

RESEARCH REPORTS

Reviews of new research by public agencies and private institutions

"Prospects for Medicare's Hospital Insurance Trust Fund."

Staff Memorandum, Congressional Budget Office, U.S. Congress, Washington, D.C. 20402. 22 pp.

Even as Congress celebrates the apparent resolution of the Social Security crisis, it may have to start worrying about another impending U.S. trust fund bankruptcy.

According to the staff of the Congressional Budget Office (CBO), Medicare (health insurance for the elderly and disabled) faces almost certain insolvency by 1988. Ironically, Congress hastened the problem by authorizing Social Security to borrow some \$12.4 billion from Medicare to balance the books, reducing the latter's trust fund to \$8.3 billion.

Medicare consists of two programs: Supplementary Medical Insurance (1983 outlays: \$19.2 billion), which covers doctors' services, and Hospital Insurance (\$41.1 billion), which pays for stays in hospitals and nursing homes and for home health care.

The Supplementary program is not in jeopardy because it is chiefly supported by general revenues.

But Hospital Insurance is financed through earmarked payroll taxes. At current rates, it will suffer an \$8.2 billion deficit in 1988, widening to \$18.3 billion in 1990 and to \$63.2 billion by 1995.

The chief source of red ink is escalating hospital costs, which account for 10.8 percentage points of the projected 13.2 percent average annual increase in outlays between now and 1995. Surprisingly, the aging of the U.S. population is a minor factor.

Payroll tax hikes alone would be too onerous to close the gap. The current 1.3 percent payroll tax on earnings is scheduled to rise to 1.45 percent in 1986; it would have to climb to 2.38 percent by 1995 to keep Medicare in

the black. But when scheduled boosts in the Social Security payroll tax are also factored in, the burden would be 8.5 percent—a big chunk of workers' paychecks. And, since employers pay an equal percentage, this is a deterrent to new hiring.

Financing the deficit out of general revenues would simply redistribute the tax burden.

Another option is to raise recipients' "coinsurance" costs, thus encouraging shorter and fewer hospital stays. Currently, Medicare beneficiaries pay a "first day" fee of \$304, but nothing else for the next 59 days. Closing the budget gap would require a stiff daily payment of \$100.

Cutting hospital charges is a fourth possibility. Congress could adopt a "prospective reimbursement" system—establishing in advance rates Medicare will pay hospitals—but to maintain Medicare's solvency, payments would have to be 38 percent below projected full reimbursement costs. The probable result: either an overall decline in the quality of hospital care or a dual hospital system, one for private patients and an inferior version for Medicare patients.

Relying on any single measure to staunch the Medicare red ink is probably impractical. Combining all three is probably the best alternative.

So far, Congress has been myopic about Medicare's growing difficulties, content to tinker and hope. [In March, it adopted a limited form of prospective reimbursement. This, in effect, merely replaces hospital cost control measures now in force and does not alter the CBO projections.] But it will take radical steps to save the system.

"A Palestinian State: Implications for Israel."

Harvard Press, 79 Garden St., Cambridge, Mass. 02138. 190 pp. \$16.00.
Author: Mark A. Heller

Amidst all the debates over whether a new Palestinian state should be created in the Middle East, few analysts have pondered what such a state actually would be like—or how much of a threat it would pose to Israel.

Heller, a research associate at Tel Aviv University's Center for Strategic Studies, believes that, over the long run, a Palestinian state could increase Israel's security. His hypothetical state, negotiated with a Palestinian Liberation Organization (PLO) willing to renounce its aim of eliminating Israel, would encompass the West Bank and Gaza Strip.

Added to the 1.3 million Palestinians now in the two areas, he estimates, would be 750,000 exiles returning over a five-year period. The new settlers would need 195,000 jobs, requiring new investments of \$3.3 billion. Diverting some \$220 million from the United Nations Relief and Work Agency's budget for Palestinian refugees and tapping personal savings in the new state would provide \$2 billion. The remainder, about \$260 million annually, could be supplied from other sources. The major Arab powers, for example, have pledged \$250 million annually to the PLO.

