Made worse by the 2001–2003 tax cuts, the looming federal fiscal crisis means more government intervention in human lives.

The New Age of Big Government

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For many decades, a major theme in American conservative thought and politics has been battling "big government." While partly waged on the regulatory front, the main action for at least three decades has centered on the fiscal system. This theme is well conveyed by Ronald Reagan's famous, oft-repeated charge that the Democrats liked nothing better than to "tax and spend." Conservative Republican advocacy of tax cuts, which first took the national stage during Reagan's 1980 presidential campaign and the ensuing 1981 tax act, became a core ideological and policy aim with the 1994 "Contract with America." More recently, broad tax cuts were a central plank of George W. Bush's 2000 campaign, and he followed those promises with significant tax cuts in 2001–2003.

Controversial though the Bush tax cuts have been, their supporters and opponents alike generally agree that they are steps toward smaller government. People figure that reducing the government's tax intake while simultaneously increasing spending and borrowing will lead to much tighter spending controls in the future, including cuts to Social Security and Medicare. (Never mind that the administration has just added an unfunded $12 trillion prescription drug benefit to Medicare.)

The Bush administration itself has been coy about the pressures on future spending that its tax policy is creating. But well-connected conservative activists are more forthcoming. Tax-cutting advocate Grover Norquist of the Americans for Tax Reform, for example, was quoted by *The Nation* as saying that his "goal is to cut government in half in 25 years," and thus "to get it down to the size where we can drown it in the bathtub."

The English writer Saki once observed, "When one's friends and enemies agree on any particular point, they are usually wrong." So it is this time. Though supporters and opponents of President Bush's tax policy agree that the 2001–2003 tax cuts are steps toward smaller government, they appear to misunderstand the notion of the "size of government." Their belief rests on spending illusion, or confusing the amount of the nominal dollar flows between individuals and government with the actual size of government. In fact, the 2001–2003 tax cuts probably are steps on the road to larger government because their main effect will be to increase wealth redistribution from younger to older generations.

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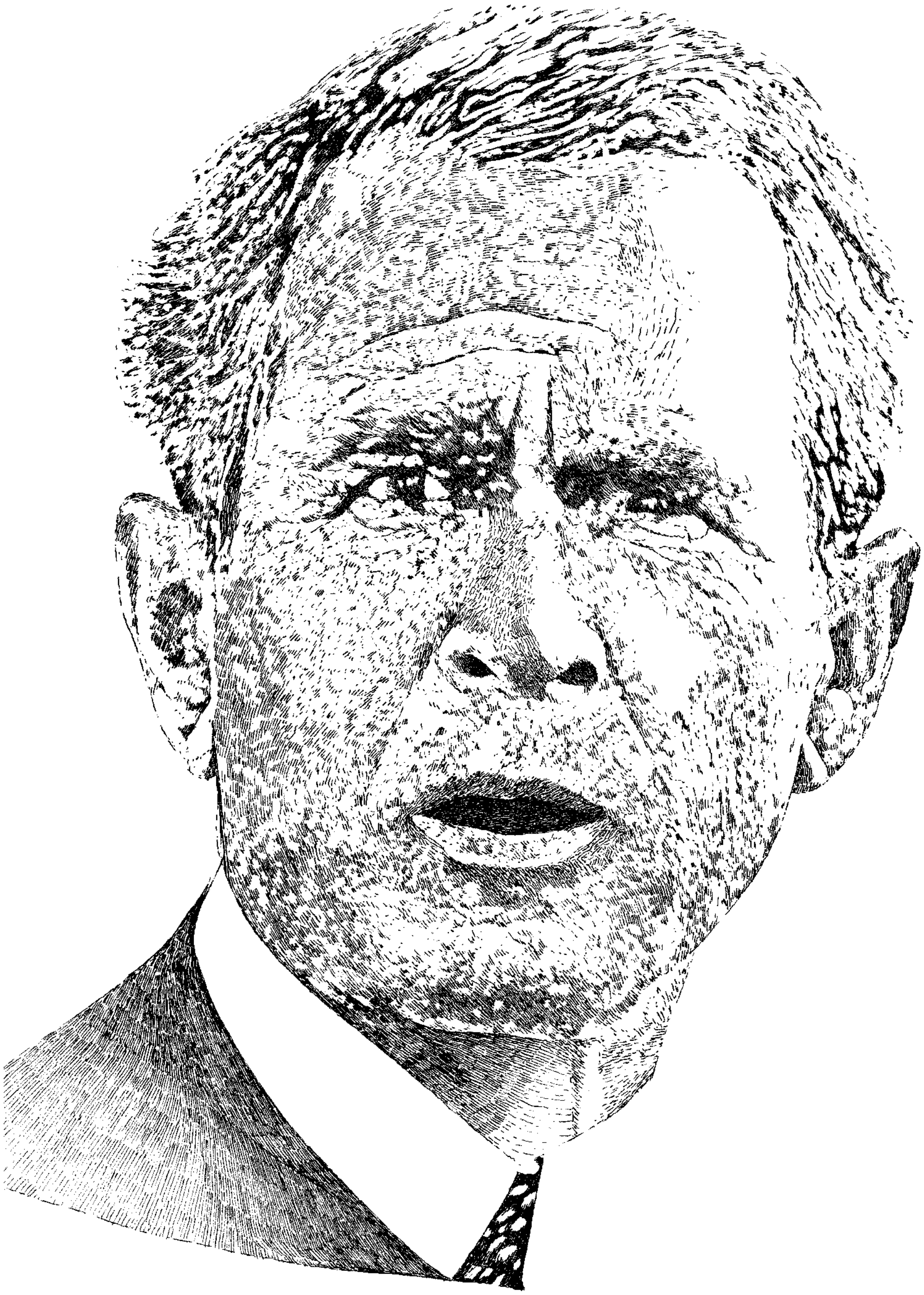
THE SIZE OF GOVERNMENT

