

# NATIONAL REVIEW

## How Sunk Costs Keep Government Deficits Growing

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As the Biden administration promises the most ambitious spending package in the nation's history, conservatives have quickly pointed out how inefficient and wasteful such packages are. While these critiques tell us how or why the government is wasteful, we need an understanding of government inefficiency that helps us find a solution. Americans already agree that the way to tackle our budget deficit is by cutting “waste and fraud,” and that citing Milton Friedman or repeating “the government is inefficient” won't solve the problem. One reason government spending is so needlessly costly is somewhat paradoxical: The state is wasteful precisely *because* people are so concerned about wasting money.

Beginning in 2009, the Department of Defense and the Veterans Affairs Department spent four years and \$1 billion fruitlessly trying to build an integrated health-record system. Eventually, a report came out revealing that wildly overpaid contractors, along with “staffing challenges [and] bureaucratic red tape,” created the issue. This familiar tale has an even more concerning ending, though: Democrat Bernie Sanders and Republican Jeff Miller both criticized the decision to cancel the project because so much money had already been spent.

This is a classic sunk-cost fallacy: Costs that can't be recovered are “sunk,” and therefore irrelevant for future decision-making. But while this fallacy is well known in economics, sunk costs are a big deal in the practical world of politics. Nobody wants to waste money, and politicians don't want to cause waste directly. No member of Congress wants to be publicly responsible for a half-built bridge, *especially* when they have to tell taxpayers they still have to foot the bill for it.

This phenomenon can be seen most acutely in spheres where extensive R&D is needed because it's hard to estimate costs, but unused research feels wasted. Take the James Webb Space Telescope, a NASA project significantly over budget and severely delayed. When Congress considered cutting the program in 2011, there was an outcry from researchers claiming that cutting the telescope project “would waste more taxpayer dollars than it saves.” Congress caved, and a decade later the telescope still hasn't launched, while continuing to rack up high costs.

In 2008, former NASA associate administrator Alan Stern said NASA has a systematic problem of overspending, which comes from “managers and contractors who accept or encourage [unaffordable] assignments, expecting to eventually be bailed out.” Using the Mars rover project as an example, Stern said that “NASA’s main defense for paying still more for this new Mars rover: the \$1.8 billion or more in already sunk cost.”

Researchers at the Cato Institute found Congress’s unwillingness to cut the funding of poorly run projects is a significant reason government projects always spend too much. It doesn’t take a Ph.D. in economics to see this kind of thinking in practice. Funding is cut only when construction becomes prohibitively expensive, and even then, only after years of pushback.

This type of behavior results in more than just unnecessary spending. The folks who write government grant proposals know that their cost estimates won’t be accurate. Economists at Oxford uncovered a statistical difference between estimated costs and final budgets. They noted that “cost inaccuracies have a striking systematic bias, with overestimates being significantly more common than underestimates.” Furthermore, members of Congress know the projected budgets given to them aren’t reliable, making it hard for representatives to know which projects are worth the cost.

There is some hope, however, that Congress may stop throwing good money into poorly conceived projects, and it comes from an unlikely place: Adam Smith. Not the Scottish economist, but the Democrat from Washington. This spring, Smith put the F-35 Joint Strike Fighter under scrutiny for its high cost relative to comparable fighters. Not only is the fighter missing important support equipment, such as engines, it’s highly expensive. The jet currently costs 30 percent more than other fighters to operate, adding up to a significant price difference over time.

Smith decried these expenses, saying he wants to “stop throwing money down that particular rathole” and asking, “Is there a way to cut our losses?” Smith is asking the right questions. In fact, *every* member of Congress should have these questions in the back of his mind. Yes, conservatives should push back against efforts to gut the military, but that’s not happening here. This is the way forward for Americans to differentiate the kinds of government waste.

Politicians are nervous about cutting ongoing projects because they don’t want to leave taxpayers empty-handed, but stomaching sunk costs is worth it. Not only is it economically sound to stop government agencies from bleeding money, but it also sets the precedent that shoddy work will be held accountable. Just as not all spending is equal, not all waste is equal, either. Americans, and conservatives in particular, must recognize that to save money, sometimes you have to lose money.