

Reason Magazine

## **Paul Ryan's Budget Plan: The Good, The Bad, & The Ugly**

Nick Gillespie & Veronique de Rugy | April 6, 2011

Rep. Paul Ryan (R-Wis.) has released the official House Republican proposal for the 2012 federal budget. It compares extremely favorably to President Barack Obama's own plan, but that is damnably faint praise.

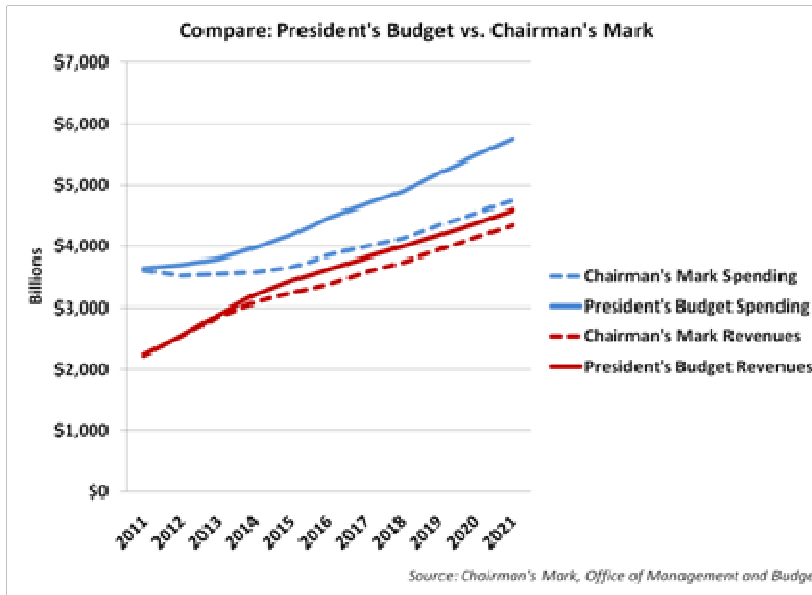
From every possible perspective, Obama's budget was and is a disaster waiting to happen, memorable only for reminding all Americans that you can't spell "Winning the Future" without WTF.

Indeed, Obama's plan for 2012 is so awful that it should make us feel lucky that he and the Democrats failed to pass a budget for the current fiscal year (the only time such a thing has happened since 1974). Obama's dream budget would mean a 2021 budget that spends \$2 trillion more than we do today, increase debt held by the public from 62 percent to 77 percent of Gross Domestic Product (GDP) and maintain massive annual deficits. And that's if things go according to his plan, which they won't (built into his budget are unrealistic assumptions about the rate of economic growth, revenue collection, health care savings, and more).

So compared to such an exercise in recklessness, Ryan's plan is refreshingly engaged with reality. Unfortunately for taxpayers and citizens, Ryan's plan looks better when standing in the shadow of Obama's. Neither budget provides a good way forward for a country still battling the effects of recession and the non-stop, self-inflicted spending binge that began with George W. Bush and has proceeded unabated since then. Ryan's budget is indeed a positive break from past efforts by Republicans and Democrats alike, but it doesn't provide the solutions the American people deserve.

We made the case against Obama's budget here. Now, we discuss the good, the bad, and the ugly of Ryan's budget.

### **The Good**



Ryan's budget spends considerably less money over the next decade than does Obama's. As the chart above shows, Obama expects to spend almost \$6 trillion by 2021, while Ryan's plan comes in at more than a trillion dollars less, around \$4.7 trillion (these amounts are in nominal dollars). Ryan's plan also calls for less revenue (taxes) than the president's and posits a significantly smaller set of annual deficits. So the amount of borrowing built into Ryan's plan is less too. That's all to the good. Lower levels of government spending and debt and taxes leaves more money in the hands of private citizens and businesses, who are far more likely to generate economic growth.