The "size of government" is an empirical notion, presumably concerned with the magnitude of government's effect on some set of outcomes. That is, expanding government's role in education or increasing the size of the military or initiating a new wealth-transfer policy to help the poor can all be understood as increasing the size of government, whatever the merits of those policies.

So, how can we measure the size of government and thus determine the effects of the 2001–2003 tax cuts? One part of the analysis should involve considering "allocative outcomes" — how many of society's resources are directed by government to particular goods and services. The other part should involve considering "distributional outcomes" — to what extent government redistributes those resources between different groups in society.

ALLOCATIVE OUTCOMES Allocatively, one might start by measuring the goods and services that government directly supplies. Cost rather than value might need to be the metric because efforts to specify the value of those goods and services would be too difficult and controversial.

But the basic cost of those services, in and of itself, is not enough to fully measure this "allocative size." We should also take into account the allocative consequences of people's



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responses to government rules that change the relative prices of different commodities. For instance, consumption and income taxes discourage people from working as much as they would otherwise. Income taxes also typically raise the price of future consumption relative to current consumption and thus discourage saving. In those cases, the taxpayers' rational responses can be interpreted as contributing to the size of government because economic behavior is being changed by government rules.

DISTRIBUTIONAL OUTCOMES Distributionally, we could try to ascertain the size of government by netting people's taxes against the transfers they receive, and then comparing their net taxes to their net benefits from other government policies. The "baseline" for this would be to have no net redistributive effect between any group. There would be no redistribution if what each person pays to government roughly equals what he receives from it.

A complicating factor in this assessment is that people's benefit from public goods, such as national defense and police protection, is prohibitively hard to measure. So we might instead exclude the value of public goods from the calculus, and ask what net taxes people are paying, i.e., the taxes they pay minus the cash or in-kind transfers they receive. This measure should be done over the course of a lifetime. That way, the taxes that a person pays in middle age would be offset against the benefits she receives as a child (e.g., public education) and as a senior (e.g., Social Security, Medicare). If, when looking at various demographic groups, we observe that lifetime net tax payments and lifetime net tax rates are much higher for some demographic groups over others, then it is reasonable to infer that redistribution is afoot. The low-tax groups are presumably benefiting from redistribution at the expense of the high-tax groups, unless differences in the value of public goods received negate the disparity.

