

# In the Rubble of Disasters, Politicians Find Economic Incentives

By Molly D. Castelazo and Thomas A. Garrett

Taxpayers spend an average of \$3 billion each year to help victims of natural disasters rebuild their lives. The public expects that the money the federal government spends on disaster relief goes to those people who need it most and that the amount of disaster relief doesn't go beyond the actual cost imposed by the natural disaster. As with any compassionate public policy—such as food stamps, welfare and unemployment insurance—the public has the right to expect that elected officials carry out disaster relief policies to improve social welfare without regard to their own political agendas and self-interests.

However, public choice, a discipline that applies economic theory to political science, demonstrates that political agents behave just as private agents do; that is, they act in their self-interest and change their behavior in response to economic incentives. Recent studies applying this doctrine to disaster relief reveal that we may be paying for politicians to build their political capital as well as for families to rebuild their homes.



Rescuers walk past apartments damaged in the Northridge, Calif., earthquake in 1994. Some families in the area received federal aid they didn't request. Others got payments for damage too minor to be covered.

(AP Photo)

## Private vs. Public Self-Interest

The private sector consists of firms and consumers. A firm's self-interested goal is to maximize profit, and a consumer's goal is to maximize well-being. A firm will produce the level of output that maximizes its profit. Any change in input prices or product demand gives a firm an incentive to change production levels. Consumers, faced with certain prices and a fixed budget, purchase various quantities of goods and services that maximize consumers' well-being. Price or income changes provide consumers the incentive to change their bundle of consumption goods.

Elected officials in the public sector are also motivated by self-interests. These include maximizing political support, campaign contributions and, ultimately, votes. As with private agents, the fact that public actors are motivated by self-interest does not imply that they are not altruistic—self-interested behavior is different from selfish behavior. A firm that earns profit provides a benefit to society because the firm is producing what society wants at the lowest cost possible. For consumers, self-interest

can take shape as charity, concern for others and a desire to increase public welfare. Public actors often promote policies such as unemployment compensation, minimum wage legislation and food stamps. These policies are designed to improve people's lives, while at the same time the policies increase the support that politicians receive from those people who benefit from such policies.

## Private vs. Public Cost

Public officials can enact policies that are in their self-interest without regard to the social cost of such policy. The primary reason political agents can conduct such policy is that, unlike private agents, political agents often do not incur the cost of their decisions. A firm will affect its profit when it changes production levels or input mix. Consumers who choose to consume one good over another will incur the opportunity cost of foregone consumption. The actions of political agents, however, are often hidden from the public, thus allowing a disconnect between the cost and benefit of any policy. In addition, the cost of any policy is often spread across thou-

sands or millions of taxpayers, making it unlikely that the cost per taxpayer is high enough to incite taxpayers to come together and oppose the policy. These facts provide political agents an incentive to conduct policy that provides benefits to them, but generates excessive cost to society as a whole.

Such politically motivated decisions are especially common where regulation and strict guidelines are absent. In support of this idea, one public choice model suggests that the executive branch behaves as an electoral vote maximizer and that congressional oversight committees make sure that bureaucrats implement the policy preferences of legislators on these oversight committees. The idea is relatively simple: Because legislators and the president have budget and regulatory power over bureaus, these bureaus will implement policies that are beneficial to legislators and to the president. Several studies have examined the relationship between bureaus and their overseers. One study shows that IRS audit rates are lowest in states

that are politically important in the next presidential election, as well as in the states whose congressional members serve on IRS oversight committees.<sup>1</sup> Another study finds that Federal Trade Commission (FTC) case rulings are more favorable in congressional districts having representation on FTC oversight committees.<sup>2</sup> By highlighting the motivation behind public decisions, these studies show that economic incentives affect public decision-makers just as they affect private actors.

### Incentives and Disaster Relief

The Federal Emergency Management Agency (FEMA) spent nearly \$22 billion on disaster relief between 1991 and 1999. Sometimes, aid disbursement is not motivated by need, however. For example, on Feb. 3, 1994, the *Los Angeles Times* reported that after the Northridge earthquake, FEMA had made thousands of payments for \$3,450 each to homeowners who had not even requested the aid.<sup>3</sup> *Forbes* later reported that FEMA distributed 6,590 payments to “families whose homes were not even damaged enough to be covered.”<sup>4</sup>

Recent research has applied the public choice model to disaster declaration and aid allocation.<sup>5</sup> The process of disaster declaration and aid disbursement is most vulnerable to political motivation at two points: presidential disaster declaration and FEMA appropriation of disaster aid.

