CONTROLLING THE BUDGET

6. *Downsize the* **Domestic** *Budget and Cut Taxes*

***Congress** should*

- enact a balanced-budget amendment to the Constitution;
- establish a federal spending freeze at $1.65 trillion through 2002;
- pass a "peace dividend" tax cut by reducing income or payroll tax rates, or both;
- cancel all foreign aid—including Pentagon "peacekeeping" operations unrelated to protecting America's national security;
- eliminate corporate welfare spending programs;
- transform Medicare into a catastrophic coverage plan by gradually raising the deductible;
- allow medical savings accounts for all workers to reduce public and private health care inflation;
- increase the retirement age for Medicare and Social Security by three months per year for the next 24 years;
- end the federal role in welfare by devolving all public assistance programs to the states and private charities;
- terminate more than 100 major federal programs and agencies;
- terminate the U.S. Department of Transportation and repeal the federal gasoline tax, thus leaving highway, road, and transit responsibilities to the states and the private sector; and
- privatize at least $100 billion worth of federal assets and use the proceeds to lower the national debt and interest payments.

Introduction

In 1995 and 1996 the Republicans and moderate Democrats in the 104th Congress fought—at times valiantly—but ultimately lost the battle of the federal budget.

Despite hopeful rhetoric from the Republican majorities about balancing the budget by 2002 and despite impressive—though temporary—progress in reducing the 1996 deficit to $107 billion, the long-term prognosis for the budget of the U.S. government remains depressingly bleak. Federal expenditures, which took more than 200 years to surpass the $1 trillion mark 10 years ago, will have doubled to $2 trillion by 2002. The deficit is expected to gallop in the wrong direction in the coming years, hurdling the $200 billion mark by 2002 and the $300 billion mark by 2005.

Clearly, a new fiscal strategy must be employed if the budget is to be balanced and the U.S. economy restored to its full potential. That new strategy must recognize an unfortunate political reality: *in the absence of a balanced-budget amendment to the Constitution, Congress will never summon the political will power to balance the federal budget, or even come close to balancing the budget.*

For that reason, the crusade in recent years to balance the budget by 2002 without an amendment has been honorable but futile. The unilateral effort by the GOP and moderate Democrats to balance the budget by 2002 without a balanced-budget amendment has been a political trap—used by the spending lobbies all too successfully to block tax and spending cuts without having to propose a serious alternative deficit reduction agenda of their own. The mantra of "balanced budget by 2002" has also diverted public attention from the real fight of consequence, which is over the amendment itself. In other words, establish the rules of the game before making a move.

The 105th Congress should concentrate on cutting taxes and vulnerable spending programs wherever and whenever possible. The larger the spending reductions, and the larger the tax cuts that can be enacted, the better. The aim should be to halt the relentless expansion of the size of the federal empire. Public enemy number 1 in Washington, D.C., is *not* $110 billion of government borrowing; it is $1.65 trillion (and rising) of government spending.

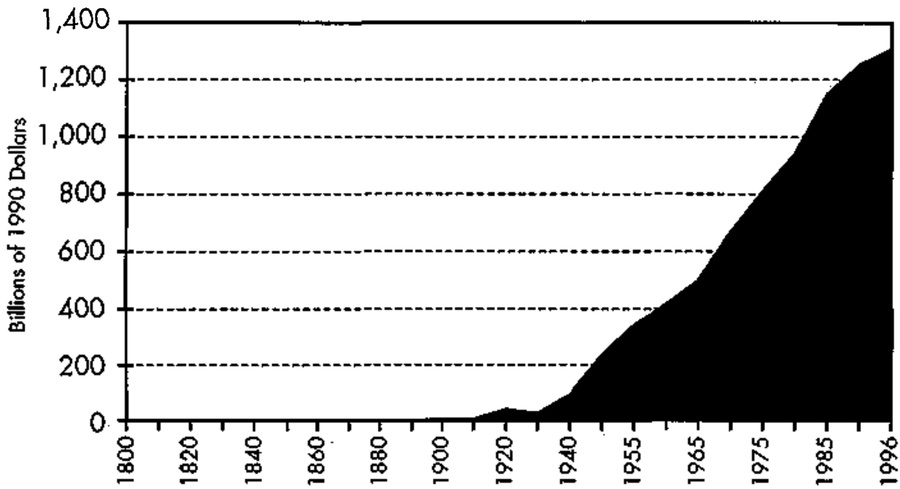
Is the Era of Big Government Over?

In his January 1996 state of the union address, Bill Clinton issued his memorable proclamation that "the era of big government in America is over." One month later the White House released its fiscal 1997 budget proposal, which called for a six-year *increase* in federal spending of roughly $300 billion. The Clinton administration has requested a total six-year budget of $11.2 trillion. That is twice as much money in constant dollars as the combined cost of fighting World War I and World War II. It is more money than the federal government spent cumulatively from 1800 to 1980.

The relentless media coverage of a "revolutionary" GOP budget with "massive and draconian budget cuts" conceals the reality of America's current fiscal predicament. The unreported truth is that the U.S. government is much larger today than was even imaginable in previous eras.

Figure 6.1 shows the expansion of the federal budget since 1800. Real federal outlays climbed from $100 million in 1800 to $8.3 billion in 1900 to $235 billion in 1950 to $1,510 billion in 1995 ($1.31 trillion in 1990 dollars). The federal government now takes 23 percent of gross domestic product, up from 18 percent in 1960 and 4 percent in 1930. Today's massive federal government no longer resembles in any way that established by the Founders, which gave Congress very limited spending authority.

Figure 6.1
Real Federal Outlays, 1800–1996



SOURCES: *Historical Tables: Budget of the United States Government, Fiscal Year 1997* (Washington: Government Printing Office, 1996), Table 1.1; and Bureau of the Census, *Historical Statistics of the United States, Colonial Times to 1970,* part 2, p. 1104, Series Y336.

The price tag for government has not risen just in Washington; it has risen at all levels—state, county, and city hall. Total government expenditures today exceed $2.6 trillion. That is roughly $25,000 in spending for every household in America. When the $6,000 per household cost of regulation is added to the price tag for the direct expenditures of the state, the government now reduces average household income by more than $30,000 per year. That is more than half of the income of the typical middle-income family.

No matter how we measure it, and notwithstanding Bill Clinton's proclamation to the contrary, the nanny state in America has never been bigger or better funded.

Where Did All the Money Go?

Table 6.1 highlights the tremendous growth rate of federal programs over just the last 45 years. Entitlements, no surprise, have been the real race horses of the budget. A federal entitlement, simply defined, is any program that says that Peter is entitled to Paul's money. The three major entitlements are Social Security, health care, and welfare.

- Social Security's budget has swelled from $25 billion to $336 billion. But mention the program in the context of budget downsizing and Reagan Republicans are the first to stampede for the exits.
- Federal health care outlays have catapulted from $2 billion to $272 billion—a 16,000 percent increase in spending.
- Welfare spending is up from $30 billion to $225 billion—even though poverty rates are no lower now than before the War on Poverty started.

What Washington refers to as "discretionary spending" has also experienced a surge in funding over the past four decades. Despite the rhetoric about Ronald Reagan's assault on social programs, virtually every civilian program has a far more bloated budget today than it did 10, 20, or 40 years ago. Since the 1950s, education and social services programs have grown from $2.5 billion to $56 billion. Community development is up 1,600 percent, science and technology are up 4,000 percent, and transportation is up 500 percent.

Here is one way of conceptualizing the expansion of the government. If nondefense spending had risen at only the pace of defense spending over the past 40 years, total expenditures would have been $800 billion—or about half the amount that has actually been spent. America would now have a $600 billion budget surplus rather than a $110 billion deficit.

Table 6.1
Federal Spending Growth by Function, 1950-96

	1950	1996	
	(millions of 1987 dollars)		Change (%)
National defense	83,990	197,675	135.4
Veterans benefits and services	54,064	28,099	-48.0
International affairs	28,599	11,039	-61.4
Income security	25,073	169,973	577.9
Agriculture	12,540	5,745	-54.2
Energy, natural resources, and environment	10,006	18,436	84.2
Commerce and housing credit	6,334	-7,998	-226.3
General government	6,034	10,116	67.6
Transportation	5,918	29,603	400.2
Social Security	4,780	261,221	5,365.2
Health and Medicare	1,640	222,418	13,460.9
Education, training, employment, and social services	1,475	40,294	2,632.0
Administration of justice	1,181	13,968	1,082.5
General science, space, and technology	337	12,563	3,632.3
Community and regional development	184	9,586	5,121.2
Net interest	29,449	179,439	509.3
Undistributed offsetting receipts and allowances	11,120	-31,707	185.1
Total outlays	260,477	1,170,471	349.4

SOURCE: *Historical Tables: Budget of the United States Government, Fiscal Year 1997* (Washington: Government Printing Office, 1996), Tables 3.1 and 10.1.

