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Who Knew? Cutting Government Spending IS Actually Possible

By John Lott

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Federal government spending is on a course with disaster. $2.7 trillion has been added to the national debt in just 2009 and 2010. Under current budget plans, the federal government's debt will likely exceed our income in just over a decade from now. President Obama's Debt Commission (The National Commission on Fiscal Responsibility and Reform) released its solution today.

The commission, composed of twice as many Democrats as Republicans, proposes limiting federal government revenue and spending to 21 percent of GDP. Assuming that promises are actually kept, that would mean an increase in what revenue the federal government has traditionally taken in and a return to what government spending has been prior to the huge surge we have seen over the last two years. -- Over most of the last 60 years, federal government revenue has been about 19 percent of GDP. Spending over that period has been around 21 percent or less.

To make up this revenue, some people with high incomes are going to be hit with large tax increases. One change would dramatically raise the current maximum taxable income for Social Security. In today's dollars, that effectively means a 12.4 percentage point increase in income taxes for those making between $106,800 and $168,000. Higher income individuals will also bear a disproportionate share of the benefit cuts.

Nevertheless, the commission did accomplish something important: it showed that cutting government spending is indeed possible. While their approaches on Social Security and Medicare can only be classified a timid and many other policies may be criticized, a reasonable observer can easily infer from their suggestions that the budget can be balanced without any tax increases.

Take the commission's proposed gradual increase in the retirement age for Social Security and Medicare from the current 67 years to 68 years by 2050. Even such a small change would save $21 billion per year immediately and $127 billion per year by 2030. By contrast, a three-year increase to 70 years of age by 2050 would save $351 billion per year in 2030.

Using a more accurate measure of price changes for indexing Social Security benefits -- the so-called Congressional Budget Office option -- would make a big difference immediately. In contrast to the current measure, it does not overestimate inflation and therefore Social Security benefits would not rise as fast. Such a change would likely save another estimated $60 billion a year immediately.

When Social Security started paying out benefits in 1940, babies born in the United States had a life expectancy of 63 years, compared to today's 78 years. Though some of this increase is the result of declining infant and child mortality, it is very clear that the one year increase in the Social Security retirement age proposed by the commission will not come close to keeping pace with the increased longevity past 65. This isn't saying that people can't retire earlier if they want to. Just that if they do want to retire early, they should save up the extra money to pay for it. A safety net would still be there for those who are unable to save the extra money.

The debt commission is a good starting point. Reducing discretionary spending back to its 2008 levels after accounting for inflation seems to be conceded as reasonable. But we should be able to do much more in order to avoid the wealth destroying tax increases. According to the Cato Institute at www.downsizinggovernment.org, over a trillion dollars in annual government spending can be cut without much adverse consequences.

For instance, the Department of Education should be eliminated altogether as education is not the federal government's business to begin with. Education aid, public housing subsidies, and state and local government aid involves taking money from the states and then giving it back with a lot of federal strings on it.

Competition between states would help ensure the money is spent more efficiently and creatively. Let states make those decisions and cut out the middleman.

Indeed, even more savings are possible. Cato never explains why it only wants to cuts the Department of Health and Human Services grants to state and local governments by 50 percent.

It is hardly obvious why the government should be picking the winners and losers in small and large businesses and what types of energy usage is the most efficient. People who have their own money at stake have better incentives in determining what investments make sense. Cato proposes gutting the Small Business Administration and the Department of Commerce business subsidies. These programs throw away taxpayer money, making us all poorer, but create political corruption as the government buys votes.

Cutting the federal budget will not only be about saving money, but it will also cut down on the many stifling rules and regulations that states and businesses now have to suffer under. Federal control prevents states from innovating and discovering new policies that work. But change won't be easy. There are obviously many interest groups that have a vested interest in getting this money. It is therefore essential that the sweeping cuts be made at the same time so that no particular group feels that they in particular are singled out.

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