DANIEL BENJAMIN
The administration's counterterrorism efforts
PAGE 5

ROSS DOUTHAT
Obama's failure to change Washington
PAGE 14

DANIEL GRISWOLD
Taking free trade on the road
PAGE 12

Cato Policy Report

March/April 2010 Vol. XXXII No. 2

Limiting Government, 1980–2010

BY JOHN SAMPLES

Ronald Reagan won the 1980 presidential election decisively. He beat incumbent president Jimmy Carter by 10 points in the popular vote. In the Electoral College, Reagan carried 24 states by more than 10 points, 14 of them by more than 20 points. Reagan had a mandate to pare back the federal government.

In 1981 and again in 1995, Reagan or leaders inspired by him would try to realize that goal. To accomplish that would have required a domestic revolution that overthrew the institutions and policies of the New Deal and the Great Society. Reagan and his successors did have some success at restraining the growth of the state. But they did not overturn the old order. Why did the effort to limit government produce such modest results? American politics tends toward incremental changes absent a major crisis. The problems that brought Reagan to power (and later elected the 1994 Congress) were not deep enough to foster major liberalizations. But that does not mean the hope for limited government will come to nothing. The New Deal order will face future crises that may yet bring a revival of limited government. Understanding the successes and failures of past struggles can inform our future striving to limit government.

JOHN SAMPLES is director of the Cato Institute's Center for Representative Government and author of *The Struggle to Limit Government: A Modern Political History*, just published by Cato.

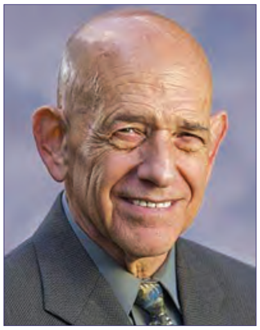
SUCCESSES

Let's begin with the (modest) successes of this era. In 1981, the president signed into law significant cuts in government spending and tax rates. Reagan's "historic" turnaround cut the projected spending of the federal government by 4.7 percent for the next fiscal year. Taking inflation into account, the Reagan cuts amounted to 5 percent of the total cost of government. Overall, discretionary domestic spending dropped about 14.2 percent during Reagan's first year. Several Great Society programs were sharply cut. The Community Development Block Grant program, for example, lost two-thirds of its funding. Reagan also won a 32 percent cut in mass transit spending.

Sen. Pete V. Domenici was correct to call the 1981 budget "the most dramatic reduction in the ongoing programs in the history of the country"—but mostly because federal spending had risen relentlessly for three decades both absolutely and relative to the nation's wealth. Had that trend continued, the federal government would have grown relative to national income by about 25 percent (from one-fifth of GDP to one-fourth). Instead of increasing, the relative size of government stayed roughly the same as it had been in

Continued on page 6

Cato senior fellow in constitutional studies Ilya Shapiro speaks to the media after the landmark Supreme Court decision, *Citizens United v. Federal Election Commission*, which struck down decades of campaign finance regulation in a sweeping victory for freedom of speech. The Cato Institute filed an amicus brief during this important case, one of 26 such briefs Cato sent to the Court in 2009. **PAGE 3.**



BY ROBERT A. LEVY

“The insurance mandate might still be resurrected — an insidious federal power that can force Americans to purchase private goods they don’t want.”

Chairman’s Message

Taking Government to a Whole New Level

Imagine this conversation:

PRESIDENT OBAMA: “We need to bend the health care cost curve. I want the food industry to cut chocolate sales by 25 percent.”
INDUSTRY: “But we would lose $100 million from the cutback.”
OBAMA: “Just raise the price of celery to recoup the $100 million.”
INDUSTRY: “Nobody will buy celery at the inflated price.”
OBAMA: “Not to worry. We’ll impose a fine on any family that doesn’t buy a sufficient quantity of celery.”

Sounds inconceivable, doesn’t it? Scandalously, it’s more than conceivable; it may be reality. Obamacare—temporarily frustrated by Massachusetts voters—doesn’t require the purchase of celery, but it does require the purchase of health insurance. Here’s (roughly) how Obama’s actual conversation with the industry unfolded:

PRESIDENT OBAMA: “A lot of sick people can’t get insurance. I want the industry to cover preexisting conditions.”
INDUSTRY: “But we would lose a fortune if we did.”
OBAMA: “Just raise premiums paid by healthy people and sell more policies to those who aren’t insured.”
INDUSTRY: “If we have to cover preexisting conditions, healthy people won’t buy policies until they’re sick.”
OBAMA: “Not to worry. We’ll impose a fine on any family that doesn’t buy a policy now.”

Whether it’s celery or health insurance, the federal mandate is a thinly disguised subsidy to special interests who agreed to play ball with the government. When similar legislation was considered in the context of Hillary-care in 1994, the Congressional Budget Office wrote: “The government has never required people to buy any good or service as a condition of lawful residence in the United States.”

Some legal scholars insist that the mandate is authorized under the all-encompassing Commerce Clause. Indeed, the infamous 1942 case *Wickard v. Filburn* vastly expanded the commerce power. Roscoe Filburn grew more wheat than allowed under FDR’s Agricultural Adjustment Act. Filburn didn’t sell the excess; he used it to feed his family and farm animals. Still, he was ordered to destroy the wheat or pay a fine. Understandably, Filburn protested that growing and eating his own wheat didn’t involve commerce and occurred within a single state. No matter, said the Supreme Court. By not buying and not selling, Filburn affected the supply and demand for wheat in interstate markets.

Fast forward nearly seven decades: Compulsory health insurance is essential, we are told, for national health care regulation. According to *Wickard v. Filburn*, even an intrastate market can be regulated if failure to do so would undercut a federal regulatory scheme.

Well, not quite. Just because Congress could regulate Filburn’s wheat production doesn’t mean Congress can require consumers to purchase bread in order to subsidize wheat farmers. In the same fashion, even if Congress can regulate health care, that doesn’t mean Congress can require consumers to purchase insurance in order to subsidize insurance companies. The power to regulate interstate commerce does not extend to penalizing nonpurchase of health insurance—a product, by the way, that is barred by state laws from being sold across state lines.

Proponents of Obamacare had a fallback position. The insurance mandate, they contended, falls within Congress’s power to tax in order to provide for the general welfare. In *Helvering v. Davis* (1937), the Supreme Court cited that power in upholding the Social Security system. By extension, the Court would no doubt uphold Medicare. And if a mandate to buy insurance from a government insurer is constitutional, why not a similar mandate to buy from a private insurer?

Three points in response: First, private insurers under Obamacare are not mere government subcontractors. They are special interests who receive above-market prices for unwanted policies as a subsidy for covering pre-existing conditions. Second, the General Welfare Clause is triggered by taxes; yet the penalty for not buying insurance is a fine, not a tax. It’s like the fine paid for speeding or violating other government edicts. That’s why the entire process is off-budget, exempt from the usual fiscal rules and oversight. Third, if the penalty were indeed a tax, it would be a direct tax, imposed on families, and must therefore be apportioned by population to be constitutional.

Despite those objections, the health bill may yet become the law of the land. Never mind the backroom deal that taxed Cadillac health plans, unless they were sponsored by labor unions. Never mind the Medicaid exemption for Nebraska that bought a 60th vote from Sen. Ben Nelson. Those deals are behind us. Now, through parliamentary shenanigans the insurance mandate might still be resurrected – an insidious federal power that can force Americans to purchase private goods they don’t want. Beware the new role for government that the political class has put on the table.

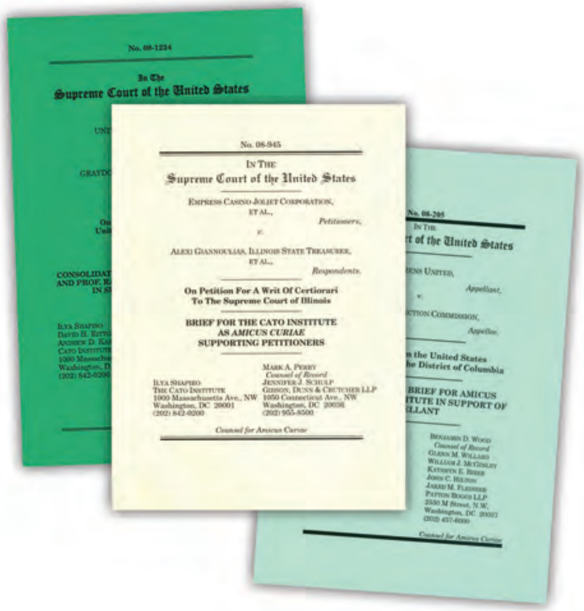
Robert A Levy

Cato files 26 briefs with the Supreme Court

Amicus Avalanche

While much of Cato's activities focus on keeping Congress and the president from inflicting too much harm on Americans' liberties and pocketbooks, our scholars have not neglected the government's third branch, the one most directly responsible for enforcing the Constitution's ideals of limited government.

