

YG NETWORK

# ROOM TO GROW!

CONSERVATIVE REFORMS FOR  
A LIMITED GOVERNMENT AND A  
THRIVING MIDDLE CLASS

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First Edition

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Dear reader,

The YG Network\* recognizes that today's challenges won't be met by yesterday's solutions. We commissioned the following essays to outline an innovative agenda that empowers individuals by increasing competition and replacing failed government policies. The demonstrable failure of the liberal welfare state provides an opportunity to advance conservative reforms, firmly rooted in our constitutional order, that advance the aspirations of middle class Americans.

These policy essays were the subject of a conference that took place in Middleburg, Virginia, this March. We are deeply grateful to the authors and the other talented policy experts who engaged in lively discussions during the conference and for their commitment to devising solutions to our country's most pressing challenges. We owe special thanks to two of our authors, Yuval Levin and Ramesh Ponnuru, who skillfully edited all of the essays in this book. They were there when we first conceived of this collection of reform conservative ideas, and together with Pete Wehner, have continued to offer support and direction. The conference discussions were expertly led by YG advisor Kate O'Beirne, who has provided invaluable advice over the course of this project. And we are grateful for the participation of Kristen Soltis Anderson, John Cusey, Ross Douthat, Michael Gerson, John McLaughlin, Henry Olsen, Reihan Salam, and others in our conference. Their contributions to our discussions were critical to the success of this project.

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**John Murray**  
Senior Strategist

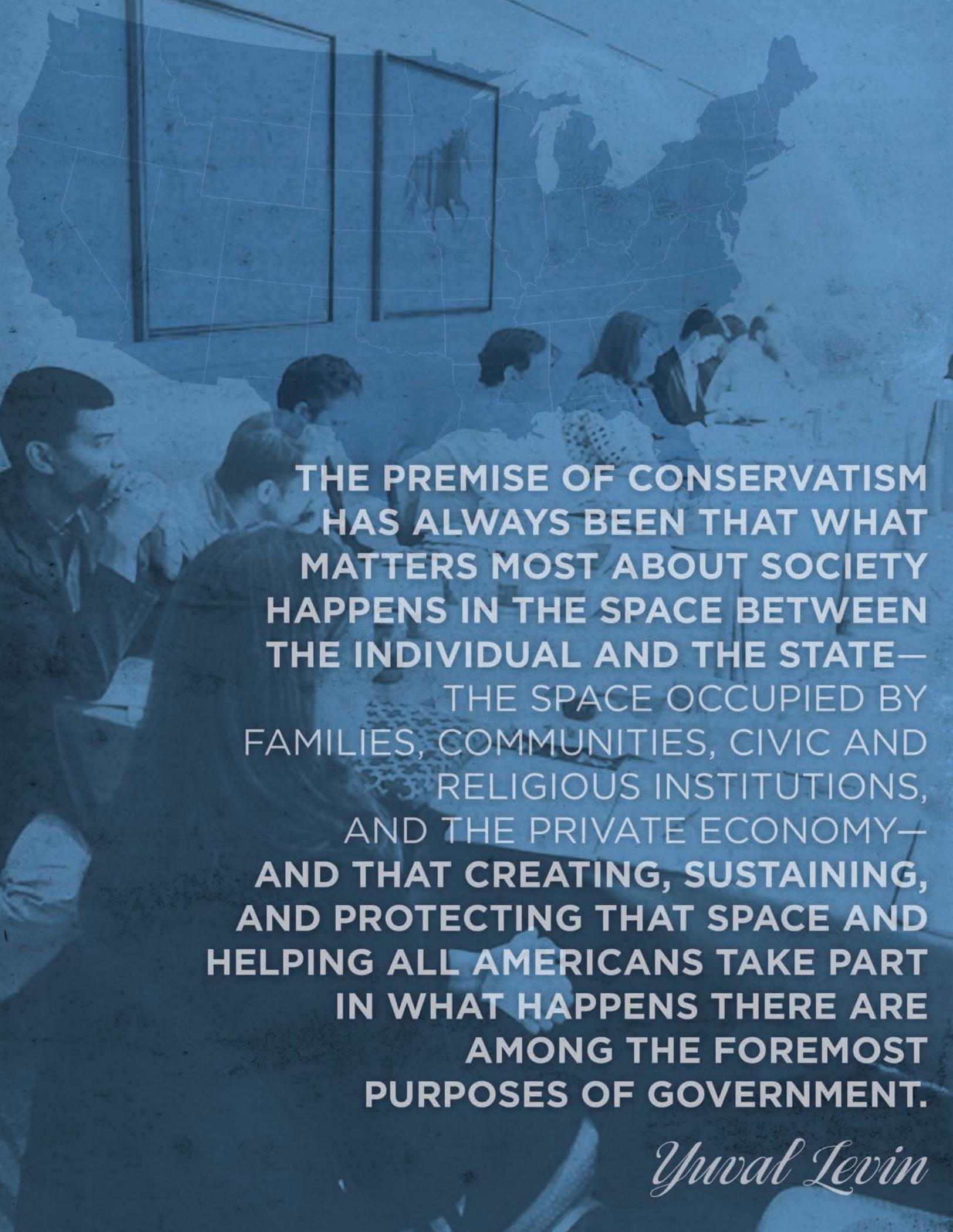
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\*The YG Network (YGN) is organized as a non-profit 501(c)(4) dedicated to broadening the Young Guns movement by supporting next-generation conservative policies and the efforts of those who advocate for those policies. All Section 501(c)(4) organizations must operate primarily to advance social welfare. The YG Network does so through issue advocacy, which includes survey research, data collection and policy and message development coupled with aggressive earned and paid media strategies. The YG movement began with House Majority Leader Eric Cantor, House Majority Whip Kevin McCarthy, and House Budget Chairman and former Vice Presidential candidate Paul Ryan.



**THE PREMISE OF CONSERVATISM  
HAS ALWAYS BEEN THAT WHAT  
MATTERS MOST ABOUT SOCIETY  
HAPPENS IN THE SPACE BETWEEN  
THE INDIVIDUAL AND THE STATE—  
THE SPACE OCCUPIED BY  
FAMILIES, COMMUNITIES, CIVIC AND  
RELIGIOUS INSTITUTIONS,  
AND THE PRIVATE ECONOMY—  
AND THAT CREATING, SUSTAINING,  
AND PROTECTING THAT SPACE AND  
HELPING ALL AMERICANS TAKE PART  
IN WHAT HAPPENS THERE ARE  
AMONG THE FOREMOST  
PURPOSES OF GOVERNMENT.**

*Yuval Levin*

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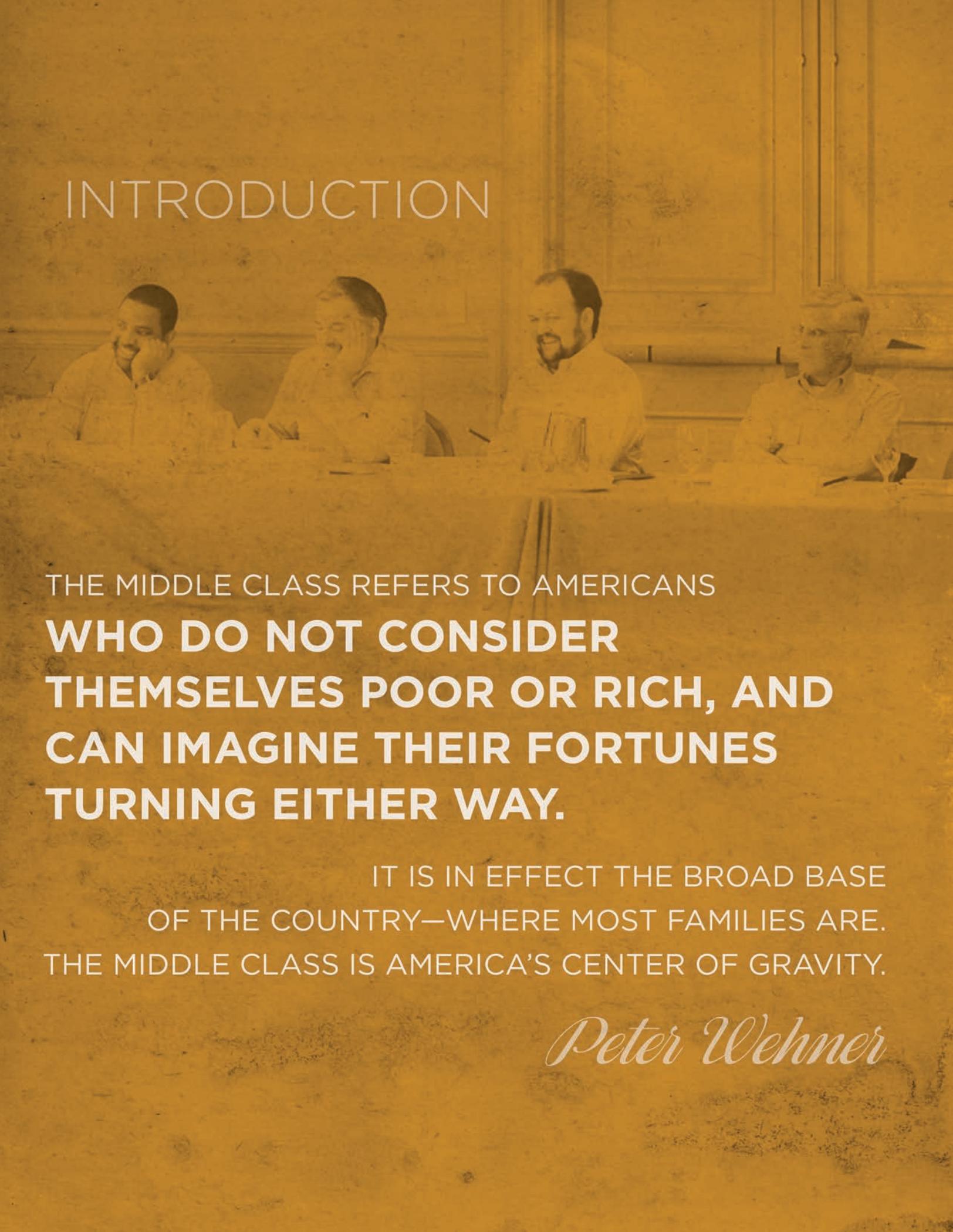
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# INTRODUCTION



THE MIDDLE CLASS REFERS TO AMERICANS  
**WHO DO NOT CONSIDER  
THEMSELVES POOR OR RICH, AND  
CAN IMAGINE THEIR FORTUNES  
TURNING EITHER WAY.**

IT IS IN EFFECT THE BROAD BASE  
OF THE COUNTRY—WHERE MOST FAMILIES ARE.  
THE MIDDLE CLASS IS AMERICA'S CENTER OF GRAVITY.

*Peter Wehner*

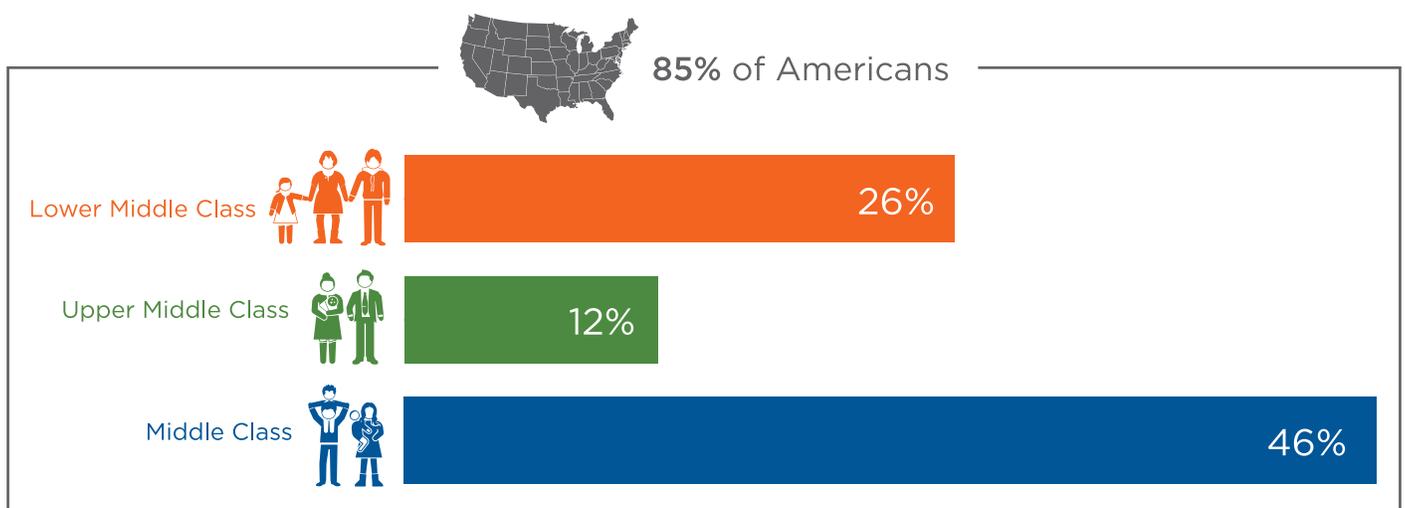
# THE ANXIETIES AND WORRIES OF MIDDLE AMERICA

PETER WEHNER

Policy is problem solving. It answers to principles and ideals, to a vision of the human good and the nature of society, to priorities and preferences; but at the end of the day it must also answer to real needs and concerns. And public policy today is clearly failing to address the problems that most trouble the American people.

This book suggests some ways forward, with special emphasis on what can be done to assist and empower working families—those who are, and those who want to be, in the middle class. It is an effort, then, to offer a concrete conservative governing agenda that is equal to this moment. The place to begin, though, is by exploring, in an empirical and disinterested way, the problems and worries of middle-class Americans. What is their sense of things? What are their greatest concerns and fears? And what explains them?

“Middle class” is of course in some respects a loaded term. It means both more and less than meets the eye. According to a recent Allstate-*National Journal* Heartland Monitor Poll, that focused on the middle class, the vast majority of Americans (85 percent) consider themselves part of an expanded definition of middle class that includes lower middle class (26 percent), upper middle class (12 percent), and simply middle class (46 percent).<sup>1</sup>



People often think of the middle class in terms of income, and the Pew Research Center defines the core of the middle class as households with incomes ranging from \$39,418 to \$118,255 in 2011 dollars. But the broad self-definition suggested by the Heartland Monitor Poll is more telling and more useful, and it gets at what we in this book mean by the term: The middle class refers to Americans who do not consider themselves poor or rich, and who can imagine their fortunes turning either way. It is in effect the broad base of the country—where most families are. The middle class is America’s center of gravity.

The Heartland Monitor Poll also offers a good general sense of contemporary middle-class concerns. It found, as other polls have found, that the dominant mood of the country is anxiety, insecurity, and unease.

“Here, you used to work 40 hours a week and you had enough to pay your rent, your utility, your car,” is how Veronica Tovar, a food-service worker in Los Angeles, put it to the pollsters. “And you could even spend some money to go out to eat two or three times a week. And that kept the money moving around.... It’s not that way now. Now you only buy what you need.”

To be sure, there is some evidence of hope and optimism. Fifty-six percent of those surveyed said they thought it was very or somewhat likely they would

reach a higher economic class at some point in their lives, for example, and most Americans still believe their fate is determined by their own effort rather than by forces beyond their control (like the state of the economy). In another recent survey, three-fourths of those polled agreed with the statement that “the American Dream is still possible and achievable for ... people like you.” On the flip side, two-thirds of Americans think it is harder to reach the American Dream today than it was for their parents, and three-quarters believe it will be harder for their children and grandchildren to succeed.<sup>2</sup>

**Two-thirds of Americans think it is harder to reach the American Dream today than it was for their parents, and three-quarters believe it will be harder for their children and grandchildren to succeed.**

*National Journal’s* Ron Brownstein, in analyzing the data from the April 2013 Heartland Monitor Poll, said, “The overall message is of pervasive, entrenched vulnerability—a sense that many financial milestones once assumed as cornerstones of

middle-class life are now beyond reach for all but the rich.” Brownstein added, “After years of economic turmoil, most families now believe the most valuable—and elusive—possession in American life isn’t any tangible acquisition, such as a house or a car, but rather economic security.”<sup>3</sup>

The findings of the survey itself tell that tale. By a two-to-one margin, those surveyed said members of the middle class have less, rather than more, opportunity to get ahead than their parents’ generation. Fifty-nine percent

of those surveyed were concerned about falling out of their current economic class over the next few years—including 28 percent who are very concerned. Seventy-six percent of workers older than forty without a college degree expressed fear of losing ground, including 45 percent who are very concerned.

These Americans are so concerned about losing ground because they believe others around them are doing just that. Asked whether more Americans recently had “earned or worked their way into the middle class” or had “fallen out of the middle class because of the economy,” nearly eight times as many said the latter.

These middle-class respondents have some ideas about what might improve their or their children’s prospects. Given a choice of four public policies to help ease their financial insecurity, 38 percent picked making higher education more affordable and accessible; 26 percent said make health care more accessible; 16 percent said make retirement benefits more secure and reliable; and 12 percent said make home loans and refinancing more affordable and accessible. But they do not believe such policies are in the offing at the moment.

The American middle class, then, is in a bleak mood and has been for some time. And it is crucial to understand that this is not simply a morale problem. These concerns are rooted in real circumstances and actual struggles. A Pew Research Center analysis of government data, for example, found that since 2000, the middle class has shrunk in size, fallen backward in income and wealth, and shed some—but not all—of its characteristic faith in the future. An overwhelming

majority of self-described middle-class adults (85 percent) said it is more difficult now than it was a decade ago for middle-class people to maintain their standard of living.<sup>4</sup>

A rising cost of living amid stagnant wages has a lot to do with these worries and pressures. Eduardo Porter of the *New York Times* points out that health-care spending per person, adjusted for inflation, has roughly doubled since 1988, to roughly \$8,500. The cost of going to college, meanwhile, has been rising faster than inflation. Two-thirds of people with bachelor’s degrees relied on loans to get through college, up from 45 percent two decades ago. Average student debt in 2011 was \$23,300. (For middle class families, the cost of one year of tuition equals about half of household income.)

In 2012, according to the Census Bureau, the typical household made \$51,017, roughly the same as the typical household made a quarter of a century ago. “America has been standing still for a full generation,” writes Porter.<sup>5</sup>

At the same time, those in the middle class have been working longer hours—an average of more than 200 more hours per year than they did in 1979 (and an average of more than 300 hours per year for the upper middle class).<sup>6</sup> So middle-class Americans are working longer even as, in several important respects, they are losing ground.

Then there’s the matter of upward mobility. Upward mobility is the central moral promise of American economic life; the hallmark of our system is the potential for advancement and greater prosperity rooted in merit and hard

work, rather than in the circumstances of one's birth. Yet the odds of moving up or down the income ladder in the United States are roughly the same as they have been for decades. Many European countries now have more social mobility and opportunity than the United States. And today a child's future income depends on parental income

Americans do not have a sense that conservatives offer them a better shot at success and security than liberals. For that to change, conservatives in American politics need to understand constituents' concerns, speak to those aspirations and worries, and help people see how applying conservative principles and deploying conservative policies could help make their lives better.

more in America than it does in Canada and Europe. (The odds of escaping poverty are about half as high in the United States as in more mobile countries like Denmark.) So while mobility isn't getting worse, it isn't getting better, and according to Lawrence F. Katz, a Harvard economist and mobility scholar, "What's really changed [are] the consequences of it. Because there's so much inequality, people born near the bottom tend to stay near the bottom, and that's much more consequential than it was 50 years ago."<sup>7</sup>

There's no simple answer to what ails America's economy. As many observers have noted (and as President Obama frequently reminds us), our economy has gone through some massive transformations in recent decades, including huge advances in technology that have allowed businesses to do more with less. We've moved toward an economy that more significantly favors skilled over unskilled labor. In addition, jobs, including even higher-skilled jobs, are being outsourced to countries like China and India as the economy grows more globalized. All of this has caused painful dislocation.

While President Obama has shown he's able to effectively describe these trends, he has proved singularly unable to improve the economy in light of them. Indeed, a slew of economic indicators have worsened during the Obama presidency.

No president has amassed as bad a record when it comes to job creation. We still have not fully made up for the number of jobs lost since the job market's peak in early 2008. The workforce-participation rate is at the lowest point since the late 1970s. Income inequality has worsened. A record number of Americans are collecting food stamps and living in poverty. And in the aftermath of the financial collapse of 2008, we have experienced the weakest recovery on record. Median annual household income has actually gone down more during the so-called recovery than during the recession itself. The median income of American households decreased by as much in the two years after the official end of the Great Recession as it did during the recession. All of this has tended to deepen the mood of pessimism among middle class Americans.

So whom does the public hold responsible for these stifled opportunities? According to Pew, a majority of middle-class adults put most of the blame on the government for the difficulties they have faced in the past ten years, and people blame Congress more than any other institution. Fully 62 percent placed “a lot” of blame on Congress, followed by banks and financial institutions (54 percent) and large corporations (47 percent).

The Heartland Monitor Poll, meanwhile, found that 64 percent of Americans believe Congress has made things worse for the middle class while only 8 percent believe legislators are making things better. And when asked to choose between three competing explanations for the increasing struggle facing average Americans, 54 percent of those surveyed blamed “elected officials making the wrong policy decisions.” Twenty-three percent named “business leaders not paying their employees enough.” And only 17 percent blamed “the economic impact of technology and globalization.”

As for political parties, Pew found that middle-class adults are more likely to say the Democrats rather than the Republicans favor their interests. Sixty-two percent of those in the middle class say the Republican Party favors the rich while 16 percent say the Democratic Party favors the rich. Thirty-seven percent of those in the middle class say the Democratic Party favors the middle class while 26 percent say the Republican Party does. And 34 percent say the Democratic Party favors the poor, while only two percent say the GOP favors the poor.

When asked which groups are helping the middle class, 17 percent had a positive response to Republican elected officials; 46 percent were negative. For Democrats, the numbers were 28 percent positive and 40 percent negative.<sup>8</sup>

Among the public, then, there is a very deep sense of unease and apprehension. Ground that people once believed was stable is seen as crumbling, and many Americans seem unsure what to make of it. But one thing they do believe: Right now politics is out of touch with what they’re experiencing. We’re witnessing a collapse of trust in government, most especially the federal government, and when it comes to Republicans and Democrats, the public’s attitude is: A pox on both your parties.

This is not an unreasonable attitude. Both parties are in important respects disconnected from the problems of ordinary Americans. Most Americans have lost confidence in President Obama; they are deeply unhappy with both his policies and their consequences, especially when it comes to his signature domestic achievement, Obamacare. Yet most of these Americans have not so much turned to the Republicans as they have turned against the Democrats.

Americans do not have a sense that conservatives offer them a better shot at success and security than liberals. For that to change, conservatives in American politics need to understand constituents’ concerns, speak to those aspirations and worries, and help people see how applying conservative principles and deploying conservative policies could help make their lives better.

As a starting point, conservatives need to set aside their habit of speaking as if the very same solutions we offered a generation ago would work equally well today. The truth is that many conservative policies worked in the 1980s—but conditions have changed, often dramatically, and conservatives haven't changed sufficiently with them. Conservatives today need to show Americans how the principles that led to successful solutions when applied to the problems of that era can do the same when applied to the rather different problems of this one. The same principles applied to new problems will yield new solutions.

Rather than speak about the economy in broad abstractions, moreover, conservatives need to explain how government policy now places needless burdens on the shoulders of working families and how they would lift those burdens and put government on the side of people working to better their conditions. Rather than talk about the poor and those Americans receiving government assistance as “takers” or dependents, conservatives need to explain how emphasizing and enabling work and mobility would be better for the poor and better for the country. Rather than talk about conservatism

exclusively as a set of rules about what government should not be doing, they need to help Americans see the conservative vision of American life—and of America's government—as a way to unleash the nation's potential.

The chapters that follow offer some models of how such an approach could proceed. They begin by elucidating how a conservative vision of government could speak to today's public concerns, proceed to show how such a vision would translate into concrete policy reforms in some of the most important arenas of our public life, and conclude by explaining how that vision and those reforms embody the spirit of our constitutional system and could help reinforce the public's commitment to that system.

That system is profoundly threatened today by an assertive progressive ideology advanced by an increasingly radical American liberalism. And with it, America's prospects are threatened as well. Conservatives need to respond not only by helping Americans understand how the Left's approach to government is hurting them, but also by helping them see how the Right's approach could improve their lives and those of all Americans.



Peter Wehner, a senior fellow at the Ethics and Public Policy Center, served in the last three Republican administrations.



# A CONSERVATIVE GOVERNING VISION

YUVAL LEVIN

As Americans attempt to adjust to the challenges of twenty-first-century life, our government has too often been getting in our way rather than helping us along. Many families now face stagnating wages, excessive tax burdens, rising health and higher education costs, barriers to mobility and work, disincentives to marriage and childbearing, and an economy increasingly held back by over-regulation, cronyism, institutional sclerosis, and mounting public debt. All of these burdens have left Americans uncharacteristically pessimistic about the country's prospects. And in each case an overreaching, hyperactive, unwieldy, and immensely expensive federal government lies near the root of the problem.

This has often led conservatives to appeal to the public by calling first and foremost for restraining that government—restricting its reach, reducing its scope, cutting its cost. These are surely essential goals, but a failure to put them in the context of a larger vision of the proper role of government risks leaving the public with the impression that what conservatives want is less of the same: the liberal welfare state at a lower cost. This is in fact how many on

the Left would like Americans to understand our public debates.<sup>1</sup>

But the size and cost of the liberal welfare state are a function of its basic character, and it is that character that is really at issue in most policy debates between liberals and conservatives. The fundamentally prescriptive, technocratic approach to American society inherent in the logic of the Left's policy thinking is a poor fit for American life at any scale. The liberal welfare state ultimately cannot be had at an affordable price. It is not the architecture of one or another particular program that makes it unsustainable. It is unsustainable because the system as a whole must feed off of the innovative, decentralized vitality of American life, yet it undermines both the moral and the economic foundations of that vitality.

This is in part because the Left tends not to see the decentralized, boisterous character of American society—with its uneasy but constructive tension between moral traditionalism and economic dynamism—as a great good to be protected and nurtured but rather as at best an unruly source of material wealth and at worst a barrier to the achievement of

important social objectives. The means of the liberal welfare state are centralizing and consolidating mechanisms intended to bring order to this chaos. And liberals rarely offer a defense of that managerial outlook. They take both its means and its ends for granted and defend the welfare state as though it were identical to the broad social objectives it purports to advance.

They therefore treat attempts to alter or eliminate liberal programs as attempts to abandon the most general objectives of those programs—to provide a safety net for the poor, say, or a foundation of economic security for the elderly and the vulnerable. Even alternatives that would achieve those goals in less heavy-handed ways and at a lower cost are assumed to be less committed to the goals, and so are taken to be steps in the wrong direction. It hardly seems to matter how well the Left's favorite programs actually work: What matters is that they exist, and must not be undone.

