

# A ROAD MAP FOR REFORM:

## 10 Policy Priorities for the New Congress

As a new Congress prepares to convene, the nation's trust in its lawmakers hangs by a thread. James Madison once described Congress as the "confidential guardians of the rights and liberties of the people," but today, a majority of Americans have little or no confidence at all in the legislative branch, according to Gallup polling.

Their skepticism is not misplaced—lawmakers have routinely ignored runaway spending, mounting debt, unchecked government overreach, and other issues that demand immediate action. To guide Congress back toward sound governance, Cato Institute scholars have crafted 10 key policy recommendations. These proposals—including tax reform and addressing Social Security's looming crisis—offer a road map for restoring fiscal sanity, reining in big government, and rebuilding public trust.

## 1. Slash Taxes Across the Board and Eliminate Subsidies and Loopholes

By Adam N. Michel, director of tax policy studies

At the end of 2017, Congress passed the Tax Cuts and Jobs Act. The law included wide-ranging reforms that simplified the tax code and reduced taxes for Americans at every income level. By lowering business taxes, the law boosted investment, wages, and economic growth.

Those individual tax cuts and some of the most economically consequential business provisions are set to expire at the end of 2025. This will present challenges and opportunities for tax reform in the 119th Congress.

To capitalize on this legislative opportunity, Cato recently released an aggressively pro-growth proposal to overhaul the US tax system. It is a roughly revenue-neutral reform that slashes tax rates to near 100-year lows by cutting the top income tax rate to 25 percent, the capital gains rate to 15 percent, and the corporate rate to 12 percent. Cato's plan also consolidates individual tax brackets to approximate a flat tax system, institutes full expensing for all investments, and repeals the estate tax, alternative minimum tax, and net investment income tax.

To offset the revenue loss and improve the tax base, the tax cuts are paired with the elimination of more than \$1.4 trillion in annual tax loopholes and other subsidies, including those for politically popular energy sources, families, education, housing, and health care.

The Cato plan could be adopted without spending cuts or growing the deficit. However, there remains a dire need for cuts to the spending-based drivers of America's fiscal imbalance. Spending reform is the only way to sustainably cut government revenue collections and ensure that taxes stay low for the long term.

## 2. Establish a BRAC-Like Fiscal Commission to Stabilize the Debt

By Romina Boccia, director of budget and entitlement policy

The United States faces a dire fiscal situation, with federal debt and interest costs spiraling out of control. Despite efforts to rein in spending, Congress has repeatedly failed to implement lasting reforms, largely due to the political unpopularity of necessary but difficult decisions that would stabilize the debt.

A promising solution is the creation of a fiscal commission modeled after the Base Realignment and Closure (BRAC) process. This commission would devise reforms that prevent US public debt from exceeding the country's economic output (measured in gross domestic product). Achieving that goal requires curbing the fastest-growing areas of federal spending.

Social Security and Medicare are unsustainable because retiree benefits have grown beyond workers' ability to support them. The unchecked growth of these programs is the primary driver of the debt crisis, as their financing shortfalls account for all the federal government's long-term unfunded obligations. The commission could propose targeted reforms to these

programs that encourage people to work more and save more money, reducing their dependency on government-provided benefits. This approach would slow the rate of spending growth while preserving a safety net for those in need.

The BRAC model provides a blueprint for implementing politically difficult changes. With Congress setting key policy goals while leaving the details to a carefully chosen group of experts, the commission's recommendations would be guided by economic realities, not short-sighted political agendas. Instead of requiring an affirmative vote to enact the commission's proposals, Congress could reject the commission's plan entirely, without amendments. This "Odysseus measure," as *Washington Post* columnist George Will calls it, allows legislators to support necessary reforms while shielding them from direct political fallout.

Congress long ago decided to abdicate its fiscal responsibilities by putting large and far-reaching government programs on autopilot, without any meaningful

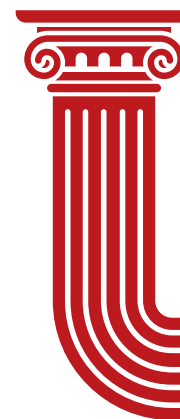
requirement for regular review. Congress should establish a BRAC-like fiscal commission to reclaim fiscal control.

