Addressing our Nation's Future Fiscal Challenges," March 2004, GAO-04-477T, and GAO, "Major Management Challenges and Program Risks: Department of Defense," GAO-03-98, January 2003.

<sup>55</sup> GAO, "Major Management Challenges and Program Risks: Department of Commerce," GAO-03-97, January 2003 and GAO, "Major Management Challenges and Program Risks: U.S. Department of Agriculture," GAO-03-96, January 2003

<sup>56</sup> Alice Lipowicz, "Just in Time for Christmas: Homeland Security Department Gives \$150 Million to Poor for Food and Shelter," Congressional Quarterly, December 11, 2003. See also *Budget of the United States, Analytical Perspective*, FY2004.

<sup>57</sup> Martin Kady II, "Homeland Security Appropriations: Disaster Aid Finds a Place in Senate Bill, but Most Amendments Left Behind," Congressional Quarterly, September 14 2004.

<sup>58</sup> Data prior to FY2001 comes from Office of Management and Budget, "Securing the homeland, Strengthening the Nation," [http://www.whitehouse.gov/homeland/homeland\\_security\\_book.pdf](http://www.whitehouse.gov/homeland/homeland_security_book.pdf)

<sup>59</sup> Author's calculation based on Office of Management and Budget, Budget of the Government and Mid-Session review for FY2005, p.29.

<sup>60</sup> Department of Homeland Security, Budget in Brief Fiscal Year 2005, p 3.

<sup>61</sup> House Select Committee On Homeland Security, "An Analysis of First Responder Grant Funding," p. 2.

<sup>62</sup> The data on funding can be found in House Select Committee On Homeland Security, "An Analysis of First Responder Grant Funding," p. 25.

<sup>63</sup> In FY2003 the amount covered by the formula was \$2.066 billion. The \$15.5 million is calculated with the following formula:  $\$2.066.000 * 0.0075 = \$15.49$  million.

<sup>64</sup> Author's calculation based on data collected from The Office of Domestic Preparedness, FY2003, State Homeland Security Grant Program (SHSGP), part I,

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<http://www.ojp.usdoj.gov/odp/docs/ODPApplication.txt> and Part II

<http://www.ojp.usdoj.gov/odp/docs/fy03shsgp2.pdf>

<sup>65</sup> Amanda Ripley, "How We Got Homeland Security Wrong," Time Magazine, Monday March 22, 2004.

<sup>66</sup> The Insurance Services Office, "ISO continues to help you response to the Terrorism Insurance Act of 2002," May 2003. For more detailed information see [www.iso.com](http://www.iso.com).

<sup>67</sup> Author's calculation based The Office of Domestic Preparedness, FY2003, State Homeland Security Grant Program (SHSGP), part I, and Part II.

<sup>68</sup> Congressional Quarterly, "Republican Cox Delivers Remarks at McGraw-Hill Homeland Security Summit," June 4, 2004.

<sup>69</sup> House Select Committee On Homeland Security, "An Analysis of First Responder Grant Funding," p. 6.

<sup>70</sup> James Jay Carafano, "Homeland Security Dollars and Sense #1: Current Spending Formulas Waste Aid to States," 2004.

<sup>71</sup> This is not surprising considering that as until recently the planning to spend the grant often occurs after the grants are actually received.

<sup>72</sup> Congressional Quarterly, "Transcript of Senate Budget Committee Hearing on FY2005 Homeland Security Department Budget," February 25, 2004.

<sup>73</sup> House Select Committee On Homeland Security, "An Analysis of First Responder Grant Funding," p. 7.

<sup>74</sup> Ibid, p. 7.

<sup>75</sup> Ibid, p. 8.

<sup>76</sup> Kate O'Beirne, "Introducing Pork-Barrel Homeland Security," National Review, Monday September 8, 2003.

<sup>77</sup> Ibid.

<sup>78</sup> Jo Becker, Sarah Cohen and Spencer S. Hsu, "Anti-terrorism Funds Buy Wide Array of Pet Projects; Some of Region's Unused Million Could be Lost," The Washington Post, A Section; A01, November 23, 2003.

<sup>79</sup> Mimi Hall, "Homeland Security Money Doesn't Match Terror Threat, USA Today, Wednesday October 29, 2003.

<sup>80</sup> Ibid.

<sup>81</sup> Alice Lipowicz, "For Michigan Volunteers, Free Training Course Proves Too Expensive," Congressional Quarterly, March 11, 2004.

<sup>82</sup> Mimi Hall, "Anti-terror Funding Questined," USA Today, First Edition Section, News, Monday July 14, 2003, p. 3A.

<sup>83</sup> Alice Lipowicz, "North Pole Receives Homeland Security Funds," Congressional Quarterly, October 22, 2002.