Criticisms aimed purely at the size or cost of those programs only contribute to this baleful dynamic. Conservatives must instead help the public see that the agenda they offer is rooted not just in fiscal concerns but in a political, moral, and social vision much better aligned with the realities of American life and the character of Americans' aspirations.

At the core of this difference of visions are quite different ideas of just how human beings prosper and thrive and therefore of the proper relationship between American society and its government.

To begin with, the Left's social vision tends to consist of individuals and the state, so that all common action is state

action, and its purpose is to liberate individuals from material want and moral sway.<sup>2</sup> The premise of conservatism has always been, on the contrary, that what matters most about society happens in the space between the individual and the state—the space occupied by families, communities, civic and religious institutions, and the private economy—and that creating, sustaining, and protecting that space and helping all Americans take part in what happens there are among the foremost purposes of government.

Progressives in America have always viewed those mediating institutions that stand between the individual and the government with suspicion, seeing them as instruments of division, prejudice, and selfishness or as power centers lacking in democratic legitimacy. They have sought to empower the government to rationalize the life of our society by clearing away those vestiges of backwardness and putting in their place public programs and policies motivated by a single, cohesive understanding of the public interest. This clearing away has in some cases consisted of crowding out the mediating institutions by taking over some of their key functions through direct government action. In other cases, it has involved turning elements of civil society and the private economy into arms of government policy—by requiring compliance with policy goals that are foreign to many civil-society institutions or consolidating key sectors of the economy and offering protection to large corporations willing to act as public utilities or advance policymakers' priorities.

In each case, the idea is to level the complex social topography of the space between the individual and the

government, breaking up tightly knit clusters of citizens into individuals but then uniting all of those individuals under the national banner—allowing them to be free of the oppressive authority of family or community norms while building solidarity through the common experience of living as equal citizens of a great nation.

Dependence on people you know is oppressive, this vision implies, especially because it always comes with moral and social strings. But dependence on larger and more generic and distant systems of benefits and rules is liberating, because it frees people from the undue moral influence of traditional social institutions even as it frees them from material want. A healthy dose of moral individualism combined with a healthy dose of economic collectivism make for a powerful mix of freedom and equality. And this mix is to be achieved through public programs and institutions that address material problems by applying technical knowledge—that organize and rationalize the economy in accordance with social-scientific expertise.

Conservatives have always resisted such gross rationalization of society, however, and insisted that local knowledge channeled by evolved social institutions—from families and civic and fraternal groups to traditional religious establishments, charitable enterprises, private companies, and complex markets—will make for better material outcomes and a better common life. The life of a society consists of more than moving resources around, and what happens in that vital space between the individual and the government is at least as much a matter of character formation as of material provision and wealth creation.

Moral individualism mixed with economic collectivism feels like freedom only because it liberates people from responsibility in both arenas. But real freedom is possible only with real responsibility. And real responsibility is possible only when you depend upon, and are depended upon by, people you know. It is, in other words, possible only in precisely that space between the individual and the state that the Left has long sought to collapse.

What happens in that space generally happens face to face—between parents and children, neighbors and friends, buyers and sellers. It therefore answers to immediately felt needs, and is tailored to the characters, sentiments, priorities, and preferences of the people involved. That kind of bottom-up common life, rather than massive, distant systems of material provision, is what makes society tick and what holds it together. While it can certainly be reinforced by public policy, it could never be replaced with centralized administration, however capable or rational it might be.

And what is more, centralized administration really cannot be all that capable or rational. Just as conservatives tend to differ with liberals about the sorts of circumstances in which people thrive, we also differ about the sort of knowledge that can help address social problems. The Left tends to champion public programs that consolidate the application of technical expertise: that try to take on social problems by managing large portions of society as if they were systems in need of better organization and direction. Again, it views government as organizing the interactions of individuals.

The Right tends, instead, to champion public policies that draw upon decentralized, dispersed social knowledge by empowering and incentivizing people nearest to the problems to find and apply solutions that work for them. This still involves a crucial and active role for government, but it is a much less intrusive and managerial role. It involves enabling and sustaining markets and other arenas of common action, ensuring competition, aiding the development of physical infrastructure and human capital, protecting consumers and citizens, and allowing the poor and vulnerable to participate along with everyone else. It is about creating the circumstances in which society can thrive and improve, not prescribing everyone's place and function. And it proceeds not through the concentration of power but through its dispersal.

In practice, the conservative approach to public policy therefore points toward putting in place programs that enable a kind of bottom-up, incremental, continuous learning process, rather than imposing wholesale solutions from above. Generally speaking, this is an approach to problem-solving that involves three steps: experimentation (allowing service providers to try different ways of solving a problem), evaluation (enabling recipients or consumers of those services to decide which approaches work for them and which do not), and evolution (keeping those that work and dumping those that fail).

Markets are ideally suited to following these steps. They offer a huge incentive to try new ways of doing things, the people directly affected decide which ways they like best, and those ways that are rejected are left behind. Government programs on the model of the liberal

welfare state, however, generally do not allow for any of these elements. Administrative centralization and regulation proscribe experimentation, beneficiaries of services are not the ones who decide what is working and failing, and interests grow around existing programs making it very hard to eliminate failures.

That is why conservatives often reach for the model of markets in public policy—not necessarily always for actual markets, but for a process that follows these three steps to the extent possible in various policy arenas and so achieves incremental improvements by learning from experience. Conservatives tend to think society is much too complicated to be amenable to consolidated technical solutions that assume we already have all the answers and just seek to impose them. We therefore believe that long-evolved, decentralized social institutions are more likely to be able to help and that public policy should reinforce such institutions, should help all citizens take part in them, and should sustain the space in which they can function.

This involves not a return to some fabled past but a modernization of our antiquated, lumbering, bureaucratic, mid-twentieth century governing institutions that enables a leaner and more responsive twenty-first-century government to help a complex and diverse twenty-first-century society solve its problems. By recovering the animating principles of American government, we can overcome the flabby lethargy of the progressive welfare state.

Many of the social and economic problems for which we seek public-policy

solutions require us to balance competing needs in very complex circumstances. In health care, for instance, we must find a way to simultaneously pursue broad access to coverage, high-quality care, and affordable cost. In primary and secondary education, we need quality instruction that meets the needs of

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enormously diverse groups of students in a vast array of circumstances. In welfare policy, we need to help low-income people meet their basic needs and rise out of poverty without creating perverse incentives for poor choices.

In each of these cases, and many others like them, the Left's ideal approach is to put enormous faith in the knowledge of experts in the center and empower them to address the problem—to enable a single public payer to command the appropriate arrangement of resources to yield the desired outcome. The Right's ideal approach, meanwhile, is to put some modest faith in the knowledge of the people on the ground and empower them to try ways of addressing the problem incrementally. Thus conservative policy ideas often seek to enable countless individual consumers to follow their individual preferences, allowing the resources they bring to the table (with the

help of public subsidies for those who lack market power) to create incentives for producers and providers to try different ways of meeting their needs and so of addressing the underlying problem.

The first approach takes power out of the space between the individual and the state and has the state use it on behalf of individuals. The second puts power into that space and has the state build platforms and arenas to help society address its problems through localized trial and error.

What has come lately to be called the conservative reform agenda, some elements of which may be found in the chapters that follow, consists in many instances of efforts to transform the first sort of public policy or program into the second, and so to move from the model of consolidated technocracy toward the three-part process of dispersed, incremental learning in one policy arena after another. And it consists in every instance of efforts to strengthen and reinforce the space between the individual and the state and to enable people to thrive and flourish in that space. That is what conservatives generally take the proper role of government to be.

It is also what America's government was originally designed to do. Our constitutional system builds a frame around the space between the individual and the state—empowering the government to sustain that space while restraining the government from invading or collapsing that space. That is why the system often feels liberating to conservatives (who tend to think liberty is what happens in that protected space) and constricting to liberals (who tend to think the system binds government's

hands far too much and keeps it from acting in ways essential to enabling social progress).

The liberal welfare state envisions a role for government that goes far beyond these bounds, and that in practice has involved both invading and collapsing that space to various degrees. And while the conservative response has focused on pulling back that overly expansive state, the vision motivating conservatives should compel us also to reinvigorate the original American political vision: a government that treats us fairly and seeks to sustain the circumstances in which we might thrive—rather than one that insists on strictly defining and managing the outcomes of our national life. This means that conservatives must advance a concrete public-policy vision and agenda, and not just a set of restraints on the Left’s vision and agenda. Friends of the idea of free and limited government have long found it difficult to do this in America. “A good government implies two things,” James Madison wrote in *Federalist 62*. “First, fidelity to the object of government, which is the happiness of the people; secondly, a knowledge of the means by which that object can be best attained. Some governments are deficient in both these qualities; most governments are deficient in the first. I scruple not to assert, that in American governments too little attention has been paid to the last.”<sup>3</sup>

Conservatives today need to pay more attention to the means by which our vision of government should be advanced—more attention, that is, to the details of public policy. It is not hard to understand why some conservatives have been reluctant to do that: The federal government has grown so large

and complicated that any attempts to transform it into a far more bounded, decentralized, nimble set of institutions must begin from an understanding of its particulars, and this feels to some conservatives like a concession to technocracy.

But conservatives today must develop some technical policy expertise precisely to combat the technocratic impulse and to advance an anti-technocratic, genuinely constitutionalist vision of American government. As Friedrich Hayek put it, “Liberty in practice depends on very prosaic matters, and those anxious to preserve it must prove their devotion by their attention to the mundane concerns of public life and by the efforts they are prepared to give to the understanding of issues that the idealist is often inclined to treat as common, if not sordid.”<sup>4</sup>

The chapters that follow enter into just such prosaic matters and mundane concerns of public life. They are about concrete policy questions—about how we can help the poor to rise, lift burdens off the shoulders of working families, end cronyism and special privileges for those well connected at the top, and prepare America to flourish again. But they are also about advancing a vision of American life in which government does not use society as an instrument to advance progressive aims but rather sustains and strengthens the space in which society can thrive and enables all Americans to take part in what happens in that space.

Such a government would no doubt be much smaller, more restrained, and less expensive than the one we have today. It would be fiscally sustainable, averting the catastrophe we face if our entitlement programs are not reformed

and reinforcing the private economy rather than draining it of resources. That is certainly part of what should appeal to us about it. But more important still, it would be far better suited to our soci-

ety, our Constitution, our needs, and our nature—far better suited to serving and sustaining our republic in the twenty-first century.



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# THE AGENDA

CONSERVATIVES

NEED TO EXPLAIN HOW

**GOVERNMENT POLICY NOW  
PLACES NEEDLESS BURDENS ON  
THE SHOULDERS OF  
WORKING FAMILIES**

AND HOW WE WOULD LIFT THOSE BURDENS  
AND PUT GOVERNMENT ON THE SIDE OF  
PEOPLE WORKING TO BETTER THEIR CONDITIONS.  
RATHER THAN TALK ABOUT CONSERVATISM  
EXCLUSIVELY AS A SET OF RULES ABOUT  
WHAT GOVERNMENT SHOULD NOT BE DOING,  
WE NEED TO HELP AMERICANS SEE THE  
CONSERVATIVE VISION OF AMERICAN LIFE AS  
A WAY TO UNLEASH THE NATION'S POTENTIAL.

*Peter Wehner*



# HEALTH-CARE REFORM

## TO LOWER COSTS AND IMPROVE ACCESS AND QUALITY

JAMES C. CAPRETTA

Public opinion polls have consistently shown that more voters oppose Obamacare than support it, and that opposition to the law is more intense than support for it.<sup>1</sup> This resistance seems to perplex many of the law's defenders. How could voters oppose what the authors of the law plainly view as a well-intentioned effort to promote more widespread enrollment in health insurance?

The answer, of course, is that the public does not oppose sensible steps toward more secure and widespread health-insurance coverage. What voters oppose is the heavy governmental and technocratic approach that Obamacare embodies, and its consequences for affordability, quality, and choice. Though many left-leaning politicians assume it is self-evident that this kind of technocratic approach is necessary to fix the problems with American health care, voters are not so sure. They have first-hand experience with many public programs, and are wary of handing over something as complex and important as health care to the federal government. Their fear is that Obamacare will ultimately harm the quality of their care, inflate their costs, diminish their job prospects, and vastly increase the

expense of the federal government and thus ultimately their taxes. The launch of Obamacare confirmed that all of these fears are well-founded.

The Obama administration got one thing right in its health care push: The system was badly in need of reform when the president took office. Unfortunately, administration officials misdiagnosed the cause, and then prescribed the wrong solution.

The core problem in American health care has been, and continues to be, that there is not a functional marketplace in health insurance or health services to discipline costs and promote quality and value for consumers. The Obama administration pays lip service to market-driven reform, but the real thrust of Obamacare is to expand governmental authority over the system, not to empower consumers or to encourage innovation.

Enthusiasts for government intervention, including the authors of Obamacare, often argue that a free-market approach to health care was tried in America and failed. But that is false. American health care has been dominated for decades by the federal government, through

vast subsidies for insurance and through payment regulations shaping the provision of medical services by hospitals and doctors. The result was a system dominated by third-party insurance arrangements, not consumer choice, and by federal regulations setting the terms for reimbursing hospitals and physicians.

Providers were often restricted from trying new approaches to organizing and financing coverage and care, most consumers did not have the power to choose among real options, and failed price-control systems in massive federal programs persisted despite a proven inability to control costs. In sum, American health care before Obamacare was very far from a genuine marketplace.

Looking at that landscape in 2009, the Obama administration came into office and somehow concluded that the problem with American health care was insufficient governmental involvement. And so the law that was passed by a heavily Democratic Congress in 2010 doubled down on many of the worst features of the existing system: heavy public subsidies for third-party insur-

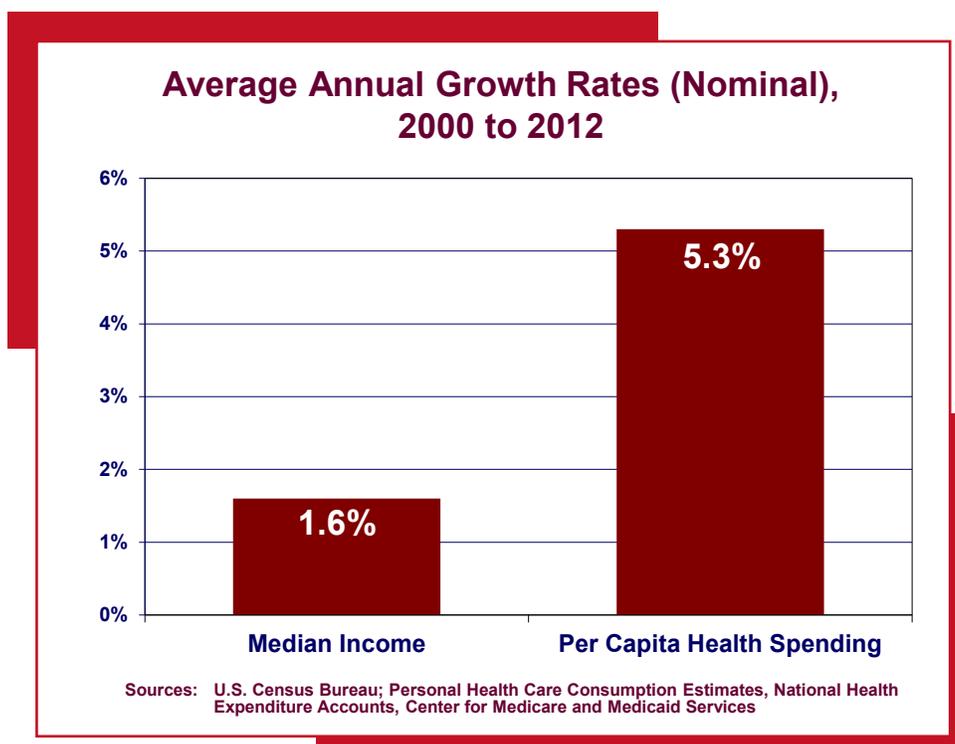
Enthusiasts for government intervention, including the authors of Obamacare, often argue that a free-market approach to health care was tried in America and failed. But that is false. American health care has been dominated for decades by the federal government, through vast subsidies for insurance and through payment regulations shaping the provision of medical services by hospitals and doctors.

ance enrollment and new and more restrictive federal regulations governing payments for medical services. It also handed vast new regulatory authority over the insurance sector to the Department of Health and Human Services and empowered new federal agencies and bureaucracies to step up the government's influence and control over the manner in which doctors and hospitals organize themselves to care for patients. All this tends to make it even more difficult for providers and insurers to try new approaches, for consumers to make real choices among real options, and for bad ideas to be abandoned.

In short, Obamacare was a step in exactly the wrong direction. More than anything else, the law set in motion a massive shift of decision-making authority from states, employers, insurers, and consumers to the federal government. In a way, that was the point. The authors of the law believe that muscular federal control is essential to expanding coverage in an equitable manner.

**In short, Obamacare was a step in exactly the wrong direction. More than anything else, the law set in motion a massive shift of decision-making authority from states, employers, insurers, and consumers to the federal government.**

But average middle-class families do not expect this shift of power to do anything to help them, especially with respect to rising health costs, which are their chief concern. From 2000 to 2012, median household income rose at an average annual rate of just 1.6 percent, according to the Census Bureau. During that same period, per-capita health spending rose at an average annual rate of 5.3 percent. Rising health costs have contributed directly to the stagnation of cash compensation as employers have kept pay raises low in response to the rising costs of employee health benefit plans. Obamacare's substantial new subsidies for third-party insurance look likely to increase cost pressures, not decrease them.



The centralization of power within the federal government, and specifically within HHS, will also have serious negative consequences for the quality of the health system. Government rulemaking and demonstration projects have already begun to displace private initiative. Instead of taking the lead to solve problems and improve care, the major players in the health system—employers, states, providers, and insurers—are now waiting for the latest pronouncements from HHS about what is and is not acceptable under Obamacare. Over

time, it will become more difficult to find investment capital for initiatives that have to be given regulatory approval by the government. The spreading passivity among private actors will undermine innovation and adaptation, and thus also hinder improvements in the quality of care for patients.

The economic costs of the law are also coming into sharper focus. The Congressional Budget Office (CBO) recently issued new estimates for the law's impact on the labor market, and

found that it will reduce employment in the United States by the equivalent of some 2.5 million workers by 2024.<sup>2</sup> CBO's new projections also show that, even after a ten-year gross expenditure of \$2 trillion, the number of uninsured Americans will still total 31 million in 2021 and beyond.<sup>3</sup>

For all of these reasons, public unease with the 2010 reform plan has grown, not receded, since the law was enacted. And therein lies an historic opportunity.

### **The Opening for an Appealing Conservative Alternative**

Conservatives are united in their belief that Obamacare needs to be repealed. There is also near unanimity that the law needs to be replaced with an effective, market-based alternative. But there is still a great deal of disagreement among conservatives about the content of that alternative plan.

There shouldn't be.

If a plan is to appeal to middle-class Americans—as it must to gain traction—then it will need to address middle-class concerns, and particularly the need to provide coverage for persons with pre-existing health conditions, to ensure all Americans have access to stable insurance, and to slow the pace of rising costs. These objectives need to be met without increasing the deficit and without handing over too much power to the federal government, as Obamacare would do.

It will also be necessary to have independent verification—in practice that means by the Congressional Budget Office—that a replacement plan could address these issues in a credible

way. For instance, if a plan to replace Obamacare is found by CBO to do little or nothing to reduce the number of uninsured Americans, it is unlikely to get the political momentum necessary to fully displace Obamacare.

These objectives will narrow the policy options available to policymakers. Lower-income households will need public subsidies, for example, to be able to secure at least catastrophic insurance coverage and participate in a thriving consumer market, and those subsidies will have a budgetary cost. The new plan will also have to be designed so as not to unduly disrupt the insurance arrangements of the millions of middle-class families who now have coverage they are happy with.

Some conservatives get nervous at the prospect of engaging in this kind of policy discussion. They would prefer to repeal Obamacare and then proceed with a series of very small, incremental changes to the pre-Obamacare health system. But that approach is unlikely to succeed because it will be criticized as undoing protections for pre-existing conditions and doing nothing to help low-income households without health insurance. It also falls short of the significant step toward a market-oriented system that we should take.

Conservatives must see the present opportunity, provided by Obamacare, clearly. We have an opportunity to move our health-care system to the right not only of Obamacare but also of the pre-Obamacare status quo. The middle class is ready to hear from conservatives about their practical and realistic proposals to improve their lives. If conservatives seize the political moment, they

could displace the largest expansion of governmental power in a generation with a program that would unleash, for the first time, the real potential of consumer choice in health care. It would be the most significant conservative policy victory in many years.

### **Four Keys to Reform**

The ideas that would inform a practical conservative alternative have been around for many years now, developed and advanced by a cadre of health-policy analysts and economists. All that is needed at this point is a persistent effort to pull those ideas together in a reform plan that can appeal to America's middle class and around which a stable center-right political coalition can form.

In early 2014, two plans were introduced that conservatives should look to as politically viable and credible blueprints for replacing Obamacare. The first was released by Republican Senators Richard Burr, Tom Coburn, and Orrin Hatch.<sup>4</sup> The second was put together by the 2017 Project, a non-profit organization dedicated to building and promoting a conservative reform agenda.<sup>5</sup> Though some of the

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details of these two plans differ, and future proposals from various conservatives could well differ in some key particulars too, they share a common structure and vision that will likely define any plausible conservative replacement for Obamacare. This structure consists of four key parts: a decentralized, market-oriented approach to the health-care system; tax credits for people outside the

employer system achieved with minimal disruption of employer coverage; continuous coverage protection for all Americans; and significant state flexibility.

First, the basic market orientation of this approach is in a sense its overarching characteristic. Addressing the complex problems bedeviling American health care will require the dynamism and discipline of a functioning marketplace. Rather than assume that bureaucrats in Washington have all the answers, such a market would allow providers on the ground to try new ways to deliver quality care at a low cost, would allow consumers on the ground to choose among these options to enable incremental progress toward a better system, and would allow those approaches that do not succeed to fall away and create both the incentives and the space for further improvement.

The Obama administration claims that Obamacare is a marketplace, but the reality is that it is a top-down, bureaucratic solution, with all of the critical decisions made in Washington. HHS strictly defines the insurance product and then compels insurers to sell it while the IRS compels consumers to buy it. That is not a market. The conservative alternative must employ a decentralized approach, with consumers driving the system

by the decisions they make about insurance coverage and the use of medical services. It must therefore feature far less prescriptive insurance regulation and much more room to experiment with options for consumers to consider. A model for these reforms can be found in the Medicare Part D program, a real marketplace that has restrained cost growth while also yielding high levels of choice and satisfaction for seniors.

Second, economists of all political stripes have long agreed that the open-ended tax subsidization of employer-paid health insurance is one of the main distortions of the existing system. It encourages excessively costly employer plans and discriminates against households that do not have access to employer coverage and thus must rely on the individual market for insurance. But conservatives must resist the temptation to simply undo current tax policy in an Obamacare replacement plan. Approximately 160 million people in the United States are enrolled in employer-sponsored insurance. Any widespread disruption of that coverage, as a complete rewrite of the federal tax treatment would surely involve, would be strongly resisted by the families benefitting from that coverage and would likely doom the entire reform effort. A better approach, pursued in both the Republican Senators' plan and in the blueprint offered by the 2017 Project, among others, would leave in place the tax preference for employer coverage, but place an upper limit on the amount of employer-paid premiums that would enjoy tax-preferred status. This approach would allow these plans to continue operating as they do today, just with a greater incentive for cost discipline. The upper limit could be set to affect only

the most expensive plans (such as plans with premiums in the top tenth or twentieth percentile, by cost).

At the same time, households that do not have access to employer coverage should be given a tax credit that is roughly equivalent to the value of the tax subsidy afforded to employer-sponsored plans. The credits could be adjusted by age categories (such as 18 to 34, 35 to 50, and 51 to 65), so that older citizens would get credits more reflective of their health risks, as would younger workers. The reform plans offered by the Republican Senators and the 2017 Project both provide age-adjusted credits.<sup>6</sup> The credits would also be entirely under the control of the households to which they are provided, and could be used only to secure insurance (or, if the credit exceeded the premium for coverage, to deposit into a health savings account).

A tax credit of this kind would help generate intense price competition in the marketplace. Consumers receiving the credit would have every incentive to find good value in health insurance because any premium charged by an insurance plan above the credit would be paid by the consumer, not the government. The upper limit on the tax preference for employer coverage would also encourage both firms and workers to shop around for good value in insurance plans.

Third, continuous-coverage protection would help address the challenge of covering Americans with pre-existing medical conditions. Americans must often switch insurance when they switch jobs, and a law passed in 1996 has largely worked to smooth out transition problems between job-based plans. Specifically, workers (or their family

members) with a pre-existing condition can't be penalized when they sign up with insurance at a new job so long as they have had insurance for a specified period of time. Unfortunately, that law did not adequately extend the same protection for people who transition from job-based coverage to individually purchased insurance.

This gap needs to be filled in the context of a broad commitment to the American people. Under the emerging conservative alternative to Obamacare, people who remain continuously insured, with at least catastrophic insurance, will never be forced to pay high premiums solely on the basis of developing a costly health condition. This new assurance would provide a powerful incentive for Americans to stay continuously enrolled in insurance. In combination with the new federal tax credits for coverage (provided to anyone without access to an employer plan), this reform would provide a direct and ready mechanism for all Americans to afford insurance and to have coverage that does not penalize them for their health conditions. Of course, for this new system to work, insurers must be allowed to assess the risks of those who opt out of insurance and then seek to enroll later in a plan.

This approach to solving the pre-existing condition problem is more or less the exact opposite of the approach taken in Obamacare. Under Obamacare, insurers are never allowed to take health risks into account, even if someone has dropped out of insurance and is signing up only because of a recently diagnosed condition. The law tries to counteract the strong incentive to wait until the last minute to enroll by

taxing anyone who fails to buy qualified insurance. This “mandate and tax” scheme, which is a central feature of Obamacare, is one of the main reasons the current law is highly unpopular. By instead putting coverage within everyone's reach and rewarding the decision to obtain it, a conservative reform could cover more people while avoiding heavy handed and constitutionally dubious policies.

Finally, any solution to the problems in American health care will necessarily entail some uniform national policies. But the plans offered by the Republican Senators and the 2017 Project, like any plausible conservative approach, also leave plenty of room for states to adopt policies suited to their needs within a federal framework.