The Supreme Court heard a lot from Cato over the last year. Thanks in part to the addition of senior fellow Ilya Shapiro, Cato filed 26 amicus briefs in 2009, a record for the Institute and a testament to the richness of libertarian legal thought. Many of these briefs focused on those rights we often feel are most central to classical liberalism: freedom of speech and religion and assembly, of the right to bear arms, and to be free from arbitrary detention.



Among the most notable were briefs in *McDonald v. City of Chicago*, arguing that the Supreme Court should extend freedoms it upheld in *District of Columbia v. Heller* to the states, and that it should do so through a rebirth of the Constitution's privileges and immunities clause, what Shapiro called a "cornerstone of the libertarian legal movement."

The case *United States v. Comstock* presented Cato scholars with the opportunity to tackle a horror both Orwellian and Kafkaesque. At issue is the federal government's power to civilly commit anyone it decides is "sexually dangerous," even after that person has served his time and even without proof of a new criminal violation. Cato, joined by Georgetown law professor and Cato senior fellow Randy Barnett, quoted the Supreme Court itself, which recognized almost 150 years ago in *Ex Parte Milligan* that "no graver question was ever considered by this court, nor one which more nearly concerns the rights of the whole," than the government's unconstitutional assertion of power against its own citizens.

Early in 2010, adjunct scholar Richard Epstein wrote a brief on the pending case, *Christian Legal Society v. Martinez*, which addresses Hastings College of the Law's ability to exclude religious student groups from using its facilities if those groups discriminate in their membership in ways the law school disapproves of. Epstein urges the Court to safeguard public university students' right to form groups—which by definition exclude some people—and to do so free from government interference or censorship.

With one of these briefs cited during oral argument, and another vigorously attacked by the solicitor general, it was clear they had a significant impact, too. With an increasingly unresponsive government, the battleground for libertarian ideas has often moved to the courts. This has lead to victories like *Heller*'s upholding of the Second Amendment and *Citizens United*'s rolling back of the government's restrictions on freedom of speech.

Courts have often been more amenable than the other branches to many of the arguments libertarian thought thrives on, such as the rule of law, original intent, and strong protections of rights. Cato's 26 amicus briefs in 2009 kept pressure on the Supreme Court to remember this—and future briefs will continue to do the same.

Cato News Notes

WE'RE NO. 1!

Throughout January Cato@Liberty was the #1 U.S. political blog available on Kindle. Or at least it's been the #1 U.S. blog in the "News, Politics, and Opinion" category, and the #3 politics blog in the same category. What's the difference? We're not sure. So we'll just stick to "we're #1." Visit www.cato-at-liberty.org on the web or subscribe at Amazon.com.

WE'RE NO. 5!

The Cato Institute was rated no. 5 in a rating of "Top Think Tanks—Worldwide" in the 2009 edition of "Global Go To Think Tank Rankings," compiled by James G. McGann of the University of Pennsylvania. McGann asked some 300 experts worldwide to rate 6,300 think tanks. Cato was also listed in the top 5 in various sub-categories, including U.S. domestic economic policy, health policy, science and technology, best use of the internet, and "most innovative policy."

WE'RE 33!

The Cato Institute was founded in January 1977 by Edward H. Crane and Charles G. Koch. That makes us 33 years old this year. In fact, when we host the Milton Friedman Prize for Advancing Liberty Dinner at the Washington Hilton on May 13, we'll be 33⅓ years old, exactly a third of a century. To see our beautiful and comprehensive report on our first 25 years, search for "25 Years at Cato" at www.cato.org.

Former director of the Congressional Budget Office Douglas J. Holtz-Eakin speaks at a Capitol Hill Briefing in December. Holtz-Eakin was joined by Cato's Dan Mitchell (left) and Chris Edwards (right), as well as Rep. Paul Ryan (R-WI), in discussing whether a budget task force would accomplish anything meaningful—or if it might even do more harm than good.

Ian Vásquez, director of the Cato Institute's Center for Global Liberty and Prosperity, talks with Rep. Jeff Flake (R-AZ) before an event on Capitol Hill in December on the need to end the travel embargo on Cuba. Representative Flake said that it's time for a get-tough policy with Cuba—which means not continuing the failed policies of the past 50 years.

In January, the Cato Institute ran another session of its popular Cato University, this time with the Universidad Francisco Marroquín in Guatemala. During a tour of Francisco Marroquín's campus (left), the participants were introduced to one of the high-tech multimedia classrooms in that university. Cato's distinguished senior fellow, José Piñera (right), gave the inaugural lecture on how Latin America can defeat poverty and underdevelopment.

ANTHONY DOWNS, senior fellow at the Brookings Institution, speaks at a January book forum for Cato senior fellow Randal O'Toole's new book, *Gridlock: Why We're Stuck in Traffic and What to Do about It*. Downs praised the book, saying, "The Government Accountability Office should buy hundreds of copies of this book and use them to persuade the Department of Transportation to start paying more attention to what they're supposed to be doing but aren't."

Harvard law professor LAWRENCE LESSIG, founder of Change Congress, spoke with Cato scholars at an informal lunch in January. Lessig discussed his proposal for addressing the problems caused by money in politics. His proffered solution, public funding, was met with deep skepticism by the attendees, who argued that it is concentrated benefits and diffuse costs, not campaign contributions, which create many of the problems in our legislative process.

MICHAEL GERMAN (third from left), policy counsel at the American Civil Liberties Union, analyzes the last year of counterterrorism efforts at a January Cato Policy Forum, "The Obama Administration's Counterterrorism Policy at One Year." On the panel with him were (from left to right) Cato's JIM HARPER; former Department of Homeland Security inspector general CLARK KENT ERVIN; PRISCILLA LEWIS, co-director of the U.S. in the World Initiative; JACOB SHAPIRO of Princeton University; and PAUL PILLAR, a former CIA official now at Georgetown University. Their panel discussion was followed by a keynote address from Daniel Benjamin, coordinator for counterterrorism at the U.S. Department of State.

Continued from page 1

the 1970s. Reagan thus shrank the size of government compared to what it would have been if past trends had continued.

Reagan also reduced tax rates. The Economic Recovery Tax Act of 1981 was expected to return $749 billion to taxpayers over the next five years. Two-thirds of both chambers of Congress voted for it, and Gallup found that the public approved the tax cut by two to one. Here again Reagan succeeded relative to a worse outcome. The last Carter budget foresaw steady increases in revenue, culminating in taxes taking 24 percent of GNP in 1986. The average federal tax burden from 1961 to 1980 was about 19 percent of GNP. In 1981, the Reagan administration predicted federal taxes would take just over 19 percent of GDP by 1984. In that sense, Reagan's tax cuts returned the nation to normal. Without the cuts, however, we would have paid unprecedented taxes.

The tax reform of 1986 stands as the major, and perhaps only, achievement in limiting government in Reagan's second term. That law lowered rates and eliminated many tax preferences or "loopholes." Congress often says to a taxpayer: if you do something we want you to do (say, invest in "green technology"), we will grant you a partial dispensation from taxation. Such tax preferences represent a kind of political control through offers rather than threats. True, such tax breaks might seem like a tax cut, at least to those who receive them. But tax preferences do not reduce the power of government in general. Others must pay higher taxes unless spending elsewhere is cut just as much as the tax preference, and tax preferences have no relation to spending cuts. Hence, the amount of coercion remains the same.

Eliminating tax preferences—known as tax reform—faced serious opposition. Beneficiaries had reason to organize and defend their preferences. Only presidential leadership could give reform a chance. Some Democrats found preferences unfair and favored reform. Republicans were skeptical. They thought the Democrats saw in reform a chance to raise taxes on business. Ronald Reagan saw that reform might reduce government intervention in the economy and further lower tax rates. He convinced the Republicans to support reform against their political instincts and voting histories. As a result of the 1981 and 1986 laws, Reagan obtained lower tax rates for most people. When Reagan took office, the federal marginal rate on income was 70 percent. After the 1986 reform, the marginal rate was 28 percent. What accounts for these achievements against the grain of history? Reagan's political judgment and popularity mattered. But larger forces helped him. Reagan's victory followed a decade of crisis for the New Deal political order. The old way of governing had promised to end risk, increase wealth, and assure justice. The Johnson-Nixon years delivered instead an unstable economy, rising taxes for all, and with time, a growing sense of stagnation and national decline. Things had to change. The only question was how much they had to change.

> "The New Deal order will face future crises that may yet bring a revival of limited government."