Lessons Learned in the Bush-Clinton Era

America has now completed eight years of what may be described as the "Bush-Clinton era." The defining domestic policy events of George Bush's and Bill Clinton's presidencies were the 1990 and 1993 budget deals, respectively. Budget analysts across the political spectrum agree that the major components of those two five-year budget packages with large tax increases were nearly indistinguishable. Both were dramatic departures from the economic strategy of the 1980s, which included cutting tax rates, preventing new regulations, and restraining domestic spending.

We should have learned the following fiscal lessons from the Bush-Clinton fiscal-economic strategy.

Tax Hikes to Balance the Budget Are Counterproductive

The top marginal income tax rate has risen by 50 percent—from 28 percent in 1989 to 42 percent this year. Yet, as Table 6.2 shows, overall tax receipts grew at a faster rate (24 percent) in the seven years (1982-89) following the Reagan tax cuts than they will have (19 percent) in the seven years following the Bush-Clinton tax hikes (1990-97). In fact, if tax revenues had continued to rise in the 1990s at the pace they did in the 1980s, the deficit would be $50 billion lower this year. Even receipts from the income tax (rates were cut in the 1980s and raised in the 1990s) rose at virtually the same pace in the Reagan years (16.1 percent) as they have in the Bush-Clinton years (16.8 percent).

Table 6.2
Reagan Tax Cuts vs. Bush-Clinton Tax Hikes: Overall Real Revenue Growth (billions of 1990 dollars)

After Reagan Tax Cuts			After Bush-Clinton Tax Hikes		
Year	Revenue Growth	(%)	Year	Revenue Growth	(%)
1982	738		1990	914	
1983	684	-7.3	1991	895	-2.1
1984	730	6.7	1992	895	0.0
1985	777	6.4	1993	922	3.7
1986	790	1.7	1994	982	6.5
1987	854	8.1	1995	1,034	5.3
1988	877	2.7	1996	1,082	4.6
1989	916	4.4	1997	1,090	0.7
Total		24.1	Total		19.3

SOURCES: *Historical Tables: Budget ofthe United States Government, Fiscal Year 1997* (Washington: Government Printing Office, 1996); and Congressional Budget Office, August 1996 revenue forecast (for growth in 1996, 1997, and Bush-Clinton total).

Nondefense Spending Has Rapidly Accelerated in the 7 990s

It is a widespread myth that federal outlays on civilian programs have been constrained as a result of the 1990 and 1993 budget deals. *Federal spending on civilian programs now accounts for a larger share of national output (18 percent) than at any previous time in American history.* In 1995 dollars, federal nondefense spending has surged by $250 billion since the end of the Reagan presidency.

Social Welfare Programs Are Growing at an Unsustainable Pace

In constant 1995 dollars, since 1989 real Medicare spending has grown by $75 billion, or 73 percent; Medicaid spending has grown by $47 billion, or 112 percent; and welfare spending has climbed by $93 billion, or 72 percent (see Table 6.3). If the current pace of growth in entitlement spending continues, by 2015 entitlements will eat up all federal revenues.

Table 6.3
Social Welfare Spending 1989–95
(billions of 1995 dollars)

	1989	1995	Growth 1989-95 (%)
Low-income support			
Aid to Families with Dependent Children	13	18	38
Child nutrition programs	8	9	12
Earned Income Tax Credit*	6	15	150
Food stamps	17	26	53
Housing assistance	12	21	75
Medicaid	42	89	112
Supplemental Security Income	15	24	60
Unemployment compensation	17	21	26
Total low-income support	130	223	72
Medicare	103	178	73
Social Security	210	252	20
Total	443	653	48

SOURCE: Cato Institute calculations based on data from *Historical Tables: Budget of the United States Government, Fiscal Year 1996* (Washington: Government Printing Office, 1995), Table 8.6, p. 108.
*Includes only outlay portion of EITC.

The Temporary Reduction in the Deficit Has Been Almost Exclusively a Result of Post-Cold War Reductions in the Military

Defense spending now constitutes a smaller share (17 percent) of the federal budget than at any time in American history. Over the past eight years the Pentagon budget has fallen by almost $110 billion in real terms. That's almost precisely how much the real budget deficit has fallen over that period. The defense cutbacks, which ought to be continued, have helped camouflage the large nondefense spending increases in the 1990s.

The 1990 and 1993 Budget Deals Were Failures

Table 6.4 shows that, from 1990 to 1995, the national debt was $622 billion higher than anticipated in January 1989 when Reagan left office. As a share of GDP, the budget deficits were nearly 2 percentage points higher than anticipated. Measured in real dollars, the 1990-94 period showed the worst five-year deficit performance in the post-World War II era.

The budget picture has clearly brightened in the short term under Bill Clinton. The 1996 budget deficit came in at a 20-year low of $107 billion and 1.9 percent of GDP. That was good news. Most of the improvement was a result of the (temporary) spending restraint imposed by the 104th Congress and the shutdown of the government in late 1995. In April 1995, just before the 104th Congress's budget was drafted, the Congressional Budget Office predicted a Clintonomics baseline deficit for 1996 of $210 billion.

Table 6.4
Deficits in the 1990s
Reagan Baseline vs. Actual Performance

	CBO 1989	Actual	Difference
		Billions of Dollars	
1990	141	221	80
1991	140	269	129
1992	135	290	155
1993	129	255	126
1994	122	203	81
1995	110*	161	51
Total	*111*	1,399	622
		Percentage of GDP	
1990	2.6	4.0	1.4
1991	2.4	4.7	2.3
1992	2.2	4.9	2.7
1993	2.0	4.1	1.9
1994	1.7	3.1	1.4
1995	1.5*	2.4	0.9
Average	2.1	3.9	1.5

SOURCES: Congressional Budget Office, "Economic and Budget Outlook," January 1989; and Congressional Budget Office, "Economic and Budget Outlook," March 1990 (for 1995 projections).

Economic Growth Is a Necessary Condition for Deficit Reduction

The U.S. GDP has grown at an average rate of just 1.8 percent in the 1990s. That compares with a 3.2 percent growth rate in the 1980s and a 4.9 percent growth rate in the 1960s. Even during the cyclical recovery since the end of the 1990-91 recession, economic growth has averaged below 3 percent per year. If economic growth in the 1990s had kept pace with growth in the 1980s, national output would be $510 billion higher today and the budget deficit $100 billion lower. If current trends continue, the 1990s will produce the largest budget deficits and the slowest economic growth rate of any decade in the past half century.

The Fiscal Legacy of the 104th Congress

The 104th Congress promised a dramatic change in budget and tax policy in Washington. Was that promise kept? The first-year budget enacted by the GOP-controlled Congress for FY96 was an impressive accomplishment by Capitol Hill standards. The 1996 budget deficit was chopped to $107 billion—$100 billion less than the Clinton budget plan would have produced. Federal spending grew by only 3 percent—the slowest rate of increase since 1982.

But the 1997 budget was an embarrassing fiscal retreat for the GOP. Most of the spending programs whose budgets were cut in 1996 saw spending restored in 1997. Congress added about $15 billion of spending to accommodate Clinton administration demands. The power of the purse in 1997 was handed to the White House.

In sum, two years after the Republicans took control of Congress, the budget closely resembles the one the GOP inherited. Congress still is appropriating funds for failed social programs, such as the Legal Services Corporation and the Low-Income Home Energy Assistance Program; for programs that politicize our culture in ways that many Americans find objectionable, such as the Corporation for Public Broadcasting and bilingual education; for corporate welfare handouts including the Export-Import Bank and the Small Business Administration; for New Deal-era programs that lost their purpose in life at least a generation ago, such as the Rural Electrification Administration, the Tennessee Valley Authority, and the Davis-Bacon Act; and for Clinton's new generation of muddle-headed social policy initiatives, such as midnight basketball, the Goals 2000 program intended to federalize public school standards and curricula, and the $7.25 an hour Americorps "volunteer" program. Not a single cabinet-level agency was shut down.