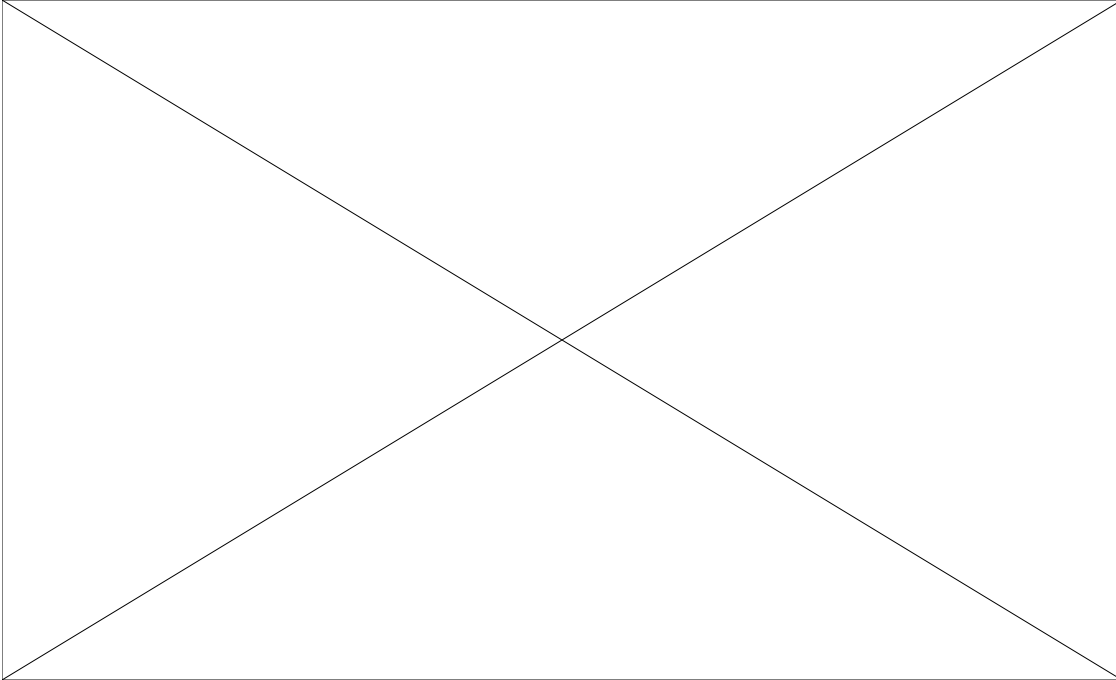
More important, Ryan's budget, like his 2010 "Road Map For America's Future" (from which much in the budget is inspired), is a serious attempt to think through the implications of the past decade's wild spending spree, in which federal outlays increased by more than 60 percent in real terms and debt held by the public exploded from 36 percent of GDP in 2007 to its current 62 percent level. Ryan should be commended for refusing to be passive in the face of spending trends that threaten to swamp the nation's economy. Shockingly, the "new normal" for the 21st century has been massive expansions in government spending and reach, first under Bush and now under Obama. Ryan, who voted in favor of No Child Left Behind, the Medicare Part D expansion (which gave free and reduced-price prescription drugs to seniors), TARP, and all major war funding, has certainly been part of the problem, but more recently he seems to have discovered his inner cheapskate. Better late than never.

Given that spending on Social Security, Medicare, and Medicaid comprises around 40 percent of annual outlays, Ryan's emphasis on reforming two of the nation's major entitlement programs is among the most attractive part of his plan. He is largely responsible for starting a much-needed discussion of changing "entitlements" from open-ended obligations on the government that get paid out regardless of their effectiveness or need. The three major entitlements - Social Security, Medicare, and Medicaid - are not just fiscally unsound, they have proven time and again to yield poor results (Social Security yields anemic 2 percent annual returns on investment for current beneficiaries) and increase health care inflation.

Ryan's budget proposes block granting Medicaid, which provides health care for the poor, so that states have more flexibility in how they deliver care and control expenses.

Essentially, the states would get a fixed pile of money each year that they would be free to spend as they see fit. When the money's gone, that's it. According to Cato's Chris Edwards, full block-granting of Medicaid could save around \$95 billion a year while delivering more effective care. Critics worry that states would simply cut care to save money, but that assumes that voters in states simply don't care about the poor or the quality of services. And it assumes the current system is actually performing well, which it is not. Most spectacularly, several studies confirm that current Medicaid recipients often have worse health-care outcomes than similar people not in the system. Changing the funding and control structure of Medicaid is the best hope lower-income people have at this point when it comes to health care.