LIMITS OF REFORM

Less than one might have hoped, it turned out. Reagan failed to radically reduce the size of government. The 1981 budget eliminated one program: the Comprehensive Employment Training Act of 1974, a public sector employment boondoggle that had grown rapidly under Carter. Budget experts John Cogan and Timothy Muris discovered that overall domestic discretionary spending (including defense spending but not entitlements) grew only slightly less than the inflation rate during Reagan's presidency. By 1989, such spending almost equaled its 1981 level, adjusted for inflation. Initial cuts were followed by spending increases. Spending by the Department of Education, for example, which Reagan had promised to eliminate in 1980, rose by 14 percent during his two terms after being reduced in 1981. Between 1980 and 1987, the three largest entitlements (Social Security, Medicare, and Medicaid) increased their spending by 84 percent, a total of $145 billion.

The Reagan administration tried to restrain Social Security spending. The proposals went nowhere, to put it mildly. A week after the proposals were introduced, the House Democratic Caucus unanimously adopted a resolution calling Reagan's changes "an unconscionable breach of faith." Republicans ran in fear of the public reaction. On May 20, 1981, with Reagan at the peak of his popularity, a Republican Senate and the Democratic-controlled House approved resolutions rebuking Reagan's Social Security proposals. The administration backed off. A little over a week had passed from proposal to retreat.

The same story would be repeated in early 1982. Nonetheless, the administration and Congress had to deal with the financial crisis of the program. Reagan created a national commission led by Alan Greenspan that proposed tax increases, delays in cost-of-living adjustments, and taxation of benefits. These "reforms" also fostered larger government over time. The increase in taxes officially went into the Social Security "trust fund," but Social Security is part of a unified federal budget. Increases in the payroll tax thus increased the revenues available for federal spending. If payroll taxes had not created a Social Security surplus, Congress would have had to raise taxes to pay for the current spending.

Medicare costs had been rising quickly, and Congress agreed they had to be controlled. The Reagan administration wanted to cut Medicare benefits and increase patient costs. Congress would have none of it. Eventually, Congress decided to empower bureaucrats to set prices for hospitals and physicians. Even so, Medicare spending continued to increase even as the power of the federal establishment over health care grew.

Reagan's tax cuts also failed in their larger goal of reducing spending. Reagan said at the beginning of his presidency: "Government spends all the taxes it gets. If we reduce taxes, we'll reduce spending." If tax rates were cut and indexed to inflation and members feared voter wrath for running deficits, Congress would have to raise taxes to spend more. Forced to choose between higher taxes and more spending, Congress might well favor lower taxes and, therefore, less spending. As it turned out, Congress preferred to borrow rather than cut spending deeply or raise taxes.

Reagan's most radical effort to restrain the federal government also came to nothing. In 1982, as the economy declined, Reagan proposed turning over nearly $50 billion in programs to the states and local governments over a period of eight years. State officials no doubt were tired of the heavy hand of Washington. But they did not wish to have the responsibilities that went along with the power, not least the responsibility of either paying for or ending the programs. Reagan's New Federalism went nowhere politically.

TYRANNY OF THE STATUS QUO

Reagan failed to radically cut back the federal establishment because American government is biased against big changes. All three branches of government must agree to changes in the status quo. The most crucial parts of Reagan's coalition in Congress had programs to protect. Conservative Democrats were willing to cut government spending except for farm subsidies, water projects, and the military. Liberal Republicans supported cuts except in transportation, fuel assistance, and education. Reagan's difficulties in Congress also reflected what might be called "the political strategy of the welfare state." Franklin Roosevelt and Lyndon Johnson both expected that programs once enacted would attract support and grow over time for two reasons. First, those who benefit from such spending are organized and motivated to protect it. Second, entitlement programs create an expectation that future benefits are earned by past contributions. Moreover, much of the general public also adapts to the increased government as time passes; what an earlier generation would have deemed tyranny, their grandchildren see as part of the status quo.

Big changes in the political status quo require a big crisis to sweep away the forces preventing change. By 1980, the order created by Roosevelt and Johnson was hampering economic growth and losing support. The 1970s crisis, however, was not severe enough to sweep away the old order. Reagan ended up reforming, not destroying, the New Deal order. Growth resumed. Most of the old ways survived to see "Morning in America."

"By 1980, the order created by Roosevelt and Johnson was hampering economic growth and losing support. The 1970s crisis, however, was not severe enough to sweep away the old order."

The struggle to limit government almost ended in 1988. Reagan's successor, George H. W. Bush, accepted tax increases in exchange for . . . nothing really. Yet the nation was entering a new crisis; this time the difficulties were more political than economic. Congress no longer worked. Corruption was rife. The Speaker of the House resigned from office for ethical shortcomings. Five senators—the infamous Keating Five —were investigated for wrongdoing. These failures notwithstanding, Congress seemed immune to change through elections. Incumbents rarely lost. Public confidence in government reached new lows, for good reason. The times seemed ripe once again for fundamental change.

THE SECOND TRY

In 1994, Congress itself changed. Republicans took control of the House of Representatives for the first time in 40 years. They appealed to voters on a platform of political reform and limiting government. The authors of the Contract with America said its economic proposals were "designed to enhance private property rights and economic liberty and make government more accountable." Newt Gingrich, who led the 1994 effort, promised that there would be a "pretty big" package of spending cuts early in 1995. He remarked: "This is a genuine revolution. We're going to rethink every element of the federal government. We're going to close down several federal departments." The GOP leadership seriously discussed abolishing the Departments of Energy and Housing and Urban Development.

But they were also cautious. The 1994 group promised not to cut Social Security, defense, and interest on the debt, the three largest kinds of federal spending.

The tax relief proposed by the GOP meant that the fourth largest category of spending—Medicare and Medicaid—would have to be cut. By 1996, Medicare was expected to cover 36 million people at a cost of $178 billion, or 11 percent of total federal spending. Medicare spending on hospitalization insurance had experienced near double-digit annual increases or above from 1992 to 1994. The House Republicans decided to restructure the programs to reduce spending by $430 billion over seven years. The largest previous reduction in Medicare had been $56 billion in five years, enacted in 1993.

They seemed ready to enact the deep changes Reagan had failed to attain. But the president had to agree to such changes. President Bill Clinton vetoed the cuts, and the government shut down. Democrats found tax cuts easy to demagogue. Rep. Pete Stark (D-CA) said Republicans "have decided to reward their rich friends and stick it to the women and sick people." Losing the battle for public opinion, the Republicans relented and sent Clinton appropriations bills. He used the veto to protect federal spending on education, job training, and the environment. The budget did reduce domestic spending from earlier baselines, but the new majority had suffered terrible political damage. A 1994 freshman House member concluded that the budget confrontation "was a disaster . . . the momentum of 1994 came to an end."

House Republicans lost the battle for public opinion, but they did not suffer an electoral debacle in 1996. Seventy Republican freshmen ran for reelection. Fifty-nine of them won—an 84 percent reelection rate. These freshman incumbents, on average, received about the same proportion of the vote in their districts as they had in 1994. Analysts found no evidence that voting for less government hurt Republican incumbents in moderate to liberal districts. The political story was much the same as it had been with Reagan. Voters supported con-

> "A majority of Americans will have to truly want less government and persist in that desire when programs begin to be cut back."

straints on government spending and taxing but not the big changes the 1994 House freshmen sought to enact.

The summer of 1997 brought a budget deal and thereafter budget surpluses for a while. In retrospect, that summer marked the end of the struggle to limit government until the summer of 2009. After the budget deal, many Republicans concluded voters had lost their taste for cutting back the state. The Republicans, the only party that had shown any desire for cuts in theory (if not always in practice) were also changing politically.

Social conservatives, practicing a politics informed by conservative Christianity, had become a larger part of the GOP base. Republican leaders responded to their new voters, first by impeaching Bill Clinton, and then by nominating George W. Bush, who won the presidency on a modified Christian evangelical platform, "compassionate conservatism." Bush proposed an active and "caring" government prepared to spend and regulate without restraint. Compassionate conservatism abroad fostered the war in Iraq which the president saw as part humanitarian mission and part crusade to transform the Middle East. The electoral consequences of the Republican turn away from limited government: bloated federal spending, declining presidential popularity, and disastrous electoral outcomes in 2006 and 2008.

THE CRISIS TO COME

What now? Just after the 2008 election, White House adviser Rahm Emanuel said, "You never want a serious crisis to go to waste." Libertarians rightly reject Emanuel's Big Government agenda. As we have seen, however, he was correct about a crisis. The problems of the 1970s and the early 1990s were serious enough to foster mild reforms restraining Big Government. They were not serious enough to bring fundamental liberalizing changes.

But the New Deal order faces deeper crises to come. Spending (and borrowing) seem set to increase until they cannot, leading to what may be an unprecedented fiscal crisis of the state. Officials may try to raise taxes to cover the spending. Such unprecedented tax hikes may expose what might be called Big Government's crisis of consent. In general, Americans are unwilling to pay for the government they have, much less additional spending equal to five percent of national income. Why should they? Except in times of severe threats to national security, a majority of Americans have never trusted the federal government. The fiscal crisis to come may simply reveal the lack of support for many of the institutions and policies enacted after 1937.

