

Keep federal hands out of our local purse

By Daniel J. Smith, Ph.D.

State and local governments are seeking \$915 billion in aid from the federal government on top of the lending facilities already being offered by the Federal Reserve. While requested under the guise of helping ease the burden of COVID-19, it would amount to a bailout of state and local governments that engaged in years of fiscally irresponsible behavior.

In addition to putting further strain on our already out-of-control federal finances, a bailout of this magnitude would undermine federalism and encourage more fiscally reckless behavior by state and local governments, making us less prepared to respond to the next crisis or pandemic.

The fiscal stress that these state and local governments are experiencing is certainly being exacerbated by COVID-19. But the pandemic is not the primary reason why the state and local governments in the direst conditions are struggling. Those in the worst financial shape, such as Illinois and Connecticut, made imprudent financial decisions—not just for years but for decades—despite the warnings of financial experts and the experience of the financial crisis of 2007-08.

If these states were truly experiencing hardship just from COVID-19, they would not seek a bailout of *unrestricted* funds. It belies the fact that they have intentions other than pandemic-related expenses for this money.

Academics, think tanks, and citizens calling for fiscal reforms were simply tuned out, or even ridiculed. At the same time, unfunded pension liabilities continued to grow, economic incentive deals and stadium subsidies were doled out, and rainy-day funds were neglected. A federal bailout would only accelerate this type of irresponsible behavior going forward, removing one of the last remaining incentives for fiscal restraint at the state and local level.

A state and local bailout would also give the federal government relatively more control over state and local governments, further



PUBLIC DOMAIN IMAGE

compromising the strength and flexibility of our federalist system of government. The strength of federalism, when it comes to public finance, is in allowing lower levels of government to exercise their judgments and bear the responsibilities for their decisions. After all, it is much easier for citizens of lower-level governmental units to monitor expenditures and to hold policymakers accountable. But the system only works if these governments are held responsible for their decision-making. Subsidizing bad behavior throws a monkey wrench into federalism by distorting the incentives for properly managing the public purse.

The fact of the matter is that the federal, state, and local governments should have been prepared for a potential downturn in the economy. In fact, some states, such as fiscally sound Nebraska and Tennessee, are much better situated to weather COVID-19. State and local governments who have neglected their fiduciary responsibility are in the worst position to continue to provide basic government services during this pandemic. Some, such as Illinois Governor J. B. Pritzker, even ridiculed those pressing for adopting prudent financial practices. The very same local governments now use the current pandemic to foist their irresponsibility on the rest of us. Rather than encourage this bad behavior we need to help ensure that distressed state and local governments come out of this pandemic leaner and on the path, albeit reluctantly, towards financial health.

While the current pandemic is unquestionably dreadful, this will not be the last or even worst crisis, or pandemic, our nation faces. Any bailout now will only undermine the strength of our political economic system, and our financial condition, making us less capable of addressing the next crisis.

Permission to reprint this in whole or in part is hereby granted, provided that the author (or authors) and the Political Economy Research Institute are properly cited.

ABOUT THE AUTHOR



Dr. Daniel J. Smith is the director of the Political Economy Research Institute at MTSU and an Associate Professor of Economics in the Jones College of Business. He is also the Senior Fellow for Fiscal and Regulatory Policy at the Beacon Center of Tennessee. Follow him on Twitter: @smithdanjl.



Political Economy
Research Institute
mtsu.edu/peri