Even the 1996 progress in deficit reduction appears to be short-lived. The CBO reported in August that, after 1997, the budget outlook steadily deteriorates in every year for the next decade and the deficit reaches $350 billion. Then the outlook really turns grim, as runaway entitlement expenditures—particularly for Medicare and Medicaid—hemorrhage. The CBO predicts that, unless income transfer payments are curtailed, the nation faces a future of "unsustainably high levels of federal borrowing," with the national debt ascending relentlessly from 60 percent of national output today to 150 percent by 2025.

13 Steps to Smaller Government

The fight in recent years in Washington over how to balance the budget has been a diversion from the vital task of cutting back on the size of government and giving more money and power back to workers, businesses, and families. "The true cost of government," Milton Friedman reminds us, "is not the amount it borrows, but the amount it spends." Around the world we see governments—out of economic necessity—shedding their most burdensome and unproductive state activities. In the United States today, we have a moral, constitutional, and economic imperative to reduce the size and scope of government. That can be accomplished through 13 steps.

Enact a Balanced-Budget Amendment to the Constitution

Why is it necessary to amend the Constitution and command Congress and the president to do what they once felt honor bound to do?

There are many flawed arguments for a balanced-budget amendment. For example, Republicans were wrong when they argued in 1995 that deficits per se crowd out private investment and lead to higher interest rates. In the 1980s the deficit rose rapidly and nominal interest rates fell rapidly. In the Clinton years the deficit has fallen and interest rates have risen. *Government spending, not government borrowing, crowds out private saving and investment.*

Many liberals, including just-retired Democratic Sen. Paul Simon of Illinois, argue that the budget should be balanced because federal interest payments are crowding out other expenditures in the budget. There is no evidence of that crowding-out effect. Federal spending has been climbing rapidly over the past six years even as interest expenditures have continued to reach all-time highs. If it were true that interest expenditures crowded out other spending in the budget, that would be a benign impact of budget deficits.

Conservative and liberal arguments *against* the desirability of requiring a balanced budget are even more fallacious. One flawed argument against balancing the budget offered by many liberal economists is that a balanced-budget requirement would prevent Congress and the president from using fiscal policy as a tool for stabilizing the economy. The evidence over the past 40 years suggests that fiscal policy has been more destabilizing than stabilizing. Even under the Keynesian model, the idea is to run budget deficits during recessions and surpluses during recoveries. Over the past quarter century Congress has run record deficits in good times and bad.

Many conservatives are misguided when they claim that a balanced budget would lead to higher taxes. The flaw in the thinking here is that it ignores the fact that the deficit *is* a tax. Deficits are simply deferred taxes. If conservatives truly believe that government is too big and costs too much, then it is very unlikely that voters will be willing to pay $200 billion more in taxes each year—or roughly $2,000 per household—to pay for the $1.6 trillion federal budget. More likely, they will demand substantial reductions in federal spending. (The tax consumers in Washington fully understand that, which is why every spending constituency from the Children's Defense Fund, to the American Association of Retired Persons, to major defense contractors opposes the balanced-budget amendment.) And if the balanced-budget amendment leads to less spending, then the true tax burden on the American economy will decline, not rise.

There are two reasons why budget deficits should be eliminated and then permanently constrained via a constitutional prohibition, one practical and one moral. The practical reason why budget deficits are harmful is that deficit finance is a hidden form of taxation. Federal borrowing injects a huge pro-spending bias into the budget process by allowing politicians to pass out a dollar of government spending to voters while only imposing 80 cents of taxes on them. Because the deficit is largely an invisible tax, voters demand more government than they otherwise would. Outlawing federal borrowing means that Congress has to raise a full dollar of taxes today for every dollar of spending it undertakes. That will substantially increase voter hostility to government spending.

The moral argument for requiring a balanced budget is that federal borrowing is a form of fiscal child abuse. Current deficit spending must be paid for eventually by future generations—that is, by those who have no say in the current political process. In sum, a balanced budget should become a constitutional requirement, because running deficits is the ultimate form of taxation without representation. That is why Thomas Jefferson argued that "each successive generation ought to be guaranteed against the dissipations and corruptions of those preceding, by a fundamental provision in our Constitution."

Many contemporary critics of the balanced-budget amendment contend that the amendment is not needed to balance the budget, just greater political will power. But it is precisely because Congress will never exhibit such will power that we need the amendment.

The unwillingness of Congress in modern times to balance the budget is not so much a result of malevolent behavior on the part of legislators as it is a rational response to the rules of the budget game. Those rules establish incentives that offer political rewards for spending money, which far outweigh the political rewards for saving money. The benefits of government spending are provided to narrow interests, but the cost of any individual government program is so widely disbursed that the burden on any individual taxpayer is unnoticeable. For example, during the 104th Congress, the advocates of public broadcasting lobbied furiously and effectively to save their program from the budget knife by arguing that those funds cost the average household just X per month. (Of course, there are thousands of similar programs, each of which individually costs the American household *just X* per month.) But the cost of spending programs is even more politically inconsequential when it can be shifted to future generations who cannot vote. (That is also a practical argument for term limits.)

So it should be clear, given the fiscal outcomes of the past quarter century, that without a balanced-budget amendment, there will probably never again be a balanced budget. Every other device that has been tried to eliminate federal red ink has failed: four budget deals since 1980, Gramm-Rudman-Hollings I and n, and the 104th Congress's short-lived crusade. The balanced-budget amendment is dismissed by some as a gimmick. If that were true, Congress would have adopted it long ago.

One final note on the amendment. It would be best to include a provision that would limit taxation or require a supermajority vote of Congress to raise taxes, but with or without such a provision, the amendment is urgently needed. If the only remaining objection is that Social Security is now included in the unified budget, then for purposes of getting the amendment passed, Social Security should be excluded. That is a concession worth making in order to secure final passage, especially because excluding the Social Security system would only require even deeper spending cuts.

Enact a Six-Year Spending Freeze

In 1997 the federal budget will reach $1.65 trillion. That is the most ever spent by any government in world history. This *Handbook* contains a series of budget recommendations that altogether would cut the budget roughly in half. That may seem unimaginable, but even if the budget were halved tomorrow, the federal government would still consume a greater share of national output (12 percent) than it has throughout most of American history.

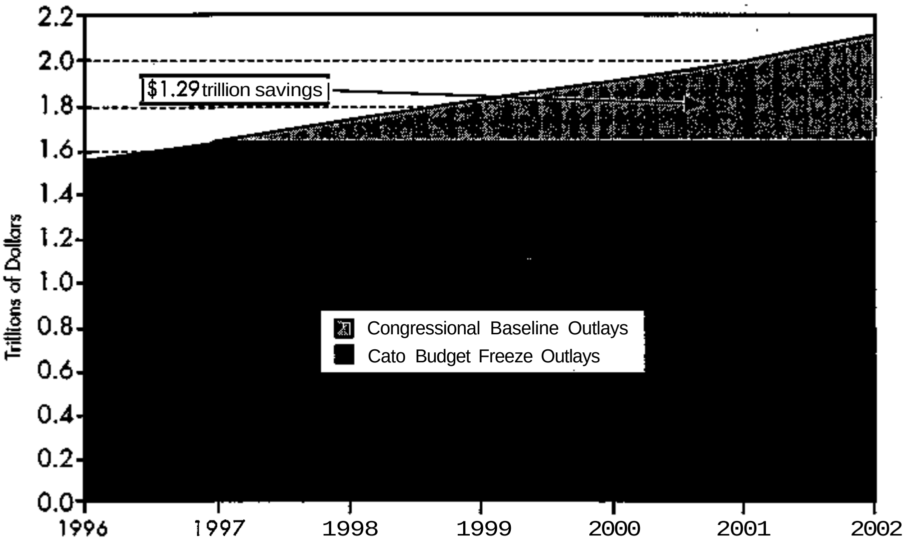
One common-sense tactic for beginning to limit federal spending is to at least stop its growth. For the past quarter century the federal budget has grown on average by more than 7 percent per year—or about twice as fast as inflation. Even the first Republican Congress in 40 years, elected on the promise of smaller, less intrusive government, approved budgets that grew by 4 percent per year.