## 3. Ditch Self-Defeating Buy American Rules

By Colin Grabow, associate director at the Cato Institute's Herbert A. Stiefel Center for Trade Policy Studies

The next Congress should prioritize repealing or significantly reforming numerous Buy American-style laws that force the federal government to purchase American products and services. Although advocates of such measures claim they benefit the US economy by supporting American firms—as is typically the case with protectionism—the reality is quite different. Such laws actually inflict considerable harm by driving up costs (thus increasing federal expenditures or ensuring less bang for the buck), extending project timelines, creating complacency among coddled domestic firms, and inviting retaliatory measures from US trading partners, among other downsides.

A prime example of this dysfunction is the 2021 Infrastructure Investment and Jobs Act (IIJA), which mandates that iron, steel, manufactured products, and construction materials used in many infrastructure projects funded with federal



dollars be domestically produced. These requirements, however, reduce the number of possible suppliers, thus increasing the cost and complexity of obtaining needed materials. While the IIJA was ostensibly passed to improve American infrastructure, including such protectionist language directly undermines this goal by making such projects more expensive and time-consuming.

Even national security suffers from such misguided protectionism. The Berry Amendment, for example, requires the Department of Defense to purchase footwear, dinnerware, eating utensils, and numerous other items from domestic suppliers. The result? A handful of firms reap government contracts while the military (and taxpayers) are stuck with higher costs and fewer options—no small matter in the search for comfortable shoes and boots. Arguments that foreign-made forks and footwear threaten national security may be laughable, but the harm (including foot pain) to those tasked with protecting the country certainly isn't.

Mandating the purchase of American-made products may make sense in limited cases (e.g., procuring certain weapons systems), but these are exceptional. Overall, such protectionist measures are best understood as exercises in rent-seeking that damage the country's freedom, prosperity, and even security. As such, they should be prime targets for reform by Congress.

#### **4. End the Distortionary Tax Exclusion for Employer-Sponsored Health Insurance**

*By Michael F. Cannon, director of health policy studies*

Shortly after Congress enacted the second federal income tax in 1913—and before modern health insurance even existed—Treasury Department bureaucrats decreed they would exclude employee health benefits from the new tax. Enacting the federal income tax and excluding employee health benefits ended up creating or exacerbating practically every health care problem Congress has tried to address since then. For 100 years, they have driven up health care prices, inflated health insurance premiums, and stripped sick people of their health insurance. Because it created the tax exclusion for employer-sponsored health insurance, the income tax is truly the original sin of US health policy.

Every president from Ronald Reagan to Barack Obama has tried to cleanse this sin. They all failed. Though the exclusion harms patients, it provides windfall benefits to health insurance companies,

health care providers, large employers, and the human-resources personnel and unions who administer employee health insurance. Reform invariably triggers massive resistance from industries without inspiring countervailing political pressure from the much larger number of people who would benefit.

Until now, perhaps. A new approach to reform holds the potential to unite Democrats and Republicans—and to create immediate benefits for identifiable constituencies that could overcome industry resistance.

Universal health accounts (UHAs) would end or limit the tax exclusion's perverse incentives and harmful consequences. They would apply the tax exclusion solely to deposits that workers or employers make into universally available, worker-owned accounts. Taxpayers could use their accounts to purchase health insurance and medical care. UHAs would improve both efficiency and equity in the health sector and labor markets by reducing health care prices and bringing health care within the reach of more vulnerable patients.

Every year throughout the economy, UHAs would free workers to control \$1 trillion of their earnings that the exclusion now lets employers control. They would increase cash wages by more than \$17,000 per worker with family coverage, with larger-than-average increases for women, older workers, union members, and workers with expensive medical conditions. They would free financial institutions to compete to provide workers greater value for that \$1 trillion.

UHAs would put patients back in charge of their spending, leading to a more consumer-centered and competitive market for health care.

#### **5. Reform Social Security and Boost Personal Savings**

*By Romina Boccia, director of budget and entitlement policy*

Social Security is facing substantial funding challenges due to its unsustainable pay-as-you-go structure that relies on taxes paid by younger workers to pay out benefits. Originally intended as a modest anti-poverty initiative, Social Security has evolved into the single largest federal program, accounting for about 5 percent of gross domestic product annually. Payroll taxes cover less than 90 percent of annual program spending, with government borrowing filling in the remaining gap. These persistent cash-flow deficits will widen as the US population ages and benefits rise in line with wages, resulting in a projected cumulative shortfall of \$4.1 trillion over the next decade. Absent reform, Social Security will experience automatic benefit cuts between 20 and 25 percent by 2033.