Even so, by 1985 the Palestinian state would have a gross national product of only \$2.5 billion, compared

to Israel's \$19.5 billion in 1980.

"A state might enhance conventional Palestinian military capabilities," Heller adds, "but it would also constitute a discrete and accessible target for Israel." Rifts would also appear in the Palestinian ranks: Many present-day residents of the West Bank and Gaza Strip would be satisfied with an end to Israeli occupation and reluctant to risk all in war; the "village patriots," hard-core PLO supporters who fled their homes after the creation of Israel in 1948, would comprise at most seven percent of the population. And Arab support for the PLO would naturally diminish once a homeland was established.

Nevertheless, Heller cautions, Israel would require safeguards: full diplomatic relations with the new nation, guarantees that the Palestinians would maintain only defensive armed forces and not enter into any military alliances, and the right to maintain monitoring posts within the new state's borders.

A West Bank-Gaza Strip Palestinian state would still pose a threat to Israel. But with the Israeli defense effort now consuming over 30 percent of its GNP annually and the political divisions within Israel growing, a negotiated settlement to the "question of Palestine" seems the wisest course.

"Underground Government: The Off-Budget Public Sector."

Cato Institute, 224 Second St. S.E., Washington, D.C. 20003. 179 pp. \$8.95.
Authors: James T. Bennett and Thomas J. DiLorenzo

The 1970s "tax revolt" spawned a new outbreak of "off-budget" activities at all levels of government, immune to taxpayers' control.

Most "off-budget enterprises" (OBEs), explain Bennett and DiLorenzo, economists at George Mason University, are quasi-public authori-

ties that sell tax-exempt bonds and use or lend the proceeds to fund particular kinds of projects—airport, road, or hospital construction, sewer and water system operation, industrial development. Their outlays do not appear in the budgets of the governments that created them. Their borrowing, the authors add, “does not require voter approval and . . . is not subject to statutory or constitutional debt restrictions.”

In Washington, federally chartered OBEs such as the Farm Credit Administration and the Federal National Mortgage Association (“Fannie Mae”) are just part of the off-budget pie. They borrowed (and spent or loaned) \$49 billion in 1982, most of it for home, farm, and business mortgages, up from \$29 billion two years earlier.

“On-budget” federal agencies, meanwhile, have shifted more and more of their business off the books. Their off-budget outlays swelled from just \$100 million annually in 1973 to \$23.2 billion in 1981. Accounting for nearly half the total was the Department of Agriculture’s Farmers Home Administration, which provides low-interest loans for rural development.

Some 150 federal agencies extend off-budget loan guarantees, insuring banks against defaults by small businessmen, homeowners, students, and other private borrowers (who therefore pay a lower rate of interest). Washington provided \$102 billion of such guarantees in 1982.

All told, federal loans and guaran-

tees, off- and on-budget, came to \$205 billion in 1982, accounting for 40 percent of all credit extended annually.

Such massive involvement in the credit markets, the authors warn, “crowds out” private borrowing. Every \$1 billion in loan guarantees, for example, costs up to \$1.32 billion in foregone private investment.

Information about state and local OBEs is sketchier. State OBEs number in the thousands; there are perhaps 10,000 at the local level. Yet their activities have expanded dramatically, largely, the authors argue, as elected officials sought to sidestep the effects of the 1970s “tax revolt.”

Until 1974, municipalities annually issued more voter-approved bonds for such purposes as building new sports arenas or sewage systems than they did OBE bonds. But the ratio was then reversed. In 1980, city OBEs raised \$34 billion through bond sales, city governments only \$14 billion. State OBEs, meanwhile, raised an estimated \$106 billion in 1980.

Why worry? While OBE debts are normally repaid out of earnings from the projects they fund, state and local governments—and thus the taxpayers—must ultimately make good on them in the event of a default.

Bennett and DiLorenzo are not sanguine about the prospects for controlling off-budget spending. Even a constitutional amendment requiring a balanced federal budget would probably just promote the growth of more “underground government.”