States are given the lead role in insurance regulation and ensuring consumers have the information they need to make informed choices. They also have the lead role in Medicaid reform. In both of the recent conservative replacement plans for Obamacare, like others before them, Medicaid recipients would be allowed to take the base part of their entitlement in the form of the new federal tax credit. States would then be allowed to establish mechanisms by which Medicaid enrollees use their credits, plus any additional Medicaid support provided by the state, to purchase from the same coverage options as other working-age people in the state. This is a crucially important reform, as it would allow Medicaid participants to stay enrolled in the same insurance plan even as they move into higher-paying jobs.

To give states the authority they need to make this kind of reform work, states

need to receive their Medicaid funds in predictable and flexible per-capita payments from the federal government. This would replace today's cumbersome and counterproductive matching program. The per-capita amounts would be tied to historical spending in the states. After the first year, the per-capita amounts would grow with an agreed-upon index, perhaps measuring medical inflation.

The per-capita payments can be calibrated to be budget-neutral to the federal government in the first year (and the tax credits paid to Medicaid-eligible participants must be counted as part of the federal Medicaid spending commitment). In other words, federal payments to the states would be equal, in the aggregate, to expected federal spending if today's matching system had been retained. After the first year, some savings would accrue to the federal government as the per-capita payments would grow more slowly than Medicaid spending is expected to grow under current baseline projections.

Moving toward per-capita payments in Medicaid would remove the distorting effects of today's matching system and provide budgetary predictability at the federal and state levels of government. It would also allow the federal government to give the states total discretion over the design of the program because state decisions could no longer increase federal spending commitments.

States would have wide discretion over how to design the new Medicaid program, including full authority to establish required benefits and other special rules that might apply to the Medicaid population. They would also establish the amounts of additional premium assistance provided through Medicaid,

and how that assistance would be phased down as incomes rise.

Obamacare included many changes to Medicare too, many of which also deserve repeal and replacement. Among other things, the law includes large cuts in the Medicare Advantage program—a counterproductive move that will push more seniors back into the inefficient Medicare fee-for-service program. There are also deep cuts in the payment systems for hospitals and other providers of care that could cause access problems for seniors. Most conservatives rightly oppose this micro-management and recognize that what Medicare needs are reforms that point the program in a more market-oriented direction (like those proposed in the House Republican budgets of the last few years).

But reversing the damaging Medicare changes in current law, and replacing them with sensible reforms, need not come in the same legislation replacing Obamacare.<sup>7</sup> Improving health care for the working age population and their families is likely to prove politically challenging enough without also adding to the mix significant Medicare reforms. Those can and should be considered in a separate piece of legislation.

### **Covering Millions at a Fraction of Obamacare's Expense**

The Obama administration has frequently cited the estimates of the Congressional Budget Office to argue that Obamacare will deliver more enrollment in health insurance than the previous system, while still providing for a small reduction in the federal budget deficit over the program's first decade of implementation. The administration tends

to omit that these estimates rely on massive cuts in the Medicare program (\$700 billion over a decade) and a \$1 trillion tax increase. By contrast, the emerging conservative alternative can deliver just as much insurance enrollment without the massive taxes and spending of Obamacare.

Recently, a new, independent analytical organization—the Center for Health and Economy—produced a cost estimate for the Burr-Coburn-Hatch blueprint.<sup>8</sup> Those estimates clearly indicate that the proposal from the Republican Senators would reduce the number of uninsured in the U.S. to essentially the same levels as Obamacare—about 30 million people. And it would do so with spending levels that are far lower than Obamacare. Consequently, there would be no need for the large taxes imposed by Obamacare either.

There is, in short, a real alternative to Obamacare. It will make secure insurance available to the uninsured and people with pre-existing conditions. It won't increase the nation's budget deficit, and, in fact, will lay the foundation for genuine cost discipline to lower health costs. And it will retain the rights of individuals, employers, and states to make decisions that are in their best interest without having to first ask

**A model for conservative reforms can be found in the Medicare Part D program, a real marketplace that has restrained cost growth while also yielding high levels of choice and satisfaction for seniors.**

permission from the federal government.

The difference between this approach and Obamacare is not a difference of degree but of kind. It is rooted in a different diagnosis of the problems with American health care and a different approach to solving complex economic and social problems more generally. Rather than empowering consolidated bureaucracies to impose strict rules, it empowers a decentralized system of continuous learning and incremental improvement to find solutions, try them out, build on those that work, and reject those found wanting. It offers a far superior approach to addressing our health-care dilemma, and a model of conservative problem-solving.

As Obamacare's implementation continues, voters are seeing up close the major flaws of handing over so much control over the health system to the federal government. It's an inflexible approach, with heavy benefit mandates, high expense, cumbersome bureaucracy, and high implicit taxes on work. As voter disenchantment with the current law intensifies, an historic, and possibly time-limited, opportunity is opening up for the law's opponents. The public is ready as it never has been before to hear about a credible, practical, and realistic market-based alternative to Obamacare's heavy-handed govern-

ment approach. It is imperative that conservatives seize this opportunity and begin to coalesce around just such a replacement plan.

There are some political risks associated with doing so. Health-care policy is complex, and moving toward a real marketplace requires placing more responsibility on the shoulders of consumers. Supporters of Obamacare will no doubt try to exploit this fact by scaring consumers about the supposed risks this shift would entail.

Proponents of the Obamacare alternative should not be deterred. They should be politically prudent of course,

to minimize the risks. But if they follow the policy roadmaps outlined by Senators Burr, Coburn, and Hatch, by the 2017 Project, and by many other conservative reformers, they will have a plan that is far more appealing than Obamacare: a plan that addresses the pre-existing-condition problem, ensures widespread enrollment in affordable health insurance, and brings real cost discipline to the marketplace, all without the mandates, the taxes, or the massive power grab of Obamacare. There is great potential here not just for a policy victory, but for a massive political victory as well.



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# TAX REFORM TO STRENGTHEN THE ECONOMY AND LIGHTEN THE BURDENS FAMILIES BEAR

ROBERT STEIN

Cutting marginal tax rates has been the Holy Grail of conservative efforts to reform the tax code for the past generation. And it certainly should be—for the highest earners and investors who respond the most to lower rates. Cutting marginal tax rates is not, however, an effective tool for delivering tax relief to the middle class. It does very little to lower their tax bills or improve their work incentives.

Instead, tax cuts for the middle class should be designed to offset the greatest fiscal-policy distortion that affects middle-class Americans: the disincentive to raise children caused by Social Security and Medicare. Tax cuts should reduce the cost of raising children, making it easier for parents (and potential parents) to pursue the family size they would desire in the absence of federal interference. Such a tax plan would also noticeably increase after-tax earnings for families just when their costs of living are greatest. It would offer meaningful relief to millions of middle-class Americans and could create a political opportunity to enact other pro-growth policies.

## **The Marginal Rate Mystique**

The primary reason many conservatives still heavily emphasize the idea of

cutting marginal tax rates is the success of President Reagan's tax cut in 1981. Before Reagan, there were more than a dozen tax brackets—and in the top one, workers paid an income tax rate of 70 percent. For every dollar earned beyond \$108,300, a worker would keep only 30 cents. Tax rates that high obviously undermine the incentive to work, save, and invest. Conservatives therefore argued that large tax-rate cuts would encourage more economic activity and greater prosperity.

Upon taking office, President Reagan cut rates across the board; marginal income-tax rates that had spanned from 14 to 70 percent were cut to a range of 11 to 50 percent. The positive impact on work incentives for high-income households was enormous, as the workers with the most control over their hours, output, and pay structures had a strong reason to increase their earnings.

These tax cuts improved work incentives much more for higher-income households than for the middle class. Cutting the income tax rate from 70 percent to 50 percent meant the highest earners could keep 50 cents instead of 30 cents on every dollar of extra earnings. Marginal after-tax earnings

rose 67 percent. By contrast, a more typical middle-class household saw an 8 percent increase in marginal after-tax pay.

The much smaller improvement in incentives for the middle class was not class warfare. It was the result of having a progressive tax code with a very high top rate. A strategy of reducing tax rates simply cannot enhance work incentives as much for those who already keep most of what they earn.

Let's say we cut the 15 percent federal income-tax rate faced by much of the middle class to 10 percent. Instead of keeping 85 cents for a dollar of extra effort, a worker would get 90 cents—an improvement of only 5.9 percent.

Meanwhile, the tax cut would make a real dent in revenues—and we could not count on its having any major effect on behavior to make up for it. Cutting the 15 percent rate to 10 percent would reduce government revenue by about \$100 billion per year over the next decade.

Even worse, IRS data show that only about one-third of the tax relief would go to taxpayers who would see even a slight improvement in incentives. The other two-thirds of the tax cut would go to workers who earned some money in the 15 percent tax bracket on their way to higher tax brackets. For these workers, cutting the 15 percent rate to 10 percent would make absolutely no difference in work incentives. For them it would be a lump-sum Keynesian-style tax cut, putting money in their pockets while leaving incentives unchanged.

### **A Better Pro-Growth Tax Cut**

In their emphasis on marginal tax-rate cuts, some conservative tax reformers

have made two silent assumptions. First, they assume incentives start and stop at the workplace door, as if people are only workers, employers, entrepreneurs, or investors and incentives have no influence outside our roles as accumulators of material wealth. Second, they assume the only goal of tax reform should be to reduce economic distortions caused by the tax code itself, even if the tax code is the best place to address other distortions to human activity caused by fiscal policy.

One of those distortions, and a crucial one, is the way Social Security and Medicare have “crowded out” the traditional incentive to raise children as a protection against poverty in old age. Today, most workers can reasonably foresee getting enough support from the public retirement system to stay out of poverty when they get older, making it less likely that they will have to call on direct aid—either in cash or in kind—from their own children.

Studies (including work by Michele Boldrin, Mariacristina De Nardi, and Larry Jones, and by Isaac Ehrlich and Jinyoung Kim) show Social Security and Medicare reduce the fertility rate by about 0.5 children per woman.<sup>1</sup> In European countries, where retirement systems are larger, the effect is closer to one child per woman. In other words, without government-run retirement systems, both the U.S. and Western Europe would have birth rates of about 2.5 children per woman: safely above the population-replacement rate.

In order to keep going, Social Security and Medicare requires each working-age generation to accomplish two tasks: first, work and pay taxes to pay benefits to the older generation; second, raise enough

productive children so current workers can get benefits when they retire. But the entitlement programs allow those without children to get similar benefits to those with children, without having spent the time, money, and effort that parents do raising their children. So, even as the old-age pension system collectively depends on a population of productive young workers, it diminishes the economic need for adults to raise them—and so undermines its own sustainability.

By making so much of the economic benefit of children accrue to society collectively—and thereby reducing that benefit for the individual mothers and fathers who make the decisions about how many (if any) children to raise—federal policy distorts family formation.

Unfortunately, these negative effects cannot be fixed by converting old-age entitlement programs into mandatory savings programs, as the Bush administration suggested for Social Security in 2005. Requiring workers to save for retirement by accumulating financial instruments would also crowd out the traditional motive to raise kids.

In theory, changes could be made directly to the Social Security system to offset the bias against raising children. Charles Blahous and Jason Fichtner have proposed raising the general Social Security tax rate to 14.4 percent from the current 12.4 percent (6.2 percent on employer and worker, each). Then, parents would have the basic rate reduced by 2.5 percentage points for each child, so that parents of two children under age 18 would pay 9.4 percent, parents of three children would pay 6.9 percent, and so on.

Enacting this proposal would, however, be extremely difficult. Under current budget and procedural rules in the Senate, the Blahous-Fichtner reforms would require a supermajority of 60 votes, even if the plan had zero net effect on federal revenue or the budget deficit. A “revenue-neutral” tax reform, on the other hand, could offset the government’s anti-parent bias with a simple majority of both houses of Congress and a willing President.

### **A New Child Credit**

At present, the income tax code provides very modest relief to parents for each additional child they raise. The code includes a \$1,000 credit and a \$3,950 personal exemption. Applying a 15 percent tax rate to that exemption generates tax relief of \$593, which means the typical middle-class parent reduces her tax bill by \$1,593 per child. But this is only a tiny fraction of the cost of raising a child.

The Department of Agriculture says the cost of raising the typical child is \$13,600 per year through age 17—and that doesn’t include the cost of saving for college. Considering that Social Security and Medicare will absorb about 25 percent of the labor income of a child born today, sharing the direct financial costs of raising children to the same extent that the benefits of their future labor income will be shared suggests reducing the annual tax bill of parents by \$3,400 per child (25 percent of \$13,600).

Another way of determining the appropriate amount of tax relief for parents is to consider the present value of future Social Security and Medicare contributions for a typical worker born today, which is about \$160,000.

For some families, the extra money could be just the boost they need to be able to send their kids to a better school. Coming at a time in life when many parents and potential parents are considering whether they can afford an additional child, the extra credit would directly make carrying the burden (and generating the future social benefits) of a growing family somewhat easier.

Rewarding parents for making these future contributions possible suggests annual tax relief of about \$9,000 per child. (The contribution figure is what matters, because today's children will get benefits only if they as a group raise children, regardless of whether they're "promised" benefits under current law.)

A recent tax reform proposal by Senator Mike Lee (R., Utah) would take a large step in this direction. He would keep the current \$1,000 child credit and the personal exemption for children, and add a new credit of \$2,500 available to all taxpayers with kids, with no phase-out of the sort that applies to the current credit. The new credit could be used to reduce income-tax and payroll-tax liabilities; it couldn't be used to increase refunds for those who have already used other credits (like the earned income credit) to reduce their tax bill to zero.

To help pay for the new larger child credit, Senator Lee would greatly simplify the income tax code, getting rid of all itemized deductions except for the mortgage interest and charitable deductions. He would also limit the deduction for new mortgages to \$300,000.

Senator Lee's plan would increase the tax relief associated with having each child by \$2,500 per year for the typical

middle-class family. So, for example, under the proposal, a married couple with two children earning \$70,000 would get a tax cut of roughly \$5,000 per year compared to current law.

For some families, the extra money could be just the boost they need to be able to send their kids to a better school. Coming at a time in life when many parents and potential parents are considering whether they can afford an additional child, the extra credit would directly make carrying the burden (and generating the future social benefits) of a growing family somewhat easier. In addition, because the size of the credit would temporarily wipe out tax liabilities for some middle-class parents it would also reduce their marginal tax rate on additional work to zero.

A recent "score" of Senator Lee's proposal by the Tax Policy Center suggests the concept needs to be adjusted to achieve revenue neutrality compared to the current tax code. But that can be done without disturbing the framework of the plan.

For example, income that is today taxed at a 25 percent rate would get a 15 percent rate under Senator Lee's proposal. But if income in the current 25 percent bracket had a 35 percent rate (the same

tax rate Senator Lee would apply to all regular income above the 15 percent bracket) the proposal would be revenue neutral.

Some supply-siders will reflexively cringe at this idea. Most of the extra revenue from applying the 35 percent rate to a lower income level would, however, come from workers who would already be paying a marginal rate of 35 percent. Alternatively, the 25 percent bracket could remain 25 percent and some extra revenue could be generated by more quickly limiting the mortgage interest deduction to the middle class or perhaps limiting the exemption for interest on municipal bonds.

### **Answering Critics**

Increasing the amount of tax credits for parents would certainly result in a smaller share of workers paying taxes in any given year. Some suggest this could increase the electorate's appetite for government spending, because fewer of them would directly feel the cost. Already, the top 40 percent of earners pay about 99 percent of federal income taxes. Factoring in other federal taxes — like those on payrolls and corporate profits, and excise taxes — the top 40 percent of earners pay about 85 percent of federal tax revenue.

But annual snapshots are deceiving. Most workers move across different income groups during their lifetimes. And just as tax cuts for the highest brackets are eventually enjoyed by many more people than those who happen to be in those brackets in any one year, so too will people who drop off the tax rolls in one year because they're busy raising children likely find themselves paying taxes again in another.

Moreover, no economic analysis has actually shown a structural relationship between moving more citizens off the tax rolls and increased support for larger government. By contrast, conservative Nobel Prize-winning economist Gary Becker has shown that countries with flatter tax systems tend to have larger governments, as the burden of additional spending proposals can be spread across a wider tax base—which means fewer taxpayers have an incentive to resist the expansion of government.

Even more important, Senator Lee's proposal does not simply reduce the tax rolls based on income. Instead, it reduces the tax rolls based on parenting. This difference is crucial. Some low earners might imagine themselves earning little for the foreseeable future. As a result, voting for more government spending might appear a bargain. But parents know their children are going to eventually leave the nest. They will know that also means their tax bills will go back up—giving parents a good reason to want government spending restrained.

Moreover, reducing the high cost of raising children could make many middle-class parents less likely to support government spending, not more—since a lack of cash during their parenting years is one reason they might favor more government activism in the first place. The constituency for government-provided pre-school, for example, would be smaller if parents had more ability to finance the child-care options they chose.

### **The Next Conservative Tax Reform**

For conservatives to move forward, we have to come to grips with both our victories and our failures. Having substantially cut top tax rates in the 1980s,

To gain popularity for a broader conservative agenda, we need to offer something more than just updated versions of plans that have failed to gain traction for decades.

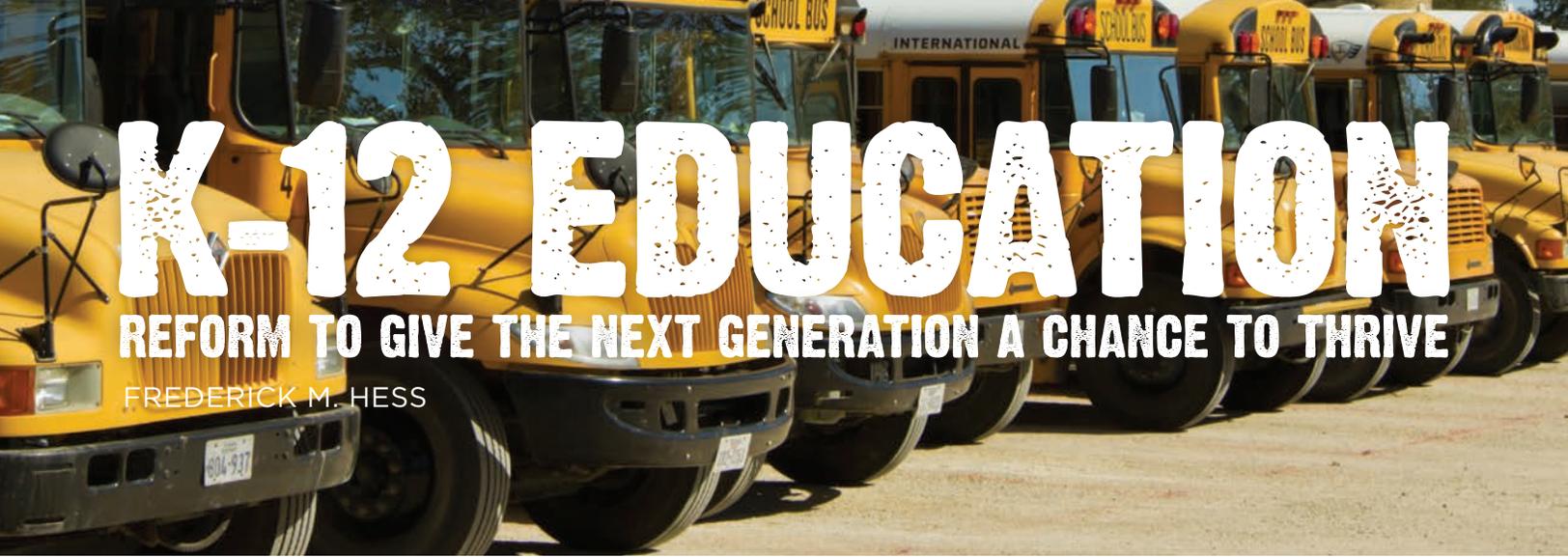
our potential gains from fighting on the tax rate battlefield are now diminished. Not gone completely, just smaller. To gain popularity for a broader conservative agenda, we need to offer something more than just updated versions of plans that have failed to gain traction for decades.

Too many free-market economists still consider the economics of the family a sideshow. They say the tax code should be “neutral” about raising children even though fiscal policy is not. Others simply ignore the way the entitlement state has distorted family life.

Unwittingly, the federal government has set up programs that deter parenting. Using the tax code to fix that problem would not only correct a distortion but could be the key to winning back the political trust and support of the middle class.



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# K-12 EDUCATION

REFORM TO GIVE THE NEXT GENERATION A CHANCE TO THRIVE

FREDERICK M. HESS

A serious commitment to human flourishing and opportunity in American life requires conservatives to think seriously about schooling. Economic opportunity and responsible citizenship become mere phantasms for children deprived of the chance to learn. Lousy schools rob their students of a full shot at the American dream, bolstering the case for redistribution and for the machinery of the welfare state.

This makes it astounding that conservatives have failed to put forward a compelling, principled vision of K-12 reform. But they have. Washington conservatives have called for eliminating the federal Department of Education even as they have refused to seriously countenance cuts in the two major federal K-12 programs actually administered by that department (Title I aid for low-income students and funding for special education). Conservatives have touted the virtues of school choice and local control, but failed to offer a roadmap for how policymakers could turn those abstractions into realities.

As a result, reform-minded liberals have been driving national education policy for the past decade. While the effort has

been nominally bipartisan, it turns out (perhaps unsurprisingly) that an agenda shaped and executed by liberals will ultimately not be bipartisan after all. Thus, while the Obama administration has admirably championed charter schooling and reforms to teacher tenure and pay, its implementation of these ideas has been marked by an unprecedented expansion of federal authority and a remarkable faith in the ability of federal bureaucrats to determine how teachers should be evaluated and how low-performing schools should be “turned around.”

The federal government foots only about 10 percent of the nation’s \$600 billion annual K-12 tab. The other 90 percent is funded by states and school districts. The federal role should be proportionally limited, but more importantly it should be focused not on micromanaging schools but on creating platforms for reform and reinforcing the work of policymakers (at the state and local level), educators, and administrators who are trying to modernize American education. If Uncle Sam is going to be involved in schooling, his role should be a constructive and constrained one—which it has not been in recent years.

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and identified 98 percent of teachers as effective.<sup>1</sup>

The time is ripe for a principled, conservative K-12 agenda, and the outlines of such an agenda are easy to see.

### **A Limited Federal Role**

Washington doesn't run schools. All it can do is write rules for schools. Congress can do little more than enact laws that tell federal bureaucrats to write rules for states, which write rules for school districts, which then give directions to schools. Washington can therefore force states and districts to do things, but it cannot make them do those things well. And when it comes to complex enterprises like public schooling (with 50 million students and nearly three and a half million teachers), whether things like teacher evaluation and school "turnarounds" are done matters far less than how they are done.

Thus, the Bush administration's No Child Left Behind (NCLB) Act and the Obama administration's education initiatives have delivered a succession of mandates that have amounted to Pyrrhic victories for reform. Race to the Top spurred enormous investments in teacher evaluation systems, designed to address the fact that principals routinely rated 99 percent of teachers as effective. After fierce political fights and enormous energy-expended, these new systems have debuted . . .

If American education looked like the nationally run systems of Britain or France (or Mexico or Cuba), the national education debate would sound quite different. But grand calls for Washington to "fix" schools must inevitably boil down to new funding formulas and mandates. Conservatives must challenge those championing Washington-centric reforms to explain how more bureaucracy will lead to better schools.

What, then, should conservatives champion when it comes to education reform? While the federal government can't fix schools, it can play a crucial role in making it easier for local families, educators, officials, and entrepreneurs to do so. Conservatives should embrace a legitimate, limited federal role in schooling. From the Land Ordinance of 1785 (under the Articles of Confederation!) through Dwight Eisenhower's 1958 post-Sputnik push on math and science and Ronald Reagan's 1983 call-to-arms in *A Nation at Risk*, we have recognized a compelling national interest in schooling. But Washington should limit its involvement to those things it is uniquely

While the federal government can't fix schools, it can play a crucial role in making it easier for local families, educators, officials, and entrepreneurs to do so.

equipped to do well, that are appropriate to its limited role in our federal system, and that don't amount to giving marching orders to states and schools. Boiled down, that amounts to an approach that can be summarized in four key points: educational options, transparency, research, and deregulation.

### **Expanding the Choice Agenda**

School choice has long and rightly been a prominent conservative cause, but it is only one part of a serious choice agenda in education. The truth is that today's school-choice programs are an enormous boon for low-income families trapped in lousy schools but of less interest to other families. After all, about two-thirds of families already "choose" their schools when they buy their residences, select private schools, or use public school-choice options. These families mostly like their schools. Gallup reports that 71 percent of parents give their oldest child's school an A or a B (though just 18 percent of adults give the nation's schools on the whole an A or a B).<sup>2</sup> In other words, Americans think there are problems with schools—just not with those their children attend. This means that, for most households, school choice can seem like a solution in search of a problem.

This is not an argument for minimizing the value of school choice, but for being clear-eyed about the limits of school choice, both as a response to educational concerns and as a political strategy. What middle-class families want and need are good, practical choices that give them more control over their children's education. The fact that they like their schools doesn't mean they like everything about their schools. Conservatives

should broaden the implications of their intuition in favor of choice and encourage more choices within school curricula. These choices would allow families to better meet the needs of their children—through more robust foreign-language instruction, for instance, or access to online instruction in math, or the ability of home-schooled students to participate in school sports or electives. (Gallup reports that 75% of adults favor allowing students to earn college credits over the internet and allowing home-schoolers to participate in activities like after-school athletics).<sup>3</sup>

To date, federal advocacy for choice has focused narrowly on supporting charter schools, the D.C. Opportunity Scholarship program, and making Title I funds portable for low-income families. A more expansive choice agenda would allow states to use a much larger share of federal funds to take steps like expanding online options, funding Louisiana-style "course choice" programs, education savings accounts, and accommodating home-schooled students.

"Course choice" presumes that families may like their children's schools but might prefer a different math program or language offerings. Rather than merely allowing a student to change schools, it allows parents to use a proportional fraction of school funding to access specialized providers in lieu of the usual offerings. Educational savings accounts are similar to health savings accounts: The state contributes a portion of per pupil funding to an individual account, enabling families to decide how to allocate those dollars among approved educational expenditures and allowing families that make cost-conscious decisions to apply

funds towards tutoring or college tuition. Such innovations require changes in state and local laws and rules, but they would also require a careful look at regulations defining permissible uses of federal funds (such as “supplement not supplant” provisions), as these can impede the provision of services that benefit a whole school rather than a narrowly targeted student population.

Another way to broaden the relevance and appeal of school choice for middle-class families is by ensuring that choice is not only a way for families to escape awful schools but also a way for more families to find schools that meet the needs of their children. For instance, because some school districts can be too focused on basic literacy and numeracy, many middle-class families are seeking schools that offer advanced science instruction, gifted programs, language immersion, or rich arts curricula. A challenge here is that the thrust of the charter school movement, for instance, has been its intense focus on “gap-closing” schools that emphasize basic skills for low-income children. Ensuring that performance metrics and accountability systems don’t stymie the emergence of a broad array of schools, and ensuring that federal start-up funds help support schools with diverse missions, are ways to ensure that school choice can also address the concerns of middle-class families.