Given the federal government's nearly bankrupt state and the low rate of return Americans receive from their tax dollars sent to Washington, why should government grow at all over the near term? If the federal budget cannot be cut in absolute terms, as it should be, Congress should at least place a ceiling on total expenditures at the current level. Figure 6.2 and Table 6.5 show that the cumulative savings for the next six years from a budget freeze would be $1.3 trillion relative to the budget path that we are now on.

Locking in a spending freeze, as has been proposed by the National Tax Limitation Committee, would certainly force tough choices on Congress. Lawmakers would have to establish spending priorities and live within a genuine budget—as most Americans define the term. A freeze would invoke fierce but healthy competition among agencies for federal dollars and create a kind of "reverse log-rolling" effect in Congress. Outlays for favored programs could be increased, but other agencies would have to be cut or eliminated to accommodate the expansion. Many obsolete programs would almost certainly have to be abolished altogether to force spending under the ceiling. Legislators would be compelled to tame the huge entitlement programs of Social Security, Medicare, and Medicaid, because if those programs were not restrained, all other programs in the budget would have to shrink rapidly.

The spending constituencies in Washington would, of course, loudly protest a spending freeze. They would argue that it requires a scorched-earth budget policy, squeezing out funding for vital programs. Fiscal conservatives will need to make the case that the government should be

Figure 6.2
Savings from Proposed Spending Freeze



SOURCES: Congressional Budget Office, "Economic and Budget Outlook Update," August 1996; and Office of Management and Budget, July 1996 revenue forecasts.

Table 6.5
Savings from Proposed Spending Freeze
(trillions of dollars)

	1996	1997	1998	1999	2000	2001	2002	Total
Baseline outlays	1.57	1.65	1.72	1.81	1.90	1.99	2.11	12.75
Budget freeze outlays	1.57	1.64	1.65	1.65	1.65	1.65	1.65	11.46
Savings	0	.01	.07	.16	.25	.34	.46	1.29

SOURCES: Congressional Budget Office, "Economic and Budget Outlook Update," August 1996; and Office of Management and Budget, My 1996 revenue forecasts.

easily capable of doing everything it is supposed to do with $1.65 trillion a year. Most businesses and households have managed to do more with less for the past five years as budgets have been pinched. Why should government be immune from the belt tightening?

But can it really be done? Contrary to the conventional wisdom, there is no law of nature, or economics, or politics that requires the federal government to grow every year. During most postwar eras in the United States (we are in one now), the federal budget has declined in size. For example,

- In 1919, the last year of World War I, the federal budget climbed to $18.5 billion. By 1926 it had fallen to $2.9 billion.
- In the seven-year period from 1945 (the peak of spending for World War II) to 1951, the U.S. government's budget tumbled by half, from $93 billion to $42.4 billion.
- During the Korean War the federal budget rose to $76 billion in 1953. By 1955 it had fallen to $68 billion.

The typical pattern in each of those postwar eras was the same: as military expenditures fell, wartime tax burdens were cut and the budget was moved quickly back into balance. We even ran budget surpluses to begin paying off the wartime debt. None of those things has happened since the Berlin Wall came down and the Soviet Union was dissolved. There has been no tax cut, no retirement of the debt, and no balanced budget. Contrary to historical precedent, since the Berlin Wall came down, the federal budget has actually increased by $350 billion. A spending ceiling would end the insidious practice of using defense savings to hike the budgets of domestic agencies.

Enact a $1 Trillion "Peace Dividend" Tax Rate Cut

The total savings of $1.3 trillion from a spending freeze would produce a balanced budget by 2002 and provide a fiscal dividend large enough to pay for a $1 trillion tax cut, as shown in Table 6.6. But a large tax cut should be enacted irrespective of what steps Congress pursues on the expenditure side of the budget.

Seven years after the Cold War ended, it is time for the peace dividend tax cut that Americans should have received in the early Bush years. A six-year $1 trillion tax cut is roughly 1.5 percentage points of GDP, or about half the savings already generated from the military downsizing since 1987 (3 percentage points of GDP).

A $1 trillion six-year tax cut would reduce static revenue collections by 10 percent, or $1 trillion out of a $10.03 trillion tax take over the next six years. That is more than twice as large as the Republican tax proposal and five times as large as the president's.

A large tax cut is critical to any government downsizing strategy. Every dollar of taxes that is not sent to Washington is one less dollar for Congress

Table 6.6
Spending freeze with Tax Cut Would Balance the Budget

	1996	1997	1998	1999	2000	2001	2002	Total
				Trillions of Dollars				
Outlays with budget freeze	1.57	1.64	1.65	1.65	1.65	1.65	1.65	11.46
Revenues with tax cut	1.46	1.35	1.38	1.43	1.50	1.56	1.67	10.35
Deficit	.11	.29	.27	.22	.15	.09	-.02	1.11
				Percentage of GDP				
Outlays	21.0	21.0	20.8	19.9	18.9	18.0	16.8	
Revenues	19.1	17.0	16.6	16.4	16.4	16.3	16.8	
Deficit	1.9	4.0	4.2	3.5	2.5	1.7	0.0	

SOURCES: Congressional Budget Office, "Economic and Budget Outlook Update," August 1996; and Office of Management and Budget, July 1996 revenue forecasts.

to spend. The evidence of the past 40 years indicates overwhelmingly that an increase in federal revenues incites more government spending, not less government debt. Federal revenues are *positively* correlated with the subsequent size of the deficit rather than negatively correlated. If taxes are cut, spending will be more restrained than otherwise. Richard Vedder has shown in a Joint Economic Committee study that every dollar of new taxes in the post–World War n era has led to $1.59 in new spending. Paradoxically, large tax cuts will facilitate the long-run effort to balance the budget, rather than impede it.

Reductions in marginal tax rates can also improve the performance of the economy and thus reduce the relative burden of government spending and deficits on the productive private sector. Marginal tax rate cuts in the 1920s, 1960s, and 1980s corresponded with substantial increases in growth and employment. Since faster economic growth is virtually a precondition for balancing the budget—if the economic growth rate were increased by 1 percentage point between 1997 and 2002, half of the budget deficit would automatically disappear—pro-growth tax cuts will enhance the prospects for a balanced budget that remains in balance. The converse is also true. If the economy continues to trudge forward at 2 to 2.5 percent per year, the federal budget may never reach balance.

The tax cut should not be a $500 tax credit, as has become part of Republican dogma in recent years. Rather, it should be aimed at reducing income or payroll tax rates, or both. That might involve one of three choices:

- an across-the-board 30 percent reduction in personal income tax rates;
- an income tax credit for all payroll taxes paid by the employee, as proposed by Sen. John Ashcroft (R-Mo.); or
- a flat tax or a national sales tax to replace the income tax at a rate below 20 percent.

Replace Foreign Aid with Free Trade

The federal government officially spends about $14 billion a year on bilateral and multilateral aid to other nations. Much of that money is contributed to the United Nations, the World Bank, and the International Monetary Fund. Israel and Egypt each receive more man $2 billion a year in U.S. foreign aid—even though Prime Minister Benjamin Netanyahu recently hinted to Congress that Israel might be better off without the cratch of welfare checks from the U.S. government.

Supporters of aid programs argue that the price tag is less than 1 percent of the total U.S. budget and thus fiscally inconsequential. But $14 billion is more than is paid in federal taxes by every family in the states of Delaware, Kansas, Maine, and New Hampshire. Moreover, the real foreign aid budget is probably closer to $100 billion—when much of the cost of NATO and other Pentagon "peacekeeping" activities that are wholly unrelated to protecting national security is factored in.

After tens of billions of dollars of U.S. taxpayer funding of aid programs over the past 40 years, there is not a scintilla of evidence that they have had any positive effect in promoting economic development. Much of the money is devoted to causes, such as population control, that are at best irrelevant to economic development. Cato scholars Doug Bandow and Ian Vásquez argue persuasively in their book *Perpetuating Poverty* that America's foreign aid programs do real harm to developing countries by rewarding economic failure and diverting policymakers' attention from the real path to prosperity, which is to adopt free-market reforms. Misguided IMF policy advice led up to the peso devaluation in Mexico. In other developing nations the IMF and the World Bank have urged policymakers to raise taxes to close budget deficits—which is exactly the wrong fiscal prescription.