“Reading, Science, & Mathematics Trends: A Closer Look.”

National Assessment of Educational Progress, Education Commission of the States, Suite 700, 1860 Lincoln St., Denver, Colo. 80295. 32 pp. \$4.00.

Author: Barbara J. Holmes

American elementary and high school students during the 1970s performed neither as well as they could have nor

as poorly as many critics contend.

The mixed bag of results turned up in a series of standardized tests ad-

ministered during the decade to one million students by the federally commissioned National Assessment of Educational Progress (NAEP).

Several clear trends emerged during the 1970s, writes Holmes, an NAEP staffer. Overall, reading skills improved while math and science scores dropped. Black students made relatively greater gains than did whites in all three fields. Both younger students and low achievers improved their performances while older students and high achievers lost ground.

The biggest single gain of the decade was recorded by nine-year-old black students in the bottom 25 percent (or quartile) of the achievement scale: an 8.4 percent gain in reading scores.

Overall, nine-year-olds made gains across the board in reading and held their own in math and science. The scores of 13-year-olds remained stable in reading and science, but dropped in math. Seventeen-year-olds lost ground in every field but reading, where their scores were unchanged.

Breaking the data down by race tells a somewhat different story. Black nine-year-olds fared best, outpacing their white counterparts' gains in reading, keeping even in science, and improving their math scores by 2.9 percent while their white classmates' declined by two percent.

Among 13-year-olds, there were only two changes for either group: Blacks improved by 3.2 percent in reading; whites dropped by 2.4 percent in mathematics. Seventeen-year-old black students lost less ground in math and more in science than their white classmates.

Despite their gains, black students, overall, consistently performed below

the national average during the 1970s, while their white contemporaries scored above average. Yet, while in 1971 only 5.8 percent of black nine-year-olds were in the top quartile of overall academic achievement for their age group, by 1980 the proportion was up to 10.4 percent.

The NAEP study also shows that, regardless of race, low achievers (the bottom quartile) were "catching up" with high achievers. Indeed, high achievers registered only one gain during the decade: a 1.4 percent increase in the reading scores of nine-year-olds. The heaviest losses were also incurred by high achievers: declines of 3.9 and 4.3 percent, respectively, in science and math among 17-year-olds.

No group of low achievers, on the other hand, suffered a drop in test scores during the decade, and several registered gains.

What is behind these trends? Holmes offers some tentative explanations. "Back-to-basics" advocates emphasized elementary skills, and Washington committed itself to compensatory education focused on young, underprivileged black children. These help to explain gains in reading and among blacks.

But the "back-to-basics" movement slights "problem-solving" skills. The exodus of top math and science teachers to more lucrative careers in the private sector, exacerbated by declining federal support for science education, also contributed to the losses.

To a large degree, Holmes suggests, American society got what it wanted from the schools during the 1970s. Second thoughts on education might now be in order.

WILSON CENTER PAPERS

Summaries of key reports given at recent Wilson Center meetings

“Why Nations Built Bombs: ‘Never in the Field of Human Conflict Was So Much Owed by So Many to So Few.’”

Paper by Arnold Kramish, presented at a colloquium sponsored by the Wilson Center's International Security Studies Program, December 9, 1982.

Reflecting, in 1962, on America's World War II race for “the Bomb,” General Leslie Groves, former commander of the Manhattan Project, observed that “without active and continuing British interest there probably would have been no atomic bomb to drop on Hiroshima.” Kramish, a physicist and himself a participant in the Manhattan Project, goes further: He believes that the British discouraged early efforts toward cooperation among the major powers for the post-war control of atomic weapons.

Franklin Roosevelt, says Kramish, “was no match [for] Churchill in coping with the new atomic challenges.” Churchill had actually envisioned, as early as 1925, an explosive of the size and yield of the Nagasaki bomb. His atomic adviser during the war was a close personal friend—physicist Frederick Lindemann, later Lord Cherwell. They kept tabs on American developments with the help of a group of 30 top British scientists working with colleagues in the United States.