Lawmakers would also do well to embrace choice legislation that is addressed to families with particular needs, regardless of income level. A model here is South Carolina Senator Tim Scott’s CHOICE Act, which seeks to let states use federal funds to support school choice for children with special

needs and for the children of military families. While many states today offer school choice scholarships for children with special needs, they cannot have those federal special education funds follow children to their chosen schools. And military families often have limited options to choose from. Scott’s bill would allow states (if they wished) to have special education funds follow the student in question, and would create a scholarship of up to \$12,000 that children in military families could use to attend any public or private school. The total cost of Scott’s two bills is just \$2 million per year, which could easily be made up for elsewhere in the budget.

As they advocate this broader notion of choice, conservatives should also recognize that school choice can create some losers as well as some winners. It makes winners of those families that were previously trapped in abysmal schools. So long as choice programs are restricted to poor communities with high concentrations of troubled schools, there are few obvious losers. Indeed, middle-class parents have proven willing to support school choice in the abstract, especially if it is targeted at helping families trapped in awful schools.

There is, however, a strong and reasonable NIMBY (“not in my backyard”) element to this sentiment. It is reasonable because expansive choice systems can make losers out of middle-class families in at least two ways. First, the largest asset a middle-class family is likely to own is its home, and a significant portion of a home’s value is based on the local school system. Homeowners who have paid a premium to live in neighborhoods with good schools might take substantial losses if choice plans attenuate the link

between residence and school. And second, families justifiably worry that they will lose access to their neighborhood school if too many families apply, and that choice systems may even result in elementary school students having to be bused long distances.

Washington can help states more readily address such concerns, making choice

The federal government should help make information available, but it cannot be charged with deciding what to make of that information. That distinction is very easy to draw, and could provide a crucial organizing principle for a conservative education agenda.

more of a win-win proposition. Federal law should make it easier for states or communities to grandfather current homeowners so that they need not fear losing access to their neighborhood school. This could take the form of transitional legislation that makes clear that choice plans will allow neighborhood schools to set aside a portion of seats, or to guarantee seats to all grandfathered families.

Conventional “school choice” can also seem threatening and unhelpful to residents in rural areas and small communities. In such places, school

choice can entail very long bus rides or bizarre efforts to subdivide a school with a half-dozen teachers into three different mini-schools. Washington should take care that it doesn’t push such communities into foolish, compliance-driven exertions, and should write choice-enabling legislation so that it permits federal funds to be used for the full panoply of educational choices (including online learning, which can be especially valuable in rural areas)—and not just providing choices among distinct schools.

### **Improving Transparency**

Conservatives should proudly embrace the one compelling legacy of No Child Left Behind: the fact that the law made it much easier for citizens to gauge and compare basic measures of school quality. Historically, public officials manipulated or hid test results for political advantage. Since 2003, the National Center for Education Statistics has used the National Assessment of Educational Progress (NAEP) to compare results across states using various tests. Data reporting and analysis poses minimal implementation headaches, does not involve the federal government in dictating practice or monitoring compliance, and equips parents, voters, and taxpayers to set priorities and make decisions.

To build on the potential of such improved transparency, the federal government should continue to require annual testing and reporting in reading and math, with results broken out by NCLB-denoted subgroups. It should also continue to use NAEP to calibrate and compare results across states. But it should do more. NCLB-style transparency focuses on student outcomes while paying no

attention to the resources needed to produce those outcomes. Yet it is difficult to make informed decisions about schools or programs if it is unclear how much was spent to achieve a given result. Federal reporting requirements should require schools and districts to report per-pupil spending, enabling parents and voters to compare cost-adjusted performance and enabling observers to calculate various “return on investment” metrics.

But while embracing transparency, Washington should end NCLB’s policy of mandating cookie-cutter remedies for schools. The dismal results of the \$3.5 billion School Improvement Grants illustrate how ineffective federal bureaucrats are at steering school improvement, with one-third of schools that received federal largesse actually getting worse.<sup>4</sup> The federal government should help make information available, but it cannot be charged with deciding what to make of that information. That distinction is very easy to draw, and could provide a crucial organizing principle for a conservative education agenda.

This would mean that reformers should also take the federal government entirely out of the Common Core debate and take a new expansive federal role in curricular development off the table by championing Section 5521 of the Student Success Act (passed by the House in 2013). The Act stipulated that, “No officer or employee of the Federal Government shall, directly or indirectly . . . mandate, direct, or control a State, local education agency, or school’s specific instructional content, academic standards and assessments, curricula, or program of instruction.” Debates about enforcing standards and the content

of curricula should play out in the states—a heavy-handed federal role would involve far more trouble than it could be worth.

### **Educational Research**

A further vital role for Washington, and one that no other actor in our federal system can play, is backing basic research in education. Market theorists have long noted that markets tend to under-produce public goods. Basic research is a classic public good. It requires substantial time and expense, and it is rarely evident whether or how early stage researchers will reap the benefits of their labor. The National Institutes of Health addresses this challenge by investing heavily in basic research, and then leaving the development and design of new drugs and medical interventions to private ventures. That division of labor is the right model for education as well.

Congress would do well to shift funds away from federal programs that seek to dictate state and local practices and toward basic research that offers long-term benefits—such as work examining how fast the adolescent brain can absorb languages and which areas of the brain are associated with specific learning challenges.

Crucial is an insistence on rigor and funding models that steer investments into areas that offer genuine promise—like cognitive science, applied reading techniques, and brain imaging—rather than to the usual suspects. Things are more promising on this front than they were a decade ago, thanks to the establishment in 2002 of the federal Institute for Education Sciences, which has emphasized efforts to apply rigor-

ous scientific techniques to education questions. While IES's establishment marked a shift toward more rigorous research in the field of education, however, the organization invests less than \$300 million a year in research—not even one hundredth of NIH's \$30 billion annual research budget. Congress could triple our investment in basic education science to \$900 million at no additional cost to the taxpayer merely by redirecting 20 percent of the \$3 billion spent on professional development under NCLB's Title II (funds that reform-minded Republicans and Democrats, alike, think do little good).

### **Constructive Deregulation**

Decades of federal education statutes have spawned a paralyzing tangle of rules, regulations, and mandates that hamper teachers, principals, and schools. Federal guidance can make it illegal for districts to cut spending (even when it's no longer productive), can prohibit funds from being distributed across schools and programs in sensible ways, and can create immense paperwork burdens for harried educators. This stifles school districts and charter schools alike. The problem is compounded because a half-century of federal rule making has fostered a compliance mindset among state and local officials, distorting the real-world impact of even reasonable-sounding rules.

Congress should embrace an “opt-in” strategy for states that want to use federal dollars to expand educational choice, like the approach modeled in Senator Lamar Alexander's “Scholarship for Kids” Act. Alexander would liberate schools from much of the federal regulatory apparatus if states commit to regular NCLB-mandated testing and re-

porting, and to ensuring that funds will serve the intended beneficiaries. In a single blow, this approach would allow states that so choose to escape shelves of overgrown regulation. States would then be free to decide what range of educational choices to fund and how those might be regulated. Meanwhile, states that so choose are free to retain the status quo. “Opt-in” ensures that states that act will have leadership committed to making choice work, avoids having the federal government force states to expand options (a tack that worked poorly under NCLB), and eschews the compliance machinery that such measures require. It also minimizes the likelihood that choice will take the form of a crudely designed federal mandate. The “opt-in” tack allows states to innovate and pursue their course as they see fit.

Washington also ought to scour federal regulations, state education agency interpretations of federal rules, and related minutiae that impede state and local leaders. This should include a series of high-profile hearings at which selected state, local, and charter school leaders can illustrate how things like “time and effort” reporting requirements undermine their work. Such hearings can inform understanding, flag specific problems, and build support for the effort. Washington can also help free reform-minded leaders from the burden of bad decisions made long ago. In the private sector, when legacy decisions leave private-sector enterprises ill-equipped to compete, due to inflated costs, bad contracts, or rigid business models, they are given a chance to reinvent themselves through bankruptcy. School-system leaders lack similar options. Every bad contract provision a superintendent ever

accepted and every inane school-board policy ever enacted remains in effect unless actively reversed. Political, legal, or contractual constraints can make that impossible; even when voters elect reform-minded school boards or mayors, their hands are often tied. The Constitution vests Congress with the authority to set a uniform bankruptcy code. Most relevant here is Chapter 9 bankruptcy, which allows municipalities to revisit existing contractual obligations. Yet, in the mid-1990s, revisions to the code allowed states to block school districts from filing for Chapter 9. As a result, not even a handful of the nation's 14,000 districts have successfully applied for Chapter 9 bankruptcy since the 1980s. Even where local governments are authorized to apply, states can veto such a course—giving special interests (like unions, retirees, and vendors) a chance to stymie even the boldest local leaders.

Washington should craft a new bankruptcy-like mechanism that permits those school districts receiving federal Title I funds and deemed (by their states) to be performing inadequately to petition for relief from contractual obligations (with unions, vendors, and others) that constrain their efforts to improve schooling.

### **Teachers and Unions**

When addressing the problems of broken systems and institutions, conservatives must always be careful to distinguish the failures of those systems from the

circumstances of people trapped in them. We should never demonize those trapped in joblessness and dependency, for instance, but rather should strive to empower them. This big-hearted stance is how conservatives have approached poor families when discussing school choice—a strategy that has been both morally right and politically astute. And it must also come to characterize the Right's approach to teachers.

There are six million adults working in K-12 education in the U.S., and they have an intense, immediate, voting interest in schools. Equally important, teachers are routinely cited as the most reliable source of educational information by parents and voters. Conservatives should not treat them as simply part of the problem with American education.

Educators are trapped in the same school systems as students, and subject to a raft of frustrations not of their making. Teachers are whiplashed by inconstant school-board governance and stymied by bizarre budgeting restrictions rooted in federal grant requirements. They experience first-hand the problems of one-size-fits-all federal accountability guidelines and federal efforts to micro-manage school discipline and improvement. Conservatives have an appealing case to make to them for slashing red tape and empowering professionals. But they need to argue more clearly and ardently, and in more venues, that they are offering teachers the freedom to escape bureaucratic bosses, choose professionally rewarding environments, and create schools equal to their ambitions. This case needs to be made as more than an addendum to critiques of

**Educators are trapped in the same school systems as students, and subject to a raft of frustrations not of their making.**

unions—which most teachers currently see as necessary safeguards in badly broken systems. For instance, in a 2011 national survey of teachers, conducted by reform-minded Education Sector, 81 percent said unions are needed to protect teachers from school politics and abusive administrators.<sup>5</sup>

Conservatives should have a lot of sympathy for teachers concerned about education politics and capricious bureaucrats. Indeed, the strength of teachers' unions is partly a response to the same ills that frustrate conservatives. Perhaps the surest way to weaken the grasp of the unions is to spend less time attacking them and more time attacking the things that make teachers look to them. Conservatives will never outbid liberals on education spending, but the Obama administration has awakened teachers' unions to the perils of federal bureaucrats run amok. There is a powerful opportunity to explain that choice, deregulation, and a limited federal role are good for students and educators.

### **An Agenda for Reform**

After the excesses of the past decade, conservatives are understandably wary of claims that “the federal government is here to help” improve the nation’s schools. But the alternative—simply denying that Washington has any role to play in education—is both insincere and counterproductive. After all, when presented with troubling educational outcomes, federal lawmakers of all stripes have made it abundantly clear that they are unwilling to stand by and do nothing. Indeed, it is the unfocused

urge to “do something” that has produced so much of today’s regulatory tangle.

There is a better course. Conservatives should adopt a trust-busting mindset, wielding the Department of Education and the federal education apparatus to reverse decades of bureaucratization. Senator Alexander, a former U.S. Secretary of Education, has observed that “Washington can’t create good jobs, and Washington can’t create good schools. What Washington can do, though, is shape an environment in which businesses and entrepreneurs can create jobs. It can do the same thing in education, by creating an environment in which teachers, parents, and communities can build better schools.”<sup>6</sup> Alexander is quite right. The conservative approach to education should follow the broader pattern of conservative policy thinking: enable the system to experiment with options; enable parents, students, and teachers to choose among those options; and let the failures fall away.

**The conservative approach to education should follow the broader pattern of conservative policy thinking: enable the system to experiment with options; enable parents, students, and teachers to choose among those options; and let the failures fall away.**

Washington can do all of these things without spending a dime. If lawmakers pay for research by shifting funds as proposed above, the entire agenda proposed here can be adopted without any new spending whatsoever. This is not an agenda of new programs and

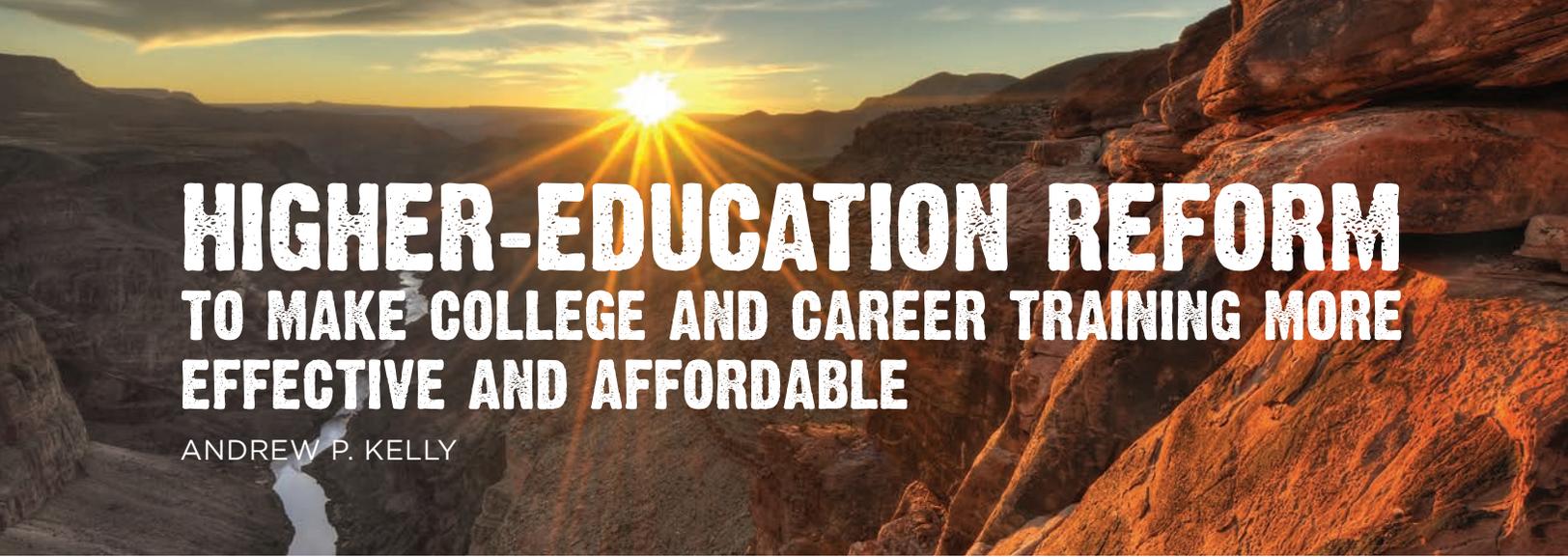
outlays, but one of unshackling and empowering problem-solvers, parents, and educators in a hidebound sector.

Washington can help ensure that parents, voters, taxpayers, and public officials have the data they need to make informed decisions. By reducing the influence of education cartels and extricating reform-minded leaders from

decades of red tape, Uncle Sam can open the field to new entrants and create room for meaningful competition. Washington can help create the preconditions for a dynamic sector, while leaving the real work where it must necessarily belong—in the hands of parents, educators, entrepreneurs, local officials, and citizens.



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# HIGHER-EDUCATION REFORM TO MAKE COLLEGE AND CAREER TRAINING MORE EFFECTIVE AND AFFORDABLE

ANDREW P. KELLY

Middle-class families are stuck between three contradictory trends when it comes to higher education. First, the cost of college has grown more quickly than just about any other good or service in the economy, and has left the median income in the dust. Between 1982 and 2013, published tuition and fees at public four-year colleges nearly quadrupled after adjusting for inflation; at private colleges, costs grew by a factor of 2.5 (see Figure 1).

In the past, a responsible middle-income family could reasonably expect to pay college tuition out of pocket without resorting to loans. Those days are over.

higher than they were at the height of the economic crisis (less than 10 percent).<sup>1</sup>

Second, the payoff to a college degree has not kept pace with tuition costs. The earnings of recent college grads have declined since the early 2000s, and research from the New York Fed has found that nearly 45 percent of recent college graduates were underemployed in 2012.<sup>2</sup> Students and families are paying more for a smaller return.

Third, even though costs are up and value is down, some form of postsecondary education—not just a bachelor's degree—is more important

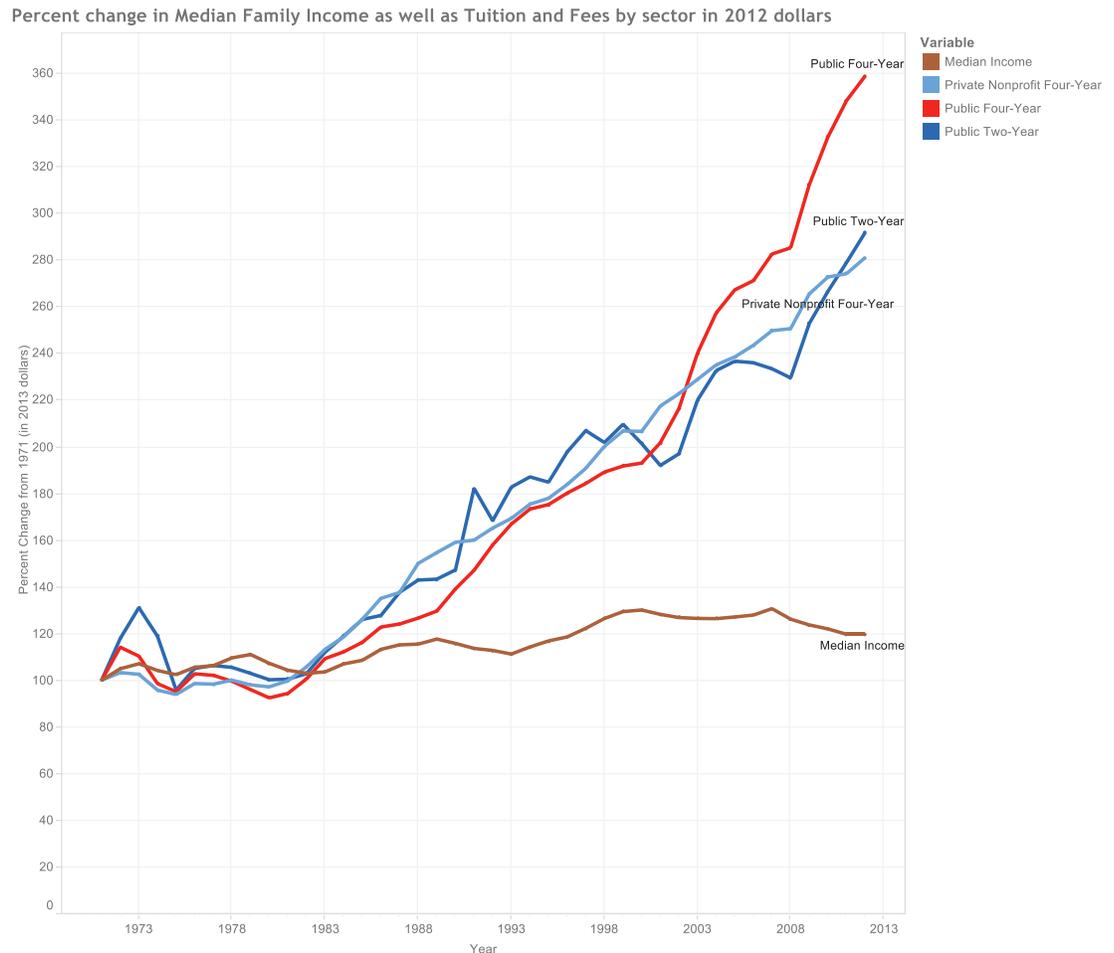
**Even though costs are up and value is down, some form of postsecondary education—not just a bachelor's degree—is more important than ever to economic success.**

College costs now eat up a quarter to a third of family incomes among those in the middle, even after accounting for grants and scholarships, and student debt is on the rise among middle-income families. The average borrower now owes about \$28,000, and delinquency rates on student loans (12 percent) are

than ever to economic success. That's because workers with only a high-school diploma have done even worse in the labor market than recent college graduates. Their job prospects and wages have declined significantly over the past three decades, meaning the college wage premium has remained robust.<sup>3</sup>

College also helps keep people in the middle class. Research from the Pew Project on Economic Mobility has found that children born to parents in the middle-income quintile had a 39 percent chance of falling to the lowest two quintiles as adults if they did not earn a postsecondary degree. Those with a college degree had only a 22 percent chance of falling out of the middle, and they were 22 percentage points more likely to reach the top two quintiles as adults.<sup>4</sup>

**FIGURE 1**



Notes: Figures were adjusted to 2012 dollars using CPI-U. 1971 serves as the index year (1971=100 (spaces)).

Sources: U.S. Census; U.S. Bureau of Labor Statistics (see <http://www.bls.gov/cpi/cpid1301.pdf>); The College Board

These trends add up to a sorry choice for most middle class families: help your children invest in an overpriced and undervalued degree, or watch them languish in low-wage jobs if they forego college altogether.

Conservatives typically respond to these data by arguing that “college” is no longer worth it and warning that “too many people go to college.” They are almost certainly right: many students would be better served by alternatives to the bachelor’s degree-like occupational training or apprenticeship programs.

Yet these criticisms are tone deaf when it comes to the anxieties of middle-income families. These families do not see college graduates working low-wage jobs as

proof that college isn't worth it, but as evidence of an even scarier proposition: "If my kid fails to go to college, they won't even be able to get a low-wage job." What these families need is a more affordable and effective set of post-secondary options, not an explanation that none of their options are promising.

Creating such options will require a fundamental shift in our approach to higher-education policymaking, a change that conservatives can foster. Much of the blame for our current predicament lies with well-intentioned policies originally designed to expand opportunity and protect consumers. Generous federal loan programs, particularly those available to parents, encourage enrollment at any college and at any price, providing little incentive for colleges to keep their tuition low or make sure their students are successful. Meanwhile, though advances in technology could increase access and reduce the cost of education, federal rules governing access to student aid programs create high barriers to entry that keep low-cost competitors out of the market.

Alas, most Democrats ignore these structural problems, choosing instead to pour more student-aid money into the system. Each time they do, affordability improves momentarily, only to be washed away by subsequent tuition increases. For instance, between 2008 and 2012, spending on the Pell Grant program doubled, and the size of the maximum grant grew by \$1,200. Yet by 2012 the purchasing power of the Pell Grant had reached an all-time low.<sup>5</sup>

Conservatives have an opportunity to counter the Left's shortsighted, counterproductive agenda, but only if they put forth a concrete alternative.

Conservatives have rightly questioned the "college for all" agenda, the profligate spending on college campuses, and the liberal politics of faculty and administrators. But up to now, they have not laid the groundwork for a broader reform effort. Thankfully, that is starting to change.

Reining in problematic student-loan policies and clearing out the regulatory thicket that surrounds colleges is necessary but not sufficient. Also essential is an aggressive supply-side strategy that creates space for entrepreneurs—both within the current system and outside of it—to offer post-secondary options and financing tools that are more affordable, efficient, and better tailored to students' needs. To see what that agenda should involve, we should begin with a snapshot of where we are and how we got here.

### **Middle-Income Families and the Rising Cost of College**

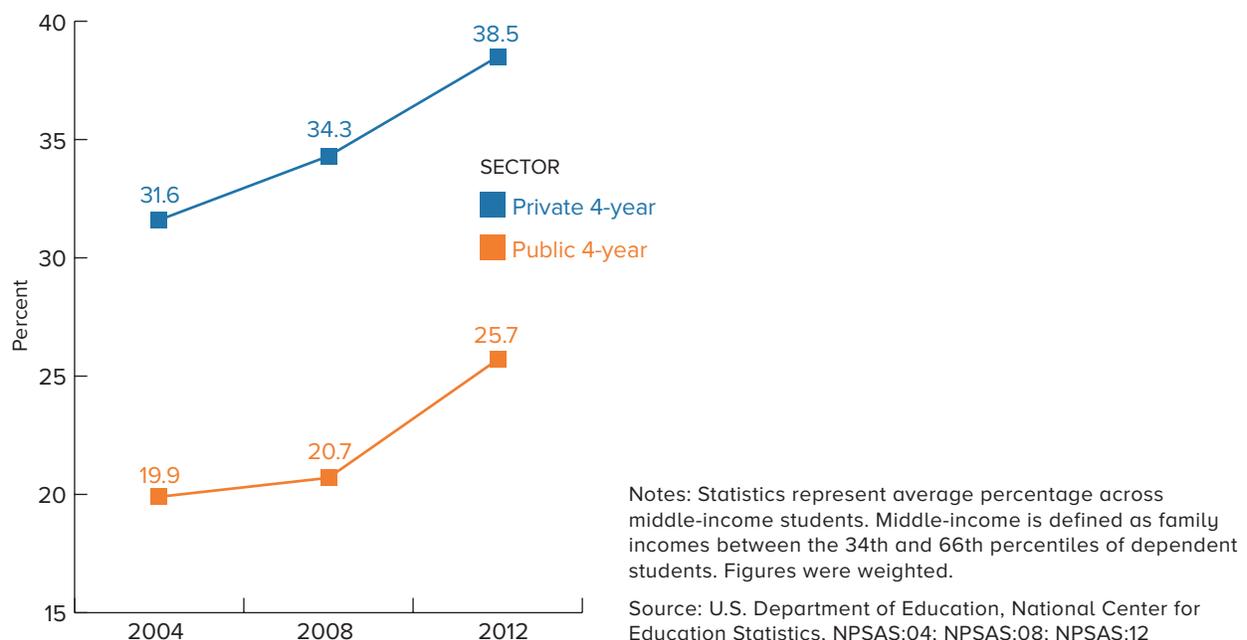
In some ways, middle class families are the "canaries" in the college-cost "coalmine." They fall between low-income families who are eligible for need-based grants and subsidized loans and more affluent families that are able (and willing) to pay high tuition prices and benefit most from higher education tax benefits. As such, middle-income families are among the most likely to feel the pinch of high tuition prices.

To get a sense of how much middle class families are paying and borrowing for college, I used the latest installments of the National Postsecondary Student Aid Study (NPSAS), a federal survey of college students that asks about family income, tuition prices, and financial aid. I divided the samples into three income

groups: low (1st to the 33rd percentile), middle (34th to the 66th percentile), and high (67th through 99th percentile). The discussion here focuses only on the middle category.