All U.S. bilateral and multilateral foreign aid should be terminated immediately. Private capital will flow to nations that lower tax rates, promote free trade, shed the welfare system, deregulate, and protect private property rights. U.S. economic development assistance to developing countries should be based on a simple principle: trade, not aid. We should be exporting our products and our democratic institutions to poor nations, not our tax dollars.

End Corporate Welfare As We Know It

The federal government currently spends $75 billion a year on direct subsidies to business. If all federal assistance to business were purged from the budget, deficit spending could be cut in half. Alternatively, if Congress were to eliminate all corporate spending subsidies, the savings would be large enough to entirely eliminate the capital gains tax and the federal estate tax. Reducing the deficit or eliminating those anti-growth taxes would do far more to benefit American industry and U.S. global competitiveness than asking Congress to pick industrial winners and losers. Then-senator Bill Bradley's attack on the corporate welfare state was accurate: "The best way to allocate resources in America is through a market mechanism. Tax and direct-spending corporate subsidies impede the market's functioning for non-economic, special interest reasons."

Last year both Congress and the Clinton administration pledged to shrink the corporate safety net. Those promises went largely unfulfilled. In 1995, for example, the corporate welfare budget was reduced by just 16 percent. In 1996 the cuts were even smaller.

Most expensive corporate subsidy programs continue to receive generous allotments of taxpayer dollars. Those programs include the Agricultural Research Service; the Conservation Reserve Program; the International Trade Administration; fossil energy research and development; the Bureau of Reclamation; the Office of Commercial Space Transportation; the Overseas Private Investment Corporation; the Export-Import Bank; the Agriculture Department's Market Promotion Program, which subsidizes the foreign advertising of U.S. corporations such as Pillsbury, Dole, and Jim Beam; and techno-grant programs, such as the Advanced Technology Program.

The villain in corporate welfare is government *spending,* not tax deductions. Tax provisions that are universally available to all companies and industries, such as faster write-offs of capital equipment or the advertising deduction, are *not* corporate welfare at all. To the extent the tax code contains unjustified tax favors carved out for specific industries or firms, the loopholes should be closed in conjunction with overall reform or elimination of the income tax.

The 105th Congress should immediately enact a budget rescission spending bill, perhaps titled "The Corporate Welfare Elimination Act," terminating a minimum of 40 to 50 business subsidy *spending* programs and close down the Departments of Commerce and Energy. Savings of at least $200 billion over six years should be targeted. The bill should be crafted in a bipartisan fashion by identifying those programs that have been recommended for extinction by groups such as the Cato Institute, the Heritage Foundation, the Progressive Policy Institute, and even in some cases the Nader group Essential Information. Many Republican deficit hawks, such as Rep. John Kasich of Ohio, Sen. John McCain of Arizona, and Sen. Spencer Abraham of Michigan, have made reductions in corporate subsidies a crusade. They should join with prominent Democrats who have also made good-faith efforts to reduce business aid, including Sen. Russ Feingold of Wisconsin and Reps. Charles Schumer of New York and Joe Kennedy of Massachusetts.

A fair and balanced budget-downsizing strategy should not spare politically well connected K Street special interests. Eliminating aid to dependent corporations adds credibility to Congress's equally vital agenda for ending failed social welfare programs. Both the social welfare and corporate welfare states need to be eliminated.

Gradually Convert Medicare into a Catastrophic Insurance Program

There is a health care crisis in America, but it is a crisis primarily driven by the runaway inflation of the two major government programs, Medicare and Medicaid, that provide subsidized health care to more than 60 million Americans. Since 1988 Medicare and Medicaid have been growing at a 12 percent annual rate. The CBO predicts a 10 percent growth rate in federal health spending over the foreseeable future. Medicare and Medicaid will consume nearly $400 billion by 2000. This stampede of government health inflation has occurred even as the rate of increase in private-sector health costs has fallen in recent years as employers have demanded greater cost sharing by their employees.

Admittedly, revamping Medicare and Medicaid won't be easy to do politically. Republicans in the 104th Congress stepped on a hornets' nest when they proposed relatively modest cost-saving reforms to Medicare. The tragedy of the GOP misadventure with Medicare in 1995 and 1996 is that Gingrich and company took the heat for trying to fix the program, but they endorsed solutions that did not fundamentally scale back the program in ways that would have gradually reduced senior citizens' reliance on government for health care.

Even more than Social Security, Medicare is a national financial time bomb. Its rapidly escalating costs will add $100 billion to the deficit by 2000 alone. The long-term unfunded liability of the system is $7.9 trillion—larger than the national debt and larger than the celebrated liability of Social Security.

The long-term goal for Medicare should be to convert what is now an unjustifiably generous, first-dollar-coverage prepaid health plan for seniors into a catastrophic insurance "safety net" program. The Part B deductible for Medicare (physician costs) is currently an absurdly low $100. If that had been indexed to medical inflation since the program was created 30 years ago, the deductible would be $400 today. The deductible for Part A (hospital stays) is $716, but most seniors have medigap insurance to cover the deductible and other copayments, so their out-of-pocket costs are often negligible.

The way to convert Medicare into a catastrophic coverage plan is to raise the Part A and B deductibles over time. Seniors should be responsible for covering the cost of routine medical expenses by paying out of pocket or purchasing medigap insurance. (Ideally, when medical savings accounts, described below, are made available to all workers, seniors too should be permitted to create tax-free accounts for expenses up to $3,000.) The goal for Medicare should be to increase the combined deductible to $3,000 in 1996 dollars as quickly as possible.

One way to make the restructuring of Medicare politically salable is by income testing. For example, the combined payments under Part A and Part B of Medicare could first be set at 1.5 percent of adjusted gross income (AGI) and then increased 1.5 percentage points each year for four years. Thus, beginning in 2001, the deductible would be 7.5 percent of AGI, the same rate that is now in the individual income tax code. Payments above the deductible, in most cases, would be fixed payments to the patient per illness or accident. A senior with an income above $40,000 would pay a total deductible of $3,000. Seniors would have the security of being financially protected for the cost of major illnesses or extended hospital stays. But a basic inequity in the health care system would be redressed. Mostly nonworking, senior citizens—the wealthiest age group in America—would no longer receive a Cadillac health insurance plan paid for out of the paychecks of relatively lower income working Americans.

Change the Tax Treatment of Health Insurance to Allow Tax-Free Medical Savings Accounts (MSAs) as a Way to Reduce the Inflation in Private and Public Health Care

In 1994 President Clinton's national health plan was soundly rejected by the voters and by Congress. Yet in the last two years, Clinton and the Republican Congress moved us incrementally toward a national health system. Unless an alternative free-market health plan is embraced soon by Congress, America will end up with a Clinton-style socialized medicine plan by the end of the century.

Thirty years of experience have taught us that a larger direct federal role in health care will almost certainly have three effects: (1) it will send medical costs soaring for everyone; (2) it will lead to a deterioration in the quality of care to which Americans have access; and (3) it will bust the federal budget.

Probably the only viable defense against a national health insurance system—under which all Americans are required to purchase uniform insurance directly or via the government and under which those with healthy lifestyles are forced to subsidize those with unhealthy lifestyles—is to make tax-free medical savings accounts (MSAs) widely available as quickly as possible. The Kennedy-Kassebaum law enacted last year provides for. a limited MSA pilot project. MSAs should be made available to all individuals and businesses that wish to participate.

MSAs have the ultimate effect of personalizing health insurance. Under this plan, each worker is allowed to put, say, $3,000 per year tax-free into an MSA, which works much like an individual retirement account for health care. (This could be implemented at the same time that conventional employer-provided health insurance tax incentives are limited or eliminated altogether.) The worker (through the employer or on his or her own) then purchases a catastrophic health insurance plan for expenditures above $3,000. For expenditures below $3,000 the worker pays the hospital or doctor directly out of his or her MSA. If the patient incurs more than $3,000 in health costs during the year, then his catastrophic insurance coverage kicks in to pay the rest. If the worker spends less than $3,000, he gets to roll the money into a regular individual retirement account, and the savings can be spent upon his retirement.