Cato scholars provide ideas to liberalize public policy. But it will take more than good policy ideas. A majority of Americans will have to truly want less government and persist in that desire when programs begin to be cut back. That majority must find their voice in leaders with the political skill and wide appeal of Reagan. But such leaders must also want less government. For a decade, the Republican Party has been dominated by social conservatives and crusading internationalists, two worldviews inimical to limiting government. A GOP that returned to market liberalism and social moderation might find in the crises to come an opportunity to restore the almost lost promise of America, the promise of liberty for all under the rule of law.

Big Business, Big Government, and Libertarian Populism

President Obama took office promising to change the way politics is done in Washington. No longer would the special interests run policy and no longer would government line the pockets of its friends at the expense of everyday Americans. But a year later, Washington looks unchanged. Big Business is still in bed with Big Government and Obama's promises have been broken. At a Cato Book Forum in January, Timothy P. Carney, lobbying editor of the *Washington Examiner*, explained why this disappointment was probably inevitable. In his book, *Obamanomics: How Barack Obama Is Bankrupting You and Enriching His Wall Street Friends, Corporate Lobbyists, and Union Bosses*, he traces the role of lobbying interests in politics. Commenting on Carney's book were Uwe Reinhardt, James Madison Professor of Political Economy at the Woodrow Wilson School of Public and International Affairs at Princeton University, and *New York Times* columnist Ross Douthat.

TIMOTHY P. CARNEY: It's April 2008. Barack Obama is up against Hillary Clinton in the primaries. He has a lead. He's got to knock her off. His whole thing, vis-à-vis Republicans and Hillary Clinton, is that he's the guy who's going to clean up Washington and limit the special interests. He runs an ad in which he says:

> The pharmaceutical industry wrote into the prescription drug plan that Medicare could not negotiate with drug companies. And you know what, the chairman of the committee who pushed the law through went to work for the pharmaceutical industry making two million dollars a year. Imagine that. That's an example of the same old game-playing in Washington. I don't want to learn how to play the game better. I want to put an end to the game-playing.

A few months later, Billy Tauzin, the Pharmaceutical Research and Manufacturers of America (PhRMA) lobbyist and former committee chairman Obama was talking about, gets a seat at the health care table. As the *Los Angeles Times* put it, "Obama gives powerful drug lobby seat at the healthcare table." What happened, according to the *LA Times*, was that White House chief of staff Rahm Emanuel met Tauzin in the Roosevelt Room, which is just a few steps from the Oval Office in the West Wing, and they cut a deal: Obama would drop his opposition to the provision that Medicare could not negotiate with drug companies (the same deal, in the April 2008 ad, he castigated Tauzin for cutting). Nor would he go after the favor the drug companies get, where our government keeps out drugs from places like Canada that have price controls. The health care bill also contains hundreds of billions of dollars a year in prescription drug subsidies. In exchange, Billy Tauzin and the drug lobbyists said that, if you're in the Medicare donut hole, drug companies will sell you discount drugs. They also agreed to spend $150 million running ads to support healthcare reform.

How did this happen? Answer: follow PhRMA cash. Barack Obama raised $2.1 million from the drug industry in 2008. That's about equal to what John McCain raised, plus what George Bush raised in both of his elections *combined*. It's the most, by far, anybody's ever raised from the drug industry.

What's going on here is that whenever government gets involved, the door opens for special interests to get their way. Contrary to the common myth, big government ends up benefiting the biggest businesses.

This is governed by a few laws—I call them the laws of Obamanomics, but they were true from George Bush all the way back to Alexander Hamilton. First, *whoever has the best lobbyist wins*. If government's not involved, having a lobbyist isn't worth very much, but once government gets involved, buying the best lobbyist wins you the little details in the bill. Second, the *overhead smash*: regulation adds to overhead and the cost of doing business. But that overhead is always easier to bear if you're a big business. Often getting regulated is *profitable* when you're a big business, because it crushes the small guys. Finally, the *confidence* game: whenever you see Republicans talking about why we need Wall Street, they say "we need to *restore* investor confidence in Wall Street." Government benefits big business because it provides confidence.

It boils down to this. Every time government gets bigger somebody is getting rich. That's the general theme through my book, and I think it's a theme that's increasingly being perceived since the Wall Street bailouts. People no longer find it easy to say that what Wall Street wants is some laissez-faire Wild West where they're left alone. But it's missed too often when people try to tell the story.

Let me give two examples. The first is climate change. Nike got applauded when they left the Board of Directors of the Chamber of Commerce over climate change, because, oh, Nike must *care* about the planet—it wants to regulate greenhouse gases! Nike makes all of its shoes in Malaysia, Indonesia, China—outside the United States. Regulating greenhouse gases here doesn't add to their costs. But New Balance, one of their smaller competitors, makes its shoes in New England. They *would* be hit by these costs. So Nike is saying *we want you to tax our competitors' energy*, and they're getting applauded for it.

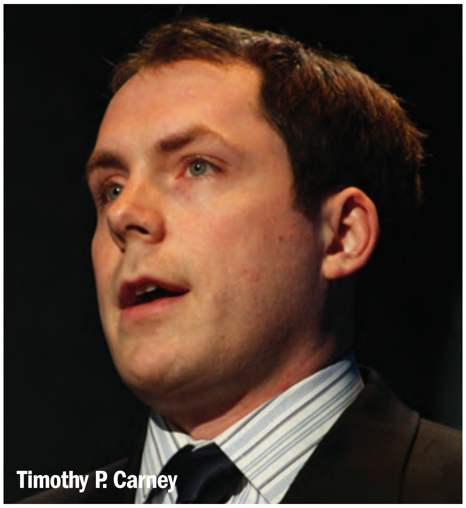
Second is the bank bailouts. There's a cartoon where a customer is standing in line at a bank and the teller says, from behind the counter, *this is a bailout!* and sticks a gun out, robbing the customer. Obama says he's battling and being tough on Wall Street, but we can poke huge holes in that. First, he re-nominated Ben Bernanke, who was Captain Bailout. The guy who came up with the original ideas for the AIG bailout and the Bear Stearns bailout was New York Federal Reserve president Timothy Geithner. And, if you've been following the headlines, Geithner has been aggressively trying to hide exactly what was going on in those early bailouts. And Obama made him the treasury secretary. Geithner's chief of staff at treasury is a former lobbyist for Goldman Sachs. Rahm Emanuel used to be a consultant for Goldman Sachs. Obama has proposed more bailouts, and his financial reform looks like it's institutionalizing bailouts.

My point is not that Obama is some sort of evil shill for big business. My point is that, when government gets bigger, big business ends up profiting. *Both parties* are the parties of big business.

UWE REINHARDT: Tim's *Obamanomics* is a stunning read. It is revealing in many ways. It's stuff we knew, but it's put together in a way that irritates you and makes you angry and reflective -- and worried about our country's future.

I liked the passage, on page four, where Tim writes Obama's "policies favor Big Business, not out of nepotism or corruption, but out of tactical necessity—he needs powerful allies—and out of economic reality: expanding the government tends to boost Big Business." And that is certainly true. Big Business owns America, not the American people. They just live and work there.

So the themes in this book are that big business makes tons of profits off federal spending and therefore favors it. Big business loves regulation. The business oligarchy can and does purchase the protection of Congress by buying legislative favors. Candidate Obama made statements and promises during his election that are belied by his conduct as president. And so on.


Timothy P. Carney

"When government gets bigger, big business ends up profiting. *Both parties* are the parties of big business."

To my mind, the central theme of *Obamanomics* is that America's system of governance sucks. Ours is a very untoward way to run a government when you come to think of it. I come from parliamentary systems—Germany and Canada—where you cannot buy legislators retail and you cannot even buy the party wholesale. I don't know how they buy influence, but it is illegal to do what is perfectly legal in this country. We have debased democracy.

Let me look at some of the chief complaints of *Obamanomics*. First, he argues, big business makes profits off government. But what, exactly, is it that bothers Tim about this? You have soldiers who need guns and tanks and missiles and stuff. So government collects money from the taxpayer and pays the private producers who make guns, and bombs, and stuff for the soldiers. How can you avoid this? The only alternative is that government collects taxes, makes the stuff itself, and then gives it to the sailors. Is that to be preferred?

When the movie *Platoon* came out in the 80s, our kids were very little. I took them to see it and they were white as a sheet coming out. And I said, "Hey, you are upper middle class kids, this isn't going to happen to you. You aren't going to be in the rice paddy. There will be others doing that, mainly from the lower income classes. You are going to be shareholders in the defense industry, and every time a gun goes *rat-tat-tat*, you'll make some profits. And every time a missile goes down, you'll make some profits." That is how national defense works these days.