<sup>84</sup> Congressional Quarterly, "Transcript of Senate Budget Committee Hearing on FY2005 Homeland Security Department Budget," February 25, 2004, p. 7.

<sup>85</sup> Congressional Quarterly, "Transcript of Senate Budget Committee Hearing on FY2005 Homeland Security Department Budget," February 25, 2004.

<sup>86</sup> Jo Becker, Sarah Cohen and Spencer S. Hsu, "Anti-terrorism Funds Buy Wide Array of Pet Projects; Some of Region's Unused Million Could be Lost."

<sup>87</sup> Ibid.

<sup>88</sup> House Select Committee On Homeland Security, "An Analysis of First Responder Grant Funding," p. 9.

<sup>89</sup> Department of Homeland Security, Budget in Brief, Fiscal Year 2005, p 10.

<sup>90</sup> For a brief history of the federal grant system see Congressional Research Service, "Federal Grants to State and Local Governments: A Brief History," Library of Congress, February 19, 2003. Also see General Accounting Office, "Federal Assistance: Grant System continues To Be Highly Fragmented," United States Accounting Office, GAO-03-718T, April 29, 2003.

<sup>91</sup> *The Budget of the United States Government, FY2005, Analytical Perspectives*, p. 113.

<sup>92</sup> GAO-03-718T, p. 4.

<sup>93</sup> For a comprehensive criticism of the Federal Grant Programs see Chris Edwards, "Downsizing the Federal Government," Cato Institute Policy Analysis no. 515, June 2, 2004.

<sup>94</sup> For an excellent discussion about federalism see Michael Greve, "Big Government Federalism," Federalist Outlook No. 3, March 1<sup>st</sup>, 2001.

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<sup>95</sup> GAO-03-718T, p. 6.