MSAs would once again make patients cost-conscious health care consumers. The primary reason that medical costs have been rising so rapidly is that the share of health care costs paid directly by the patient has declined from about 50 percent to about 20 percent since 1960. Over the same time period, total expenditures for medical care have increased from about 5 percent to 14 percent of GDP. That is no coincidence. Given the dominance of third-party payments, neither patients nor physicians have an adequate incentive to control the costs of medical care.

Where MSAs have been tested, they have reduced health costs because patients are now spending their own dollars when they go to the doctor or the hospital. Workers are rewarded for staying healthy and for avoiding placing extraneous demands on the health care system. If made available to all workers, MSAs would reduce the growth of the demand for medical care, the relative inflation of the price of medical services, and total private and public medical expenditures.

Raise the Retirement Age for Social Security and Medicare and Fix the Consumer Price Index

Social Security and Medicare, the two massive income redistribution programs for America's senior citizens, face a combined unfunded liability over the next 75 years of more than $13 trillion—according to the government's own trustees. That's twice the size of the current national debt. The combined annual budget for Social Security and Medicare is now more than half a trillion dollars. Social Security has passed defense to become the largest single program in the federal budget.

Over time, Social Security and more recently Medicare have been interpreted as a political contract between the working-age population and people who are now retired. That constrains the possibility of large savings—other than those described above—in the two programs in the near term. But it should not cause us to defer dealing with the long-term problems of the system—particularly because they are so massive and beyond dispute.

The ultimate solution for Social Security is to convert the government's one-size-fits-all program into a system of personal retirement accounts (PRAs) as described in Chapter 23. While that is being done, the 105th Congress should move immediately to accelerate the increase in the retirement age that is already scheduled for Social Security. Beginning in 1997 the retirement age (and early retirement age) should be raised by three months per year for the next 24 years. That would mean that the age at which one would receive full retirement benefits would be 66 in 2000, 67 in 2004, 68 in 2008, until the retirement age reached 71 in 2020. Workers could still retire at 65 but with reduced benefits.

Because of a quirk in current law, the Medicare retirement age is not scheduled to increase at all—despite the program's massive future deficits.

Without question, *my* increase in the retirement age for Social Security should apply to Medicare as well.

Incrementally increasing the age for receiving full benefits under those two old-age programs would be an equitable step toward cushioning the impact of the demographic time bomb that will explode in the next 20 years when the baby-boom generation begins to retire. Without a change in retirement age, the ratio of workers to retirees is expected to fall to less than 2 to 1 by the year 2030. Such a dependency ratio would place considerable strain on the economy and a larger burden on today's children—the next generation of workers. It is worth noting that if the retirement age for Social Security had been indexed to the increase in life expectancy since 1935, when the program was created, the age for receiving full benefits would today be 72.

Congress should also move immediately to fix the overstatement of inflation in the Consumer Price Index. A national commission headed by economist Michael Boskin will report soon that the CPI is overestimated by as much as one full percentage point a year. That means that increases in federal benefits, most important Social Security, that are indexed to inflation are exceeding the actual increase in the cost of living. The Boskin commission's recommendations for fixing the CPI should be adopted by Congress.

Devolve All Federal Welfare Programs to the States and Private Charities

Thirty years ago, when President Lyndon Johnson launched the War on Poverty, he declared that "the days of the dole are numbered." We have now surpassed day 10,000. Over that period, some $5 trillion has been spent on this war—more in current dollars than the cost of fighting World War II.

The federal government, along with the states and cities, spends an estimated $300 billion per year on anti-poverty programs. That is almost three times the amount that would be needed to lift every poor family above the poverty level. Still, the poverty rate in the United States remains extremely high and is no lower than when the avalanche of spending to prevent poverty began. As Charles Murray of the American Enterprise Institute emphasizes, "The tragedy of the welfare state is not how much it costs, but how little it has bought." The system does not work well for either the poor or the taxpayer.

The welfare state is fundamentally flawed because it rewards bad behavior—illegitimacy and family breakup and discourages good behavior—

work, marriage, and individual responsibility. A recent Cato study shows that welfare benefits are so high for the nonworking poor, and taxes are so high for the working poor, that a typical female head of a household that is on welfare and receiving public housing would, in most states, have to find a job that paid total benefits of $8.50 an hour to compensate for the loss of welfare benefits. By not working, the poor are not being lazy—they are simply responding to the monetary incentives that the welfare state has created.

The 104th Congress took the first positive step in 30 years to end the welfare state. The primary cash assistance program—Aid to Families with Dependent Children—will now be run by the states. The entitlement feature of the program has been ended in favor of an annually appropriated block grant. Eventually Congress should end the block grant and leave the funding to the states and the private sector. The bill also technically requires work after two years of assistance—but it remains to be seen whether the work requirement will be enforced and, more important, whether it will discourage illegitimacy and entry into the welfare system in the first place.

But AFDC is just one small brick in the modern welfare edifice. Washington now offers more than 60 means-tested programs to help the poor. Three of the most expensive "anti-poverty" programs are Medicaid, food stamps, and public housing. They too should now be returned to the states and, to the fullest extent possible, private charities.

Devolving welfare to the states would be advantageous for several reasons. First, it would allow states full flexibility in serving as innovators and laboratories to devise welfare programs that provide a basic safety net without rewarding destructive behavior. State governments have already begun to experiment with promising reforms in welfare. The most ambitious of those experiments, designed to get people off welfare and into jobs, have been adopted in Wisconsin under Gov. Tommy Thompson and in Michigan under Gov. John Engler. Devolution of welfare to the states would help quickly sort out approaches that work from those that do not. Second, interstate competition would force states to control bureaucratic costs, hold down benefit levels, and impose meaningful restrictions on eligibility—all things Washington has failed to do. Third, states are more likely to see the role of government as one of augmenting successful private charitable support systems, rather than supplanting them.

If welfare is not fully devolved to the states, a second-best option is to completely abolish all forms of welfare for able-bodied recipients—AFDC, food stamps, public housing, Medicaid, Supplemental Security Income, and the rest—and repeal the minimum wage and use part of the savings to expand the Earned Income Tax Credit. The EITC is the least harmful income support program because—unlike almost all other welfare assistance, which is predicated on the recipient's not working—the tax credit goes only to those who work. The EITC has the added benefit that it does not require a large welfare industry to deliver the benefits. Welfare providers have been the primary beneficiary and advocate of federal welfare programs.

Terminate Hundreds of Low-Priority Domestic Programs

Nearly $100 billion a year is spent on domestic programs that have been identified as candidates for termination by such independent agencies as the Congressional Budget Office, the General Accounting Office, the Grace Commission, and even by President Clinton himself in the budget submissions during his first term. They survive, not because they serve any national interest, but because of political or parochial considerations.

As noted above, the 104th Congress eradicated very few of those agencies. Although the House Appropriations Committee lists hundreds of programs terminated in 1995 and 1996, most were of minor budget consequence: the world-famous $500,000 daily ice delivery to the House of Representatives, the $12.5 million Cattle Tick Eradication Program, the $4.3 million Nutrition Education Initiative, the $148,000 House barber shop, the $30 million we've been spending each year for consumer and homemaker education, $1 million for Native Hawaiian and Alaskan cultural arts, and other such absurdities. The bigger fish got away. The original budget resolution crafted by House Budget Committee chairman John Kasich would have terminated 300 programs and closed down the Departments of Education, Energy, and Commerce. Unfortunately, Congress retreated from the plan.

The appendix to this chapter contains a list of recommended program terminations with a total annual taxpayer savings of $170 billion per year. What has been missing in recent years is a political strategy for eliminating those programs. In addition to attacking corporate welfare and foreign aid, as mentioned above, here are six more strategies that should be pursued:

Start *with the Easy Targets.* Many programs have almost no constituency outside of Washington, D.C., and thus should be relatively painless to zero out. Virtually all of the programs within the Department of Energy fall into that category, for example. Programs that incite public hostility, such as the National Endowment for the Arts and Goals 2000, also should be targeted for elimination.