Figure 2 displays the net price of tuition, after accounting for grants and scholarships, as a percentage of family income for middle-income respondents in 2004, 2008, and 2012. Data are for four-year colleges only, and are disaggregated by private and public colleges. The figure shows a clear upward trend since 2004, with middle-income families now paying 25 to 40 percent of their annual incomes to attend college. Remember, this is after accounting for any grants and scholarships that students receive.

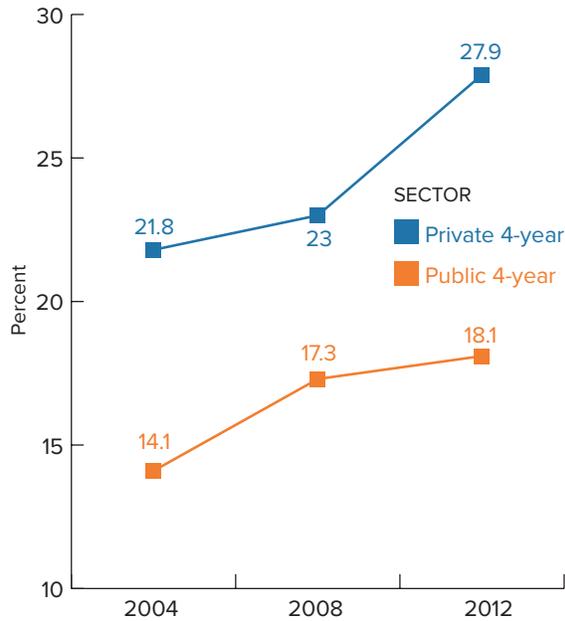
**FIGURE 2: Net price of attendance as a percentage of family income for middle-income students (2004–2012)**



How are middle-income families paying for these increasing costs? By taking on student loans. In 2012, 66 percent and 78 percent of middle-income undergraduates attending public and private four-year colleges (respectively) borrowed to attend. Across all students in the survey, average debt balances grew by 25 to 30 percent between 2004 and 2012.

Perhaps more troubling: parents are also going into debt to finance their children's education, taking on increasingly large federal loans through the Parent PLUS program. Parent PLUS allows parents with a child in college who pass a basic credit check to borrow up to the cost of attendance (minus any other aid received) at a 6.4 percent interest rate. These loans have no aggregate lifetime limit, meaning that as long as a parent has a child in college, he or she can borrow to cover any out-of-pocket costs, year in and year out.

**FIGURE 3: Percentage of dependent undergraduates whose parents have taken out a PLUS loan (2004–2012)**

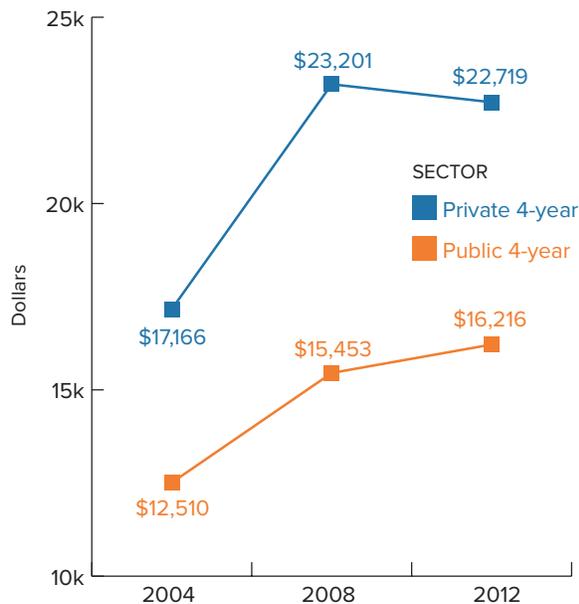


Notes: Middle-income is defined as family incomes between the 34th and 66th percentiles of dependent students. Figures were weighted by WTA000.

Source: U.S. Department of Education, National Center for Education Statistics, NPSAS:00; NPSAS:04; NPSAS:08; NPSAS:12

Figures 3 and 4 show the increase in Parent PLUS borrowing among middle-income families. Figure 3 reveals that a higher percentage of parents are borrowing PLUS loans than before, while Figure 4 shows that those balances have grown by roughly 30 percent across both sectors. While these numbers may not look high compared to the six-figure debts that captivate the popular media, keep in mind that many of these parents have only a few years of work left ahead of them. As balances grow, so too will delinquencies and defaults.

**FIGURE 4: Average amount borrowed in parent PLUS loans among parents of middle-income students (2004–2012)**



Notes: Middle-income is defined as family incomes between the 34th and 66th percentiles of dependent students. Figures were weighted and converted to 2012 dollars using CPI-U.

Sources: U.S. Department of Education, National Center for Education Statistics, NPSAS:00; NPSAS:04; NPSAS:08; NPSAS:12; Bureau of Labor Statistics

In short, the federal government has become the primary financier of higher education and the gatekeeper for new entrants and competitors, but federal policies act mostly to prevent experimentation with new approaches and to inflate prices. It is time for reform.

Families recognize that they are paying far more for the same product, raising questions about whether college investments are “worth it.” A 2011 Pew survey found that 57 percent of survey respondents saw the value of college as “fair or poor,” and that 75 percent disagreed with the statement “Most people can afford to pay for college.”<sup>6</sup> As Peter Wehner’s introduction to this volume points out, middle-class families are particularly anxious about their ability to pay for college.

Two aspects of federal higher education policy have helped drive these trends. First, easy credit from federal loan programs has given colleges little reason to worry about increasing tuition. Second, regulatory policies have limited price competition by keeping potential competitors out of the market.

Ironically, the current struggles of middle-class families are partly the result of shortsighted federal efforts to help them. The early federal student-aid programs were targeted toward low-income students. Prior to 1978, federal student loans were need-based and not available to families with incomes above a certain threshold. States were the main funders of higher education.

The Middle Income Students Assistance Act (MISAA) of 1978 changed all that. For the first time, middle- and upper-income students were eligible for guaranteed federal student loans, a decision that changed the trajectory of the federal role in financing higher education and the trend in college costs. Families

now had access to easy credit to pay the cost of college, and loan amounts were pegged to the cost of attendance, providing colleges with little reason to worry about increasing tuition.

Then, in 1980, Congress created PLUS loans, opening the floodgates even further. These loans carried loan limits, but in 1992 Congress eliminated these limits and (as noted above) allowed parents who passed a credit check to borrow up to the cost of attendance each year with no lifetime cap.

Whether or not the expansion of these loan programs “caused” increases in tuition, they certainly changed the incentives for colleges. By the 1980s, private colleges began to increase their tuition prices apace, building lavish campuses to attract students. To compete for the best students, top public colleges soon followed suit. And as federal aid increased, states gradually began to spend less on their public higher education systems, confident that federal student loans would fill in any gaps. The result: higher tuition, higher debt, and no discernable increase in quality.

The problem is not just the easy money, but the lack of price competition. Federal regulations governing eligibility for student aid have kept new providers out and propped up high-priced, low-quality incumbents. Under the Obama administration, federal regulators have defined what constitutes a “credit hour” and tried to force online providers to be authorized by each state where they

serve students, both of which circumscribe what is possible.<sup>7</sup>

Likewise, in order to access federal money, colleges must be accredited. But accreditation is a peer-review process that is not well suited to quality control. Faculty members from other campuses visit a college, evaluate its offerings and faculty, and then decide whether to certify it as a quality institution.

In other words, the regulators are the regulated. Accreditation agencies subsist on fees from the campuses they evaluate and use faculty from one accredited institution to assess another. Accreditation reviews also enshrine the traditional college model because they focus on things like faculty credentials, facilities, and even the number of books in the library. This system simultaneously keeps shoddy colleges afloat while barring new providers who might generate price competition.

In short, the federal government has become the primary financier of higher education and the gatekeeper for new entrants and competitors, but federal policies act mostly to prevent experimentation with new approaches and to inflate prices. It is time for reform.

### **A New Approach to Higher-Ed**

We cannot spend our way to college affordability. Simply investing more in student aid is like bailing out a sinking boat with a Dixie cup. You might be able to stay afloat for a little while, but eventually you go under.

But we can do much more to cultivate the kind of competitive higher education market that can rebuild and sustain the middle class. Five opportunities stand out.

**1. Reform student loans.** Student lending is on an unsustainable path, and PLUS loans are particularly problematic. They are the ultimate Pyrrhic policy: They solve families' liquidity problems in the present but almost ensure that more families will have even bigger liquidity problems in the future (because of the likely effect they have on tuition). These programs need to be reined in. Eliminating PLUS loans entirely and substituting new options described below would be the boldest solution, but it would also be politically difficult. At the very least, imposing reasonable loan limits would improve the incentives for both schools and borrowers.

More broadly, existing loan programs give institutions no "skin in the game." Policymakers could provide colleges with a direct stake in the success of their students by requiring them to pay back a percentage of any defaulted dollars.<sup>8</sup> Such a policy would encourage colleges to guide students to programs that are likely to provide a positive return. It would also have them share some of the risk that students and taxpayers now bear on their own.

**2. Create space for new financing options.** In place of Parent PLUS loans, policymakers should create space for market-based financing instruments like Income Share Agreements (ISAs). Under an ISA, private investors fund students in return for a share of their income over a fixed period of time.<sup>9</sup> These agreements are not loans in that there is no outstanding balance. If graduates do better than expected, they pay more, but they will pay less—perhaps nothing at all—if higher wages do not materialize.

Because ISA investors only earn a profit when a student is successful, they offer students better terms for degree programs that are expected to be of high value. This process gives students strong signals about which institutions and fields are most likely to help them be successful.

Legislators who wish to support the development of ISAs should set out to clarify the legal and regulatory status of these products, set limits on existing loan programs, and create the data infrastructure necessary to process contracts.<sup>10</sup>

**3. Break down barriers to entry.** The components of a college degree—content, instruction, and assessment—are more readily available than ever before. Online delivery, competency-based education, and short-term career training could dramatically reduce the cost of a postsecondary education. Yet regulatory barriers like accreditation and federal rules keep promising innovations out of the higher education market.

As was the case for airlines, trucking, and telecommunications, higher education needs a deregulatory agenda that breaks down these barriers to entry. Rather than trying to hammer an antiquated accreditation system into something well suited to innovative ideas, policymakers should instead develop a new, parallel pathway to the market.<sup>11</sup> This could mean a new accreditation agency that is designed to certify innovative programs (as Senator Rubio, among others, has proposed), or it could mean devolving accreditation power to a new set of actors (like state governments, as Senator Mike Lee has proposed).

Whatever the approach, these new pathways could allow low-cost education and training providers—many of which will look nothing like a college—to compete with incumbent colleges on an even playing field. In this new market, students could accumulate low-cost credits from different online providers at a fraction of what it costs to take a traditional college course, forcing existing institutions to lower their prices or lose market share. This is the kind of competition that could bend the cost curve.

#### **4. Support occupational opportunities.**

Conservatives warn that the “college for all” mentality has led many students down a blind alley when they would have been better off learning a trade. This is correct: The BA is not the only path to the middle class. Evidence suggests that many short-term sub-baccalaureate programs—like occupational certificates and associate’s degrees—can provide a significant wage premium.<sup>12</sup>

Yet these programs are still treated as an option of last resort by high schools, federal policy, and families themselves. The federal apprenticeship program is a particularly telling example. The Department of Labor currently runs a highly successful registered apprenticeship program, but we spend almost nothing on it and it has few political champions.<sup>13</sup> In fiscal year 2013, the federal government spent about thirty times as much (\$839 million) on ineffective college access programs (TRIO) as it did on the registered apprenticeship program (\$28 million).<sup>14</sup>

The best way for conservatives to counterbalance the “college for all” agenda is to support and tout occupational options like apprenticeships and job training.

## 5. Promote Data and Transparency.

This reform agenda will work best if built on a foundation of data and transparency. Today's higher education market does not function as efficiently as it could because consumers lack clear, comparable information about the value of particular programs at particular institutions. How do graduates fare once they enter the labor market? Are they able to pay back their loans? Without answers to these questions, students cannot know *a priori* which options are worth investing in, and far too many choose programs that are unlikely to pay off. Schools with pitiful labor market outcomes are able to stay in business, and taxpayers and policymakers have no way of knowing whether public investments are reaping a return.

These information problems are self-inflicted. The federal government is uniquely positioned to collect and make available the kind of data that consumers need—a database that merges postsecondary records with wage and employment information of graduates. Unfortunately, in 2008 Congress explicitly banned federal agencies from creating this kind of database.<sup>15</sup> Most congressional Republicans on the education committees have supported the ban from the start, though leaders like Majority Leader Eric Cantor and Senator Marco Rubio have recently come out in favor of data and transparency.

Better data on postsecondary outcomes can lay the groundwork for other reforms. Information on the wage premium attached to various occupational programs could show families that the path to the middle class does not always require a BA. These data would also help ISA investors tailor contracts to reflect

likely outcomes, and allow innovative programs to compete on a level playing field with more traditional offerings.

Republicans have every reason to be concerned that collecting these data will enable Democrats to build them into a ham-handed, arbitrary accountability scheme. But congressional policymakers can easily place prohibitions on how the data are used without prohibiting the collection and dissemination of the data itself. These data are a public good, and families, taxpayers, and policymakers would be better off if they had access to them.

In all of these ways, reformers can help modernize America's system of financing higher education and open far wider the gates into the middle class. Today's accreditation system stands in the way of experimentation with new models and approaches; the lack of data about outcomes makes it nearly impossible to evaluate the options that do exist; and the broken federal loan system enables even failing institutions to continuously increase costs. It is a classic example of a system built to resist innovation and improvement. But by applying core conservative insights about how to turn failing systems around, policymakers can offer middle-class families more options, more control, and a far better shot at the American dream.



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# SAFETY-NET REFORMS

## TO PROTECT THE VULNERABLE AND EXPAND THE MIDDLE CLASS

SCOTT WINSHIP

“In the sixties we waged a war on poverty, and poverty won.” So declared Ronald Reagan in 1987, twenty-three years after Lyndon Johnson’s State of the Union address launching his crusade against deprivation.<sup>1</sup> The War on Poverty is fifty years old this year, and while we have made real progress in reducing material destitution, in a broader sense, Reagan was right and remains so. Today’s welfare state

**By advocating an attractive, reform-minded anti-poverty agenda, conservatives have a chance to do what Great Society liberalism did not—increase upward mobility out of poverty and into the middle class.**

has trapped beneficiaries in deeply problematic circumstances—living in hardship and insecurity, with powerful incentives to behave in ways that keep them and their children there.

By advocating an attractive, reform-minded anti-poverty agenda, conservatives have a chance to do what Great Society liberalism did not—increase upward mobility out of poverty and into the middle class. A conservative anti-poverty agenda must build on the past success of work-promoting welfare reforms while addressing their shortcomings. In so doing, it could help beneficiaries of aid take the initiative to move into the world of work and thereby reap the benefits of employment and self-sufficiency. Just as important, it stands to deter young adults from being pulled into dependency in the first place and to inspire them to be more deliberative about the life choices they make.

### **A History of Mixed Results**

In the narrowest sense, it is not quite fair to say that we lost the war on poverty. Trends in the official poverty rate suggest that there was a major decline in poverty between 1964 and 1969, from 19 percent of Americans living below the poverty line to 12 percent in just five years.<sup>2</sup> It is true that the poverty rate was 14 percent in 1967, 13 percent when Reagan made his quip in 1987, 12.5 percent in 2007 on the eve of the Great Recession, and 15 percent in 2012. But the official measure suffers from several

important flaws.<sup>3</sup> If we corrected for these flaws, we would find that poverty actually fell roughly from 30 percent in 1967 to 16 percent in 2012.<sup>4</sup> In other words, we have cut poverty by more than half since 1964.<sup>5</sup>

Of course, it wasn't cheap. Between 1965 and 2008, federal and state spending on means-tested programs came to around \$16 trillion. This is well over twice the amount we have spent fighting actual military wars since the American Revolution.<sup>6</sup> In 2008, federal and state spending on means-tested programs totaled \$760 billion, and that figure does not include spending on Social Security pensions, Medicare, unemployment compensation, worker's compensation, or Social Security disability benefits.<sup>7</sup> The total, divided among the poorest fifth of Americans, would amount to \$12,500 per person, compared with \$2,000 per person in 1968 (in inflation-adjusted dollars).<sup>8</sup> By 2011, anti-poverty spending at the federal level alone was \$750 billion, and it is safe to say that with state spending, the total amount was in the neighborhood of a trillion dollars.<sup>9</sup>

President Barack Obama's Council of Economic Advisors earlier this year touted the role of the federal safety net in enabling for the decline in poverty, citing figures from a team of Columbia University researchers.<sup>10</sup> But the Columbia paper offers little evidence that Great Society liberalism won the war on poverty. Among children, the safety net prior to the 1990s primarily served to lift some from deep poverty to less severe poverty.<sup>11</sup> The Columbia team shows that the trend in the child poverty rate through 1990 is the same whether or not federal taxes and benefits are accounted for.

For that matter, many parents might have made better long-run decisions in the absence of various welfare programs. While these programs functioned as a temporary stop-gap in hard times for most recipients, for a sizable fraction of beneficiaries they collectively became a poverty trap in periods of economic expansion.<sup>12</sup> They did so by lowering the cost of mobility-inhibiting decisions, such as having children out of wedlock at a young age or choosing not to obtain more education, and by making the transition to work unacceptably costly. If the Great Society safety net discouraged independence, then it may have actually prevented poverty from falling more than it could have. And while material deprivation has declined, upward mobility among young adults who grew up poor is no higher today than it was in the mid-twentieth century.<sup>13</sup>

It is in this sense that President Reagan could speak of defeat in the war on poverty. In a 1986 radio address making the case for welfare reform, he warned, "We're in danger of creating a permanent culture of poverty as inescapable as any chain or bond; a second and separate America, an America of lost dreams and stunted lives."<sup>14</sup> After Johnson's declaration of war, Reagan argued, "Poverty, as measured by dependency, stopped shrinking and then actually began to grow worse. I guess you could say, poverty won the war." Indeed, Johnson's stated goal in 1964 suggests he might have agreed with Reagan: "We are not content to accept the endless growth of relief rolls or welfare rolls. We want to offer the forgotten fifth of our people opportunity and not doles."<sup>15</sup>

Reagan's push for welfare reform would bear fruit in the 1990s. The Columbia



families.<sup>19</sup> And child poverty rates did not rise much during the 2001 recession or even during the Great Recession according to the Columbia team's research.

### **Building on Welfare Reform**

PRWORA replaced the old Aid to Families with Dependent Children program with Temporary Assistance for Needy Families (TANF), but its successful features were not extended generally to other safety-net programs. Most programs give states comparatively little flexibility to tailor their approaches to local needs and preferences. Nor do they involve the work-first approach of TANF. Only able-bodied adults who do not have dependents are subject to work requirements or time limits for receipt of Supplemental Nutrition Assistance Program benefits (food stamps). No one receiving federal housing assistance is required to work or is subject to time limits, outside of a handful of demonstration projects. Medicaid includes no such restrictions.

The Supplemental Security Income (SSI) program for children has become, since welfare reform, a safety net within a safety net for families with children who would otherwise be subject to work requirements and time limits under TANF. Increasingly, families seek and obtain disability status for children with comparatively minor (and often dubious) learning disabilities or behavioral problems. States use the program to make TANF federal work requirements less binding and to avoid having to manage the hardest-to-employ cases. These families would be better served on TANF, even if the adults in them remained non-working; many children receiving SSI under dubious circumstances "graduate" into the SSI program for disabled adults without ever accumulating

any work experience. They thus become dependent adults themselves.<sup>20</sup>

Finally, the Social Security Disability Insurance program increasingly supports not only former workers who have suffered career-ending injuries or debilitations, but able-bodied adults with unattractive job prospects. With persistence, it is not difficult to qualify for benefits, and once on the rolls, there are few real incentives to leave.

These programs all have their own particular objectives and legislative histories, and there is often little coordination between them. Eligibility for the programs is based on disparate requirements, and benefits phase out at different rates. Given these complications, rather than instituting work-promoting reforms program-by-program, there is much to be said for consolidating them, thoughtfully modifying phase-out rates to transparently encourage people move to work, and offering work supports outside the confines of specific programs.

Two such approaches are currently gaining traction in Congress. Senator Marco Rubio has proposed an approach based on an idea developed by Oren Cass (director of domestic policy for Mitt Romney's 2012 presidential campaign). Rubio would package means-tested programs into a "flex fund" that would then be sent to the states. The states would have broad discretion to redesign their anti-poverty policies using this money. At the same time, Rubio would provide wage supplements to low-income workers similar in spirit to the Earned Income Tax Credit, except that the add-on amount would be included in each worker's paycheck rather than received at tax time.

In the House, Congressman Paul Ryan, who chairs the Budget Committee, has spoken favorably of the United Kingdom's "universal credit." Under this approach, various means-tested programs would again be consolidated, and benefits would be distributed to families as a single amount rather than through separate programs with their own application procedures and bureaucracies. A universal credit may be designed with a single phase-out schedule as beneficiaries move into work, calibrated to encourage greater and greater work, with the "stick" of time limits, work requirements, or both to further promote independence.

Either of these approaches (or any alternative) would have to address some key questions, including the appropriate balance between federal and state responsibilities, the nature and extent of work supports, and how to ensure that an adequate safety net is maintained for those who cannot find work. Either a unified block grant to the states or a universal credit could be made more or less generous in terms of federal spending, depending on the extent to which policymakers believe that states should absorb the cost of the safety net. A flex fund could attach conditions to its use, such as time limits or work requirements, leaving it to states to determine whether to fund families who do not qualify for federal dollars. A universal credit could consolidate some programs and drop the federal commitment to others, or it could time-limit benefits in such a way that states would be on their own in supporting families beyond the cut-off date.

What form work supports should take is another key question. Rubio's approach would qualify large numbers of low-wage workers for subsidies, creating

the possibility that employers of such labor would lower the wages they offer over time in response to the subsidy. A universal credit might or might not retain existing work supports like the Earned Income Tax Credit, but designing optimal phase-out rates for the credit would depend on taking into account the interactions between work supports and the credit as people move to employment. The evidence is clear, however, that in order for welfare recipients to end up materially better off by taking employment, work supports are generally necessary.

It will also be important to ensure that a safety net of some sort remains available to those who confront barriers to work and in times of weak demand. The Columbia University research suggests that poverty would have risen by quite a bit during the Great Recession if not for federal tax and transfer policies. (The SNAP work requirement for able-bodied adults without dependents, for example, was temporarily discontinued.) More generally, policymakers should be explicit about who is expected to take care of the hardest-to-employ individuals as anti-poverty policy continues to move toward work promotion. If we will continue to rely on a receptacle like SSI, then there should be an explicit decision to do so. If responsibilities are to be shifted to the states on balance, that too should be part of the conversation around welfare reform.

Apart from reforming the safety net to promote work, policymakers should continue wrestling with the problem of out-of-wedlock childbearing. PRWORA, and especially its 2005 reauthorization, set out to reduce single parenthood and births to single mothers. There is little evidence we have succeeded at all in

doing so. Marriage-promotion programs have proven largely unsuccessful. Interestingly, teen pregnancy has declined markedly since the 1980s, and while the link to welfare reform is difficult to establish, one study found that it reduced teenage motherhood among the daughters of single or less-educated parents and encouraged them to live with a spouse or parent if they did become mothers.<sup>21</sup> This would be

## When less than one-third of poor children can expect to reach the middle class as adults, conservatives cannot afford to simply shrug apologetically and regret that there is nothing to be done.

consistent with provisions of PRWORA that required dependents to live with an adult and stay in school in order to receive TANF benefits. The lesson may be that instead of trying to make relationships succeed once couples find themselves expecting, the better strategy is to try to discourage early child-bearing in the first place.

Welfare reforms along these lines might end up costing rather than saving money in the short- to medium-run, as the 1990s reforms did. However, there are plenty of ineffective federal programs—even within the trillion-dollar anti-poverty budget—that could be reformed to yield additional funding. Indeed, given that anti-poverty policy to date has failed to increase upward mobility, and considering the scarce evidence that federal programs to promote opportunity have worked, at least some programs could

be completely shuttered without harming their “beneficiaries.”<sup>22</sup>

Finally, policymakers should complement welfare reforms with an economic-growth agenda and an early-childhood agenda to promote mobility. The elements of the former are suffused throughout this volume. Meanwhile, the phrase “early childhood agenda” justifiably evokes skepticism in conservative policy circles, as we have little evidence that previously adopted programs run by federal or state bureaucracies have succeeded when scaled up.

But when less than one-third of poor children can expect to reach the middle class as adults, conservatives cannot afford to simply shrug apologetically and regret that

there is nothing to be done.<sup>23</sup> Welfare reform is likely to improve upward mobility by exposing children to the world of work, reorienting their understanding of what is expected of them, and turning working parents into role models. But as the education chapters in this volume recognize, conservatism can help parents who want to invest in the skill development of their children. It can succeed where liberalism has failed because it recognizes the basic flaw of the Left’s approach: centralized bureaucracies that distribute money to local monopoly providers and write rules that constrain their creativity are unlikely to produce desirable child outcomes.

Instead, a conservative approach to early childhood would arm disadvantaged parents who want to do well by their children with a voucher to fund one of any number of investments in their

human capital. Private providers would then compete for the vouchers and be subject to rigorous evaluation. Such an approach would strengthen the “space between the individual and the state” that Yuval Levin’s essay above rightly trumpets, taking advantage of local knowledge and demanding responsibility of beneficiaries while expanding their choices. Policies along the lines of the “Early Learning Family grant” proposed

by Russ Whitehurst could inexpensively transform ineffective programs like Head Start along these lines.<sup>24</sup> Doing so would build support for choice-maximizing approaches to primary and secondary education. It would identify successful models to help disadvantaged children in a decentralized way, and it would make it possible to abandon and de-fund models that prove ineffective.