We therefore have a very rough basis for evaluating the likely effects of the 2001–2003 tax cuts on the allocative and distributional size of government. Do they seem likely to increase or reduce government's allocative effect on the economy via direct provision of goods and services plus responses to the effects on relative prices? And, do the cuts seem likely to increase or reduce redistribution, gauged by differences in lifetime net taxes or tax rates, if we have no reason to think that any such differences are being offset on the benefit side?

SPENDING ILLUSION

One more preliminary step remains before we consider the effect of the 2001–2003 tax cuts on the size of government. I suggested above that Norquist's cut-taxes-to-shrink-government theory (accepted empirically by liberals and conservatives alike) reflects spending illusion, or confusion between the actual size of government and the gross amounts of the nominal dollar flows between people and government. There certainly are situations where he would be correct in assuming that we can reduce the size of government by cutting taxes and spending. For example, if we reduce government spending on national defense and public education by $50 billion per year and cut taxes by the same amount, then we have made government smaller, at least allocatively. Things are not always that straightforward, however, and especially not in the currently prevailing long-term budgetary setting.

To see through spending illusion, think of government's adoption of special tax deductions and tax credits, such as the "targeted tax cuts" that Bill Clinton and Al Gore used to advocate. Those targeted tax benefits are often used in the place of traditional tax-and-spend policies to provide funding for some goal that proponents assert is not adequately supplied by the free market — be it education, housing, or sewage plants. Use of the special tax benefits cause both "taxes" and "spending" to be nominally lower than under the direct spending route. Yet the tax benefits may cause the government's allocative effect on the economy to be just as great as the tax-and-spend approach. This equivalence of the actual empirical results of government policy would be entirely missed by people who focused on the official budgetary measures of taxes and spending.

Social Security and Medicare, under which people pay taxes during their working years and then receive benefits after reaching age 65, provide another instance where people can become confused by spending illusion. To see the problem, think of a very simple two-person society that contains Jill and Bill, both of whom remain in that society for two periods of time. In Period 1, the government spends $10 supplying a public good that benefits Jill and Bill equally. It finances the expenditure by borrowing the entire $10 from Jill at the market interest rate of 10 percent per period. In Period 2, the government provides no benefits, but it is supposed to pay Jill $11. To do so, it will either levy a uniform head tax of $5.50 in order to raise the money it owes her, or renege on the debt.

Suppose first that the government reneges. Using formal, conventional definitions of taxes and spending, this means that the government will have levied taxes of zero in both periods while spending $10 in Period 1 and zero in Period 2. If instead it levies the head tax, then in Period 2 taxes will rise from zero to $11 and spending will rise from zero to $1. So reneging appears to lead to smaller government — it would neither spend nor tax in Period 2, while spending the same amount in Period 1 no matter what. In fact, however, reneging would mean that the government over the two periods engaged in substantial redistribution from Jill to Bill, rather than zero redistribution, while supplying the same public goods.

Many people who prefer smaller government would not like the decision to renege because it involves the expropriation of a contract right, and thus a government taking that is equivalent to taxation. However, the conclusion that Period 2 reneging would make the government bigger, rather than smaller, did not require violation of Jill's contract right. To understand this, suppose that, instead of selling a bond (and thus giving Jill a contract right that could later be violated), the government instead taxed Jill $10 in Period 1 in order to provide $5 in benefits to her and another $5 to Bill. Then, in Period 2, the government has a choice between doing no additional taxing or else levying a $5.50 tax on both Bill and Jill and giving $11 to Jill (or alternatively just taking $5.50 from Bill and giving it to Jill). The allocative and distributional consequences of the second option would generally be the same as those from honoring the bond in our earlier scenario. Thus, despite the absence of a Period 1 promise to Jill to even out the distribution in Period 2, assessing the tax on Bill and redistributing that money back to Jill would mean smaller government overall, because it would make up for the redistribution the other way in Period 1. From the standpoint of nominal cash flows, however, redistributing from Bill back to Jill would look like it involved even bigger government than in my earlier example. Indeed, if the government went through the motions of levying a $5.50 tax on both individuals and then handing $11 back to Jill (rather than simply taking $5.50 from Bill and giving it to Jill), then in Period 2 it would have engaged in both "taxing" and "spending" of $11.