Approve the Spending Cuts Contained in President Clinton's Budget. President Clinton's budgets have been lean in the spending reduction department, but they do call for the elimination of or substantial funding reductions for low-priority programs with annual savings of nearly $10 billion a year. Those programs include

- wastewater treatment grants
- nuclear reactor research and development
- HUD special purpose grants
- Small Business Administration grants and loans
- Impact Aid
- uranium enrichment programs
- selected student loan programs
- Agency for International Development
- international security assistance
- Appalachian Regional Commission

End Welfare for the Affluent. Many federal domestic programs primarily benefit Americans with above-average incomes. Examples:

- An estimated 40 percent of the $1.4 billion sugar price support program benefits the largest 1 percent of sugar farms. The 33 largest sugar cane plantations each receive more than $1 million. One family alone, the Fanjuls, owners of several large sugar farms in the Florida Everglades, captures an estimated $60 million a year in artificial profits thanks to price supports and import quotas (and to generous campaign contributions to both political parties).
- The wool and mohair subsidy program (now called the National Sheep Industry Improvement Center) at the USDA is supposed to help herders of small herds of sheep. The *Wall Street Journal* reported in 1995 that the third largest recipient of wool and mohair subsidies in Lincoln County, New Mexico, is none other than ABC's Sam Donaldson. Each year $97,000 in subsidy checks is delivered to his house in suburban Virginia. The *Journal* reported that millions of dollars of farm price support checks are delivered to "farmers" who live in cities.

- Amtrak riders—particularly on the Northeast Corridor routes—have average incomes *far* higher than the national median.
- Much of the money spent on the National Endowment for the Arts finances operas and art exhibits for wealthy clienteles in affluent areas. The beneficiaries can afford to pay for those programs themselves if they have value.

End Welfare for Lobbyists. Many federal programs fund nonprofit organizations that then use those tax dollars to lobby for more taxpayer dollars. Examples include the Legal Services Corporation, which funds legal aid centers that lobby for a larger LSC budget, and the Title X program, which funds Planned Parenthood. The American Association of Retired Persons, which has endorsed nearly $1 trillion in new federal spending, receives some $80 million a year in federal grants. And perhaps the worst abuser of all, the National Council of Senior Citizens, receives 96 percent of its budget from grants from the Environmental Protection Agency and other federal agencies, according to the Heritage Foundation's Government Integrity Project. To end the practice of taxpayer funding of lobbyists, Congress should enact legislation sponsored by Rep. Ernest Istook (R-Okla.) that would prevent organizations that receive any federal grants from lobbying. That restriction should apply to for-profit companies and nonprofit groups.

Create a Constituency for Spending Cuts by Coupling Tax Relief with Budget Reductions. Income tax cuts for families should be combined with cutbacks in programs and regulations designed to "help" families, such as day-care subsidies, Head Start, sex education funding, school lunch programs, the "family leave" bill, and so forth. A reduction in the capital gains tax should be paired with elimination of business subsidies.

Challenge the Constitutionality of Federal Spending Programs. Where in the Constitution does it say anything about Congress's having the power to spend money on swimming pools, Beef Jerky TV advertisements, parking garages, and midnight basketball leagues? The U.S. Constitution confines Congress's spending authority to a select few areas. The enumerated powers of the federal government to spend money are defined in the Constitution under article I, section 8. They include the right to "establish Post Offices and post roads; raise and support Armies; provide and maintain a Navy; declare War"; and fund other mostly national-defense-related activities.

The Constitution grants no authority for the federal government to run the health care industry, impose wage and price controls, provide job training, subsidize electricity and telephone service, lend money to business or foreign governments, require businesses to give their employees leave when they have a child in the hospital, or build football stadiums and tennis courts.

Much of this spending is erroneously defended under the general welfare clause of the Constitution. But as Cato constitutional scholar Roger Pilon explains, it is clear from a reading of history that the general welfare clause "was not meant to be a carte blanche for Congress to spend money, but rather was meant as a restrictive clause to prohibit any special interest spending which did not 'promote the general welfare.' " Thomas Jefferson was concerned that the general welfare clause might be perverted, and so to clarify its meaning he wrote in 1798, "Congress has not unlimited powers to provide for the general welfare, but only those specifically enumerated."

Members of Congress take an oath to uphold the Constitution. They should start taking that oath seriously. When dubious spending programs come before them for funding, they should first ask, Is there constitutional authority for Congress to appropriate this public money? In that way, Congress should establish a "constitutional veto" on federal spending that is clearly outside the bounds of the Constitution. For too long, Congress has simply asserted an unlimited power of the purse. That attitude has undermined the role of the Constitution. It has also helped inflame our current fiscal crisis.

Close the Department of Transportation and Repeal the Federal Gas Tax

The original rationale for the U.S. Department of Transportation was to build the interstate highway system. That was a legitimate federal function, since all U.S. citizens benefit from a coordinated network of interstate highways. The interstate highway system was completed 10 years ago. The vast majority of DOT funding is now spent on noninterstate highways, local roads, and urban transit systems. It makes no sense to collect the federal gasoline tax, send it to Washington, D.C., pass it through a federal bureaucratic maze at DOT, and then send it back to the states where the funds originated.

In transportation policy, the federal government has become not just a costly and unnecessary but also a meddlesome middleman. Until last year, states were forced to comply with a federal 55-mile-an-hour speed limit in order to get back their gas tax revenues from Washington. Federal highway funds come with other strings attached that inflate construction costs: the Davis-Bacon Act (requiring union wages on federal highway projects), minority set-aside programs, and buy-American provisions. Those add about 30 percent to the cost of federal construction projects and thus contribute to the decay of America's public infrastructure. Moreover, increasingly Congress uses the DOT budget as a pot of money from which to deliver pork-barrel projects that states would rarely fund if they were spending their own taxpayers' money.

All of the inefficiency and redundancy could be ended by closing down the DOT and repealing the 18.4 cent federal gasoline tax. States could then raise the gas tax themselves (as much as they wished) to pay for whatever road building and repair were needed. Eliminating the cost of the federal bureaucracy of 65,000 workers in Washington will cause construction and maintenance costs for highways, bridges, and transit systems to fall. Many governors have endorsed this idea as consistent with federalism and the Tenth Amendment.

Privatize Federal Assets

Government owns about one-third of all the land in the United States—and in most years it adds to its holdings by purchasing or confiscating properties. Under the Clinton administration, for example, hundreds of thousands of acres in California and Utah have been seized by Uncle Sam. Yet only a tiny fraction of the vast federal land holdings are of environmental or historical significance.

The market value of oil lands alone is estimated to be roughly $450 billion. Government also owns tens of billions of dollars worth of other assets, including mineral stockpiles, buildings, and other physical capital. Most of those assets are not put to productive use and thus yield little or no return to the taxpayers. Federal holdings that should be transferred to private ownership include

- nonenvironmentally sensitive federal lands
- federal oil reserves
- certain Amtrak routes
- the $250 billion federal loan portfolio
- the federal helium reserve
- public housing units
- federal dams

- the Naval Petroleum Reserve
- the air traffic control system

The 105th Congress should begin a campaign to privatize those and other unneeded federal assets with a goal of raising $25 billion a year. The funds raised from asset sales should be dedicated to retiring the national debt and reducing federal interest payments.

Conclusion

The Economist recently assessed the accomplishments of the 104th Congress. "Mr. Gingrich saw 1994 as marking a change in direction," the magazine wrote. "But the pattern of the half century argues otherwise. It shows a series of expansions of government's reach, punctuated by conservative pauses and corrections.'' Then government resumes its relentless rise.

Despite some notable early successes, the Republican-controlled 104th Congress made only slight progress in reversing the underlying trend toward bigger government in America shown in Figure 6.1. The federal government still consumes nearly one-quarter of national output. In the end, big government survived the GOP assault almost unscathed.

The challenge for the 105th Congress is to end the federal government's relentless rise in the 20th century. The goal is not primarily to balance the federal budget—though that is worth doing. The goal is to greatly shrink the federal budget—through a combination of tax and spending cuts.

The budget alternative presented here would dramatically reverse the trend of government expansionism. Table 6.6 shows that government spending and taxes as a share of national output would shrink to below 17 percent of output by 2002. In future years federal spending would be reduced to roughly 15 percent of GDP when all the budget recommendations were fully implemented. This is a budget blueprint that would make America freer and more prosperous entering the 21st century.

