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From the desk of Hon. Maurice McTigue

Applying Full Cost Recovery in Government Budgets

Preamble:

When governments make decisions about requiring a certain procedure, a license, a permit or an authorization then the next logical decision should be how this service or process will be funded. There are basically two choices for funding the taxpayer or the user/consumer of the service. Theoretically the decision should be based on who benefits. If the new activity is entirely a public good then it is the taxpayer who should pay. When it is a private benefit then the user consumer should pay. Then on other occasions the cost might be apportioned between the two when there is both a public and private good. Ultimately it is a political decision to determine the means of funding the activity. Often at the time of making the original decision there are vested interests at work trying to move the cost to the taxpayer. It is in my view a quite legitimate budget practice to test these decisions from time to time and is often as much matter of equity to shift cost from the taxpayer to the user or vice-a-versa as it is a mechanism to diminish budget expenditures.

In the analysis I have done for the Streamlining Commission, I have made a large number of recommendations that certain goods and services should be subjected to "full cost recovery". I use the term "full cost recovery" very deliberately because I wish to distinguish this process from the concept of "fees". I wish to make the distinct differentiation between the concept of "cost" and the concept of "fees". The concept of "cost" includes all of the expenses that were incurred in providing the service or goods but absent any profit or reward. The concept of "fees" is best compared to the standard practice of lawyers, accountants, architects, doctors or engineers who charge us for their services through a schedule of "fees" and these are clearly inclusive of both the costs incurred and reward. For the public to accept this process of "cost recovery" then they need to believe that there is no reward or profit in the costs they have to pay for these government services. The credibility of this process is entirely dependant on the level of transparency and authentication that is used in calculating the costs imposed.

I have posed this question when looking at a number of activities and concluded that there are currently a significant number of activities in the Louisiana Budget that should really be paid for by the users and consumers of those services. I also understand the concerns that will be raised as the public views this process with some cynicism so I have also outlined a set of the criteria that should apply to "full cost recovery".

How Should Cost Recovery Work?

First Principle: This process is a recovery of costs only so Government agencies must not be allowed to recover any more than the exact cost of the service or good provided. (If they recover in excess of the actual cost then it must be returned to the payer otherwise that excess is a tax and government agencies do not have taxing authority.)

The Procedure: The Governor would issue an Executive Order stating that agencies would be required to recover the cost of designated services but were forbidden from recovering money in excess of the cost of services.

- The Executive Order would lay out the criteria for setting the amounts for cost recovery and all charges existing and new would be subject to these criteria. (The elements of the criteria follow, but this is not an exhaustive list. Other criteria might be added according to the requirements of the Governor's Office.)
 - The Executive Order would make it clear that the Governor's budget and the decisions of the Legislature would determine what activities of agencies are to be funded by cost recovery. That same process would determine whether it will be full cost recovery (100%) or proportional recovery (75%) or some other amount.
 - The advice of the accounting profession would be sought to specify the process to be used and the elements of the agencies operation that may be included in cost recovery.
 - The data and information used, as well as the process employed to calculate the specific charge must be prominently displayed on the agency's website in a readily accessible manner and in a user friendly format.
 - The charge, when determined, must be subjected to audit and the audit report must be placed online and linked to the charge concerned. The audit report must include an assessment of what proportion of cost this fee represents. E.g. 90%, 100%, 105%
 - The Executive Order would state that if an agency overcharges customers it must return the excess that has been collected. (This requirement probably needs some minimum rules attached to it. E.g. the over charge exceeds 1% or \$5, so as to avoid dealing in ridiculously small amounts.)
 - The Executive Order would also define what activities would be subjected to cost recovery.

Examples of Cost Recovery:

- *Public good - private benefit – or a portion of each.*
- The FDIC is funded by levies and charges imposed on banks to carry out its mandate of insuring the deposits of all depositors up to a certain limit. The banks make the payment but in the end all the customers of banks pay except that process is invisible. Should the taxpayer pay? No clearly the benefit is to the depositors.
- Vehicle drivers and owners pay for licenses safety inspections and registration of their vehicles. While it could be argued that part of the benefit of safety inspections is to the rest of the public clearly the major benefit is to the driver and the owner so they pay.
- Airport Security is funded almost entirely by passengers and safe planes clearly give the greatest benefit to passengers.
- Building Permit – private benefit - owner pays
- Policing – public benefit – taxpayer pays
- Military – public benefit – taxpayer pays
- Prosecution of criminals – public benefit – taxpayer pays
- Border protection – public benefit – taxpayer pays
- Environmental pollution & damage – polluter pays - taxpayer pays
- Outbreak of hoof & mouth disease – public pays
- Weight & measures inspection – cost of doing business – business pays
- License to be a hairdresser – cost of doing business – business pays
- License to apply chemicals – cost of doing business – business pays