But what seems to bug Tim the most, and me too, is that the business oligarchs whose firms produce things for government do not just deliver efficiently produced stuff to government at reasonable prices, but that with their tax-financed profits they can then literally purchase the affection of the legislators who then steer even more profits to them. It is a sort of circular flow of money, but not the one we teach students in macroeconomics.

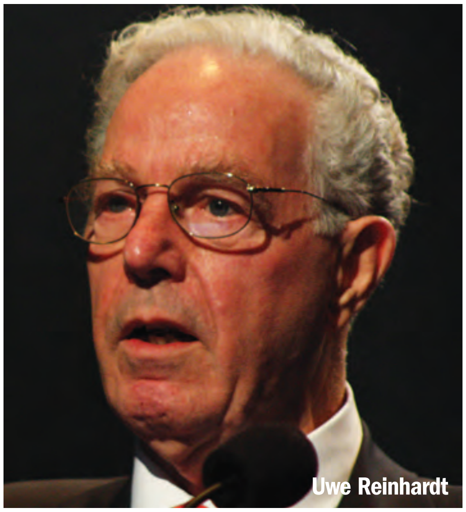
And here you have to blame the First Amendment—who ever thought that that purchasing legislators is an expression of Free Speech protected by the First Amendement. I didn't think that's what was meant by the First Amendment, but the *Wall Street Journal* pushes it all the time.

Now imagine an elderly woman without any net worth. That is not uncommon in American life —you come to sixty-five without much net worth. Would the private health insurance industry take care of her? No, it can't. Should she just be left alone to die? Do we want this? No. So you're going to have government look after her, and you have the same circular-flow-of-money story here once again. Her health care can be government produced, like for veterans. But typically we use private producers to serve government-insured Americans. The board of directors of the largest insurance company in America can't actually take money from vendors, but the House Ways and Means Committee and the Senate Finance Committee can do exactly that, and they are the board of Medicare. Once again we see why big business might like government spending.

Secretary of State Hillary Clinton was recently reported to have raised private money for a pavilion in China. Why does our secretary of state have to do this for a private-sector pavilion? I would tell American businesses, if you can't get your act together, don't go to China. Let the Chinese have that spot. They would probably know what to do. But don't ask the secretary of state of a great country to go fundraising for you to put up a pavilion for the United States. Why didn't you pay for this yourself? And heaven knows what favors the Secretary of State now owes the folks who ponied up money for the pavilion. "None," they'll protest. Oh, yeah?

And all this is going to get worse. OpenSecrets.org observes that every four years the cost of a presidential election doubles. This leaves health spending in the dust. Every four years, from $340 million in 2000, to $740 million in 2004, to $1.3 billion in 2008. Soon our politicians will need to mortgage their souls unless we stop this mad trend.

Tim writes that President Obama made statements during the campaign that were lies. Like Captain Renault in the movie *Casablanca*, I am shocked, just shocked. Now let me be truly outrageous and sacrilegious. Suppose President Ronald Reagan had said during his campaign, "If I'm president, I may deploy US marines to the Mideast, and if they get hurt there, I'll just pull out again, pull down the flag and run." He didn't say that in the campaign, of course. Far from it! But he did just that when he was president. Or suppose he'd said in the campaign, "I'm going to expand the government run health insurance program called Medicare to give the elderly coverage for prescription drugs and call it "catastrophic coverage." On top of that, if elected I will implement administered prices for hospitalized Medicare patients, a Soviet style system in which the central government sets prices for the whole country," which he actually did, in 1983. Finally, if he had said that "I'm going to give the American people a massive tax cut, but I also won't cut government spending, so I propose to increase the federal deficit throughout my term and hope my successor will do the same." Spending was out of control in both the Reagan and Bush administrations. Reagan ran on the slogan that he'd balance the budget by 1984, but



"[The American people] want mellow messages that if the candidate before them wins, everything will be made right painlessly."

no such thing ever occurred. Do we remember him as an inveterate liar?

A major tragedy in our democracy is that the American people just do not want to hear the harsh truth during an election campaign. They want mellow messages that if the candidate before them wins, everything will be made right painlessly. That's what we want. And that is why politicians say one thing during an election and often do the opposite once they govern. They are not liars in the ordinary sense of that pejorative word. They merely state "unavoidable and justifiable untruths"-- unavoidable by any candidate who seeks to win an election among a people that, as Jack Nicholson puts it in the movie *A Few Good Men*, cannot handle the truth. If we the people want to know why politicians lie to us, we should look into the mirror. We'll see the culprits.

Tim's is an eye opening book that should give American citizens pause as they boast to the rest of the world that we have the best government in the world. I'm no longer convinced of that, given how we finance it. I would offer two alternative titles for Tim's book, however. One is *If You Ever Again Trust a Presidential Candidate's Word, You May Want to Buy My Oceanfront Property in Iowa*. That would have been a very good title. Here's another: *What Were the Founding Fathers Smoking When They Gave Us a Government that Sells Economic Favors Retail?*

ROSS DOUTHAT: That's kind of a tough act to follow! But it's part of something very interesting about the current political conversation in Washington; you have a fascinating left-right convergence as the realities of liberal legislating become more apparent. This is happening, I think, because there are a lot of people on the American left who cut their teeth in politics during the Bush era and for whom this was their first profound experience of government and misgovernment. They came into the Obama era with blithe assumptions about what governance by their own side would mean. Now they are coming to terms with the fact that a lot of what they hated about contemporary Washington in the Bush years was actually the direct result, as Tim rightly points out, of having built a big, expensive government that every corporate big shot in America feels the need to influence.

It's also been interesting to see the liberal response, which has been defined by complaints about the "structure" of the U.S. government. And this is, I think, one of the most interesting turns in the political conversation in Washington recently. You have prominent liberal pundits, young and old, at a time of seeming liberal triumph crying out that our government is broken.

On the conservative side, I thought I'd just talk briefly about what the conservative response should be and whether one is really possible, or whether conservatives should

Continued on page 12

Dan Griswold tours in promotion of Mad about Trade

Free Trade's Tireless Crusader

If there is any area of policy that ought to be settled, it's the economic benefits from unrestricted free trade. Adam Smith made the case convincingly the same year America declared its independence, but almost two and a half centuries later there are still those who would use protectionism to shackle the many for the benefit of the few.

Free trade remains a message every bit as worth fighting for today as it was in 1776. Daniel Griswold's book *Mad about Trade: Why Main Street America Should Embrace Globalization* has been both a hit for the Cato Institute and an important salvo in this fight. First reviewed in the November/ December 2009 issue of *Cato Policy Report, Mad about Trade* presents a clear-eyed, optimistic, and accessible argument for the virtues of open and unencumbered trade. *Publishers Weekly* praised the book for explaining "the complicated mechanisms of world trade with brisk, easy-to-read prose."

The story of this significant book did not end with its publication, however. In the months since its release, Griswold, the Cato Institute's director of trade policy studies, visited sites along the West Coast, as well as the Carolinas, New England, San Francisco, San Diego, Florida, and Chicago, speaking to student groups, think tank scholars, and concerned citizens. And even when he couldn't appear in person, Griswold spread the book's message through 10 radio appearances, from *Bob Harden's Morning Edition* on WGUF in Naples, Florida, to the *David Boze Show* on KTTH in Seattle, Washington, to the *Mike McConnell Show* on WLW in Cincinnati, Ohio. Among all this, Griswold wrote frequent *Mad about Trade* related editorials in newspapers, magazines, and journals.

"Americans are bombarded everyday with misinformation about free trade from populists on the left and the right. *Mad about Trade* challenges the critics on their own turf," says Griswold. "The book tour has allowed me to explain how free trade affirms basic American values of compassion and fairness, competition and freedom, progress and peace."

Daniel Griswold speaks about his book *Mad about Trade: Why Main Street America Should Embrace Globalization* in December at the Yankee Institute for Public Policy in Connecticut.

Continued from page 11

just say "Our government sucks and we have to deal with it." And that may be the place where we all end up. Tim, at the end of his book (as all political books must do), makes some targeted suggestions for reform, and he also makes a broader point about the spirit that the Republican party—if it is a conservative, free market, limited government party—should have in the age of Obama. It's a spirit of "libertarian populism." I think that's exactly right. I'm less of a libertarian than Tim myself, but I think libertarian populism is, in fact, the appropriate, American response to the frankly extreme marriage of government and business that has taken place in the last couple of years. (Of course this has been going on for decades, but it is a pretty astonishing state of affairs when you have the government essentially running the nation's largest auto manufacturer, its largest insurance company, its largest banks, and so forth.) So I think that spirit is exactly right. You see it in the Tea Party movement and in politicians who are trying to harness the Tea Party movement (or be harnessed by it). I think that's healthy.