To address these challenges, Congress should reduce benefits by focusing on the system's original goal of preventing old-age poverty while avoiding further tax increases. Key reforms include raising the early and full retirement ages by three years and indexing these ages to life expectancy, switching from wage indexing to price indexing for initial benefits, adopting the Chained Consumer Price Index for cost-of-living adjustments to curtail excessive spending growth, and reducing benefits for higher-income earners instead of raising their taxes. The long-term goal should be to transition Social Security into a predictable benefit focused on preventing poverty in old age. This transition should also enhance personal savings, allowing Americans to own and control more of their income while



**“The United States, a nation founded on the principles of limited government and free enterprise—and one that, at its Founding, had protections against the direct government provision of money—should be leading the fight for greater financial privacy and monetary competition, not restricting it.”**

ensuring the program’s fiscal sustainability. The government should neither dictate Americans’ retirement savings nor overburden workers by redistributing their income to retirees, regardless of need.

Beyond Social Security reform, legislators can strengthen private retirement savings through the introduction of universal savings accounts, which would offer the flexibility to access funds at any time without penalty. This would appeal to younger and low-income workers, who are often reluctant to commit to traditional retirement accounts.

## **6. Rein in the Federal Reserve and Restore Sound Monetary Policy**

*By Jai Kedia, research fellow at the Cato Institute’s Center for Monetary and Financial Alternatives*

The Federal Reserve’s history is marred by monetary policy decisions that have negatively affected financial markets and the US economy. In earlier periods, the Fed operated with a narrower mandate and had fewer tools at its disposal. Today, its mandate is excessively broad and ill-defined. Since the 2008 financial crisis, the Federal Reserve has exercised increasing discretion, and its operational framework has grown opaque, becoming detached from clear, objective policymaking principles.

Throughout much of the 2010s and following the COVID-19 pandemic, the Fed kept interest rates low and relied on large-scale asset purchases under its quantitative easing program. Consequently, the central bank now holds risky securities, and its balance sheet has ballooned to \$7.1 trillion—roughly 30 percent the size of the entire US commercial banking sector. Crucially, the Fed failed at its most fundamental job: to keep prices stable. Yet, some government officials want to expand the Fed’s responsibilities further, including tasks such as addressing climate change.

The Fed’s performance requires a broader discussion of its mission. This conversation should explore private alternatives to the current centralized monetary regime. However, if the Fed exists in its current form, it must be reined in immediately. Congress should move the Fed away from discretionary decisionmaking and toward objective, clearly defined goals and policy decisions. Its current focus on a

“broad-based and inclusive” interpretation of maximum employment and its vague approach to average inflation targeting should be replaced by clear, measurable targets for both employment and inflation. These targets must be insulated from political influence. The Fed should commit to a monetary policy rule to meet these goals, as proposed in the 2015 Fed Oversight Reform and Modernization Act. These changes would provide transparency for consumers and the private sector while allowing Americans to hold the Fed accountable.

## **7. Unlocking America’s Potential Through Immigration Reform**

*By David J. Bier, director of immigration studies*

The next Congress should recognize the need to reform America’s legal immigration system, which legislative dysfunction has preserved for decades like a prehistoric bug in amber. The last notable reforms occurred in 1990, and the basic structure of the system dates to 1924, when Congress invented the caps on visas and category preferences for family members.

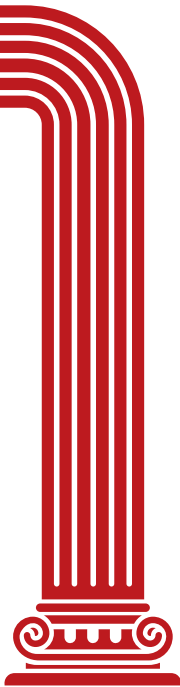
America’s economy drives immigration. As more Americans retire than enter the labor force, immigrants will become even more critical to economic growth. Recent experience with illegal immigration should clearly demonstrate the urgent need for a wholesale restructuring of how immigrants enter the United States.

According to Cato research, only 3 percent of the individuals applying for permanent residence in the United States this year will receive it. Congress should start reform by addressing three critical issues: (1) the lack of

any option for low-skilled guest workers to enter legally for year-round jobs; (2) the low caps on H-2B visas for seasonal nonagricultural workers and on H-1B visas for high-skilled workers; and (3) the removal of the overall and per country caps for employer-sponsored immigrants—particularly for individuals already living and working in the United States.