First, the researchers tested whether the electoral importance of the state and whether it was an election year motivated presidential disaster declarations in a state. Of course, the largest amount of aid was given to states like California and Florida, with large numbers of people and a disproportionately large incidence of natural disasters. In order to isolate the political impacts of disaster declaration and relief, the researchers controlled for disaster size, private insurance disaster payments, state population and other state effects. As shown in the table, the studies found that those states with a higher measure of electoral importance had a higher rate of presidential disaster declaration. The studies also found that the mean rate of disaster declaration was higher in election years compared to non-election years.

The second question is whether states having representation on FEMA oversight committees receive larger relief payments than states without representation. Researchers concluded that for each legislator a state had on a FEMA oversight committee, that state received an additional \$31 million in disaster aid each year. As a result, the researchers calculated that nearly 45 percent of all FEMA

disaster payments were motivated by political incentives rather than by need.

This type of behavior is consistent with current models of congressional behavior and public choice theory, which claim that congressional members, like firms and consumers in the private sector, are guided by incentives. As in the case of presidential disaster declarations, aid disbursement is only very loosely guided by the Stafford Act, which stipulates that disaster aid should be granted in cases where the disaster “is of such severity and magnitude that effective response is beyond the capabilities of the state and the affected local governments and that federal assistance is necessary.” And the act itself is loose—in fact, it specifically prohibits using mathematical formulas to determine appropriate aid amounts and provides the president no strict criteria for declaring a disaster.

Given the loose guidelines regarding disaster declaration and appropriations, these decisions are left to the discretion of the president and FEMA officials, respectively. The passage of the Stafford Act was followed by nearly double the rate of disaster declarations. They jumped from

### ENDNOTES

- 1 Young, Reksulak and Shughart II (2001)
- 2 Faith, Leavens and Tollison (1982)
- 3 Rivera (1994)
- 4 Darlin (1995)
- 5 Downton and Pielke (2001) and Garrett and Sobel (2003)

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## State Electoral Importance and Presidential Disaster Declaration

TOP 10 STATES	Electoral Importance	Disasters Declared 1991-1999	BOTTOM 10 STATES	Electoral Importance	Disasters Declared 1991-1999
California	309.4	18	Vermont	17.2	9
New York	283.5	19	Nebraska	16.1	8
Texas	274.6	14	Utah	16.1	3
Pennsylvania	205.9	12	Montana	15.4	6
Illinois	165.4	11	Idaho	12.9	3
Florida	158.1	25	Alaska	10.6	5
Ohio	157.9	6	South Dakota	9.7	12
Michigan	154.7	7	North Dakota	9.7	8
North Carolina	120.3	14	Wyoming	9.7	1
Georgia	116.4	12	Arizona	7.9	15
<b>Average</b>	<b>194.7</b>	<b>13.8</b>	<b>Average</b>	<b>12.5</b>	<b>7</b>

25 a year between 1983 and 1988 to 41 a year between 1989 and 1994.

Because of this connection between the absence of strict guidelines directing presidential disaster declarations and excessive FEMA aid disbursement, it makes sense that by strengthening the guidelines for disaster declaration and aid disbursement, we can alter the incentives that the president and FEMA officials face. As a result, we can better ensure that tax dollars are used only in the public's best interest.

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NOTE: Electoral importance is a function of each state's electoral votes and the degree to which the state has been a battle-ground state (presidential re-election chance of near 50% in the state) in the last 11 presidential elections. See Garrett and Sobel (2003) for a complete description. The largest amount of aid is given to states like California and Florida, with large numbers of people and a disproportionately large incidence of natural disasters. To establish a causal relationship between electoral importance and disaster declaration, the impact of electoral importance on disaster declaration was evaluated by controlling for disaster size, private insurance payments, population and other state effects.