There are two problems with trying to implement libertarian populism, though. First, which is something Tim gets into in the book, is that Democrats may be becoming America's *other* party of business, but the idea of taking sides against corporate America is still foreign to many Republicans. The second problem—a deeper and longer term problem for partisans of limited government—is that the most successful arguments that are being made by Conservatives against the Obama administration's proposals tend to be defenses of middle class entitlements. So the only way you could imagine an American government that simultaneously lives up better to the ideals that Tim is speaking about and does some of the necessary things that Professor Reinhardt is talking about, is a much more rigorously means-tested welfare state. That is something that the free market side of the argument should be supporting. But, in fact, the free market party in America oscillates wildly between sweeping denunciations of big government, on the one hand, and support for existing middle class entitlements on the other. So, in the long run, even if some particular victories on regulatory fronts are won, if you look at the trajectory of government spending and government power in the United States over the next fifty years, it's all driven by entitlements. There's a great danger that the Tea Party movement, libertarian populism, and so forth could win some short-term battles, but use tactics that cause them to lose the larger war.

Site shows how to cut the government down to size

Laying Bare Leviathan

In his State of the Union address, President Obama called for fiscal responsibility and the need for Congress to work to reduce the budget deficit. Lawmakers looking for ideas on how to accomplish this feat are visiting Cato's newest website, DownsizingGovernment.org.

Created by director of tax policy studies Chris Edwards and budget analyst Tad DeHaven, the site is designed to help policymakers and the public understand where federal funds are being spent and how to reform each government department. It describes the failings of federal agencies and identifies specific programs to cut. It also discusses the systematic reasons why government programs are often obsolete, mismanaged, or otherwise dysfunctional. Edwards describes the site with more brevity, calling it "a great aid to help the layman understand where his money goes in Washington."

By visiting the sections dedicated to the various agencies, users can quickly find such depressing statistics as the fact that last year the Department of Agriculture, with its 96,000 employees, spent $991 for every U.S. household. The Department of Education spent $667, while the Department of Commerce came in at a relatively frugal $101.

DownsizingGovernment.org contains detailed information about the Departments of Agriculture, Commerce, Energy, Education, and Housing and Urban Development, but will soon expand to cover everything from Defense to Justice to Veterans Affairs.

By visiting the pages dedicated to each department, users can quickly assess the growth of budgets over time and how the money is spent, and look at proposed spending cuts. The "Reading Room" feature provides background studies by Cato Scholars, while "Downsize This!" lists quick fixes to runaway costs. Drilling down exposes a wealth of additional detail, from timelines of growth—in 1965 the Department of Education had 2,113 employees and a budget of $1.5 billion, a far cry from its 4,100 workers and $78 billion budget today—to lists of Cato experts.

Videos and podcasts round out the content, along with comparisons of the departments based on federal spending, employee compensation, number of subsidy programs, and more. Nowhere is more information about the awesome and increasing size of the federal government more readily accessible.

Says Edwards, who is also the author of a 2005 book, *Downsizing the Federal Government*, "Government is too big and needs to be cut." DownsizingGovernment.org shows how to do exactly that.

Sensible policies toward Iran, North Korea, and the War on Drugs

Tour for Global Peace

Promoting peace both at home and abroad has long been a goal of the Cato Institute, and two recent speaking tours, made possible by grants from the Ploughshares Fund and the Open Society Institute, have provided an opportunity for Cato scholars to spread this important message in person.

The first tour, sponsored by Ploughshares, featured Christopher A. Preble, director of foreign policy studies, Ted Galen Carpenter, vice president for defense and foreign policy studies, senior fellow Doug Bandow, and associate director of foreign policy studies Justin Logan, discussing the nuclear programs of Iran and North Korea. The talks ranged from Cato Policy Forums and Hill Briefings to presentations at the World Affairs Council of Oregon, the Utah Council for Citizen Diplomacy, Texas A&M University, and Northern Michigan College, to name just a few of the venues. Their goal was to draw out the lessons of Iraq as they apply to Iran and North Korea. With that war as a model, Preble said that the costs of a conflict with the latter two countries would "likely be enormous." Carpenter, in a speech in Colorado, criticized the isolation strategy being engaged in with Iran and North Korea, saying that it would create incentives for those countries to sell their nuclear technology to the highest bidder.

Carpenter and Bandow were joined on the second tour, sponsored by the Open Society Institute, by Ian Vásquez, director of the Center for Global Liberty and Prosperity, and Juan Carlos Hidalgo, project coordinator for Latin America. They spoke about the tragic human cost of the international War on Drugs. At a speech at the World Affairs Council in Indianapolis in October, Vásquez discussed the benefits of drug legalization with close to 100 participants, including professors and students from local colleges. Vásquez and Carpenter spoke together at a Cato Institute Capitol Hill Briefing in May, and Hidalgo gave three lectures in Michigan, including one to an audience of more than 200 people at the Dennos Museum Center at Northwestern Michigan College.

New York Times columnist Ross Douthat speaks to the media after a forum for Timothy P. Carney's book, *Obamanomics: How Barack Obama Is Bankrupting You and Enriching His Wall Street Friends, Corporate Lobbyists, and Union Bosses*. Douthat examined the reaction to current politics of those who "came into the Obama era with blithe assumptions about what governance by their own side would mean." His remarks are part of the Policy Forum feature on page 9.

Alvaro Vargas Llosa, author of *Liberty for Latin America*, commented on a talk by Carlos Alberto Montaner, renowned Cuban exile writer and author of Latin Americans and the West. Montaner insisted that the roots of Western culture in Latin America run deep. Vargas Llosa agreed, saying that even the anti-Western populism sweeping many South American countries is itself an aspect of Western political thought—albeit one the West moved on from long ago.

Cato's newest analyst, research fellow Julian Sanchez, debated renewing the Patriot Act at a Policy Forum in December. Sanchez traced the remarkable shift the Patriot Act represents in the way the United States conducts surveillance and argued that we need to turn the renewal debate around, demanding that proponents justify each of the act's provisions.

Cato senior fellow Tom G. Palmer (left) meets with Governor Abdul Qadeer Fitrat (center) of Afghanistan's Central Bank during a tour of the country in December. Afghanistan was just one of 27 countries Palmer visited during 2009, giving speeches on liberty and limited government at think tanks and universities, to student groups and politicians.

DECEMBER 1: *Realizing Freedom: Libertarian Theory, History, and Practice*

DECEMBER 2: Time to End the Travel Embargo on Cuba

DECEMBER 3: The Great Debate: Can Smart Growth Cost-Effectively Reduce Greenhouse Gas Emissions?

DECEMBER 3: The USA Patriot Act: Renew, Revise, or Repeal?

DECEMBER 9: *Latin Americans and the West*

DECEMBER 15: Would a Deficit Task Force Fix the Budget or Punish Taxpayers?

DECEMBER 15: Rethinking Trade Policy

DECEMBER 17: Made on Earth: How Global Economic Integration Renders Trade Policy Obsolete

JANUARY 7-9: Fourth Annual State Health Policy Summit in New Orleans

JANUARY 12: *Obamanomics: How Barack Obama Is Bankrupting You and Enriching His Wall Street Friends, Corporate Lobbyists, and Union Bosses*

JANUARY 13: The Obama Administration's Counterterrorism Policy at One Year

JANUARY 19: Liberating Bone Marrow Donors

JANUARY 20: *Gridlock: Why We're Stuck in Traffic and What to Do About It*

JANUARY 21: Driverless Cars: The Next Transportation Revolution

JANUARY 24-30: Cato University at Universidad Francisco Marroquín in Guatemala

JANUARY 27: Lunch with Lawrence Lessig

Audio and video for all Cato events dating back to 1999, and many events before that, can be found on the Cato Institute website at www.cato.org/events. You can also find write-ups of Cato events in Ed Crane's bimonthly memo for Cato Sponsors.

Cato Calendar

POLICY PERSPECTIVES 2010
New York
Waldorf-Astoria • April 1, 2010

THE MILTON FRIEDMAN PRIZE FOR ADVANCING LIBERTY

MILTON FRIEDMAN PRIZE PRESENTATION DINNER
Washington
Hilton Washington • May 13, 2010
Speakers include George F. Will.

CATO UNIVERSITY SUMMER SEMINAR
San Diego • Rancho Bernardo Inn
July 25–30, 2010

CATO CLUB 200 RETREAT
Stowe, Vermont
Stowe Mountain Lodge • September 23–26, 2010

ASSET BUBBLES AND MONETARY POLICY
28th Annual Monetary Policy Conference
Washington
Cato Institute • November 18, 2010
Speakers include Charles Plosser, Steve Hanke, Gerald P. O'Driscoll Jr., Adam Posen, and George S. Tavlas.