The key to those scenarios — and to current real-world tax cuts that lead to future reductions in Social Security and Medicare spending — is that the Period 2 decision comes in midstream. It is easy to accept that government would have been smaller in the example if taxes and spending had been zero in both periods. Once government has sprung into action, however, an immediate shutdown — or even one constrained by honoring express contractual commitments in place — does not necessarily lead to a smaller government. It may instead lend to increased redistribution if the alternative in Period 2 would have been to even things out on an all-periods basis.

THE 2001–2003 TAX CUTS

In evaluating how the 2001–2003 tax cuts will affect the size of government, an initial problem is that they are only part of the story. Over the long run, the present value of government inflows and outlays must be equal. Only resources on hand can be spent, and everything must ultimately be paid for, whether through express taxes or default. There is no free lunch, so to speak. Accordingly, reducing cash inflows through the tax cuts implies compensating changes in the form of reduced outlays and/or offsetting future tax increases. What ought to be evaluated, then, is the full package of present and future taxes, spending, and borrowing, not the 2001–2003 tax cuts alone. The problem analytically is that the rest of the package has not yet been specified, and will not be any time soon.

Our long-term fiscal picture is clear enough to permit highly educated guesses about the broad character of the offsets. There is a clear tension between the long-term budget constraint and the announced long-term fiscal policy path of the U.S. government. Economists Jagadeesh Gokhale and Kent Smetters recently developed a measure called the fiscal gap or fiscal imbalance (FI) that indicates the government's long-term fiscal health. Gokhale and Smetters define the FI as "current federal debt held by the public plus the present value of all projected federal non-interest spending, minus [the present value of] all projected federal receipts [under current policy]." They go on to note that a "sustainable fiscal policy requires FI to be zero." They estimated that, as of the end of 2004, the FI would stand at $46.9 trillion if the president's 2003 budget proposals, which included a less costly Medicare prescription drug benefit than the one Congress actually passed, were enacted. Gokhale and Smetters estimate that more than 100 percent of the FI is attributable to Social Security and Medicare.

THE FUTURE The FI illustrates a counterfactual: what would happen if current policy were continued indefinitely. Because that is impossible given the long-term budget constraint, the unavoidable implication is that actual future policy will not match currently announced future policy. At some point, taxes will have to increase and/or spending will have to decline. Moreover, to the extent that spending declines, discretionary domestic spending is too small a component to bear the major brunt. Social Security and Medicare cuts will almost certainly have to do most of the heavy lifting on the spending side.

Based on the 2003 budget, Gokhale and Smetters estimated that the FI could be eliminated by adopting one of the following actions beginning in 2004:

- raising federal income tax collections by 70.1 percent,
- raising payroll tax collections by 96.7 percent,
- cutting discretionary spending by 107.8 percent (which is mathematically impossible and also would imply no defense budget), or
- cutting Social Security and Medicare outlays by 45.9 percent.

Even before the 2001–2003 tax cuts, it was clear that the looming liability from Social Security and Medicare would require either significant tax increases or large cuts in the two programs' benefits. The 2001–2003 cuts have heightened the necessity of those actions. So, what do increased future taxes and/or decreased future benefits mean for the size of government?

