The Corner

Will Tax Hikes Reduce the Cost of Government?

By Ryan Ellis
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Milton Friedman famously said that “the government will spend every penny it takes in taxes, and whatever more it can get away with.” Those in the mainstream media, the Washington establishment, and the gullible Right should remember that as calls begin to emerge for the debt-reduction “super-committee” to raise taxes.

Washington has an over-spending problem. For as long as most people have been alive, the federal government has spent 20.6 percent of what the real economy has produced. The non-partisan Congressional Budget Office (CBO) projects, however, that federal spending will hover around 24 percent each and every year this decade (a record not even matched by Jimmy Carter or Lyndon Johnson) before getting above 30 percent in the decades to come.

Taxes, however, are coming in as expected. Also for as long as most people have been alive, the federal government has stolen by taxation 18.2 percent of what families and employers have earned. In boom times this has gotten as high as 21 percent, and in tough times (like this year) it’s gotten as low as 15 percent. But the average stands the test of time. In fact, according to the same CBO, federal tax revenues will be 18 percent of economic output by the last year of this decade (even if the Bush tax cuts, AMT patch, and business extenders are all made permanent).

But that’s not enough for Washington. Instead of calling for spending to come down closer to its historical average, some have called for taxes to chase the tail of record spending growth. This is a futile effort. If history is any guide, Congress will spend all the new tax revenues collected, and then some (just like Milton Friedman said).

Back in 1982, President Reagan was promised $3 in spending cuts for every $1 in tax hikes. The spending cuts never happened, but the tax hikes sure did. In 1990, President George H. W. Bush was promised $2 in spending cuts for every $1 in tax hikes. He agreed, breaking his “read my lips” tax promise to American voters. According to CBO, the spending baseline after the deal didn’t only fail to come down, it actually went up! So did everyone’s taxes.

One of the most important metrics produced in Washington is the Americans for Tax Reform Foundation’s “Cost of Government Day” report. It tracks how long into the year every American has to work to pay the total cost (spending, taxes, and regulation) of government (federal, state, and local). Thanks to the rampant over-spending and over-regulation of the Bush-Obama years, Cost of Government day now comes on August 12. Americans must toil 224 days before they have earned enough money to pay for the full cost of government. Before 2009, this day never came before July 21. American families and employers must surrender over 61 percent of their income to pay every tax, finance every over-spending deficit, and comply with every regulation that national, state, and local governments have seen fit to impose.

Would raising taxes help? No. The government will simply take the money, spend it, and then spend even more through borrowing. Raising taxes will push Cost of Government Day even later into the year, as higher taxes financing even bigger government completes another cycle in the death spiral that has been the American economy.

Instead, the “super-committee” should focus squarely on the actual problem — the fact that Washington already spends more money than it ever has by any measurement, and that this spending is driving our economy into a debt-ridden ditch. The goal is simple — end the over-spending crisis by bringing government spending down to its historical average of 20.6 percent of economic output. Then balance the budget by bringing spending down to match the historical level of taxation — 18.2 percent of the economy. Doing this allows for a balanced budget without raising taxes.

This isn’t that difficult. Dan Mitchell of the Cato Institute has noted frequently that capping federal spending growth at 2 percent annually would achieve this goal in a decade. Capping discretionary spending at the agreed-upon 2012 level would reduce anticipated spending by $1 trillion over this period, getting a good way toward the goal. Whatever the means or methods, spending is where the fall fight over the debt limit needs to be focused. “Tax reform” (which really means tax hikes in this environment) should wait for a more taxpayer-friendly president and Senate.

— Ryan Ellis is tax policy director at Americans for Tax Reform.

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