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Opportunity Costs--A Lesson Not Learned

The fundamental reality of economics is scarcity. Simply put, there are not enough resources to satisfy all of everyone's wants. Scarcity leads to the concept of opportunity cost. If we use a scarce resource for purpose A, then we have to forgo using it for purpose B, C, or D. The best alternative use represents the true cost of doing A.

For some reason, this concept seems to have bypassed the government and authorities in Pittsburgh. Case in point: the Urban Redevelopment Authority has touted the Summerset at Frick housing development as an example of how government can improve the tax base by subsidizing construction. As of mid 2003, 58 homes with an average price of $400,000 had been built and sold. Meanwhile, public funds of $30 million had been spent in site acquisition, preparation, water and sewer, etc.

Assuming a foregone interest rate of 5 percent, the annual opportunity cost of the public funds would be $1.5 million. Compare that to the $240,000 in yearly property tax revenues Pittsburgh will receive from these homes-- assuming they are appraised at full market value. Even factoring in county and school taxes, this is a poor investment of public funds.

Spending public dollars to help underwrite upscale homes averaging $400,000 calls this venture into further question. When did it become a role of government to subsidize homes for well-to-do buyers? There is also a concern that adding to the housing supply in a City that is losing population could have a depressing effect on existing house prices.

Unfortunately, this example is all too typical of the way government in Pittsburgh, and to a large extent Pennsylvania, approaches the spending of public money. First, they make extravagant claims about benefits, in terms of jobs that will be created or tax revenues that will be realized while understating the costs of the projects, including the corollary costs that stem from preventing the private sector from employing the property in its true best use.

We need only look at the hundreds of millions of dollars spent on stadiums. Obviously, this is money that could have been used on real infrastructure or left unspent altogether to reduce the burden on taxpayers. Or we could look at the plan to spend over $300 million to dig a tunnel under the Allegheny River to extend light rail to the North Shore. There is

so little benefit to be derived from the project that the mind boggles to see officials seriously advocate the expenditures. When one looks at the other important transportation projects that could be funded with these hundreds of millions, it becomes apparent that those who decide how taxpayer money will be used have abandoned any notion of opportunity cost--if they ever had one.

And that is the problem. Wasteful spending of other people's money is the norm because government officials, unlike private sector investors, do not actually have to show a return on their investments. Government officials who make decisions on how to spend tax dollars did not earn the money, thus they are not compelled to consider opportunity costs the way private citizens and businesses are forced to do. As long as taxpayers cannot restrain governments through required referenda on tax increases and there are no tight controls over spending increases, the situation will not change.

Before another taxpayer dollar is spent on one of these grand schemes, the Commonwealth, the cities, the authorities, and the counties should have all their previous schemes audited fully to determine whether the citizens and taxpayers got their money's worth. Despite massive spending on government schemes and projects, Pennsylvania's economy is virtually stagnant as are those of Pittsburgh and Allegheny County.

There is a lesson to be learned here. Sadly, for those who view government as the creator of wealth and jobs, that lesson will never be learned. It is too bad we cannot require anyone in government with authority to spend tax dollars to have taken a basic course in economics that drives home the concepts of scarcity and opportunity cost.

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