Winter 2010 Cato Journal

Unions and the American Economy

The new year brings a new issue of the *Cato Journal*, a special edition made possible by a generous grant from the Arthur N. Rupe Foundation, that focuses on a single question of great importance for the nation's economic health: "Are Unions Good for America?"

While unions have shrunk, in both size and influence, in the private sector, they continue to exercise pernicious control in public sector jobs. They extract large wage premiums, erect barriers to entry, and advocate protectionist policies that harm consumers. In 12 articles, scholars dissect the role of unions, expose their economic and political impact, and offer free-market alternatives to protect jobs while promoting sanctity of contract and the rule of law.

Randall G. Holcombe and James D. Gwartney look at "Unions, Economic Freedom, and Growth," while Chris Edwards addresses "Public Sector Unions and the Rising Costs of Employee Compensation." Daniel Griswold, in "Unions, Protectionism, and U.S. Competitiveness," warns that "a return to the era of more closed and regulated markets should be strongly resisted." Nine other articles cover topics ranging from "Unions and Discrimination" to "Prevailing Wage Laws: Public Interest or Special Interest Legislation?" to "The Effects of Teachers Unions on American Education."

Also included are three book reviews, with William Poole on *In Fed We Trust: Ben Bernanke's War on the Great Panic* by David Wessel, Mark Calabria on *Unchecked and Unbalanced: How the Discrepancy between Knowledge and Power Caused the Financial Crisis and Threatens Democracy* by Arnold Kling, and Neal McCluskey on *The Making of Americans: Democracy and Our Schools* by E. D. Hirsch Jr.

This special issue of the *Cato Journal* challenges the myth that unions benefit all workers and exposes the fallacy of the "high-wage doctrine." It shows that the threat from public sector unions is real and that recent post-election concessions to unions may be only the beginning of a new round of political rent seeking and even more onerous labor laws.

Winter 2009–2010 Regulation

Documenting the State's Clumsy Grasp

The newest issue of *Regulation* is out with a wealth of information on the harm of an overreaching state—as well as policies to make government function better. Richard A. Epstein looks at the constitutional repercussions of an important property rights court decision in "Takings Law Made Hard," and discusses the "the dubious distinction between physical takings and regulatory takings."

Richard B. McKenzie takes on conventional wisdom with "In Defense of Monopoly," showing how monopoly rents, far from being destructive of efficiency and innovation, are actually crucial to the health of markets. Rather than forcing young people to buy insurance through individual mandates, Tom Baker and Peter Siegelman draw on an idea from insurance history to offer an incentive-based alternative in "Tontines for the Young Invincibles." John H. Cochrane scrutinizes the recent economic turmoil and makes a series of policy recommendations to prevent its recurrence in "Lessons from the Financial Crisis."

Other topics covered include the runaway federal criminal code, "restoring" environmental protections as a guise for a regulatory power grab, the impact of securities law on private capital markets, and a call by Thomas A. Lambert for permissible insider trading.

The issue also includes several book reviews, with Tim Stonesifer on *The Ascent of Money*, Jonathan H. Adler on *Retaking Rationality*, David R. Henderson on *Taming the Beloved Beast and Offshoring of American Jobs*, and Richard L. Gordon on *Acting in Time on Energy Policy.*

A history of the struggle to control the state

Taming the Beast

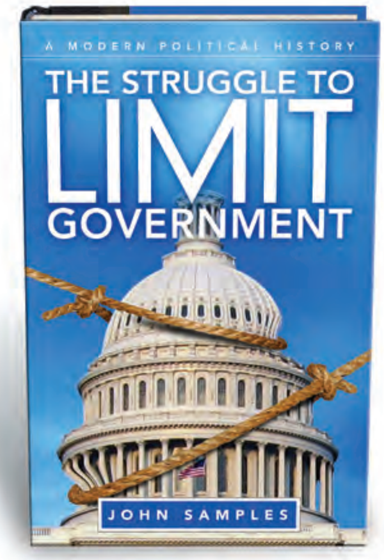
Limiting government turns out to be a whole lot more difficult than having a charismatic president and popular opinion on your side. John Samples, director of the Cato Institute's Center for Representative Government, traces the attempts to do so through the last 20 years of United States political history in his new book, *The Struggle to Limit Government: A Modern Political History*.

Samples begins with a brief glance further backwards, to the Great Depression and its aftermath, and shows how the progressive quest for technocratic excellence and, later, the rise of welfare liberalism, expanded the state well beyond what the Founders had envisioned. He shows how the massive entitlements that now threaten America's fiscal stability were carefully constructed to be politically popular, even while being economically irresponsible. All Congress had to do was enact the plans, no matter how small they were initially, for "even if funding were small, a program once started could build its basis of support in Congress and generate interest groups and executive agencies willing to work for expansion." This was an early lesson in public choice theory, demonstrating that "self-interest, if not a faith in progressivism, would sustain the federal ambit."

It was not until Ronald Reagan—whose 1980 election victory and subsequent presidency form the heart of Samples's book—that a president seriously took on the task of fighting those interests and restoring government to its proper size and scope. But Reagan faced a difficult challenge, Samples writes, for "a president who restored liberty would ask voters to take on risks and renounce benefits."

The political battles Reagan fought with Congress and the American people are recounted in detail, demonstrating the awesome hurdles that entrenched interests, the constant election cycle, and simple inertia erect in the way of political and economic change. Given these difficulties, perhaps it was too much to expect radical reform from the Reagan administration; and Samples is careful to point out that, "while Reagan's rhetoric might support such expectations, the concrete details of his proposals suggested a more modest agenda." Rather than significantly limit government, "the Reagan years saw neither growth nor reduction of domestic discretionary spending."

Reagan's successor, President George H. W. Bush, failed to sustain even his predecessor's limited legacy. But this wasn't entirely unexpected, for, as Samples points out, the voters "wanted more government than they were willing to pay for and were also willing, if not eager, to overcome that mismatch by shifting its costs into the future." Samples follows this conflict between the desire for



entitlements and the reality of paying for them through the first Bush and President Clinton, through the Republicans' stunning 1994 election victories and their regaining of the presidency with George W. Bush in 2000. And he shows how the Republican party abandoned the mission begun by Regan in 1981 when, in 1997, they repudiated the idea of limited government and, instead, embraced social conservatism and, later, national security. By carefully recounting the day-to-day struggles over votes in both houses of Congress and the swinging allegiances of the American public, he tells a fascinating—if often discouraging—story of what the theory of "limiting government" turns out to look like in practice.

Visit www.catostore.org or dial 800-767-1241 to get your copy of *The Struggle to Limit Government* today; $24.95 hardcover.

Massachusetts Is Not the Model

The Massachusetts health insurance law, proposed by then-governor Mitt Romney and enacted in 2006, is a model for much of what Congress is trying to impose at the national level. The plan was supposed to expand coverage and lower costs. With data now available to evaluate this claim, how does the so-called "RomneyCare" actually perform, and what lessons does this have for ObamaCare? In **"The Massachusetts Health Plan: Much Pain, Little Gain"** (Policy Analysis no. 657), University of Kentucky economist Aaron Yelowitz and Michael F. Cannon, Cato's director of health policy studies, use data from the Current Population Survey of 2008 to answer these questions. They find the law's impact on coverage rates overstated by the Commonwealth by as much as 45 percent. They also find evidence of significant crowding out of private insurers among low-income adults and children. As a result, RomneyCare has discouraged young adults from relocating to Massachusetts, dropping the number coming into the state by more than 60 percent. Many of these same problems are likely to occur if similar legislation is enacted by the federal government. "The costs of the legislation are therefore far greater than members of Congress and voters believe," Yelowitz and Cannon conclude, "while the benefits may be smaller than the conventional wisdom about Massachusetts suggests."

Stand Up and Be Counted

Pundits and pollsters obsess over the political tastes and whims of voting demographics from the soccer moms to the NASCAR dads. But they rarely turn their attention to what may be the largest nonpartisan group of all: libertarians. In **"The Libertarian Vote in the Age of Obama"** (Policy Analysis no. 658), Cato associate policy analyst David Kirby and executive vice president David Boaz explore this often forgotten voting bloc, assessing its size and voting patterns. While their own poll finds that libertarians represent 14 percent of American voters, other surveys place that number as high as 59 percent when defining libertarian broadly as "fiscally conservative and socially liberal." Kirby and Boaz trace the shifting libertarian support of Republican candidates, from the swing against George W. Bush to the dramatic 71 percent vote in favor of John McCain in 2008. Rather than being merely mercurial, they argue that libertarians reacted against the growth of government when voting against both Bush and Obama. After a look at the libertarian youth vote and the impact of abortion views on libertarians' party preferences, Kirby and Boaz close by warning pundits and politicians not to underestimate the strength of the libertarian vote, which is growing both in its significance and size. And this, they write "is good news for the cause of liberty."