FUTURE TAX INCREASES The enactment of substantial future tax increases should not be discounted just because the current political environment is strongly anti-tax. Things may look very different once the payment of Social Security and Medicare benefits is at risk. I have suggested elsewhere that, within the next 15 years, there is a significant possibility that the federal government will enact a consumption-style value-added tax on top of the existing income tax and also use inflation as a deliberate policy tool for partly reneging on current obligations. This, of course, is just speculation, and we do not really know what the tax increases will be. We can, however, confidently predict two things about them if enacted. First, because the tax increases will not take effect until the future, they will result in the application of higher tax rates to future economic activity than what is being assessed on current economic activity. Second, by applying mainly to future taxpayers, the higher taxes will result in the application of generally higher lifetime net taxes and tax rates to younger than older generations. The former of those two points significantly affects our allocative measure of the size of government, while the latter affects the distributive measure.

For two reasons, the application of higher tax rates to future rather than current economic activity is likely to cause added economic distortion, and thus to increase the real size of government by magnifying its impact on economic production. First, it may induce taxpayers to shift taxable transactions from high-tax to low-tax years, especially as the transition nears and begins to take a more definite and predictable form. Second, even if economic activity cannot shift between years, the application of higher rates to some years and lower rates to others tends to increase total economic distortion relative to having smooth rates across time. It is a public economics truism that the deadweight loss from a tax generally rises more than proportionately with the rate, and indeed with the square of the rate. As Harvey Rosen wrote in his textbook *Public Finance*, "Doubling a tax quadruples its excess burden, other things being the same." This suggests that overall distortion will be higher if the rates are high in some years and lower in others than if they are constant at the intermediate rate required for long-term revenue equivalence. That is, the reduction in distortion in low-rate years will be more than offset by the increase in distortion in high-rate years.

Accordingly, to the extent that the 2001–2003 tax cuts are offset by future tax increases, they seem likely to increase the size of government allocatively. Only if the newly enacted taxes were a great deal less distortive than those they replaced would this conclusion be likely to change. Distributionally, however, it seems even clearer that the package of current tax cuts plus future tax increases makes the size of government larger. Indeed, the distributional impact is what really makes the big-government character of the 2001–2003 tax cuts almost indisputable.

In this regard, it is instructive to consider evidence from generational accounting, a method of computing lifetime net tax rates for the members of different age cohorts. One's lifetime net tax rate is determined by dividing one's lifetime net taxes (taxes paid minus transfers received) by one's lifetime income, computed in present value terms from birth. Thus, if you had lifetime income of $10 million, paid lifetime gross taxes of $4 million, and received lifetime transfers of $1.2 million, your lifetime net tax rate would be 28 percent.

Generational accounting computations generally are made under the assumption that current policy will continue indefinitely. Because the FI is unsustainable, however, its elimination must be reflected somewhere in the accounts. The usual convention is to assume that the net tax increases (i.e., higher taxes or lower transfers) needed to eliminate the FI will be borne entirely by future generations. That is concededly unrealistic, but as Laurence Kotlikoff and Scott Burns observed in their book *The Coming Generational Storm*, it is meant to provide "an informative counterfactual, not a likely policy scenario."

Kotlikoff's most recent generational accounting forecasts, pre-dating the 2001–2003 tax acts and Medicare prescription drug enactment, showed lifetime net tax rates of 17.68 percent for the youngest members of current generations, and 35.81 percent for future generations. Leaving the entire FI to be borne by future generations therefore would cause them to pay more than twice the lifetime net tax rate of current generations. One need not exaggerate the extent to which proportionate tax rates offer a definite non-redistributive baseline in order to see that this implies sizeable transfers from future to current generations. The imbalance is the product of our having run Social Security and Medicare on a Ponzi-like basis in which early generations got free benefits. It does not reflect, say, an increase in the in-kind services that future generations would get in exchange for their greater net tax payments.

The 2001–2003 changes exacerbated this redistribution from future to current generations. By lowering current generations' already-low lifetime net tax rates in exchange for raising the rates for future generations, the package of tax cuts now for tax increases later unmistakably increased government's inter-generational redistributive role. This effect is so significant that the package very likely made the government larger in distributional terms, even if one assumes that the tax cuts reduced intra-generational redistribution, such as from rich to poor, through the fiscal system.