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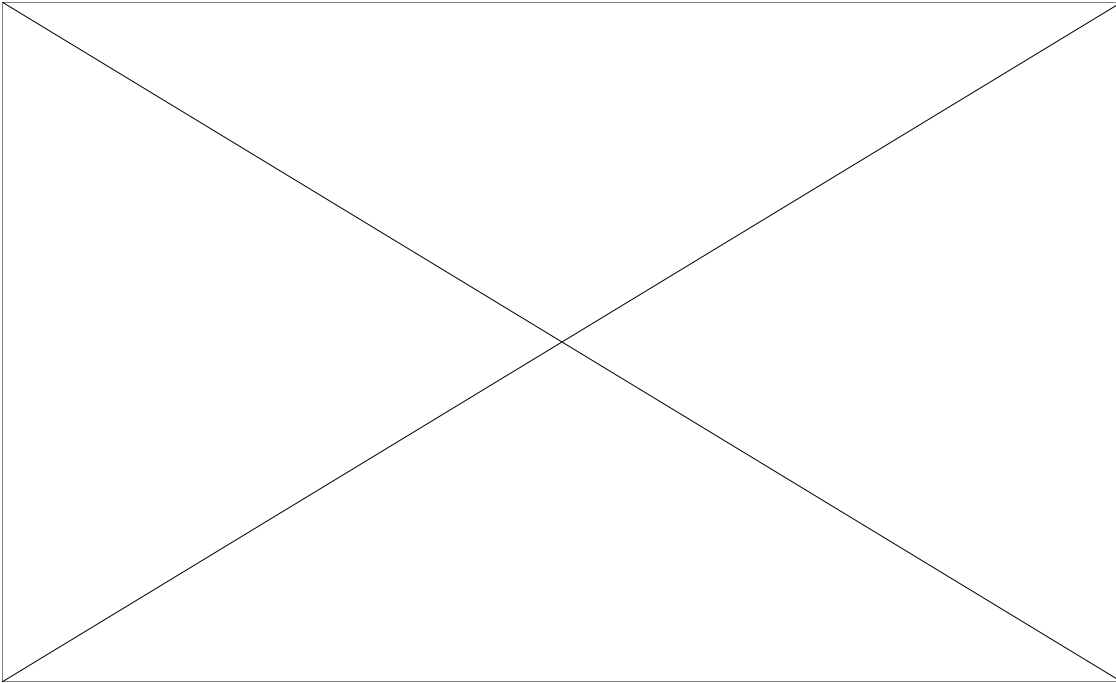


For Medicare, which provides health care for senior citizens, Ryan wisely suggests getting rid of the current system, in which payments are made for every procedure performed with no cap or restraint on overall spending. Instead, Ryan proposes shifting to subsidizing premiums for seniors, who would then choose from a range of plans that best suit their needs. The phase-in of this shift would take place over the next 10 years (those 55 years and older will stay in the current system), allowing for transition. By subsidizing premiums rather than covering payments for services rendered, Ryan's plan will ostensibly make seniors and their doctors think twice before ordering up whatever test or procedure they might want at a given moment. Injecting pricing into the health care system is the only way to bring prices down and his plan should help that along. In a more combative gesture, the plan also zeroes out spending on the new health care law ([see S-3 here](#)).

The other good conceptual element to the Ryan budget? He calls for simplifying the income tax by reducing the number of brackets and ending tax expenditures such as the mortgage-interest deduction. And he wants to reduce the corporate income tax from its current 35 percent rate to 25 percent, a figure that would make the U.S. competitive with other developed countries. That's all good, though it's worth pointing that the budget plan, while calling for any tax reforms to be neutral in relation to revenue raised as a percentage of GDP, has essentially no specifics in it beyond the corporate tax rate.

Here's a video that Ryan made about the issues that he says his budget addresses:

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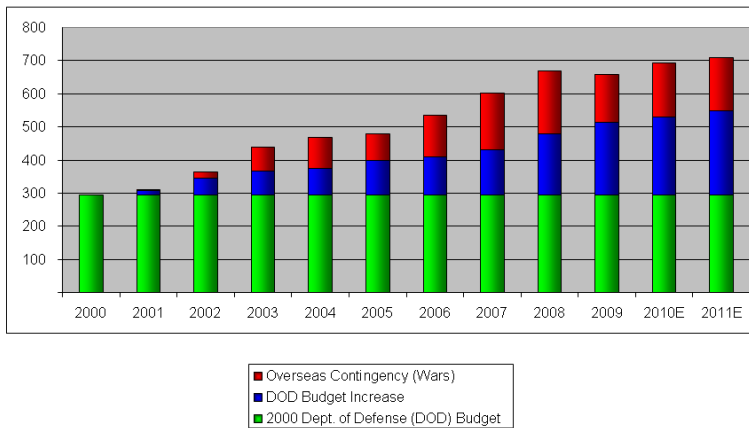
### **The Bad**

For all of its focus on the right issues - including a debt crisis that is no longer looming but already upon us - Ryan's budget fails to deliver on spending reductions in a number of ways. For starters, it's not overly useful as a document designed to map out what the government should be spending in the next fiscal year. As noted above, it stipulates that we need a radical overhaul of tax brackets but then fails to deliver specifics on what should happen for individual income taxes. It raises the need for entitlement reform that will mostly take place after the period which it covers ends, thereby starting a debate over Medicare that it doesn't really address (other than by talking about preserving Medicare funds from "raids" on it to pay for ObamaCare). In these problems, it is clearly a condensed version of the longer Road Map rather than a stand-alone document that speaks to the budgeting process rather than a larger conversation.