Appendix: Cato Institute List of Recommended Federal Program Terminations, FY96

Program	Amount (millions of dollars)
U.S. Department of Agriculture	
Economic Research Service	50
National Agricultural Statistics Service	80
Agricultural Research Service	800
Cooperative State Research, Education and Extension Service	900
Animal and Plant Health Inspection Service	400
Food Safety and Inspection Service	600
Grain Inspection, Packers and Stockyard Administration	20
Agricultural Marketing Service	500
Conservation Reserve Program	1,800
Federal Crop Insurance Corporation	2,000
Agricultural commodity price supports and subsidies	10,000
Natural Resources Conservation Service	1,100
Rural Housing and Community Development Service	1,700
Rural Business and Cooperative Development Service	100
Rural Electrification Administration subsidies	1,000
Foreign Agricultural Service	800
Market Access Program	100
Food stamps	
Children's nutrition subsidies for the nonpoor	1,000
Special Supplemental Food Program for Women, Infants, and Children	3,700
Commodity Credit Corporation export credit	200
Food donations programs for selected groups	200
Export Enhancement Program	400
P.L. 480	300
USDA land acquisition programs	100
Forest Service, renewable resource management	600
Forest Service, road and trail construction	100
Forest Service, forest and rangeland research	200
Forest Service, state and private forestry	150
Total Department of Agriculture	54,900
Department of Commerce	
Economic Development Administration	400

Economic and Statistical Analysis	50
International Trade Administration	200
Export Administration	40
Minority Business Development Agency	40
National Ocean Service	200
National Marine Fisheries Service	350
Oceanic and Atmospheric Research	200
Fishery products research, development, and promotion	20
Advanced Technology Program	250
Manufacturing Extension Partnership	100
National Institute of Standards and Technology	300
National Telecommunications and Information Administration	90
Total Department of Commerce	2,240
Department of Education	
Goals 2000	500
School-to-Work Programs	200
Elementary and Secondary Education Grants	7,100
Impact Aid	800
School Improvement Programs	1,200
Safe and Drug-Free Schools Act	400
Office of Vocational and Adult Education	1,500
Office of Bilingual Education	150
College Work-Study Grants	600
Office of Educational Research and Improvement	500
Direct Student Loan Program	500
Office for Civil Rights	60
Total Department of Education	13,510
Department of Energy	
General Science and Research activities	1,000
Solar and Renewable Energy, research and development	300
Nuclear Fission, research and development	200
Magnetic Fusion, research and development	300
Energy Supply, research and development	3,400
Uranium Supply and Enrichment activities	50
Fossil Energy, research and development	400
Naval Petroleum and Oil Shale Reserves	200

Energy conservation programs	400
Strategic Petroleum Reserve	300
Energy Information Administration	70
Economic Regulatory Administration	20
Clean Coal Technology	160
Power Marketing Administration subsidies	200
Departmental administration	300
Total Department of Energy	7,300
Department of Health and Human Services	
Health Professions Curriculum Assistance	300
National Health Service Corps	100
Maternal and Child Health Block Grant	700
Healthy Start	100
Title X Family Planning Program	200
Indian Health Service	1,900
Substance Abuse Block Grant	1,200
Mental Health Block Grant	300
State day-care programs	1,300
State welfare administrative costs	1,700
State child support administrative costs	1,900
Low-income home energy assistance	1,200
Refugee assistance programs	400
Family preservation and support grants	100
Payments to states for Job Training (JOBS)	1,000
Child Care and Development Block Grant	900
Social Services Block Grant	3,200
Head Start	3,300
Child Welfare Services	300
Community Services Block Grants	400
Child Abuse Grants to States	20
NIH overhead cost reimbursements	100
Total Department of Health and Human Services	20,620
Department of Housing and Urban Development	
Public Housing Programs	4,200
College Housing Grants	20
Community Development Grants	5,100
HOME Investment Partnerships Program	1,200

Community Planning and Development	500
Low-Income Housing Assistance (Sec. 8)	10,000
Rental Housing Assistance	600
Fair Housing Activities	20
Federal Housing Administration	300
Total Department of Housing and Urban Development	21,940
Department of the Interior	
Bureau of Indian Affairs	1,700
Bureau of Reclamation water projects	500
U.S. Geological Survey	600
Helium fund and reserves	20
Migratory Bird Conservation	40
North American Wetlands Conservation	10
Cooperative Endangered Species Conservation	30
National Wildlife Refuge Fund	20
Sport Fish Restoration Fund	200
National Park System, fee collection support	10
Land Acquisition programs	150
Total Department of the Interior	3,280
Department of Justice	
Community Oriented Policing Services	1,800
Violence against Women Act	120
Byrne Law Enforcement Grants	140
Correctional Facilities Grants	600
Substance Abuse Treatment for State Prisoners	20
State and Local Law Enforcement Assistance	100
Weed and Seed Program	20
Antitrust Division	20
Drug Enforcement Administration	700
Interagency Crime and Drug Enforcement Task Force	200
Total Department of Justice	3,720
Department of Labor	
The Job Training Partnership Act	1,000
Adult Training Grants	800
Dislocated Worker Assistance	900
Youth Training Grants	100
Summer Youth Employment and Training Program	600

School-to-Work Programs	100
Job Corps	1,100
Migrant and Seasonal Worker Training	60
Community Service Employment for Older Americans	400
Trade Adjustment Assistance	300
Employment Standards Administration	200
Total Department of Labor	5,560
Department of State	
United Nations organizations	600
Inter-American organizations	100
North Atlantic Treaty Organization	40
Organization for Economic Cooperation and Development	60
United Nations peacekeeping activities	200
International Fisheries Commissions	20
Migration and Refugee Assistance	700
Foreign aid to Egypt	2,000
Foreign aid to Israel	3,000
Narcotics control assistance to foreign countries	100
Agency for International Development	2,900
Total Department of State	9,720
Department of Transportation	
Motor Carrier Safety Grants	60
Highway Traffic Safety Grants	200
Federal Railroad Administration	20
Amtrak subsidies	600
Federal Transit Administration	4,500
Grants-in-Aid for Airports	1,500
Payments to air carriers program	20
Maritime Administration	500
Cargo Preference Program	500
Transportation Systems Center	200
Partnership for a New Generation of Vehicles	200
Total Department of Transportation	8,300
Department of the Treasury	
Presidential Election Campaign Fund	100
Customs Service, Air and Marine Interdiction Program	60

Interagency Crime and Drug Enforcement Task Force	60
Total Department of the Treasury	220
Department of Veterans Affairs	
VA benefits for non-service-related illnesses	200
VA health care facilities construction	600
Total Department of Veterans Affairs	800
Other Agencies and Activities	
African Development Foundation	20
Appalachian Regional Commission	200
Consumer Product Safety Commission	40
Corporation for National and Community Service	600
Corporation for Public Broadcasting	300
Davis-Bacon Act	1,000
Equal Employment Opportunity Commission	200
EPA Wastewater Treatment Subsidies	2,400
EPA Superfund	1,400
EPA Environmental Technology Initiative	60
EPA Science to Achieve Results grants	80
Export-Import Bank	500
Federal Labor Relations Board	20
Federal Trade Commission	40
High-Performance Computing and Communications	800
Inter-American Foundation	20
International Monetary Fund	40
International Trade Commission	20
Legal Services Corporation	300
NASA International Space Station Program	2,000
NASA New Millennium Initiative	400
NASA Reusable Launch Vehicle Technology Program	100
NASA Aeronautics Initiative Research Partnerships	300
National Endowment for the Arts	200
National Endowment for Democracy	40
National Endowment for the Humanities	200
National Flood Insurance	200
National Labor Relations Board	100
National Science Foundation Program to Stimulate Competitive Research	40

Neighborhood Reinvestment Corp.	40
Office of National Drug Control Policy	40
Office of Science and Technology Policy	20
Overseas Private Investment Corporation	40
Peace Corps	200
Securities and Exchange Commission	100
Service Contract Act	600
Small Business Administration	800
Tennessee Valley Authority, development activities	100
Trade and Development Agency	40
U.S. Global Change Research Program	1,700
U.S. Information Agency	1,200
World Bank	40
Total other agencies and activities	16,540
Total Cato budget savings	168,650

Suggested Readings

Congressional Budget Office. *Reducing the Deficit: Spending and Revenue Options.* Washington: CBO, August 1996.

Hodge, Scott A. *Rolling Back Government: A Budget Plan to Rebuild America.* Washington: Heritage Foundation, 1995.

Moore, Stephen. *Government: America's #1 Growth Industry.* Lewisville, Tex.: Institute for Policy Innovation, 1993.

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