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Tax Cuts Without Spending Limits Will Not Make America Great Again

James A. Dorn

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When the states ratified the 16th Amendment in 1913, the top marginal personal income tax rate was 7% and federal spending was less than 10% of GDP; today the top rate is close to 40% and spending is 21% of GDP.

The tax code has become more and more complex, tax preferences (loopholes) have politicized the system, and high rates are penalizing success. Meanwhile, the mammoth IRS continues to oppress people's liberties.

President Trump's tax reform would simplify the individual income tax by closing loopholes and reducing the number of brackets from seven to three — with marginal rates of 10%, 25% and 35%.

Those changes would take us closer to the flat-tax system first proposed by Robert E. Hall and Alvin Rabushka in 1981, which motivated President Ronald Reagan and Congress to cut the top marginal personal income tax rate from 70% to 28% while closing loopholes to make the reforms "revenue neutral."

There is a strong case for a simple, flat-tax system on grounds of both efficiency and freedom. But tax reform must be tied to downsizing government.

The total tax burden is current taxes *plus deferred taxes*. Unless spending is cut, the current portion may fall, but the deferred portion will rise, which doesn't reduce the overall tax load over time.

Limits on taxing and spending ultimately need to be embedded in constitutional limits on the size and scope of government — and those limits can only be enforced if there is a public ethos of liberty. When government is asked to do too much, the private sector suffers along with civil society.

"The sum of good government," said Thomas Jefferson in his 1801 Inaugural Address, is "a wise and frugal government, which shall restrain men from injuring one another, shall leave them otherwise free to regulate their own pursuits of industry and improvement, and shall not take from the mouth of labor the bread it has earned."

That vision of limited government — and the extension of that vision to all Americans — is what made America great.

Getting back to first principles is essential if America is to be great again. When President Reagan signed the Tax Reform Act of 1986, he noted, "But for all (the) tax reform's economic benefits, I believe that history will record this moment as something more: as the return to the (Founders') first principles."

The Reagan tax reform indicates, however, that unless tax reform is linked to spending limits there will be a strong incentive to raise tax rates to gain revenue and expand government.

Soon after President Reagan left office, marginal income tax rates started to climb. The top rate of 28% lasted only three years: 1988, 1989 and 1990. In 1991, the rate went to 31%, and then rose to 39.6% in 1993, where it stands today. Meanwhile, federal spending, especially on entitlements, has continued to grow, with mounting unfunded liabilities — and thus deferred taxes.

Cutting the top rate to 35% would take us back to 2003, but not to 1988. Hong Kong, the freest economy in the world, has a simple flat tax of 15%. It has also lived within its means and limits government spending to about 18% of GDP. Its mantra is "small government, big market."

It is not sufficient for prosperity and freedom to reduce tax rates without at the same time reducing the size and scope of government. Unless spending is constrained — for example, by a constitutional cap that limits annual spending growth to population growth plus inflation — there is no guarantee that lower tax rates and fewer loopholes will survive political gamesmanship.

When tax rates were lowered in the 1980s the economy benefited, but the federal budget deficit went from $74 billion in 1980 to $221 billion in 1986.

The budget was in surplus from 1998 to 2001, but has been in deficit ever since. The accumulated deficits have increased federal debt to more than 100% of GDP, and that doesn't include the trillions of dollars of *implicit* debt — that is, the unfunded liabilities in Social Security, Medicare and Medicaid.

The true cost of government is spending, not taxes. Federal spending is expected to reach 22% of GDP in fiscal year 2018, a figure that is twice the share extracted by all state and local governments — and a figure that would have astonished the Founding Fathers.

Tax reform is necessary to make America great again, but so are effective limits on the size and scope of government. Ultimately, it will be up to the American people to restore an ethos of liberty and choose leaders who put the principles of the Constitution first.

Dorn *is a senior fellow at the Cato Institute and editor of the Cato Journal.*