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# EMPLOYMENT

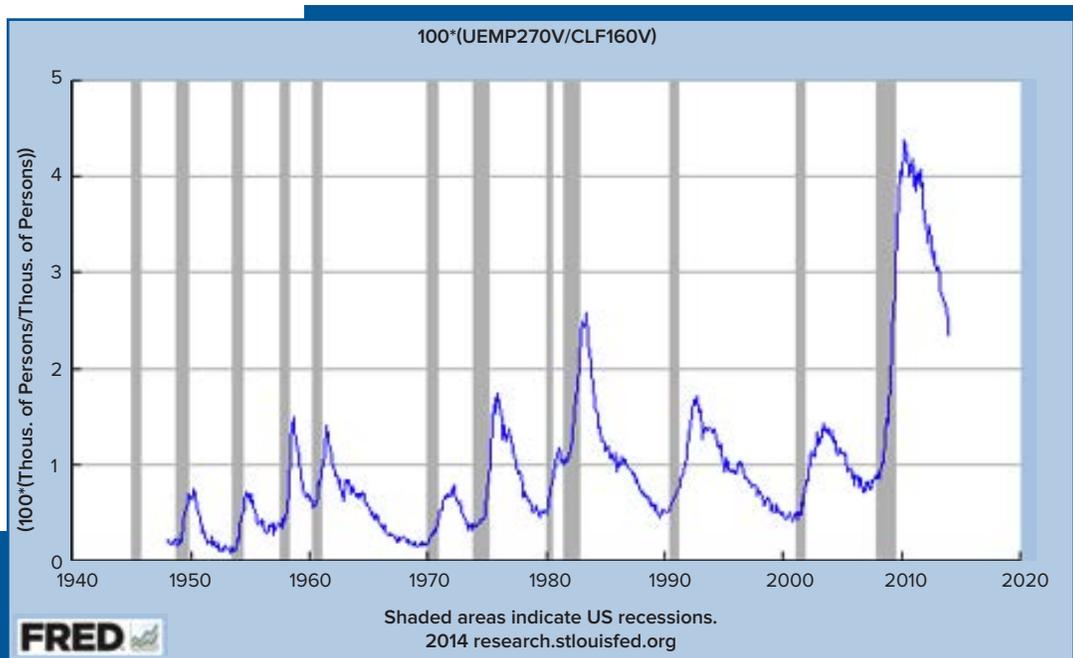
## POLICIES TO GET AMERICANS WORKING AGAIN

MICHAEL R. STRAIN

Work is at the core of the American dream of earned success. Building a thriving job market must be at the heart of the effort to improve America's economic prospects, to strengthen the middle class, and to move more people into the middle class. Unfortunately, that means we have an awful lot of work to do, because America's labor force and labor markets confront some urgent near-term problems and some daunting long-term challenges.

The effects of the Great Recession are still with us. Long-term unemployment—spells of unemployment lasting six months or longer—has been an unprecedented problem in the current downturn, and although it has been declining it remains well above its postwar average nearly half a decade after the end of the recession.

### The long-term unemployment rate



The long-term unemployed face serious problems because of their particular difficulty in getting jobs. Economists have carefully studied the long-term unemployed during the Great Recession, and have found that the chances of finding a job decrease significantly after a worker has been unemployed for six months.

The economic impact of long-term unemployment is significant. Millions of workers sitting on the sidelines or asking to be employed constitute a massive waste of economic resources. (Imagine if we let many factories or vast swaths of farmland sit idle, unused, for long periods.)

More importantly, long-term unemployment is a human tragedy. Divorce rates go up when unemployment is high for extended periods. The long-term unemployed have worse health outcomes. There is some evidence that the probability of suicide increases with extended unemployment. The children of the long-term unemployed suffer, sometimes for years after their parents' unemployment ends.

The sidelining of millions of workers also adds to social idleness and creates a less dynamic, less vibrant society.

And while long-term unemployment presents an urgent challenge, we also face some profound employment problems that long predate the Great Recession and may well speak to structural changes in our society that will shape our prospects for the future.

A principal concern is the declining rate at which men participate in the workforce. The chart below shows the share of the male population of prime working age that is either employed or actively looking for work. As you can see, over the last thirty years this share has dropped dramatically.

**Labor force participation rate for men aged 25–54**



Much of this decline is driven by men with less than a college education. Along with other changes to the labor market, falling wages for these men are likely an important cause of this decline. The consequences of this trend are, again, not merely economic. When men are not working, they are less likely to be married and more likely to be incarcerated. Such chronic unemployment diminishes economic mobility: It is harder to move up the relative income scale if you don't have a

job, and it will be much harder for your children to do better than you as well. Stagnation today robs the next generation of opportunity.

We have near-term and long-term employment problems, and America's political leaders are not doing a good job of confronting either. In the years since the Great Recession, liberal ideas have been tried and found wanting. Conservative ideas and intuitions have not yet been put to work on the problem. If they were, they could well point to some promising answers.

### **Make It Easier to Find Work**

A good first step toward building a stronger labor market would be to lower the barriers that now keep workers from potential jobs.

Rolling back oppressive licensing requirements would be a big help. The Institute for Justice reports that the average cosmetologist spends 372

days in training to receive an occupational license from the government, while the average emergency medical technician trains for thirty-three days.<sup>1</sup> Which occupation seems like it should require more training? Government (especially at the state and local level) certainly has a role in ensuring that certain occupations are practiced only by well-trained workers, but it seems

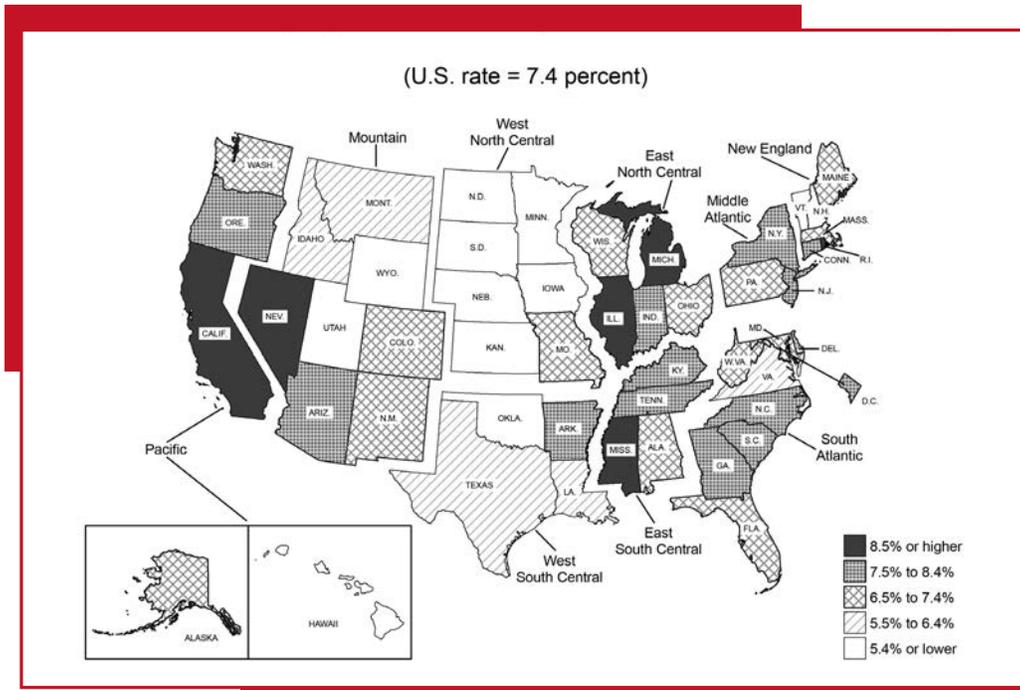
**As part of their effort to put Americans back to work, conservatives should support scaling back unnecessary occupational licensing at every level of government in order to advance economic liberty and create jobs.**

obvious that we have gone too far. As part of their effort to put Americans back to work, conservatives should support scaling back unnecessary occupational licensing at every level of government in order to advance economic liberty and create jobs.

Conservatives should also rethink the way unemployment benefits are provided and allow workers interested in moving in search of employment to receive relocation assistance in place of continued unemployment benefits.

Labor market conditions vary quite a bit across America. In 2013, the unemployment rate in Rhode Island averaged 9.5 percent; in Illinois, 9.2 percent; and in California, 8.9 percent. Compare that with North Dakota's 2.9 percent, South Dakota's 3.8 percent, and Nebraska's 3.9 percent.

## Unemployment rates by state, 2013 annual averages



Source: Bureau of Labor Statistics

It makes sense, therefore, to at least provide a long-term unemployed California worker with information about employment and earnings for his occupation and demographic group in different places, both in California and in other states. And it makes sense to help him to move to another state if he so chooses. This help could take the form of a grant (replacing potential unemployment benefits) to cover his moving expenses, a low-interest government-backed loan with repayment capped at a certain share of future earnings, or some combination of the two.

Using government to help workers connect with jobs could help more Americans earn their own success without requiring the government to manage complicated programs. These policies advance economic liberty and use limited but energetic government action to advance conservative goals.

### Make It Easier to Hire Workers

While making it easier for workers to connect with jobs, policymakers should also champion policies that will make it easier for employers to hire new workers—and perhaps especially to hire the long-term unemployed.

About one in five of the long-term unemployed are young workers, and about one in five have no high school diploma. Many of these long-term unemployed workers are likely applying for minimum wage jobs, but they aren't getting them.

The federal minimum wage requires that potential employers take a \$7.25 per hour risk on long-term unemployed workers—workers who are already seen as quite risky compared to applicants who are coming from other jobs or have been employed more recently. The government should lower the risk associated with hiring long-term unemployed workers

by temporarily lowering the minimum wage that firms must pay them.

Temporarily lower minimum wages for the long-term unemployed should be coupled with a temporary subsidy (through an enhanced Earned Income Tax Credit or a wage subsidy) to ensure that no one who works full time and heads a household lives in poverty. (More on that below.)

A similar approach to help the long-term unemployed would involve tax credits for hiring such workers. The evidence regarding the effectiveness of such credits is mixed, but they appear to work best when they are targeted at unemployed workers. By reducing a firm's tax liability in exchange for the firm's hiring a long-term unemployed worker, these credits create an incentive to get the long-term unemployed back into jobs. And could be more effective than a lower minimum wage for the long-term unemployed because they could apply to all long-term unemployed workers, not just minimum-wage workers. Likewise, we could exempt the long-term unemployed from the payroll tax (both the employer and employee side) for the first several months after they are hired as a targeted incentive to get them back to work.

Of course, lower minimum wages, hiring credits, and payroll tax holidays for only some workers will create winners and losers. For example, it is likely that some firms would hire a long-term unemployed worker at a \$4 minimum wage rather than a short-term unemployed worker at a \$7.25 minimum wage. The short-term unemployed worker would clearly be made worse off because of this policy.

But the fact that a policy creates winners and losers is not necessarily a reason not to pursue it; conservatives should not automatically oppose a government program simply because it causes a small distortion in the market. Some circumstances call for exceptions, and we should recognize that economic efficiency and other social goods will sometimes be in tension. Prudence must be employed on a case-by-case basis to determine which should trump. In this case, encouraging firms to hire the long-term unemployed is likely to be worth the cost of the distortion. Given how hard it is for long-term unemployed workers to get jobs, the benefits—both to them and to society—of moving them up in the queue are worth the costs that will be borne by other job seekers.

After all, relative to the size of the labor force there aren't that many long-term unemployed workers, so the distortions imposed on the labor market would be minimal. And in this case, encouraging firms to hire the long-term unemployed has a large upside—keeping these workers in the labor market, supporting their aspiration to provide for themselves and their families and to stay connected to society, offering partial relief from the damage done to them by the Great Recession, and removing the stigma of long-term unemployment from their résumés by helping them find jobs.

### **Keep Workers Working**

Connecting workers with jobs and making hiring easier are essential steps. But policymakers also need to provide employers with more options for keeping workers in the jobs they have.

One policy that could advance this goal is worksharing. Imagine a firm with one

hundred workers, all of whom earn the same amount of money. A recession hits, and the firm needs to trim 20 percent from its payroll to survive. Today, that firm would lay off twenty workers, each of whom would receive a weekly unemployment benefit. Under work-sharing, every worker would reduce their hours by 20 percent—staying home on Fridays with no pay, for instance—and collect 20 percent of a weekly unemployment benefit. In both situations, the firm would cut its payroll by 20 percent and taxpayers would be on the hook for the same amount of money in unemployment benefits. But under work-sharing, no one would be laid off.

Of course, we wouldn't want to *force* firms to use work-sharing. Firms often use recessions to reorganize their production processes, and sometimes that means letting workers go. This process is necessary in a dynamic economy, and should not be discouraged.

But some firms would very much like to keep the workforce they have in place (think of a small shop with four or five workers, where everyone knows their corner of the store), and would take a hit if they had to lay off employees. Moreover, hiring is expensive, as is

training new workers in jobs that laid-off workers had down cold.

It stands to reason that many firms would welcome worksharing as an option. But worksharing is only available in about half the states, and most employers are not aware of it even in states where it is legal. Conservatives should work to set up worksharing programs in the states where it is now not available, and to make employers more aware

of it everywhere. Giving employers more flexibility is always preferable to forcing their hands—and giving them the flexibility to keep workers employed in a downturn would be a policy win-win.

Keeping employed workers working means keeping them in jobs, but it also means allowing them to work more hours if they choose. Obamacare poses an important obstacle to both

of these goals, as it is projected to significantly reduce labor supply over the next ten years among certain groups of people. How significantly? A whopping 2.5 million full-time equivalent workers, according to the Congressional Budget Office.

All else being equal, mitigating “job lock”—the situation in which workers stay in a job only because they don't

Simply put, we need public policies that help keep workers working, rather than ones that nudge workers to leave their jobs and to reduce the number of hours they work. Amazingly enough, a commitment to that principle increasingly forms a dividing line between the Right and Left.

want to lose their health-insurance benefits—is a good idea, and reductions in labor supply caused by weakening the link between employment and health insurance should not lightly be criticized by conservatives. But the high implicit marginal income-tax rates in Obamacare are another matter. The law gives subsidies to households with income up to 400 percent of the federal poverty line (this year, that would mean up to \$94,200 for a family of four) in order to help with the cost of purchasing health insurance. The more money you make, the smaller the subsidy you receive. Because a little extra work results in losing some of the benefit workers receive from the government, the “subsidy phaseout” operates as a tax that discourages work.

Conservatives should oppose the work disincentives in Obamacare while working to further (and prudently) weaken the link between employment and health insurance. There are good ideas out there for how to do this—including the kinds of proposals discussed by James C. Capretta elsewhere in this book. Simply put, we need public policies that help keep workers working, rather than ones that nudge workers to leave their jobs and to reduce the number of hours they work. Amazingly enough, a commitment to that principle increasingly forms a dividing line between the Right and Left.

### **Make Work More Attractive**

The deeper problem of declining workforce participation is connected to another public-policy challenge that conservatives must confront. It is tied to the ways in which some public anti-poverty programs tend to make work less attractive, and so to drive

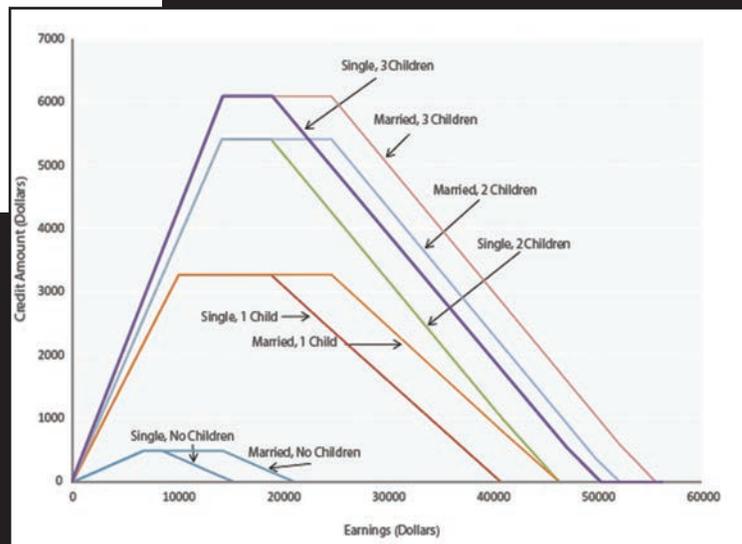
Americans with lower incomes and lower levels of skill away from employment.

The Social Security Disability Insurance (SSDI) program is particularly problematic in this regard. As of the end of 2013, nearly 11 million disabled workers and their dependents were receiving SSDI benefits. The share of adults receiving such benefits doubled between 1989 (2.3 percent) and 2009 (4.6 percent). A just society must ensure an adequate standard of living for the truly disabled, but there is compelling evidence that SSDI operates as a permanent unemployment program for many. Conservatives should make work more attractive for SSDI beneficiaries by making the program much more work friendly—changing it from the permanent exit from the labor force that it too often is today into a program that recognizes disability as a continuum and helps beneficiaries to work as many hours as they reasonably can.

Reforms of the Earned Income Tax Credit are also essential to making work more attractive. The EITC is one of the most successful anti-poverty and pro-work programs we have. It functions as an earnings subsidy for low-income households. In order to qualify for the refundable tax credit, you have to have a job, and the size of the credit increases with earnings over a sizeable range.

Given its design, it is no surprise that the EITC has increased the number of people who enter the labor force. In addition to drawing people into the workforce by increasing the rewards to working, it is also very well targeted to working-class households—it has lifted millions of people out of poverty.

## Earned Income Tax Credit by Number of Children and Filing Status, 2014



Source: Tax Policy Center

The EITC is much more generous to households with children than to those without; in 2014, the most a childless worker will get from the EITC is \$496, while a worker with three or more children will get up to \$6,143.

As mentioned above, a major social and economic problem facing the United States is male non-employment—and many of those men do not have children in their households. Expanding the EITC for workers with children in the 1990s brought a lot of single mothers into the workforce. We should expand the EITC for childless workers in order to do the same for them.

There are, of course, good reasons for offering more generous support to workers with children than to workers without. But we could increase the maximum size of the credit for a childless worker by a factor of six and the maximum credit for a worker with one child would still be larger. So policymakers

should double or triple the credit available to childless workers, and fund the expansion by reducing tax benefits (like the mortgage-interest deduction and the state and local tax deduction) that now almost exclusively benefit higher-income households.

Conservatives should also make the case for an expanded EITC as part of their bottom-up, organic alternative to the Left's top-down, technocratic job-training programs: The EITC provides assistance to workers at the bottom of the labor market to acquire skills and to build careers, but uses employers to provide this training in an individualized way rather than pretending that a central bureaucracy knows what skills people need.

### Conservative Labor-Market Reforms

Our labor market is badly damaged, suffering from both urgent and slow-burning problems. Workers cannot properly connect with jobs, employers

face too many obstacles to hiring, we are failing to make alternatives to layoffs available, and our welfare system makes work unattractive for too many able-bodied Americans.

Policymakers need an approach to reforming our labor-market policies that empowers individuals and supports their higher aspirations—giving them the

the danger of dependency. We must not try to direct the market; instead, we should try to use the market as a means to promote positive ends.

Ultimately, this is not a technical debate but a philosophical one. Work is essential to any notion of the good life. The policies of the Left often undermine the good life by denying people access to the

**Policymakers need an approach to reforming our labor-market policies that empowers individuals and supports their higher aspirations—giving them the chance to lead flourishing lives through work.**

chance to lead flourishing lives through work. In some cases, such reforms should get government out of the way. In others, limited but energetic government should be prudently deployed to support work, to match workers with firms, and to help the long-term unemployed.

What these problems require is not the Left's approach, with its over-emphasis on making unemployment and non-employment materially comfortable, its relative lack of concern about fostering dependency and the limits of government competence, its desire to "support" the economy through massive spending programs, and its tendency towards top-down, technocratic micromanagement.

Instead, we need reforms that advance social dynamism and vitality while evincing skepticism about government's ability to do complicated things well. We must promote earned success while recognizing the power of the law of unintended consequences and

preconditions for thriving. The Right needs to offer an alternative that is neither liberalism-lite nor a cold shoulder to neighbors in need. Instead, conservatives should encourage the good life by encouraging the virtue and dignity that only work can provide.



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# ENERGY REFORMS TO CUT UTILITY BILLS AND ENABLE GROWTH AND INNOVATION

ADAM J. WHITE

Because energy policy is the sort of subject that is usually discussed in national or even international terms, it is not always easy to connect it to daily life. But during his 2008 presidential campaign, President Obama captured the point perfectly:

*In the struggle with higher energy prices low-income families are suffering the most and receiving the least attention. Across the nation, poor families this winter will increasingly face the choice between heating and eating as prices for natural gas, heating oil, propane and electricity skyrocket.<sup>1</sup>*

And that goes not just for heating homes, but also fueling cars, as he more recently explained:

*If you're someone who works in a relatively low-wage job and you've got to commute to work, it takes up a big chunk of your income. You may not be able to buy as many groceries. You may have to cut back on medicines in order to fill up the gas tank. So this is something that everybody is affected by.<sup>2</sup>*

Yet in recent years middle-class and low-income Americans have needed to spend more and more of their income on energy, according to Bureau of Labor Statistics data. In 2000, the lowest-income 20 percent of American households spent 3.2 percent of their income on natural gas, electricity, and fuel oil; in 2011, they spent 6 percent. In 2000, they spent 4.7 percent of their income on gasoline or public transportation; in 2011, they spent 6.4 percent.<sup>3</sup>

The trend is similar for the middle 20 percent: in 2000, they spent 3.6 percent of their income on natural gas, electricity, and fuel oil; in 2011, they spent 4.6 percent. In 2000, they spent 4.7 percent of their income on gasoline or public transportation; in 2011, they spent 7.3 percent.

There are several possible policy responses to these problems, of varying degrees of hospitality to middle-class interests and preferences. But the most promising

## In utilizing these new resources, of course, we must be ever mindful of important questions of risk and regulation, property rights, and the public interest.

opportunity, especially in the short run, appears to be the nation's newly abundant supply of natural gas: "Recent innovations have given us the opportunity to tap large reserves—perhaps a century's worth of reserves, a hundred years worth of reserves—in the shale under our feet," President Obama explained in 2011. The "potential for natural gas is enormous."<sup>4</sup> For that reason, there is strong bipartisan support for developing our natural gas resources, at least among the broad majority of Americans who recognize (in White House adviser John Podesta's words) that "if you oppose all fossil fuels and you want to turn that switch off tomorrow, that is a completely impractical way of moving toward a clean-energy future."<sup>5</sup>

In utilizing these new resources, of course, we must be ever mindful of important questions of risk and regulation, property rights, and the public interest, which are inherent in energy infrastructure policymaking. The middle class will be the ones most affected by those considerations, and thus they must be allowed a real voice in striking those balances—something they have lacked in recent years.

### **The Shale Gale**

It is difficult to overstate how dramatically the nation's energy fortunes have changed in the span of just a few years. A decade ago, when the nation's demand for natural gas far exceeded its own plausible domestic supply, Energy

Secretary Spencer Abraham had good reason to urge that the nation would need to attract well over \$100 billion in investment to develop import facilities capable of receiving

15 billion cubic feet of liquefied natural gas (LNG) from tanker ships every single day. "North America is moving to a period in its history in which it will no longer be self-reliant in meeting its growing natural gas needs," he warned; "production from traditional U.S. and Canadian basins has plateaued." Hence the pressing need to import vast quantities of gas from overseas.<sup>6</sup>

But in the decade that followed, our fortunes turned 180 degrees. Where the Energy Information Administration predicted in 2005 that America's natural gas imports in 2025 would be nearly 18 billion cubic feet per day (Bcf/d),<sup>7</sup> it now expects us to export nearly 10 Bcf/d by 2029.<sup>8</sup> (To put this in perspective, the nation consumed roughly 70 Bcf/d of natural gas in 2012.)<sup>9</sup>

**It is difficult to overstate how dramatically the nation's energy fortunes have changed in the span of just a few years.**

The source of this sudden supply is by now well known: advances in hydraulic fracturing, coupled with advances in horizontal drilling, have unlocked vast stores of shale gas (and its petroleum equivalent, "tight oil") long thought inaccessible or uneconomical.<sup>10</sup> Daniel Yergin, the nation's most prominent energy analyst, calls this the "Shale Gale," the single most transformative energy moment of a generation: Estimates

of the entire natural-gas resource base, taking shale gas into account, are now as high as 2,500 trillion cubic feet, with a further 500 trillion cubic feet in Canada. That amounts to a more than 100-year supply of natural gas, which is used for everything from home heating and cooking to electric generation, industrial processes and petrochemical feedstocks.<sup>11</sup>

We already are beginning to benefit from these natural gas supplies: The American Enterprise Institute's Mark Perry reviewed data produced by the Energy Information Administration and found that households spent 14 percent less (in dollar terms) on natural gas in 2012 than in the year before—and 37 percent less than in 2008.<sup>12</sup>

Americans may reap immense benefits from these new natural gas reserves. First and foremost, they will reduce the cost of electricity. The EIA estimates that new supplies of shale gas will help allow the nation to rely on natural gas for 35 percent of its electricity by 2040 (up from 30 percent in 2012). Furthermore, the availability of natural gas co-located with renewable power generation could help to facilitate renewable sources producing 16 percent of our electricity (up from 12 percent in 2012). Coal, meanwhile, will fall to 32 percent of our power generation by 2040 (down from 37 percent today).<sup>13</sup> Even in the short term, natural gas will be substantially more important: For 2020, EIA today expects natural gas to supply 7 percent more electricity than EIA expected for 2020 a year ago.<sup>14</sup>

The increased use of natural gas will save Americans a lot of money. IHS CERA, the respected energy research

firm founded by Yergin, finds that “combined-cycle gas turbines” produce electricity costing \$75 per megawatt-hour, much cheaper than coal-fired power plants (which IHS CERA estimates at \$100/mWh or more).<sup>15</sup> The EIA, too, projects that electricity produced from natural gas will be much cheaper than electricity produced from coal, both in 2020 and 2040.<sup>16</sup>

Increased supplies of natural gas also will substantially lower the cost of heating homes.<sup>17</sup> In 2010, the cost of heating a home with gas was one-third the cost of heating it with electricity (and half the cost of heating it with oil); by 2035, heating with gas may cost just one-quarter the cost of heating it with electricity (and still half the cost of heating it with oil).<sup>18</sup>

As noted at the outset, home heating and electricity aren't the only energy costs that Americans bear—transportation is another substantial part of household budgets. And natural gas can help substantially here, too, according to Resources for the Future, a think tank focusing on energy and natural resources. Natural gas can be used to fuel cars with compressed natural gas (CNG), liquefied petroleum gas (LPG), methanol, and even ethanol, each of which could offer substantial cost advantages over current fuels.<sup>19</sup> Even if the absence of widespread fueling infrastructure limits CNG and LPG primarily to centrally fueled fleets of heavy-duty trucks in the short run, the reduced demand for conventional gasoline would lower its price for other drivers.