Health Care for Me, a Big Bill for You

Young adults voted for Barack Obama in

CATO POLICY REPORT is a bimonthly review published by the Cato Institute and sent to all contributors. It is indexed in PAIS Bulletin. Single issues are $2.00 a copy. ISSN: 0743-605X. ©2010 by the Cato Institute. • Correspondence should be addressed to *Cato Policy Report*, 1000 Massachusetts Ave., N.W., Washington, D.C. 20001. • Website: www.cato.org, call 202-842-0200, or fax 202-842-3490.

record numbers. While 66 percent of them chose him for president, they may be the group hurt most by his health care proposals. Aaron Yelowitz, associate professor of economics at the University of Kentucky and an adjunct scholar at the Cato Institute, argues in **"ObamaCare: A Bad Deal for Young Adults"** (Briefing Paper no. 115) that the combination of an individual mandate (forcing everyone, regardless of their preference, to buy government-approved health insurance) and community rating (denying insurers the ability to price policies on the basis of individual risk) will lead to dramatically higher premiums for young adults. While subsidies will help those who cannot afford insurance, the cost of those subsidies will be paid through higher taxes or greater deficits—both impacting young people disproportionately. It is ironic, Yelowitz writes, that the very people who were most enthusiastic about an Obama presidency will be most harmed by the president's proposed health care overhaul.

Hurting Those Who Can Least Afford It

Frédéric Bastiat told us that "the good economist takes into account both the effect

that can be seen and those effects that must be foreseen." Michael F. Cannon, Cato's director of health policy studies, takes Bastiat's prescription to heart in **"Obama's Prescription for Low-Wage Workers: High Implicit Taxes, Higher Premiums"** (Policy Analysis no. 656), exposing the unforeseen incentives ObamaCare creates for low-wage workers. The legislation provides both mandates and subsidies for health insurance and the interaction between these would, Cannon writes, "penalize work and reward Americans who refuse to purchase health insurance." Low-wage workers will face effective marginal tax rates as high as 82 percent over broad ranges of earned income. In more narrow ranges, those rates even exceed 100 percent. With marginal tax rates that high, workers would face strong incentives not to work, trapping them in the lower rungs of the income scale. Because the legislation also forces insurers to accept enrollees at standard premiums regardless of their health status, middle-class workers could save thousands each year by dropping their existing coverage and only buying it again when they fall ill. The result is not the improved coverage at lower cost that Democrats envision. Rather, ObamaCare creates "an unstable environment that would lead to higher premiums, more government spending, and higher taxes."

Transportation for Us, Not Them

Within the next couple of years, Congress

will decide how to spend a quarter of a trillion dollars on transportation. The approach of this surface transportation reauthorization has sparked debate between two camps, one that wants to see mobility in the United States planned by enlightened bureaucrats and the other advocating a system that operates in response to actual customer use. In **"The Citizens' Guide to Transportation Reauthorization"** (Briefing Paper no. 116), Randal O'Toole, senior fellow with the Cato Institute and author of *Gridlock: Why We're Stuck in Traffic and What to Do About It*, shows what's wrong with top-down planning and why we should instead embrace customer-driven transportation. Planners want to increase congestion on the roads and instead funnel money to expensive transit projects such as high-speed rail. But these alternatives to driving are far less cost-effective—or green—than driving. Advocates of customer-driven transportation, on the other hand, call for user fees instead of taxes and support policies that make transportation providers responsive not to special-interest groups pushing pet projects and politicians dazzled by ribbon-cutting ceremonies, but to Americans who want to move about safely, freely, and at low cost.

The Changing Face of the Global Supply Chain

We're often scolded by populist politicians for failing to "buy American." But what does buying American mean in an age

of global supply chains, multinational corporations, and widespread insourcing? Daniel Ikenson, associate director of the Center for Trade Policy Studies at the Cato Institute and coauthor of Antidumping Exposed: The Devilish Details of Unfair Trade Law, shows, in **"Made on Earth: How Global Economic Integration Renders Trade Policy Obsolete"** (Trade Policy Analysis no. 42), how the nationalistic view of commerce breaks down in the face of modern trade realities. With the emergence of a global division of labor, falling trade barriers, the collapse of communism, and the rise of China as an economic power, the international economy is so integrated that distinctions between "we" and "they" no longer make sense. Firms can optimize investment and production decisions by location, using whichever country works best for each step of the process. Unfortunately, trade and investment policy have not kept up with these changes, and politicians who erect barriers in the "national interest" only harm consumers—in their own countries and abroad. Rather than persist in this outmoded thinking, governments should reduce friction in supply chains and allow the unencumbered flow of goods, services, and human capital.

CATO POLICY REPORT
1000 Massachusetts Ave., N.W.
Washington, D.C. 20001

ADDRESS SERVICE REQUESTED

"To Be Governed..."

ARNE DUNCAN'S CHICAGO SCHOOLS

This month, the mathematics report card was delivered: Chicago trailed several cities in performance and progress made over six years.

—*Washington Post*, December 29, 2009

PRESIDENT OBAMA'S TRANSFORMATIONAL LEADERSHIP

The poll also shows how much ground Obama has lost during his first year of trying to convince the public that more government is the answer to the country's problems. By 58 percent to 38 percent, Americans said they prefer smaller government and fewer services to larger government with more services. Since he won the Democratic nomination in June 2008, the margin between those favoring smaller over larger government has moved in Post-ABC polls from five points to 20 points.

—*Washington Post*, January 17, 2010

IS ENVIRONMENTALISM A RELIGION?

[Karen] Armstrong sees the role of religion as a guiding force for ethical behavior. Margaret Atwood brings that notion to life in her newest novel, "The Year of the Flood." It's set in a dystopian near future where genetic engineering has ravaged much of the planet. The survivors have created a new religion.

Ms. ATWOOD: This group, which is called God's Gardeners, has taken it possibly to an extreme that not everybody will be able to do. They live on rooftops in slums on which they have vegetable gardens. And they keep bees. And they are strictly vegetarian....

Atwood created a new pantheon of saints, including Rachel Carson, Al Gore and Dian Fossey, the murdered conservationist, as well as hymns, which have been brought to life by Orville Stoeber.

(Soundbite of song, "Today We Praise Our St. Dian")

—*Morning Edition*, NPR, January 1, 2010

SOCIALISM COULD CREATE A SHORTAGE OF SAND IN THE SAHARA

Venezuela, a country with vast reserves of oil and natural gas, as well as massive rushing waterways that cut through its immense rain forests, strangely finds itself teetering on the verge of an energy crisis.

—*Wall Street Journal*, January 8, 2010

BUSH AND OBAMA MAKE WASHINGTON THE PLACE TO BE

Main Street has had a tough year, losing jobs and seeing little evidence of the economic revival that experts say has already begun.

But K Street is raking it in.

Washington's influence industry is on track to shatter last year's record $3.3 billion spent to lobby Congress and the rest of the federal government .

—*Politico*, December 22, 2009

WE DIDN'T MEAN TO SCREW THINGS UP

In Virginia, taxi drivers are worried about a city regulation requiring them to have two dispatch calls each day. If the taxi companies don't meet the standard, city regulators can shut them down.

Alexandria created the rule back in 2005 to prevent taxi drivers from spending all their time picking up fares at hotels and the airport. Since that time, one company closed because it couldn't meet the requirement and another has been put on probation.

But Transportation Chief Bob Garback says the city doesn't want to shut anybody down: "Our objective is just to make sure that we have reasonable taxi service here. Shutting companies down doesn't really serve that purpose."

—WAMU, December 11, 2009

RACIAL POLITICKING FOR THE SUPREME COURT

Latino leaders began laying the groundwork for a Sotomayor nomination almost as soon as President Obama was elected. During the Administrations of George H. W. Bush and Bill Clinton, Latino groups had repeatedly failed to coalesce around a candidate. This time, they were determined to wield their influence as a bloc....

[Rep. Nydia] Velázquez gripped Obama by both hands. "Mr. President, you have an opportunity, here in your hands, to shape the United States Supreme Court for years to come."

Obama whispered into Velázquez's ear and smiled. "I know—there's a Puerto Rican woman."...

Latino leaders also lobbied their black counterparts to the cause. "The concern of some people, and I believe some in the White House, was with what political capital they could use in nominating a Latina in terms of the black community, who feel that Clarence Thomas doesn't represent them," Velázquez said. On the House floor, Velázquez approached the North Carolina representative Mel Watt, who serves on the House Judiciary Committee, and who formerly chaired the Congressional Black Caucus. A few days later, Watt called Velázquez on a Saturday. "Nydia, I placed a call to the White House," he said. "I said, 'If there's not a black candidate that makes the short list, we will be supportive of Sonia Sotomayor.'"

—*New Yorker*, January 11, 2010