By contrast, Roosevelt “never really understood the subject.” He thought the German effort to build an atomic bomb was further advanced than it actually was (the British, who knew better, chose not to disabuse him). His political adviser, Harry Hopkins, who was not a scientist, was in touch with Churchill and Cherwell as often as with such top U.S. physicists as Vannevar Bush.

Bush began to believe that the United States and Britain should consider sharing information in the post-war world for the sake of international control. But at Churchill's bidding, contends Kramish, Roosevelt was so secretive about the bomb that, for example, even Vice-President Truman was unaware of the September 19, 1944, Hyde Park Churchill-FDR agreement to use the bomb against Japan “after mature consideration.” According to Kramish, this secrecy convinced Stalin that the Americans were serious about building a weapon. He thus resumed his own secret atomic project on a modest scale—an institute with a staff of 50—at the end of 1942.

Churchill, explains Kramish, had his own reasons for secrecy—and for wanting to drop the bomb on Japan. He distrusted Stalin and felt that Roosevelt “was going soft” on the Soviets. He also anticipated American resentment if Britain did not join the Pacific war effort. As Churchill saw it, the best way for war-exhausted Britain to help was to encourage the use of the bomb on Japan.

On August 6, 1945, America bombed Hiroshima. Stalin, says Kramish, suddenly realized the full implications of the weapon so closely guarded by his allies. The secrecy and outright deceptions attending the birth of the nuclear age, he argues, were destined to impair East-West efforts to achieve arms control.

“Power Changes When Decentralizing: The Case of Yugoslavia.”

Paper by Eugen Pusić, presented at a colloquium sponsored by the Wilson Center's History, Culture, and Society Program, December 6, 1982.

Under Josip Broz Tito, the Communist Party of Yugoslavia (CPY) first acquired political power, then undertook to decentralize it. Pusić, a Yugoslavian political scientist, examines the results.

When, in April 1941, the royal government of the Kingdom of Serbs, Croats, and Slovenes fell to the invading Axis powers, the CPY was the most effective leader in organizing the Yugoslav resistance.

After the war, the CPY instituted a federal state, appealing to ethnic groups (Slovenes, Croatsians, Montenegrins) denied local self-government for almost 500 years by the Hapsburgs and the Ottoman Turks.

The party then proceeded to build a Soviet-type, one-party regime. Its centralizing strategies, however, threatened to reduce the federal units to a “constitutional shadow existence.”

But Marshal Tito, having witnessed the excesses of concentrated power during Stalin's ruthless purges, resisted too-faithful imitation. His independent ways drew predictable reactions from Moscow; on June 28, 1948, the CPY was expelled from the Comintern. Tito's party faced the question of how to distribute power without creating threatening new power centers elsewhere.

The Yugoslavs experimented. In 1950, elected workers' councils were established in each factory and shop. The goal: gradually to divest the State

of industrial control. But power refused to stay where it was distributed. The technical and managerial staffs in Yugoslav industries enjoyed an “expertise” monopoly that “drew the workers' council into its orbit,” away from the main body of workers.

Party congresses in 1952, 1958, and 1964 mandated a transfer of political power away from the party toward “sovereign assemblies of elected representatives at all levels from the commune to the federation.”

But the transfer was not smooth. Milovan Djilas, the Vice-President expelled from the party in 1954, has written extensively on the persistence of party domination through bureaucratic maneuvering. The 1974 Constitution attempted to limit party control of local assemblies, but the CPY Congress insisted on “the principles of ‘democratic’ centralism.”

Other moves were more successful: the shifting of public services from the central government to self-managing organizations, the creation of local militia units comparable to the American National Guard.

Decentralizing, Pusić concludes, remains a challenge. Crises arising from superpower rivalries threaten Yugoslavia's internal balance. Economic and political pressures may lead to re-concentration of power. The important thing, he believes, is to keep any one group from acquiring a permanent monopoly on power.