Finally, the new natural gas supplies offer advantages not just to households, but to the economy at large. IHS CERA finds that

lower gas prices “are currently providing a short term economic stimulus to disposable income, GDP and employment,” and that in the longer term it may increase real GDP from 2.0 percent to 3.2 percent annually (or \$500–\$600 billion), and may increase real disposable household income by \$2,000 in 2015 and more than \$3,500 by 2025, thanks to lower home heating costs, lower costs of consumer goods and electricity, and higher manufacturing wages.<sup>20</sup>

Recent events in Ukraine have highlighted the national-security benefits of shale gas. Russia’s vast reserves of conventional natural gas have long given it substantial geopolitical leverage over not just the former Soviet republics, but also Eastern and Western Europe. If the U.S. begins to export some of its new surplus natural gas reserves to those regions, in the form of liquefied natural gas (LNG), then the U.S. may succeed in substantially weakening Russia’s strategic grip on the region.<sup>21</sup> Furthermore, new U.S. capacity to export substantial volumes of LNG would provide us another useful point of leverage in free-trade negotiations generally.<sup>22</sup> But it is important to stress that this is a long-term opportunity, not a short-term one. The development of this infrastructure will take a substantial amount of time. EIA expects that the U.S. will not become a net exporter of LNG until 2016, or of natural gas until 2018.<sup>23</sup> Also, some analysts indicate that the demand side of this international equation may not mature for some time, as other nations’ import infrastructure is not fully formed.<sup>24</sup> Still, LNG exports remain an important long-term opportunity.

But the “Shale Gale” will not bear fruit if the gas cannot be produced at the well-

head and transported by pipelines to the market. And to achieve this requires important policy reforms throughout the supply chain: at the source; at the “midstream” (that is pipelines); and, for purposes of exports, at the end of the pipeline.

There has been substantial debate over how best to regulate drilling for shale gas (or “fracking”). This is a matter traditionally committed to state and local regulators, and law professors Tom Merrill and David Schizer offer compelling reasons to keep that status quo, at least so long as it proves workable.<sup>25</sup> Merrill and Schizer also have summarized the studies and experience indicating that shale gas fracking does not yet appear actually to pose a substantial threat to groundwater.<sup>26</sup> States are capable of taking primary responsibility for ensuring that the cement casing surrounding wells at the groundwater level are sufficiently strong.<sup>27</sup> There also have been concerns raised about methane leaks from natural gas infrastructure, but studies indicate that this problem, too, is quite manageable.<sup>28</sup>

At the midstream, the rise of shale gas production will require a substantial development of new interstate and intrastate natural gas pipeline infrastructure. According to ICF International, the nation may need 16,400 miles of new interstate “transmission” pipeline capacity by 2020, and 35,600 miles of transmission capacity by 2035, in addition to hundreds of thousands of intrastate “gathering” lines.<sup>29</sup> Even setting aside the intrastate pipelines, the new interstate pipelines will require approval by federal and state regulators—not just the Federal Energy Regulatory Commission, which administers the Natural Gas

Act, but also the myriad other federal and state agencies administering other relevant federal statutes (such as the Clean Water Act), as well as federal statutes giving the other agencies strong participatory roles in FERC's environmental review (such as the National Environmental Policy Act).

In the Energy Policy Act of 2005, Congress and the President attempted to reform and streamline the framework of overlapping statutes and regulations governing new interstate gas pipelines, by requiring agencies to collaborate, by setting schedules and deadlines for approvals, and by expediting judicial review of permit denials.<sup>30</sup> But nearly a decade later, it is highly questionable whether those reforms actually have had their intended effect. According to one recent study commissioned by the Interstate Natural Gas Association of America, interstate pipeline projects continue to be delayed by federal regulators (even in violation of plainly stated statutory deadlines for agency action) as well as by state regulators administering federal permit statutes (such as the Clean Water Act).<sup>31</sup>

In light of these problems (and other non-gas examples, most notably the President's slow review of the Keystone XL international oil pipeline), members of Congress have proposed further reforms to improve the federal permitting process, such as the Federal Permitting Improvement Act (S. 1397), which would do a great deal to alleviate problems caused by slow or recalcitrant regulators.

But experience counsels that legislation can only do so much. Even when Congress passes plainly worded statutes, the amount of discretion and prac-

tical leverage retained by regulators makes it very difficult for either permit applicants or Congress to force agencies to act. This, too, has been illustrated best by the case of the Keystone XL oil pipeline: When Congress finally attempted to force the President to make a good-faith decision on the longstanding pipeline application, the President effectively used the threat of a permit denial to start the application process all over again.<sup>32</sup> Simply put, in matters of natural gas infrastructure permitting, personnel is policy. Thus, to reform the permitting process will require not just legislation, but also persistently strong oversight of the regulators by Congress.

At the end of the pipeline is the choice between consuming natural gas at home and exporting it abroad as LNG. There currently is a fierce debate among those who favor exporting LNG, and those who would strictly limit LNG exports in order to promote manufacturing and other industries and consumer uses here at home.<sup>33</sup> NERA Economic Consulting recently issued a study, commissioned by the Energy Department, concluding that LNG exports would not harm domestic manufacturing;<sup>34</sup> similarly, the Deloitte Center for Energy Solutions found that LNG exports would not substantially increase natural gas prices at home.<sup>35</sup> But others, such as PIRA Energy Research, say that LNG exports would effectively tie the domestic price to volatile global prices, with negative repercussions at home.<sup>36</sup> At this point, the NERA and Deloitte studies appear compelling, but as LNG exports increase policymakers will need to continue to monitor the situation.

## **Risk, Private Property, and the Public Interest**

While the middle class stands to benefit greatly from America’s new bounty of energy supplies, it also stands to bear the risks and costs of energy policy.

The myriad federal environmental statutes serve important purposes, but at a cost. The National Environmental Policy Act, in particular, requires FERC and other agencies to consider the environmental effects that may result from new energy projects and policies. As noted above, these statutes are often exploited by regulators and interest groups who are interested less in seeing projects go forward safely than in blocking disfavored projects or policies altogether. For that reason, there occasionally are calls to radically reduce the power of such statutes, either for given projects or in general.

In striking that balance between promoting energy development and guarding against the risk of harm, we must take care not to err too far in either direction—and on the “risk” side of the ledger, we must be careful not to breeze too swiftly past small risks of immense harm. We recall energy projects that have caused catastrophic harms that were later characterized as “practically unthinkable” for the project’s original planners: the 2010 Gulf of Mexico oil spill, and the 2011 tsunami that destroyed Japan’s Fukushima Daiichi nuclear plant, to name two prominent examples.<sup>37</sup> The point is not to allow the “precautionary principle” to become the “paralyzing principle,”<sup>38</sup> but rather to remember that energy infrastructure can never be one hundred percent risk-free for surrounding communities. As conservative philosopher Roger Scruton writes,

the key is not to “dismiss the anxieties to which the Precautionary Principle is proposed as a solution,” but rather, to “make a clear effort to identify those anxieties, to state them precisely, and to see whether regulation of any kind could be an effective response to them.”<sup>39</sup> When energy development—including both shale gas drilling and pipelines—is so close to middle-class communities, including the water supplies on which they rely, policymakers must take care not to give such concerns either too little weight or too much weight. This requires prudential judgment exercised in good faith.

Second, energy infrastructure policy raises substantial questions of the use of “eminent domain”—the forced (if compensated) taking of private property for public uses. Eminent domain has always been an important part of energy infrastructure development, because it is difficult, if not impossible, to build a hundred- or thousand-mile pipeline or power line if any single landowner can block the project by refusing to sell the project the land or easements necessary for the route. Thus, not long after Congress enacted the Natural Gas Act of 1938 to facilitate the development of interstate gas pipelines, it amended the Act to give federally approved pipelines the power of eminent domain over the route. Similarly, federal law has long given eminent domain powers to certain hydropower projects and oil pipelines; and in 2005, the Energy Policy Act gave eminent domain power to certain “national interest electric transmission corridors.”<sup>40</sup>

But to grant private companies a power of eminent domain is now a politically fraught choice in the aftermath of *Kelo v.*

## Americans can benefit immensely from the new energy future, but they must be allowed to help chart that future. In recent years, middle-class households have had an energy policy imposed upon them by regulators and ideologues.

*City of New London*, in which the Supreme Court allowed a Connecticut town to use eminent domain to take property from homeowners and give it to commercial developers.<sup>41</sup> The issue is more political than strictly legal: even though pipelines and power lines are well-established “public uses” within the meaning of the Constitution’s “Takings Clause,”<sup>42</sup> the public’s newly heightened concern about the use of eminent domain by private companies has created an important new debate around energy infrastructure. Local landowners opposed to the Keystone XL project have fought back in state court,<sup>43</sup> even winning the first round of litigation over whether Nebraska’s grant of eminent domain power to the pipeline violated the state’s constitution.<sup>44</sup> As with the discussion of risk, the point here is not

that private property rights necessarily ought to prevail over energy infrastructure, or vice versa; rather, this is an issue that policymakers and the public must keep in mind, particularly when those most affected by new oil and natural gas pipeline routes may well be the middle class that stands also to benefit from the pipelines.

Ultimately, these are balances that the middle class can and should strike. Americans can benefit immensely from the new energy future, but they must be allowed to help chart that future. In recent years, middle-class households have had an energy policy imposed upon them by regulators and ideologues.<sup>45</sup> It is well past time for the middle class have a meaningful voice is deciding what our energy policy should be.



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# REGULATORY & FINANCIAL REFORMS TO COMBAT CRONYISM AND MODERNIZE OUR ECONOMY

JAMES PETHOKOUKIS

American workers deserve a safety net that protects them from the worst effects of the economy's inevitable ups and downs. But business deserves no such firewall. Corporations shouldn't get a state-supplied edge—whether a regulation, spending program, or tax subsidy—over a competitor. Nor should government provide a backstop to prevent failure. There is a big difference between crony or state capitalism and free-market, entrepreneurial capitalism. In order for our market economy to work effectively, it is the government's job to establish a level but intensely competitive playing field for business where the most innovative and dynamic companies win—not the most politically influential or connected ones. Upstart rivals and the threat of failure are key to the “gales of creative destruction” that drive innovation. And innovation is what drives long-term economic growth and broad improvement in middle-class living standards.

A lack of private-sector competitive intensity, on the other hand, results in stagnation and decline. The meager economic-growth and job-creation numbers of the Not-So-Great Recovery are well known. But the economy's

problems go beyond present difficulties. There is something deeper and more structural going on, something that predates the financial crisis of the Bush years and the multiple policy mistakes of the Obama administration. McKinsey Global Research notes increasingly lengthy “jobless recoveries” after recessions.<sup>1</sup> From the end of World War II through the 1980s, labor markets snapped back quickly after each downturn. It took an average of just six months to return to pre-recession job levels. But recovery times have grown ever longer over the past three decades. And when labor markets do normalize, the share of mid-wage jobs after the recovery is below where it stood before the

recession. Goldman Sachs research has found both that the “hollowing out in the middle is real” and that “it is not unique to the [recent] post-crisis period.”<sup>2</sup>

So what is wrong with the American economy? “Secular stagnation,” says the Left: Too much income inequality and austerity means too little spending demand. “Uncertainty,” says the Right: Businesses won't invest because they don't know what the future holds for taxes and regulation.

Each theory may well have some explanatory power. But neither is airtight or complete. So here's a third theory: Jobless recoveries and anemic growth are the result of an American economy now better at generating "process innovation" (creating cheaper, more efficient ways to make existing consumer goods and services) than what business consultant Clayton Christensen has termed "empowering innovation" (creating new consumer goods and services). Process innovation

dynamism beyond the macro evidence of slow GDP growth and weak job creation. A *Wall Street Journal* analysis of Census data finds, for instance, that new companies made up roughly half of all U.S. businesses in 1982 but just a third by 2011.<sup>4</sup> Over that same period, the share of the labor force working at new companies fell to 11 percent from more than 20 percent. What's more, total venture capital invested in the U.S. remains below its pre-recession peak. As one economist told the *Journal*,

One possibility is that rampant crony capitalism has mucked up the gears of the Great American Growth Machine. Washington increasingly protects big business from competition by hungry startups and (through bailouts) reduces the possibility of failure. As a result, the competitive intensity of American capitalism has faded.

freed up capital, Christensen explains, that is then reinvested to make business even more efficient, often substituting machines for middle-class workers. Empowering innovation, on the other hand, generates the good jobs of the future. As Christensen told the *New York Times* in 2012: "We need to reset the balance between empowering and efficiency innovations."<sup>3</sup>

But how did this innovation imbalance happen? One possibility is that rampant crony capitalism has mucked up the gears of the Great American Growth Machine. Washington increasingly protects big business from competition by hungry startups and (through bailouts) reduces the possibility of failure. As a result, the competitive intensity of American capitalism has faded.

There is some evidence suggesting just such a secular decline in U.S. business

"The U.S. has succeeded in part because of its dynamism, its high pace of job creation and destruction, and its high pace of churning of workers. The pessimistic view is we've lost our mojo."

Along those lines, a recent Kauffman Foundation study noted that the rate of new business formation has been "declining steadily for at least the last three decades."<sup>5</sup> The rate of new business formation, as a portion of all companies, is off by 40 percent since the 1980s. Take the U.S. technology sector, which Kauffman defines as industries with high shares of workers in the STEM occupations of science, technology, engineering, and math. Within that group, Kauffman focused on tech companies five years old or younger, a subset of which includes the high-growth "gazelle" firms that account for a large share of net new job creation. But the number of young tech firms—again, the

kinds of firms generating new ideas, products, services, and jobs—has fallen below 80,000 from a high of 113,000 in 2001. With reduced firm entry, perhaps it is not surprising that the age of the average S&P company has been rising in recent years.

So how exactly is cronyism stymieing the free and frequent entry of start-ups and exit of incumbents that is key to innovation and high-wage job creation? One could point to all the special breaks in the tax code, or special-interest spending like farm subsidies. More significant, perhaps, is America's "too big to fail" financial regulatory system. While the TBTF doctrine has its roots in 1950s financial legislation, it bloomed in 1984 with the federal bailout of Continental Illinois, the nation's seventh-largest bank. During a congressional hearing about that bailout, the U.S. comptroller of the currency identified eleven bank holding companies as too essential to the economy's health and stability to be allowed to fail. Banks quickly got the message that the bigger they were, the more likely they were to benefit from a government backstop.

Back then, bank assets were distributed fairly evenly among the big, medium, and small banking sectors, but today this is far from the case. The Dallas Fed recently noted that fewer than a dozen megabanks—just 0.2 percent of all banking organizations—control two-thirds of the assets in the U.S. banking industry. As Thomas Hoenig, vice chair of the Federal Deposit Insurance Corporation recently put it: "If even one of the largest five banks were to fail, it would devastate markets and the economy."<sup>6</sup> Yes, the Dodd–Frank reform legislation enacted in 2010 was supposed to end

TBTF, but instead the law explicitly permits bailouts through its resolution authority provision. Bloomberg estimates this subsidy is worth over \$80 billion a year; the IMF estimates it at around \$70 billion. And history would suggest that whatever the intention of lawmakers, another financial panic would spur Washington (in the form of either Congress or the Federal Reserve) to take action. As the Bank of England's regulatory chief Andrew Haldane has said: "The history of big bank failure is a history of the state blinking before private creditors."<sup>7</sup>

One effect of a highly concentrated and interconnected, TBTF financial system is to give a competitive edge to megabanks, an advantage that Dodd–Frank extends and worsens. Since just before Dodd–Frank's passage through the third quarter of 2013, according to the Mercatus Center, the United States lost nearly 10 percent of its small banks. Moreover, small banks' share of U.S. banking assets and domestic deposits has decreased by nearly 20 percent and 10 percent, respectively, with the five largest U.S. banks absorbing much of this market share. From the Mercatus report: "Mounting regulatory costs threaten to accelerate the shift towards big banks and away from small banks that have long been important members of the financial industry and the local communities they serve."<sup>8</sup>

So the largest banks not only drain assets away from their smaller rivals thanks to their TBTF status, but they also can better cope with Washington's tidal wave of regulation. Yet smaller banks are crucial to small business creation. As an American Enterprise Institute paper last year noted, community banks provide nearly half of small-business loans

issued by U.S. banks. Big banks, on the other hand, are incentivized to focus on taking risk of the sort the Fed and regulators care about, risk that could sink the broader economy, such as investing in mortgage-backed securities and complex derivatives. As entrepreneur and blogger Ashwin Parameswaran has written, “The attractiveness of this strategy meant that banks shunned lending exposed to non-macroeconomic idiosyncratic risks such as lending to small businesses or new firms.”<sup>9</sup>

So how to truly end TBTF and transform the U.S. financial system into one that better allocates capital to the businesses that will create the high-wage, middle-class jobs of tomorrow? Hoenig, for instance, would limit the federal safety net—like deposit insurance and the Fed’s discount window—only to banks engaged in traditional, well-understood activities such as commercial banking, asset management, and stock and bond underwriting. With those limitations in place, the largest banks would likely have to break themselves up. Another option would be to trust rules rather than regulatory discretion by gradually but substantially raising the capital requirements for TBTF banks and applying them to all assets. But how much capital? Some in Congress would force megabanks to comply with a 15 percent leverage ratio, meaning they could borrow only 85 percent of the money they lend versus 94 or 95 percent under new preliminary U.S. bank rules.

Such capital requirements—which would have been high enough to get the big banks through both the Great Depression and Recession—would also likely nudge megabanks into shrinking themselves or breaking up. Assets again would be more

evenly distributed among financial institutions, and smaller banks would not have to contend with Dodd–Frank’s oppressive regulatory regime. Finally, it should be a lot easier to start a bank, which means both deregulation and ending the TBTF competitive advantage of the big banks. Lots of financial startups would be especially important in another financial crisis. Instead of bailouts for insolvent institutions, some financial experts such as Parameswaran have suggested fast-track regulatory approval for fresh, healthy ones.

Not only do we need to end the bailout culture on Wall Street and create real financial competition, but we must also dismantle the regulatory and legal barriers more directly eroding America’s startup culture. There should be as few government hurdles as possible between a person with a good idea and the transformation of that idea into a small business with the potential to become a high-growth gazelle. Adam Thierer writes in the book *Permissionless Innovation*, “... experimentation with new technologies and business models should generally be permitted by default. Unless a compelling case can be made that a new invention will bring serious harm to society, innovation should be allowed to continue unabated and problems, if they develop at all, can be addressed later.”<sup>10</sup>

One sector known for its permissionless innovation is the Internet economy. The Internet, writes George Mason University researcher Eli Dourado, “is a global platform on which college dropouts can try new, unorthodox methods without the need to secure authorization from anyone, and ... this freedom to experi-

ment has resulted in the flourishing of innovative online services that we have observed over the last decade.”<sup>11</sup> The hundreds of thousands of people developing iPad and iPhone apps for Apple know all about permissionless innovation.

But not all entrepreneurs are so lucky. Ideas fuel innovation, and innovation drives growth. And one big way government intersects with the world of ideas and innovation is through patent and copyright law. America’s founders thought that innovators needed to earn an economic return for their efforts and be protected temporarily from imitation. But over the years, copyright and patent law has evolved into cronyist protection of the revenue streams of powerful incumbent companies—a type of regulation that hampers innovation and entrepreneurship.

The 2014 paper “Intellectual Property Rights, the Pool of Knowledge, and Innovation” by Joseph Stiglitz outlines the problem: “We have shown that tighter intellectual property regimes, by reducing the newly available set of ideas from which others can draw and by increasing the extent of the enclosure of the knowledge commons, may lead to lower levels of innovation, and even lower levels of investment in innovation, as a result of the diminution in the size of the knowledge pool.”

Take copyright, for instance. At the nation’s birth, copyright was granted for a term of fourteen years with the option for one additional term of equal length. So the traditional American approach

is one of short copyright terms. Today, thanks to effective entertainment industry lobbying, copyright exists for the life of the author plus an additional 70 years. For corporate authors, it is 120 years.

Copyright is also applied haphazardly—boat-hull designs get protection, but not fashion designs—and retroactively, such as Mickey Mouse’s copyright extensions. As technology policy expert Derek Khanna has written, “While the current paradigm may work great for content producers, it doesn’t work great for the creation of other industries. There is enormous

**We're not running out of big ideas. But a U.S. economy afflicted by cronyist regulation and laws may be less and less able to convert those ideas into game-changing, job-creating businesses.**

potential for other value-added industries on top of existing media. For example, in a world where movies, television shows and books that were thirty-plus years old were available in the public domain, you would likely see new industries crop up to offer a new experience on top of this media.”<sup>12</sup> What jobs are not being created because of cronyist copyright law? What, to use the language of Frederic Bastiat, are the “unseen” costs to the American economy and workers?

Patents have not experienced the extreme length extension seen in copyright law—terms typically stand at twenty years—but that doesn’t mean current patent law is optimal for innovation. The strengthening of patent laws in some sectors, such as software, has prompted companies to pay billions to defensively

buy up patents. And no wonder. Patent trolling costs the U.S. economy some \$30 billion a year in litigation costs and licensing fees, an amount equal to 10 percent of total private research and development investment.<sup>13</sup>

Big tech companies sometimes sue each other over patents, such as those concerning smartphone technology. But where does this leave small firms? Economist Alex Tabarrok in *Launching the Innovation Renaissance* argues that “Small firms cannot afford to protect themselves with billion dollar patent arsenals. Patent arsenals protect big firms from small firms and from each other. They are a powerful weapon to squash small firms. Small firms are often the source of radical innovations, the type of innovation that threatens big firms, so the rise of the patent arsenal could truly decrease important innovation.”<sup>14</sup> And, again, it is those breakthrough, disruptive innovations that will create new industries and high-paying jobs.

As with copyright, current patent law is far from optimal for innovation. Should a patent for one-click shopping be treated the same as one for a new wonder drug with huge research and development costs? Tabarrok has argued that patent law should be stronger in business sectors where there are high “innovation-to-imitation costs” such as pharmaceuticals (where the first pill costs a billion dollars and the second fifty cents) and weaker where costs are lower, such as software. He suggests the following reform: Patents of, say, three, ten, and twenty years could be offered with the divisions based on industry—with software and business-method patents getting three years, pharmaceutical getting twenty years and others getting ten years. Or

patent terms could be based on evidence of sunk costs.

We’re not running out of big ideas. But a U.S. economy afflicted by cronyist regulation and laws may be less and less able to convert those ideas into game-changing, job-creating businesses. Other economic reforms, such as increased energy production and better schools, are necessary but insufficient if America’s innovative process is misfiring. The old Soviet Union had plenty of natural resources and an educated population. In his famous analysis of why the Soviet’s centrally planned economy failed, economist Joseph Berliner wrote, “It is only a slight exaggeration to assert that if the Soviet Union had succeeded in matching the technological attainment of the leading capitalist countries, there would have been no Gorbachev, no perestroika, and no retreat from socialism.”

But the Soviet economy lacked the Darwinian struggle for market share and profits that would have compelled industry to seek and adopt new innovation, either technological or operational. There was, Berliner explains, no “invisible foot” of competition where firms faced the threat of failure from new rivals if they failed to innovate. The U.S. isn’t the U.S.S.R., of course, but our economy could use a hard, competitive kick in the backside.



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# LABOR, TAX, & FISCAL REFORMS TO HELP PARENTS BALANCE WORK AND FAMILY

CARRIE LUKAS

The challenge of balancing work responsibilities and familial obligations is among the foremost concerns of American families. Today, seven in ten working-age American women are in the labor force, including more than six in ten women with children under age six, so the vast majority of parents are working parents.<sup>1</sup>

Politicians often suggest that government holds the key to helping working parents meet these competing demands. Before embracing a particular policy agenda, though, we should understand the nature of the challenges parents face—which vary significantly from family to family—and the tradeoffs that come with greater government intervention.

Most important, different families have different preferences about balancing work and family, and when greater flexibility and more options are what most people crave, one-size-fits-all government solutions won't move society in the right direction. Rather, policies that lead to greater opportunity, encourage the creation of a wider variety of work options, and reduce financial pressures will better help parents by enabling them to tailor their situations to their own unique preferences.

## **A Diversity of Preferences**

Most proposals offered by progressive politicians under the guise of helping men and women achieve a work-family balance are aimed at facilitating full-time work and the use of institutional daycare centers, and are predicated on the assumption that most employers offer inadequate family-leave benefits. The actual situations and preferences of many families are very different.

While a majority of mothers work for pay, research suggests that most would prefer to work part-time. For example, in March 2013, Pew Research released a report that assessed parents' attitudes toward work and family life.<sup>2</sup> It found that nearly half

**Different families have very different preferences about balancing work and family, and when greater flexibility and more options are what most people crave, one-size-fits-all government solutions won't move society in the right direction.**

(47 percent) of mothers view part-time work as ideal, compared to one-third (32 percent) who prefer full-time work. Reality differed from the ideal: Only 19 percent actually worked part-time, while 51 percent held full-time positions and 29 percent were unemployed.

Unsurprisingly, the desire for work was heavily correlated with economic need: Women struggling to make ends meet had a much stronger preference for full-time employment than women living comfortably. Forty-seven percent of women who said they didn't have enough for basic expenses want full-time work, compared to 31 percent of those who "live comfortably." This relationship also carried into marital status, with nearly half of single mothers (49 percent) preferring full-time work, compared to only 23 percent of married mothers.

The takeaway for policymakers is that different families have different goals when it comes to balancing work and parenting obligations. Policymakers have a variety of factors to consider when crafting policies related to supporting families, including how a proposal will impact a family's potential take-home pay, the ability of employers to offer flexible work options, the availability of work opportunities overall, and the very real challenges faced by lower-income mothers in particular.

Similarly, when it comes to childcare arrangements, most parents prefer to have a parent—specifically, the mother—directly provide care for children. Just 16 percent of mothers surveyed thought that having a mother working full-time was best for children, compared to 33 percent who thought it was best for the mother not to work at all.

The preference for parental care echoes earlier, more extensive research showing that most parents prefer to have children under the supervision of either a parent or another family member, and view institutional daycare as the least appealing option. When the research firm Public Agenda asked parents of children under age five about the best child-care arrangement during a child's earliest years, 70 percent thought it was best for one parent to be at home, while just 6 percent thought a quality daycare center was optimal. More than seven in ten parents agreed with the statement, "parents should only rely on a day care center when they have no other option."<sup>3</sup>

Most parents act on these preferences. According to the Census Bureau, in 2011, less than one-quarter of children under age five were in an organized daycare facility, and just 13 percent were at daycare centers. About 60 percent of children under five spent some time in an alternative childcare arrangement, but most of that care was provided by a relative (such as a grandparent or father). Even among employed mothers, daycare remains relatively rarely used, especially for the youngest children. Just 15.9 percent of babies (under age one) of working moms were in a daycare center in 2011.<sup>4</sup>

In Public Agenda's report, parents overwhelmingly understood and sympathized with those for whom daycare was a necessity. Those using daycare mostly were satisfied with their arrangement. Policymakers should be aware, though, that most parents prefer familial care for their children. Therefore, programs or policies that favor the use of institutional daycare centers over other arrange-

ments are contrary to parents' desires and what parents perceive as children's best interests.

Proponents of greater government involvement in providing greater parental support following the birth or adoption of a child should also know that, while the United States does not have a government program providing paid leave and does not mandate that employers provide paid leave, this does not mean that all new mothers lack economic support.