FUTURE CUTS The prior section's conclusion may seem a bit too easy. It should be no surprise if cutting taxes now in exchange for raising them in the future fails to make government smaller. And surely this was not the scenario that proponents of the tax cuts envisioned, at least not the ones who were pursuing a principled long-term policy of shrinking government.

Part of the answer to any such challenge to the prior section's analysis is that the proponents should have envisioned this scenario. Future tax increases are only to be expected when one enacts massive tax cuts in the face of a huge fiscal imbalance plus predictable future political pressures to keep Social Security and Medicare going and little prospect of making much of a dent in the imbalance through reductions in discretionary government spending. Still, to make the story complete, one must also consider the scenario where government spending on Social Security and Medicare declines by reason of the increase to the FI that the tax cuts bring about. While seniors and the AARP bring enormous political power to defending Social Security and Medicare spending, relatively disguised or indirect cuts in particular may soon be politically possible, and in the long run really cannot be avoided.

Looking at the 2001–2003 tax cuts as part of a package with future Social Security and Medicare cuts does little to change the prior section's conclusion, however. Either way, lifetime net tax rates are being lowered on today's middle-age and older generations, for whom those rates are already relatively low, and raised for younger people and the members of future generations, whose rates already figured to be high. A dollar is a dollar whether one is losing it in the form of extra gross tax payments or reduced receipts through government transfers.

What about allocatively? Here, if anywhere, is where the tax cuts might be expected to lead to smaller government. However, the allocative effects of Social Security and Medicare, taking as given their transfer content, are a lot smaller than meets the eye. Under the influence of spending illusion, the two programs may look like big government because the cash flows that pass through them are so huge. In 2002, for example, government spending on the two programs exceeded $650 billion. So it is natural to think of them as having huge allocative effects. That is misleading, however. Despite the deadweight loss effects from the programs' mandated pay-as-you-go structure, Social Security is in some ways a fairly bland program allocatively, and even Medicare's allocative effects (given its transfer content) can be exaggerated.

Social Security actually deals in cash, which people can spend as they like, subject only to having to wait for retirement to get the money. It is a negative tax, paid to people who previously paid positive taxes, and cutting it is thus very much like increasing taxes directly. Indeed, Lawrence Lindsey, while he was the Bush administration's chief economist, made exactly that point when he argued that Social Security taxes should be excluded from the tax distribution tables because "when I pay another dollar for Social Security tax, I buy an explicit, legislated amount of benefits. … I pay the money in, I get the money out, and that's all there is to it." If the payment is not a tax because, supposedly, you are going to get your money back, then clearly there is a tax when, because of benefit cuts, you do not get your money back after all.

Perhaps Social Security's biggest effect on the economy over time has been its reducing national saving through its Ponzi-like transfers from workers who were still at a lifecycle stage when they had reason to save, to seniors who were now at a stage to consume most of what they got. But shrinking the program in mid-stream through tax cuts for today's seniors in exchange for benefit cuts in the future only makes this problem worse. So, cutting Social Security in such a way as to increase generational redistribution through the fiscal system should not be thought of as creating smaller government even allocatively, except in the sense that it reduces the effect of Social Security in requiring people to save a portion of their lifetime incomes (net of taxes and transfers) for retirement. This, of course, is hardly a benefit to people who "escape" being forced to save for retirement by having the money they were being forced to save simply taken away from them instead.

Medicare, concededly, has allocative effects that Social Security lacks by reason of Medicare involving in-kind benefits. Seniors get healthcare, albeit furnished by private providers rather than directly by the government, even in cases where they would have preferred the cash, and with rules poorly designed to give them an incentive to economize on healthcare that offers only modest or negligible benefits. Medicare's incentive and income effects have surely been huge contributors to the enormous growth of healthcare expenditure, both absolutely and relative to the economy, in recent decades. Moreover, the administering government agency (the Center for Medicare and Medicaid Services) prepares comprehensive price lists for covered medical services and monitors millions of payment requests. Thus, government might in an important respect be smaller allocatively if Medicare expenditure declined and the program's impact on the economy were thereby lessened.