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- <sup>96</sup> *The Budget of the United States Government, FY2005, Analytical Perspectives*, p. 114 and p. 119.
- <sup>97</sup> *Ibid*, p. 9.
- <sup>98</sup> House Select Committee On Homeland Security, “An Analysis of First Responder Grant Funding,” see Table p. 25.
- <sup>99</sup> GAO-03-718T, p. 13.
- <sup>100</sup> *Ibid*. p. 13.
- <sup>101</sup> Chris Edwards, “Downsizing the Federal Government,” p. 32.
- <sup>102</sup> *Ibid*, p.32.
- <sup>103</sup> Congressional Quarterly, “Transcript of Senate Budget Committee Hearing on FY2005 Homeland Security Department Budget,” February 25, 2004, p. 2 and p. 9.
- <sup>104</sup> Bruce Schneier, *Beyond Fear: Thinking Sensibly About Security in an Uncertain World*, (New York: Copernicus Books, 2003), p. 3
- <sup>105</sup> General Accounting Office, “Homeland Security A risk Management Approach Can Guide Preparedness Efforts,” GAO-02-208T, October 31, 2001, p. 2. Also see “Combating Terrorism: Selected Challenges and related Recommendations,” GAO-01-822 September 20, 2001.
- <sup>106</sup> Jeremy Torobin, “Preventing Terrorism Tops Cox’s Agenda for New House Homeland Security Committee,” Congressional Quarterly, Tuesday, February 11, 2003.
- <sup>107</sup> *Ibid*.
- <sup>108</sup> This of course does not mean that we think FEMA is doing an effective job. The media constantly reports about the mismanagement of FEMA and its failure to deliver disaster reliefs. See for instance Washington Post, “Housing Problems Beset FEMA in Florida,” Monday August 23 2004, p A 2.
- <sup>109</sup> House Select Committee On Homeland Security, “An Analysis of First Responder Grant Funding,” p. 6.
- <sup>110</sup> Amanda Ripley, “How We Got Homeland Security Wrong,” Time Magazine, Monday March 22, 2004.
- <sup>111</sup> *Ibid*.
- <sup>112</sup> The list of all the cities can be found in Department of Homeland Security Office of Domestic Preparedness, “Fiscal year 2004 Urban Areas Security Initiative Grant Programs,” p. 7-9.  
<http://www.ojp.usdoj.gov/docs/fy04uasi.pdf>
- <sup>113</sup> *Ibid*.
- <sup>114</sup> Information on “The Faster and Smarter Funding for First Responders,” HR. 3266, can be found at <http://homelandsecurity.house.gov/release.cfm?id=216>
- <sup>115</sup> Amanda Ripley, “How We Got Homeland Security Wrong,” March, 2004, p. 5.
- <sup>116</sup> *Ibid*.
- <sup>117</sup> Alice Lipowicz, “First Responder Groups Endorse Risk-Based Grants Formula,” Congressional Quarterly, October 22<sup>nd</sup>, 2004.
- <sup>118</sup> Alice Lipowicz, “First Responder Groups Endorse Risk-Based Grants Formula,” Congressional Quarterly, October 22<sup>nd</sup>, 2004.
- <sup>119</sup> Alice Lipowicz, “Apples to Oranges’: State\ Assessments of Terror Threats Are a Study in Subjectivity,” Congressional Quarterly, October 12, 2004.
- <sup>120</sup> Alice Lipowicz, “Apples to Oranges’: State\ Assessments of Terror Threats Are a Study in Subjectivity,” Congressional Quarterly, October 12, 2004.
- <sup>121</sup> Senator McCain has been a strong critic of pork barrel spending over the years. For details about how to measure wasteful spending see Senator McCain “Pork Statement,” <http://mccain.senate.gov/index.cfm?fuseaction=NewsCenter.Pork>
- <sup>122</sup> Tom Schatz, “Pigging Out At record levels,” Citizens Against Government Waste Pig Book, Tuesday April 8, 2004.
- <sup>123</sup> For details about the items see Veronique de Rugy, “The Republican Spending Explosion,” Cato Institute Briefing Paper no. 87, March 3, 2004.
- <sup>124</sup> Department of Homeland Security Appropriation Act of 2004, Public Law 108-90.
- <sup>125</sup> Citizens Against Government Waste, Pig Book, April 8, 2004.
- <sup>126</sup> Tim Starks, “Congress Overcomes Obstacles to Complete Homeland Spending Bill,” Congressional Quarterly, October 15, 2004.
- <sup>127</sup> Tim Starks, “Congress Overcomes Obstacles to Complete Homeland Spending Bill,” Congressional Quarterly, October 15, 2004.
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- <sup>130</sup> Bruce Schneier, *Beyond Fear: Thinking Sensibly About Security in an Uncertain World*, (New York: Copernicus Books, 2003), p. 40-41.
- <sup>131</sup> Caitlin Harrington (2004), “DHS Audit Found Significant Problems in Airport Security,” Congressional Quarterly Homeland Security, Sept. 22.
- <sup>132</sup> Department of Homeland Security, Budget in Brief FY2005, p. 14 and Department of Homeland Security, Budget in Brief FY2004, p. 9.
- <sup>133</sup> Author’s calculation based on Department of Homeland Security, Budget in Brief FY2005, p. 28.
- <sup>134</sup> Steve Miletich, Cheryl Phillips and Ken Armstrong, “Air Safety Hinges on Change of Course For Ailing Agency,” Seattle Times, July 13, 2004, report that Rep. Peter DeFazio (D-Ore.) complains about the TSA’s lack of resources.
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- <sup>141</sup> Ibid.
- <sup>142</sup> Ibid.
- <sup>143</sup> General Accounting Office, “Aviation Security: Private Screening Contractors Have Little Flexibility to Implement Innovative Approaches,” GAO-04-505T.
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- <sup>145</sup> Tom Ramstatck, “Airport Screeners Perform Poorly,” Washington Times, April 23, 2004, p. A1.
- <sup>146</sup> Zack Phillips, “TSA Interference Degraded Private Screener Performance, IG Says,” Congressional Quarterly, October 12, 2004.
- <sup>147</sup> Robert Poole, “Statement Regarding the Appointment of Admiral James Loy as Head of the Transportation Security Administration,” July 2003.
- <sup>148</sup> Ibid.
- <sup>149</sup> A good description of this program and the competitive grant system can be found at <http://www.dot.gov/affairs/tsa0302.htm>
- <sup>150</sup> For information about this program see Department of Homeland Security, “Secure Seas, Open Ports: Keeping Our Water Safe, Secure and Open for Business, June 2004.
- <sup>151</sup> Office of Management and Budget, Budget of the Government and Mid-Session review for FY2005.
- <sup>152</sup> Author’s calculation based on Office of Management and Budget, Budget of the Government and Mid-Session review for FY2005. Also, see Veronique de Rugy, “The Republican Spending Explosion,” Cato Institute Briefing Paper no. 87, March 3, 2004.
- <sup>153</sup> Ibid.
- <sup>154</sup> Republican National Committee, 1996 GOP platform, [www.rnc.org](http://www.rnc.org).
- <sup>155</sup> Ibid.
- <sup>156</sup> Chris Edwards and Tad DeHaven, “Farm Subsidies at Record Levels as Congress Considers New Farm Bill,” Cato Institute Briefing Paper no. 70, October 18, 2001.
- <sup>157</sup> *Budget of the United States Government, FY2005, Historical Tables*, Table 4.1.
- <sup>158</sup> George W. Bush, “Remarks by the President in Address to the Nation,” June 2002, [www.whitehouse.gov/news/releases/2002/06/20020606-8.html](http://www.whitehouse.gov/news/releases/2002/06/20020606-8.html).