For all the talk about bringing some basic sanity back to fiscal policy, the budget proposes spending over the next decade that averages out to 20.5 percent of GDP. That's more than 2.5 percentage points higher than the average amount of revenue raised as percentage of GDP since World War II (which has come in slightly below 18 percent of GDP). Part of the problem is due to defense spending, which Ryan does not put on the

table. He proposes spending \$801 billion on "security" and the "global war on terror" in 2012 and \$838 billion (in nominal dollars) in 2021. Over the same time period, non-defense discretionary spending goes from \$482 billion to \$422 billion. Along with entitlement spending, defense is the largest category of expenditures. When you're looking to restrain spending, you need to go where the money is, so it's simply wrong to suggest that defense spending - much of which has little to nothing to do with actually protecting American lives and property - be kept inviolate if we are in fact out of money. Defense spending has risen dramatically and not simply because of wars in Iraq and Afghanistan that even supporters acknowledge have been incompetently prosecuted. Combat operations add to the problem, but it is hardly the only driver here.

U.S. Defense Spending Trends 2000-2011 (\$ Billion)



Source Data: OMB - Annual Budget Documents  
Data excludes Homeland Security and Veteran's Affairs

And, needless to say, defense spending, like all contemporary spending levels, are starting from massively inflated totals. So when Ryan brags about bringing "spending on domestic government agencies to below 2008 levels," it's a mostly empty boast. Another empty boast in the plan is a report from the Heritage Foundation that says following Ryan's "Road Map" would lead to a massive increase in economic growth, and a 4 percent unemployment rate in 2015 and a 2.8 percent rate in 2021. While it's true that any gesture toward fiscal restraint would be welcomed by investors and actors in the domestic and international economy, such patently specific, ludicrous, and ahistorical rates can't be taken seriously. Unemployment reached 4 percent in 2000, an exceptionally rare year indeed that 2015 is unlikely to repeat. The most recent year that the

unemployment rate dipped below 3 percent was 1944. This is the sort of "support" which distracts from meaningful conversation.

### **The Ugly**

The Ryan budget punts completely on the issue of Social Security reform. There's simply nothing of substance in the document, other than vague hand-waving of the historic greatness of the system and the observation that current and near-retirees will get screwed if nothing is changed. There are statements about how it would be a mistake to increase the amount of wages subject to payroll taxes and that people are living longer, but no clear proposal for how to maintain a system that no longer makes demographic sense. Yes, people are living longer and poorer people need more help in old age, so declare what the new eligibility age should be and discuss the obvious role of means-testing in possible reforms. For a bold, visionary statement that supposedly offers a real alternative to an untenable status quo, this is weak beer. Unlike when dealing with Medicaid and Medicare, Ryan doesn't suggest a similar end to entitlement status for Social Security. Why should it be exempt from the same logic? The great libertarian economist Milton Friedman once argued for a minimum guaranteed income as an alternative to all transfer payments. Certainly it makes sense to discuss Social Security in such terms.

Similarly, it is not simply disappointing but mind-boggling that the Ryan budget, something the Republican Party has been touting for a long time as a definitive response to President Obama's dismal and unserious offering, cannot find its way to bring annual revenue and annual outlays into balance. Ryan's longer-horizon Road Map doesn't even pretend to balance the budget until 2063, which is tantamount to giving up. We're not balanced-budget fetishists, though there are many economic benefits of having a government which lives within its means (and very few to one that doesn't). But if the federal government, after a solid decade of completely promiscuous spending, cannot reform its wicked, wicked ways, the country is in far deeper trouble than Ryan understands.

