



A New Tax Revolution

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Lest the 21st century become the post-American century, we the people must rein in big government in Washington. This means drastically reducing its access to money, curtailing its functions and authority, and electing political leaders with the skills and values necessary to achieve a smaller, smarter and much less interfering government.

Step One for the voters is to put a skilled turnaround expert in charge, preferably one with a proven record of success (think Mitt Romney at the Olympics or Rudy Giuliani in New York City or both). Step One for him, even before starting to hack out the deadwood, is to end the financial fakery upon which Big Government Inc. is built. Now, when the government spends another \$1, it lists the cost as only \$1 in tax and assures us the benefit to us is greater than \$1. The truth is otherwise.

Recent works by Gregory Mankiw and Martin Feldstein at Harvard demonstrate the cost to the economy of an additional \$1 of tax for the government to spend can be as high as \$5 and is almost always at least \$2. First, there is the \$1 in tax paid, and then there is another \$1 or more in lost income and jobs the economy would have produced but for the tax. The further ugly truth is that the deadweight economic loss falls mainly on low- and middle-income wage earners.

Most government activities and expenditures have a degree of utility greater than zero -- some substantially so -- but if each one of the \$3 trillion in the federal budget were treated as the last dollar spent (and the true costs of paying for it were publicly acknowledged as at least \$2), it is certain that much federal spending would be eliminated by popular demand. On the discretionary side of the budget, when \$1 of government spending costs \$2 or more, and when government typically spends \$3 to do a \$1 job, the price tag for pork and other low-value projects becomes ridiculous.

Entitlement spending includes vast amounts of high-cost, low-value subsidies for the middle class and wealthy. This portion of the budget is already on track to force tax increases of such unprecedented magnitude that -- on a 2-for-1 basis -- the associated damage to the economy and living standards will be catastrophic. Big government must be downsized before it downsizes America permanently.

Picture a president who comes into office with a detailed plan for downsizing big government, and a coterie of experts capable of helping him carry it out. Also picture a president who assigns each Cabinet officer and agency head two tasks:

(1) Eliminate every function and cost not essential to performing the government's basic responsibilities.

(2) Perform those essential functions with less money.

Further picture an informed electorate that is, through interactive tools and calculators on the Internet, fully engaged in deciding how best to cut spending.

Voters will understand that spending cuts mean tax cuts and that tax cuts lead to economic growth and higher incomes. Extrapolating again from the works of Mr. Mankiw and Mr. Feldstein, a good rule of thumb is that a \$1 tax cut will induce at least an additional \$1 of income growth and sometimes \$2.

Because the extra income produced by tax cuts is itself taxed, big boosts to economic growth can be achieved in exchange for relatively small long-term reductions in government spending capacity. Mr. Mankiw's work shows that because a \$1 tax cut on dividends induces \$2 of extra income and 50 cents of tax revenue, the net long-term reduction in government's spending capacity is only 50 cents. Similarly, an across-the-board tax cut of \$1 -- which induces an extra \$1 of income growth and 25 cents of tax revenue -- could be paid for by only a 75-cent long-term spending cut.

The high ratio of benefit-to-cost when taxes are cut (as compared to the high ratio of cost-to-benefit when taxes are increased) will be especially important during the transition when lower-value portions of the federal sector spending are being replaced by higher-value private sector growth. America will be stronger, freer and more prosperous as a result.

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