Yet even this effect can easily be overstated. For one thing, as empirical research has shown, healthcare is an area where consumers' price-sensitivity is relatively low. Being healthy is a high priority, and doctors often make treatment decisions for their patients (who may lack the expertise to use their own judgment) on diagnostic grounds that reflect only limited consideration of cost. Thus, while price sensitivity is great enough to suggest that Medicare could save billions of dollars if restructured to make patients and doctors more cost-conscious at the margin, the allocative effects nonetheless appear to be small relative to the dollars involved. As for the distributional effects, while Medicare may result in significant lifetime redistribution within an age cohort because some individuals end up using it so much more than others, one should keep in mind that the package of current tax cuts plus future Medicare cuts is likely to increase the already huge redistribution from younger to older generations through the program.

Even for Medicare, it is far from clear that a package of the 2001–2003 tax cuts plus future benefit cuts would make the government smaller on balance. The bottom line would depend on how one compared the reduction in government's allocative effects to the likely net increase in its redistributive effects. However, when one considers that tax increases and Social Security cuts are likely as well, and that those actions more clearly increase the size of government, the case becomes quite powerful that the tax cuts will probably, over time, make government larger on balance. The overall package is one of much more redistribution to older generations, accompanied by only a possibility of commensurately reduced allocative effects.

SPEND AND TAX (TOMORROW)

If one looks beyond the tax cuts themselves to the overall budget policy of the current Bush administration, the case for an increase in the size of government becomes almost irrefutable. This, after all, is an administration that in its first two years increased federal outlays by $222 billion, or from 18.4 percent to 19.5 percent of gross domestic product. Only about 40 percent of this increase was for defense spending, suggesting that one could not attribute all (or even most) of it to the events of September 11, 2001. By its third year, the administration was busy proposing a new prescription drug benefit in Medicare that was initially expected to cost $400 billion over the following 10 years, and now is expected to cost far more than that. Sen. Judd Gregg (R-N.H.) rightly called this "the largest tax increase one generation has put on another generation in the history of this country," contrived simply to "get us through the next election."

If nothing else, the prescription drug enactment pretty much exploded any notion that the 2001–2003 tax cuts would shrink government's allocative effects via Medicare. Simply recouping the expansion of government from this new benefit would be a tall task. Rather, the administration appears to be seeking short-term political advantage and favors for particular groups, deceptively clothed in anti-government rhetoric. Conservative ideologues of the Norquist genre, even when opposed to the Bush administration's spending increases, appear not to appreciate that the 2001–2003 tax cuts will also have an undesirable effect on the size of government. They evidently do not, or choose not to, understand the long-term budget constraint under which a dollar of added government outlays today, if it does not reduce expected future outlays, implies added taxes with a present value of a dollar.

STARVING THE BEAST Perhaps the most powerful response to the above analysis would be to argue that its time frame is too limited. To be sure, the 2001–2003 tax cuts increase the already huge transfers from future generations to current seniors. One might surmise, however, that the tax cuts help point us toward a new steady state where government must henceforth, prospectively, be smaller because it can no longer afford big programs such as current Social Security and Medicare (or costly foreign military interventions).

There are two main problems with this scenario. The first is that it relies once again upon spending illusion. A steady state of chronic fiscal imbalance where government is perpetually struggling to meet crushing obligations — accompanied, very possibly, by capital market crises like those recently experienced by Brazil and Argentina — is not one in which redistributive transfers between competing groups are no longer possible. To the contrary, it is one likely to be characterized by endless games of redistributive hot potato with regard to the fiscal burden of keeping things going. Second, insofar as today's political practices shape the norms that will guide tomorrow's political practices, consider the message that the Bush administration's fiscal policy is sending. Present generations are transferring wealth to themselves from future generations, ostensibly so the future generations will adopt fiscal discipline that the current generations are unwilling to adopt. The audacity of this puts to shame Saint Augustine's famed wish when he was young that he would stop sinning, only not yet.

