Big Government: Democracy’s Deadly Creation

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Published In
The SmithKline Forum for a Healthier American Society, 2, 6.
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Commentary: presented by SmithKline Corporation

How dangerous is the growth of government? Economist Allan M.

I beheld the wretch—the miserable monster whom I had created. 
—MARY WOLLSTONECRAFT SHELLEY

In America and throughout the world, creation of wealth remains the human challenge. America’s unequaled prosperity can be matched anywhere, or even surpassed, if governments adopt policies that favor economic growth and enhance freedom. With freedom of exchange, the marketplace stimulates ingenuity, puts resources to their most efficient uses, and solves problems of scarcity and poverty. It disperses opportunity, prosperity and power.

Far from protecting economic freedom, however, democratic governments increasingly restrict it. Governments, in a word, grow.

**How Does Government Grow?**

Government grows by taxing the incomes earned in the private sector, using the revenues to redistribute income and build bureaucracies. Individuals surrender their control of spending and their freedom to choose how resources are used. The power to decide shifts from individuals and the market process to bureaucrats and the political process.

Whether measured by the share of income taken in taxes or by the portion of the labor force employed, government has grown relentlessly. At the turn of the century, American government at all levels—federal, state and local—employed 4 per cent of the labor force and absorbed 8 per cent of income. By 1951 the shares had risen to 10 per cent and 21 per cent respectively. Government today employs 15 per cent of the labor force and takes 33 per cent of our income.

In most other democracies, the growth has been even greater. **Taxes—Only the Beginning.**

These direct, easily measured costs are not the total cost. Income tax reports and other paperwork demanded by government absorb millions of hours of labor and cost billions of dollars. Each person’s effort to get or give an interpretation of an imprecise law involves energy and time that could be used to produce goods or services. Complex regulation diverts a major share of our resources to tasks that add little to our well being. Even when regulation seeks a desirable end, the costs of achieving the end often outweigh the benefits.

Modern governments have grown despite their limited success at fulfilling their basic responsibilities. Postal service, criminal justice, education, police protection—none of these services as provided today is an example of efficiency or outstanding performance. The newer activities toward which government has directed its attention, and our resources, have

brought few memorable achievements and several costly failures. Yet government continues to grow.

**Why Government Grows.**

Government grows because there is a decisive difference between the political process and the market process. The market process distributes income according to each person's perceived contribution, as determined by the tastes, talents and opportunities that are found in society. The political process redistributes income according to the accepted voting norm—one person, one vote.

In the United States, this redistribution can and does occur because of an income spread that is normal in democratic countries. 50 per cent of voters live in families that earn less than $19,000 a year, while the most affluent 25 per cent of families earn about 50 per cent of all pre-tax income—at least $26,000 per family. And though the affluent are somewhat more likely to vote, they are a minority. The majority can vote to tax them heavily, and it does.

During the past twenty years, the share of the federal budget redistributed to individuals has doubled and now approaches 50 per cent of federal government outlays. Tax revenues are redistributed as income—cash and services for specific segments of the population—and are used to pay the salaries of government employees. In addition, taxes finance universally shared benefits like defense and public works.

Common belief, aided by much repetition, suggests that the highest income earners escape burdensome taxes. Not so. A careful recent study finds that the top 10 per cent of income recipients earned 31 per cent of all income but paid 41 per cent of all taxes received by government. These percentages vary from state to state, by age and by source of income, but the numbers change very little if we consider only income taxes and disregard payroll, property, sales and other taxes. People with high incomes bear much of the direct cost of government.

Nor can the cost of government be shifted to corporations. Profits of corporations, large and small, were less than 10 per cent of total income in most recent years. If all the income left to corporations after taxes and dividends in the last five years had been taxed away, the total would not have covered the federal government deficit for the same period.

**Who Loses?**

We all do. By redistributing more we have reduced opportunities and incentives to save, invest and work.

There are two ways to get more tax revenue for redistribution. One is by saving and investing—pushing up the economy's growth rate. With economic growth, everyone has more income. Tax revenues are higher even if tax rates are lower. The rich get richer, but the poor get richer, too. U.S. history—and the history of many other countries—shows that with sustained economic growth the poor get richer faster than the rich.

The other method—higher tax rates—reduces saving. There is less investment and less growth. Standards of living are lower for an indefinite future. The poor make relative gains at the expense of the rich, but both rich and poor lose.

**For the Future.**

To provide growth, more jobs and better pay, industry must invest in new plants, modern equipment, and advanced technologies. The financing for these investments must come from individual saving and from the reinvestment of corporate profits.

There are two ways to increase incentives to invest. We can shift the tax burden from investment to consumption, or we can reduce taxes on both consumption and investment—by slowing the growth of government.

Tax rates on investment and saving are high, but so are the tax rates faced by welfare recipients when they take jobs. If we shift the tax burden to consumption, there-

(continued)

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Meltzer has served as a consultant on economic policy to Congressional committees, administrative agencies and departments and to foreign central banks and governments.

Meltzer has written or co-authored more than 100 books and articles on economic theory and policy. His current research on the size and growth of government, on which some of the ideas in this commentary are based, is a joint effort carried out with his colleague, Scott F. Richard.

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