These reforms would allow immigrants to fill the needs of Americans in many industries, including health care, construction, and information technology. Without them, illegal immigration and border disorder will continue.





## 8. Audit the Scourge of Coercive Plea Bargaining with a Trial Lottery

*By Clark Neily, senior vice president for legal studies*

The Bill of Rights devotes more words to the subject of criminal procedure—and specifically, the process for obtaining a conviction—than any other. And for good reason. The Founders understood from personal experience that the power to convict and punish is readily abused by oppressive governments. They sought to prevent that by making citizen jurors the ultimate arbiters of guilt or innocence. But jury trials have been supplanted by so-called plea bargaining, which now accounts for more than 98 percent of all federal criminal convictions.

Proponents of mass plea bargaining claim that guilty pleas are fully voluntary and every bit as reliable as constitutionally prescribed jury trials. But they're wrong. Of the more than 3,000 people on the National

Registry of Exonerations, 17 percent pleaded guilty to crimes they did not commit.

Given the outsized role that plea bargaining plays in our system, there may be no more important question in criminal law than this: How often is the government able to induce a guilty plea from someone whom it would have been unable to convict at trial?

Fortunately, there's no need to guess. We could audit the system using a so-called trial lottery. This involves sending a random sample of cases where a plea agreement has been reached but a trial has not yet begun to determine the possible outcome. If the defendant is convicted in the lottery trial, they receive whatever punishment was previously agreed upon; if they're acquitted, they walk. Over time, a robust body of data would tell us with great precision just how reliable plea bargaining really is.

Proponents of today's system assure us that plea bargaining is reliably free of coercion and the horror of false convictions that punish the innocent while leaving the real perpetrators free to victimize others. It's time to test those assurances instead of taking them for granted.

## 9. A Light-Touch Approach to Artificial Intelligence

*By Jennifer Huddleston, senior fellow in technology policy*

Both the public and policymakers have been captivated by the emergence of artificial intelligence (AI), a disruptive innovation with broader applications than those experienced during the rise of the internet over 30 years ago. While consumer products such as ChatGPT have gained the most attention, AI and other types of machine learning are much more general-purpose technologies.

Given the various technical components involved with the development and deployment of AI, generalized AI policy is best managed at the federal level. When the internet was in its infancy, the United States took a light-touch approach and limited regulation to cases that involved clear harms that existing laws did not address. Congress should do the same with AI. Before passing any new regulations for AI, policymakers should examine whether existing laws addressing issues such as discrimination or fraud sufficiently cover any harms caused by AI and whether the harms come from the technology itself or its misuse by bad actors.

Not all AI applications are general. Particularly in highly regulated industries, policymakers should consider removing occupational licensing requirements or other regulatory barriers that might prevent the deployment of beneficial AI in fields such as transportation, finance, and medicine.

Policymakers at both the state and federal levels need to focus on benefits as well as risks when considering the potential trade-offs of AI policy. We should be cautious of overly prescriptive regulation that could prevent innovative developments or dissuade entrepreneurs from solving novel problems.

## 10. Protect Financial Freedom by Preventing a Central Bank Digital Currency

*By Norbert Michel, vice president and director of the Cato Institute's Center for Monetary and Financial Alternatives*

More than 100 countries have launched or are exploring a central bank digital currency (CBDC). A CBDC is a digital liability of the federal government that poses acute threats

to financial freedom and human liberty. Although supporters claim that CBDCs are just another kind of money, such claims could not be further from the truth. A CBDC would electronically tether the government to anyone who uses it, giving the state complete control over the money going into and coming out of each person's digital wallet. CBDCs are also programmable, which means the government can prevent people from spending more than a certain amount, stop them from buying certain goods or services, and penalize them for failing to spend "enough."

Although the adoption has been lackluster, government officials throughout the world have been launching their own CBDCs. One of the most notorious examples is China, an authoritarian country that launched a CBDC in 2020. Meanwhile, government officials in many *non*-authoritarian countries have openly boasted that CBDCs will allow them to program money so that they may control how, when, and where people spend money.

The United States, a nation founded on the principles of limited government and free enterprise—and one that, at its Founding, had protections against the direct government provision of money—should be leading the fight for greater financial privacy and monetary competition, not restricting it. The 119th Congress should amend the Federal Reserve Act to ensure that neither the Fed nor the Treasury can issue a CBDC. ♦