There are alternatives on the limited-government side. Sen. Rand Paul (R-Ky.) has put forth a five-year balanced budget plan that forthrightly calls for the elimination of whole departments, agencies, and functions of government. Despite its boldness, Paul's plan is thoughtful. Hence, it calls for the elimination of the federal Department of Education which, since its creation during the Carter years, has failed to produce any significant increase in overall student outcomes at any level. Yet Paul also calls for continuing Pell

Grants, which helps students with college tuition, at 2008 levels; we can debate the wisdom of Pell Grants (and their role in inflating tuition), but the point is that Paul's proposal is not the reckless slashing some take it to be. Similarly, when it comes to Social Security, Paul's plan calls for common-sense reforms that can only be controversial among the most-timid of analysts and politicians: raising the eligibility age, indexing for longevity, tying cost-of-living-increases to wage inflation rather than the Consumer Price Index, and establishing some form of means-testing.

In a March Reason article, we proposed a 10-year balanced budget plan that would systematically reduce outlays so that they equal the 19 percent of GDP that the Congressional Budget Office projects that the federal government will raise as revenue if the current tax system is left unchanged. That is to say, we can balance the budget over the next decade without raising taxes if we ratchet down spending from its current 25 percent of GDP to 19 percent of GDP - a figure that would still place it well above the 18.2 percent of GDP that Bill Clinton spent in his last year in office. Here's a sense of how to get from where we are to a balanced tally that would still leave us fatter than we were in 2000, when no one was complaining about a skin-flint government:

**Figure 4. Cuts Necessary Relative to the CBO Alternative (Billions of 2010 Dollars)**

	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
National Defense	\$25.3	\$23.8	\$22.6	\$22.0	\$21.3	\$20.7	\$20.3	\$19.7	\$19.3	\$18.7
Non-Defense Discretionary	\$25.3	\$23.8	\$22.6	\$22.0	\$21.3	\$20.7	\$20.3	\$19.7	\$19.3	\$18.7
Medicare	\$20.0	\$20.8	\$21.6	\$21.5	\$21.5	\$21.0	\$21.1	\$21.2	\$21.3	\$21.9
Medicaid	\$9.5	\$9.6	\$9.7	\$10.7	\$11.6	\$12.9	\$13.7	\$14.0	\$14.2	\$13.9
Social Security	\$25.7	\$27.0	\$27.3	\$27.1	\$26.5	\$25.8	\$25.8	\$25.8	\$25.8	\$25.8
Other	\$22.9	\$23.7	\$24.9	\$26.1	\$27.1	\$27.5	\$28.0	\$28.3	\$29.3	\$29.6
Total Annual Cuts	\$128.7	\$128.7	\$128.7	\$129.3	\$129.3	\$128.7	\$129.2	\$128.7	\$129.2	\$128.7
New Annual Spending	\$3,521.8	\$3,292.1	\$3,275.1	\$3,337.8	\$3,409.6	\$3,504.8	\$3,562.7	\$3,625.1	\$3,690.9	\$3,761.3
Projected Annual Spending Without Any Cuts	\$3,650.5	\$3,549.5	\$3,661.2	\$3,853.2	\$4,054.2	\$4,278.1	\$4,465.2	\$4,656.3	\$4,851.4	\$5,050.5

If cuts such as these are not possible, it would be better to give up any pretense that we will ever restore the barest semblance of sanity to the federal budget and get on with fiddling as Rome burns. If we're going to continue hosting a party whose bill is unpayable, we might as well enjoy ourselves.