BIG GOVERNMENT A final point about the effects of the 2001–2003 tax cuts goes to the very existence of a huge fiscal imbalance in lieu of a sustainable long-term fiscal policy. President Bush admittedly inherited the FI, which results mainly from advances in life expectancy and healthcare technology that

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make Social Security and Medicare ever more expensive. But the consistent central feature of his fiscal policy has been to increase it as much as politically possible. (In both 2001 and 2003, still larger tax cuts would have been enacted but for political resistance in the Senate.) This raises the question: Even supposing we could specify the most likely future policy changes to eliminate the FI, how does having it unresolved compare, in size of government terms, to having those future changes already in place?

A key implication of not having the future policy changes as yet in place is that future government policy is far more uncertain than it would otherwise be. The president and Congress have placed a loaded gun to their heads, but we simply do not know when and how they (or more precisely their successors in office) will respond to it. Thus, anyone engaged in long-term planning, such as for retirement, must deal with considerable uncertainty about future government policy. For example, should I save lots more for my retirement because I simply cannot count on any specific component of the existing Social Security and Medicare commitments? Or should I instead save less because a big part of narrowing the FI will probably be to squeeze the people who had enough foresight to plan for their retirements?

This is not just a matter of people having to think about future government policy (and insure more against the downside) when they make their plans. Having a huge FI that remains unaddressed is a surefire political formula for making all of the competing interest groups in Washington continually invest heavily in seeking to influence future government policy. Nothing is really safe, and no government commitment can be taken for granted for more than a few years. With even Social Security and Medicare likely to be on the chopping block, none can afford to rely on political inertia to protect what they now have. This is an enviable setting for fundraising by politicians, albeit less enviable to the extent that they ultimately will be forced to choose between such unpalatable alternatives as raising taxes, cutting Social Security, and cutting Medicare.

Merely having a huge FI was evidently not enough for the current administration and Republican majority in Congress, however. Both in 2001 and 2003, they went out of their way to make the fiscal system even less stable, and unstable sooner, than if they merely had been larding an already immense FI. The mechanism of choice was to provide that the entire 2001 Act, and many of the provisions in the 2003 Act, would expire (barring further legislation) within periods ranging from two to nine years.

The main reason for those "sunsets" — which proponents of the tax cuts insisted would not be permitted to take effect — was to lower the official 10-year estimates of the cuts' revenue cost by more than 50 percent. Deceptive bookkeeping and gaming of the budgetary rules that are designed to induce long-term fiscal responsibility was only part of the effect, however. A further effect, unacknowledged but not necessarily unforeseen, was to guarantee that Congress would have to keep on considering major tax legislation again and again for the foreseeable future. For example, would interested parties with millions of dollars at stake really do nothing as the scheduled disappearance of bonus depreciation in 2005, or of the repeal of the estate tax in 2011, grew nearer? Indeed, would lobbying over suspending the sunsets not be expected to commence immediately? If Congress had purposely wanted to ensure that vast resources would be expended in trying to influence future policies, the 2001–2003 tax cuts would have been a rational move toward satisfying that want.

CONCLUSION

The 2001–2003 tax cuts, to the extent that they involved a principled, long-term policy view, seem to have been aimed at shrinking the size of government. The idea apparently was to force eventual spending discipline, even (or perhaps especially) with respect to Social Security and Medicare, by turning reduced tax revenues into a political fact on the ground that would be difficult to reverse. In fact, the idea that the tax cuts would make the government smaller seems to have rested on spending illusion, or confusion between the actual size of government and the observed dollar flows that are denominated "taxes" and "spending."

Given the long-term budget constraint and the huge preexisting fiscal imbalance, the tax cuts are likely to be paid for, in the main, through some combination of future tax increases and cuts to Social Security and Medicare. (Other government spending cuts are likely as well, but cannot contribute nearly enough.) To the extent that the 2001–2003 tax cuts lead to future tax increases, the combined effect is likely to make government bigger both allocatively and distributionally. To the extent that Social Security and Medicare spending bear the brunt, government still gets larger in the sense of increasing redistribution from younger to older generations, although Medicare cuts might decrease the size of government allocatively. R

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