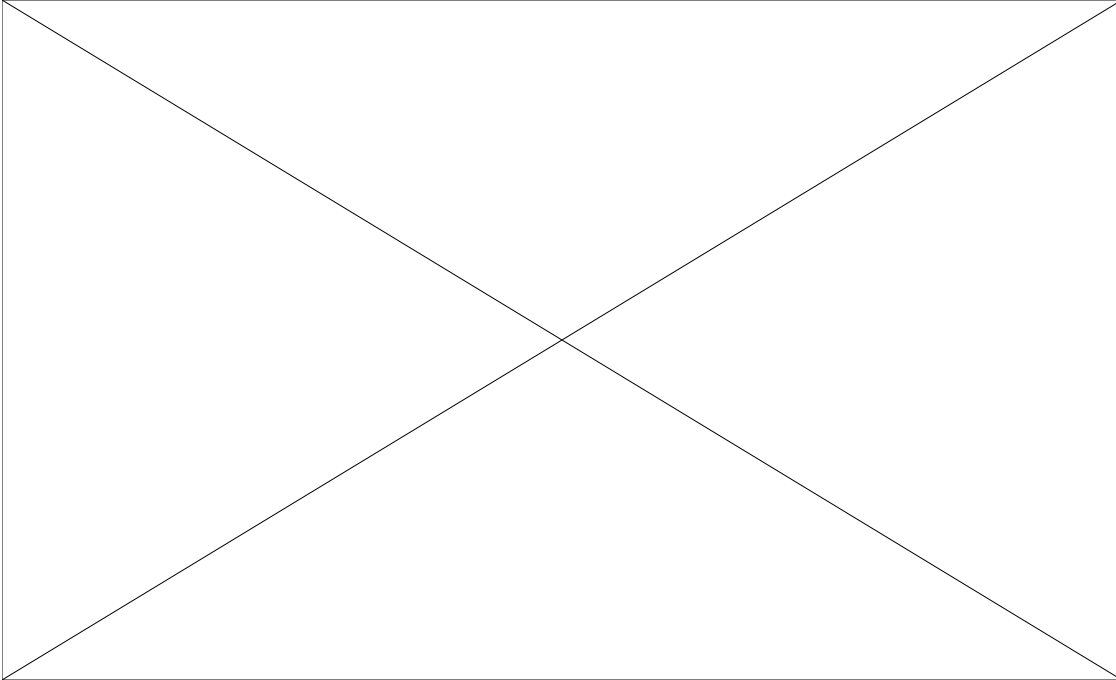
Which brings us to the major flaw in Ryan's budget: He doesn't rest his reform of entitlements on a fundamental understanding that not everyone should be receiving government money. Even as he pushes to reform Medicare, for instance, he emphasizes continuing its universality for retirees. The two of us believe it is society's responsibility



to care for the neediest and poorest among us. But it's not society's responsibility to take care of middle-class and wealthy individuals who have the means of doing so for themselves (as David Stockman told one of us recently, all government benefits should be means-tested). By failing to make this distinction, Ryan sets his plan up for political failure. When his plan was scored by the Congressional Budget Office, the CBO noted that under his reforms most Medicare beneficiaries would have to pay more for their health care costs. That's not only mathematically correct, it's morally correct. There is simply no reason that relatively well-off seniors shouldn't pay their own way. That would allow the government to take better care of those actually in need while reducing overall tax burdens on the economy. Similarly, while we think Ryan is absolutely correct about block-granting Medicaid, at least that program is specifically geared toward helping the poor. The same cannot be said about Social Security and Medicare, which suggests reforming those programs should be the highest priority when it comes to entitlements.

Budget discussions are always built around a tedious discussion of what is politically feasible, politics supposedly being the art of the possible and all that. Rand Paul's five-year plan, goes this line of thinking, is as unattainable as any Soviet five-year plan because it's simply too radical, too lapidary. A 10-year plan like our "19 Percent Solution" is similarly a dream because...well, because it would actually require making minor trims over time and across all areas of spending. Defenders of the status quo will always recoil from change, even when that change simply returns us to a recent state of affairs. In this light, it's not surprising that Ryan's plan has gotten a high-five from some liberals, such as *Slate's* Jacob Weisberg, who calls it, "brave, radical, and smart." But as long as we're talking about the art of the possible, it's worth asking: Who would have ever thought that we'd be spending 25 percent of GDP, a figure last seen during World War II? Who would ever have thought that deficits and debt as a share of the economy would be hearkening back to days when we were locked in a twilight struggle against the Nazis and their fascist and imperialist allies? At least at the end of World War II, there was a widespread expectations that spending would be reduced. As we look to the next decade and beyond, all signs are that government spending will explode higher. The real fantasy at work in contemporary America doesn't revolve around attempts to cut spending.

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And yet Obama's completely unserious plan - offered up by a transformational change-agent who somehow couldn't even pass a budget last year despite belonging to the party that controlled both houses of Congress - is deemed worthy of serious discussion. And Rep. Paul Ryan's more-thoughtful plan to increasing total spending by 30 percent over the next decade is both lauded for "grasp[ing] reality with both hands" and accused of "dismantling...key parts of government."

As we said at the outset, there's no question that Ryan's plan is far preferable to Obama's. And there's no question that Ryan's plan can and must be the starting point of a discussion about how to get serious about reforming the way the government spends money. But in an America where taxpayers and politicians have been reluctant to fully grok that "We Are Out of Money" at every level of government, Ryan's spending plan should at best represent the ceiling of what is considered worthy of discussion. If, as is much more likely, it ends up being the floor from which budget negotiations spiral upwards, then our future just got a whole lot shorter.

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