The Census Bureau studied the experience of women having their first child and found that roughly 70 percent of these women worked during pregnancy (a percentage that fell to slightly under 60 percent in the month preceding the birth), and that three months after the birth, 59 percent of the women who worked during pregnancy had returned to work; 79 percent were working by their child's first birthday.<sup>5</sup>

These working mothers made use of a variety of leave options following the birth of their children. For example, 56 percent of full-time working mothers reported using paid leave, 42 percent used unpaid leave, 10 percent used disability leave, 19 percent quit their job, while nearly 5 percent reported being let go. Part-time workers were more likely to quit (37 percent reported quitting their jobs) and they had less access to benefits: 20 percent used paid leave, 46 percent used unpaid leave, and just two percent had disability leave.<sup>6</sup>

The 2012 National Study of Employers (a survey of more than 1,100 employers, all with 50 employees or more) also found that most employers offer parental leave, and a majority offer at least

some paid leave. Larger employers surveyed (those with more than 1,000 employees) were most likely to offer some paid parental leave, with 68 percent of such companies providing this benefit. Even among the smallest companies in the survey (those with between 50-99 employees), a majority (54 percent) provided paid leave following the birth of a child.<sup>7</sup>

Policymakers should not conclude from these data that all American women enjoy sufficient leave time or have adequate pay-replacement following the birth of a child. They should instead take into account the fact that most employers voluntarily provide leave, in particular to full-time workers, and consider how any government mandate or government-administered paid leave program might disrupt current employment contracts and benefit packages. Rather than seeking to create one-size-fits-all leave policies for all employers and all working parents, policymakers ought to target their assistance to low-income families in need of support following a child's birth.

### **A Diversity of Options**

As they try to balance the needs of and their desire for paid work and family, parents—and mothers in particular—often face challenges that pull them in different directions: Some want to work more, some less. Some prefer to be at home with their youngest children, others to make use of childcare services. Government policy should not tip the balance in one direction or another, but create an environment in which parents are more likely to be able to fulfill their own objectives.

Unfortunately, most policies proposed under the guise of helping parents

achieve a work-family balance today focus on facilitating full-time work for mothers and the use of full-time, non-familial daycare arrangements. While those measures may benefit a subset of women, they won't help—and could harm—the many others who have different goals.

Consider the “Family and Medical Insurance Leave Act,” also known as the FAMILY Act, legislation to expand the Family and Medical Leave Act dramatically. Rather than the current mandate on larger employers to provide unpaid leave, the FAMILY Act would create a new federal entitlement program under which qualified workers would be entitled to 60 days of family and medical leave per year. When on leave, workers would receive two-thirds of their average pay from the federal government. This new entitlement would be funded with a dedicated payroll tax and administered through the Social Security Administration.

Proponents claim this program would inexpensively provide needed assistance to those lacking paid leave, and would particularly benefit women by providing paid maternity leave. But while it would assist some women, it would also disrupt the employment contracts of the majority of working Americans who currently have leave benefits. This new federal entitlement would encourage businesses currently providing paid leave programs—including more generous leave packages—to cease doing so. Companies and employees would also be less likely to seek mutually beneficial arrangements, such as part-time and work-from-home options, during periods of leave.

The costs would go far beyond the new payroll tax. Women would also face lower wages and constricted employment opportunities. Knowing that any worker facing a medical issue could take up to three months of paid leave creates a significant new risk for employers. While the federal government would pick up the direct costs of workers' wages during their absence, businesses would still have to identify and train a replacement, or shift work to remaining employees, which can be particularly difficult for very small businesses.

Given that women, particularly of child-bearing age, are more likely to take extended medical leave, employers may be reluctant to consider them for senior positions with significant responsibilities. This is particularly unfair to women who do not want or are unable to have children. The expectation that they may take off three months may unfairly hamper their career prospects.

These are not just theoretical risks. European countries offer women extensive paid-leave time, but European women pay a price in terms of workplace opportunities. They are far less likely than their American counterparts to be in managerial positions. Fourteen percent of American women workers are managers (compared to 15 percent of American men); just 5.9 percent of European women workers are (compared to 12.2 percent of European men).<sup>8</sup>

A one-size-fits-all paid leave program may sound like a panacea for parents, but it misses the target by failing to recognize the divergent needs of different families and the real costs of these benefits in terms of economic opportunity.

Similarly, progressive proposals to assist working parents with child-care rely on increasing funding for Head Start and Early Start, and bolstering other government support for child-care centers (such as through training and subsidies for child-care workers and through a child-care tax credit). What is notable is that the vast majority of this federal support goes to programs that benefit parents solely when they make use of their least preferred option: institutional child-care arrangements.

Such subsidies make it harder for parents to pursue their preferred option of family-based care. As the price of institutional child care goes down for the user, the value of the service provided by the stay-at-home parent or grandparent also goes down. For example, imagine if daycare was free for the user (all costs were borne by taxpayers). A working couple would be more reluctant to ask a grandparent to watch their baby. Even if all parties believe that family care is preferable, it is harder to justify asking for such help when they can costlessly enroll the baby in a child-care center.

Policymakers may want to reduce the burdens on parents, but they should strive to do so without tipping the balance of how parents choose to raise their children, and particularly not tip them away from the course they believe is best.

### **A Conservative Proposal to Advance Work-Family Balance**

Rather than government programs or mandates that attempt to assist parents pursuing specific types of arrangements, we should enact policies that

give parents the flexibility to choose the best options for their lives and families. That would include expanding workplace opportunities, giving them greater power to direct the use of government subsidies that are provided for their children, and improving their financial prospects across the board.

### *Facilitating Opportunity and Flexible Work Options*

The real key to helping parents achieve their vision of work-family balance is to encourage more job opportunities, allow greater workplace flexibility, and increase take-home pay for working families so they can spend their money as they see fit. Above all, this requires a healthy economy and expanding employment opportunities, which is why comprehensive tax reform, streamlining regulations, and reducing distorting government spending are critical. Policymakers' top priority should be to make it easier for employers to create jobs.

In addition, policymakers should seek to reform existing labor laws that discourage the kind of flexible work arrangements that would make it easier for parents to balance work and family. For example, it is past time to reform the Fair Labor Standards Act (FLSA), a law enacted during the Great Depression, when most jobs could be easily categorized and work typically was performed for certain hours during the day, at a specific place of employment.

Today, our work world has transformed, which makes it a challenge for businesses to apply many of FLSA's outdated concepts. For example, FLSA requires that non-exempt employees receive a minimum wage (currently \$7.25) and time-

and-a-half for time worked in excess of 40 hours per week. To comply, employers must carefully monitor how much time their employees work. Exempt workers (generally white-collar professionals) who receive a set salary rather than an hourly wage operate differently and do not necessarily accrue overtime.

So who can companies safely put on salary? The Department of Labor stipulates that exempt employees' work must involve the "consistent exercise of discretion and judgment." Today, employers are struggling with such questions as how this applies to accountants, computer technicians, and engineers, whose valuable technical skills command far more than minimum wage, but whose early work is often closely supervised and focused on following complicated procedures and protocols. Are they exercising discretion and judgment?

Employers face an equally difficult challenge in deciding what constitutes "work." Does checking e-mail from home count? What about other time spent on company-owned computers or other electronic devices? As a result, working from home can open a Pandora's box of questions, since at-home workers typically blur the lines of work and home life. Such flexibility can be a boon to parents, but if at-home work creates major administrative hassles—and worse, potential liability exposure—many companies simply default to disallowing it.

Congress needs to reform FLSA. Instead of exempting classes of workers from the law, it ought to instruct specifically which classes of employees must be

hourly and subject to the regulations. At the same time, they should give employees additional flexibility. Rather than requiring them to receive 150 percent of their pay, employees should have the option to receive time-and-a-half off from work for each hour of overtime.

### *Giving Parents Control of Resources*

Subsidies for specific families or programs and benefits that help only a subset of parents distort the choices parents make as well as their options and opportunities. Policymakers should instead seek to alleviate parents' financial burdens and return resources spent by the government on children to parents to spend as they see fit.

For example, the Government Accountability Office estimates that in 2012 the federal government administered 45 programs related to early learning and child care, which cost taxpayers roughly \$14.2 billion per year. In addition, there are five tax provisions to support individual spending on child-care services, which reduce tax receipts by approximately \$3.1 billion annually.<sup>9</sup> These resources solely benefit families using formal, paid child-care arrangements—overwhelmingly center-based care. Rather than favoring those choices, policymakers ought to make that support available to all families with children under age five, and give them greater power to pick the right child-care arrangements for their children. Since many of the current programs, like Head Start, are geared to assist low-income women, a new mechanism for support should be allocated on a means-based scale to help those with lower incomes most.

Policymakers should also explore increasing the child tax credit more broadly to alleviate the burdens on parents. The Urban Institute reports that: “tax expenditures on children were just 8 percent of the approximately \$1.2 trillion in individual and corporate tax expenditures identified by the Office of Management and Budget (OMB) in 2012.”<sup>10</sup> This suggests that other investments that taxpayers make—whether in their homes or in savings vehicles—receive better tax treatment than raising children.

Economists (such as Robert Stein in his chapter in this volume) persuasively argue that parents are overtaxed compared to their investment in and contribution to society, and the child tax credit should be enlarged to compensate for this inequity. Congress ought to consolidate existing child-centered tax credits and spending, and use those savings to provide added tax relief for parents, particularly to the parents of the youngest children.

This would accomplish numerous important policy goals by alleviating disincentives for childbearing, ending the current government bias against stay-at-home parents, and simplifying the tax code. It would also reduce the need for additional government entitlement programs for paid-leave, which would primarily benefit the subset of parents who are both working and currently lack leave benefits.

Of course, child care is just a small slice of what the federal government spends on children. The Urban Institute details \$348 billion in federal outlays, and \$99 billion in tax reductions that were tar-

geted toward children in 2012. Together, those amount to nearly \$6,000 per child. There may be reasons for some of this money to be allocated by the government to directly support certain populations of children (such as those with disabilities) and for programs that provide services (rather than financial support) to children and families. Policymakers should nonetheless consider how to consolidate and eliminate inefficient, redundant programs, and return those resources to parents to use as they see fit.

#### *Targeting Paid Leave Assistance to Those in Need*

On the state and federal level, numerous programs provide income support or other assistance to families with low-incomes, particularly families with young children.<sup>11</sup> Most families with children living below the poverty line lack jobs. In fact, in 2012, 74 percent of households with children under the poverty line were home to no full-time worker.<sup>12</sup> That means that programs like the FAMILY Act—which require that one must have worked for pay within the past year to be eligible for any benefits—would do little to help this population. Moreover, any government initiative that raises the cost of employment (and therefore makes it less likely that parents will find job opportunities) is counterproductive for these families.

Policymakers could instead make the child credit bigger for low-income families in the year that a child is born, in order to cover lost wages during time spent out of the workforce. Importantly, such a credit would not affect employers’ expectations about the benefiting workers’ propensity to take leave or be absent for long periods of time, and would not distort

labor-force participation or childbearing, since the credit would be available only in the year of a child's birth. The IRS should make it possible for new parents to file tax returns or a tax document to request a refund at the time of the child's birth (rather than having to wait for the following tax year).

All parents face the challenge of balancing the need to care for children with other responsibilities and desires. People have very different preferences and goals for meeting these challenges. Policymakers therefore ought to be cautious in pushing

one-size-fits-all government mandates or creating programs and policies that favor one set of choices over another.

Instead, policymakers should create an environment in which parents can pursue their vision for happiness and raise their children as they see fit, and target assistance to those truly in need. This begins with pursuing an agenda to encourage greater economic growth and job creation, and includes consolidating government spending programs and returning those resources to parents.



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# PRO-FAMILY POLICIES TO STRENGTHEN MARRIAGE AND GIVE KIDS A BETTER SHOT AT THE AMERICAN DREAM

W. BRADFORD WILCOX

One would never guess it from the marital misadventures and disappointments of the powerful and privileged—from ex-governors Eliot Spitzer (D-NY) and Mark Sanford (R-SC) to Hollywood stars Gwyneth Paltrow and Kim Kardashian—regularly chronicled on the pages of magazines like *People* and *OK!*. But in the real world, marriage is doing comparatively well in the privileged urban and suburban precincts of America, from

bedrock of Middle America: that is, small towns, rural communities, and outer suburbs across America. From Danville, Virginia, to Pine Bluff, Arkansas, to Hillsboro, Ohio, divorce is high and nonmarital childbearing is on the rise.

Middle Americans are defined here as Americans with a high-school degree and maybe an associate's degree or some college but with no college degree.

The retreat from marriage in Middle America means that the United States is in danger of becoming a separate and unequal nation when it comes to marriage, where the well-heeled have the material and cultural means to marry and stay married, and few other Americans can make good on their dreams of a happy and stable family life built around marriage.

Cleveland Park in Washington, D.C., to Los Altos, California, to Southlake, Texas. Indeed, among college-educated and more affluent Americans, divorce is down and nonmarital childbearing is low.

In the nation's poorest communities, by contrast, marriage is in full retreat, and has been declining since the 1970s. What's new, however, is that the retreat from marriage is now spreading into the

They are neither upscale nor poor. They make up a majority of American adults, and of young adults. About half of young adults (aged 25–34) have graduated from high school without getting a four-year-college degree.<sup>1</sup> Given their size in the population, and the central role that they have played in the American experiment, the growing fragility of family life in Middle America is cause for concern.

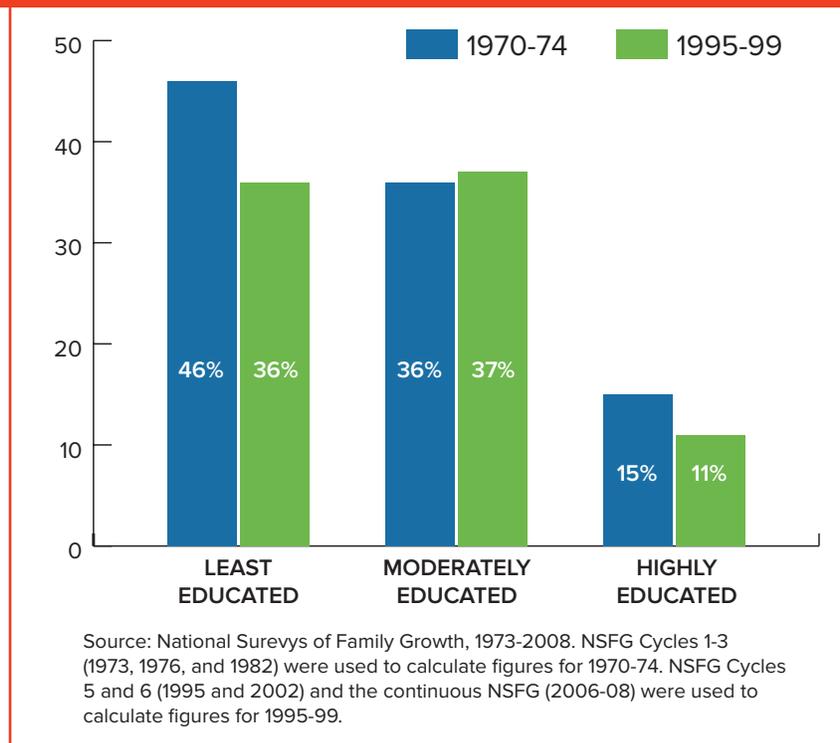
The retreat from marriage in Middle America means that the United States is in danger of becoming a separate and unequal nation when it comes to marriage, where the well-heeled have the material and cultural means to marry and stay married, and few other Americans can make good on their dreams of a happy and stable family life built around marriage. The growing divide in marriage and family life is problematic because the vast majority of Americans, including Middle Americans, still aspire to marriage.<sup>2</sup> It's also problematic because marriage remains one of the strongest engines of the American dream and one of the most important sources of social solidarity in a nation that otherwise prizes individual liberty.

### The Retreat from Marriage in Middle America

The trends below in divorce, marital quality, nonmarital childbearing, and family stability tell the basic story of what is happening to marriage in America.

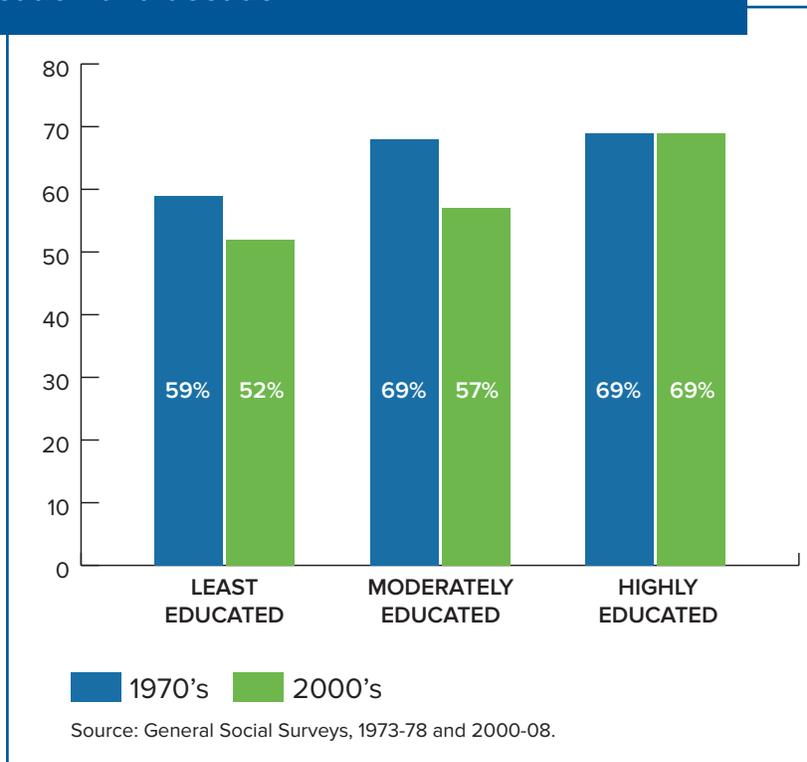
Figure 1 indicates that the odds that a marriage will end in divorce or separation within ten years of the wedding remain high among the moderately and least educated Americans but has fallen to about one in ten among highly educated Americans. By contrast, the divorce rate is more than three times as high among Americans who do not have a college degree (at about 37 percent). Clearly, divorce is much more common among Americans from both poor and Middle American households.

Figure 1. Percent chance of divorce or separation within 10 years of first marriage, 15–44 year-old women, by education and year of marriage<sup>3</sup>



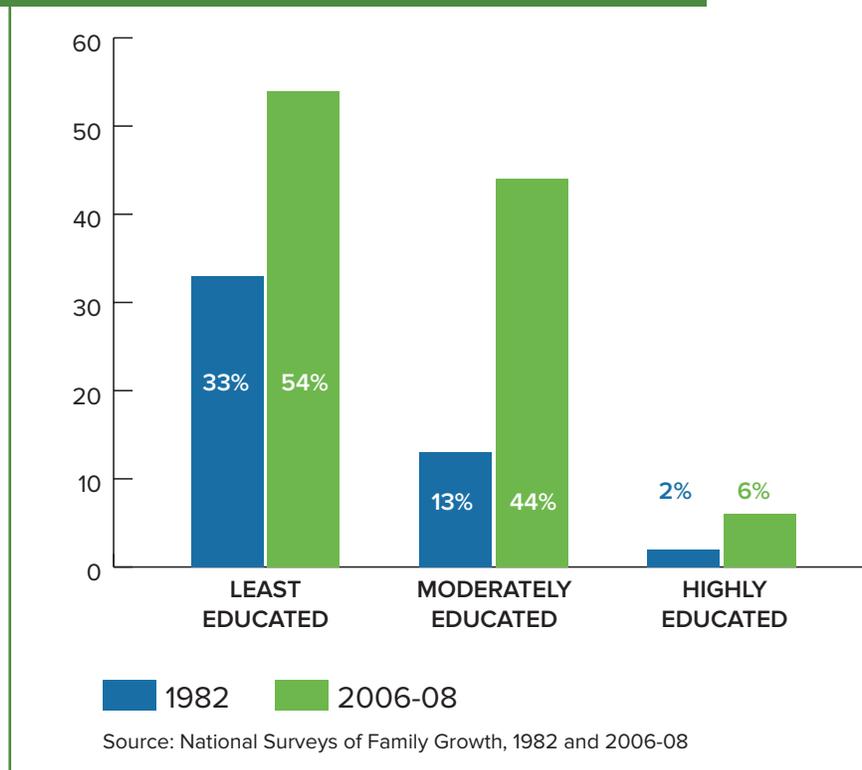
And as Figure 2 indicates, an educational divide has opened up in marital happiness as well. In the 1970s, moderately educated Americans resembled their highly educated peers in the likelihood that they reported their marriages were “very happy,” and the gap between the least educated and the highly educated was only 10 percentage points. Since then, moderately educated Americans have seen their marital happiness decline, to the point where they are now more likely to report marital happiness trends that parallel those of the least educated; the gap in happiness between the least and highly educated Americans has also grown to 17 percentage points. By contrast, 69 percent of highly educated Americans continue to report that they are “very happy” in their marriages.

**Figure 2. Percentage in “very happy” marriage, 18–60 year-old married, by education and decade**



One of the most dramatic shifts in Middle American family life is apparent in Figure 3, which details trends in nonmarital childbearing. In 1982, nonmarital childbearing was comparatively rare, and trends among the moderately educated (13 percent had births out of wedlock) were closer to the highly educated trend (2 percent) than they were to the trend among the least educated (33 percent). But now, about one in two babies born to mothers without college degrees happen outside of marriage, and the nonmarital childbearing trend among the moderately educated (44 percent) more closely resembles the trend among the least educated (54 percent) than it does the trend among the highly educated (6 percent). So, having kids outside of wedlock remains the clear exception among college-educated women but is close to becoming the norm among Middle American women.

Figure 3. Percentage of births to never-married women 15–44-years-old, by Education and Year

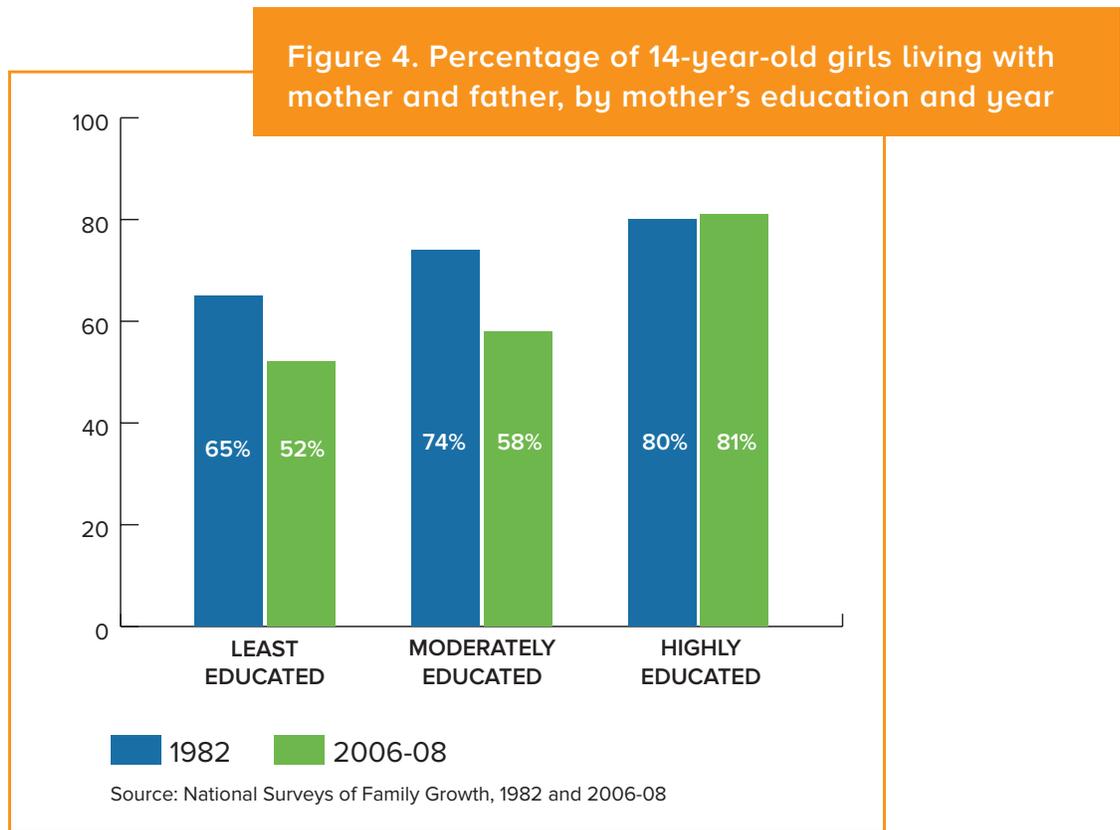


The recent growth in nonmarital childbearing has been driven by cohabiting births, which now constitute a majority of births to unwed mothers. Because cohabiting families are so unstable, the vast majority of children born to these unions will experience both family instability and single parenthood.<sup>4</sup>

Family sociologists are divided about many things but one point of scholarly consensus has emerged in recent years: Children are most likely to thrive when they are raised by two, stably partnered parents.

Family sociologists are divided about many things but one point of scholarly consensus has emerged in recent years: Children are most likely to thrive when they are raised by two, stably partnered parents.<sup>5</sup> Because highly educated Americans are more likely to have their children in marriage and to stay married, they are also much more likely to deliver this kind of stability to their children, as Figure 4 indicates. In particular, about 80 percent of fourteen-year-old girls from college-educated homes are living with their two biological parents now, a trend that has remained fairly constant since the 1980s. By contrast, as the figure makes clear, there has been

a marked decline in family stability for children from less educated homes. Once again, the trend in family stability for Middle Americans now comes closer to paralleling the trend among the least educated American families.



The United States, then, is at something of a tipping point where marriage in Middle America is on the verge of becoming the exception to the norm—at least when it comes to grounding children's experience

in boosting children's odds of making it in America. For individual children, we know that boys are about twice as likely to run afoul of the criminal justice system,<sup>6</sup> girls are about three times as

likely to become pregnant as teenagers,<sup>7</sup> and young men and women are about one-third less likely to graduate from college when they come from non-intact families.<sup>8</sup> These patterns help explain why children from intact, married families are more likely to realize the American dream, understood in terms of enjoying increased economic mobility or the same relative economic status as their parents.<sup>9</sup>

## Strong and stable marriages play a crucial role in boosting children's odds of making it in America.

of being born into and raised in an intact, married family. Public policy, civic initiatives, and cultural efforts ought to be redoubled to prevent Middle America from passing this tipping point.

Why? Among other things, strong and stable marriages play a crucial role

in boosting children's odds of making it in America. For individual children, we know that boys are about twice as likely to run afoul of the criminal justice system,<sup>6</sup> girls are about three times as likely to become pregnant as teenagers,<sup>7</sup> and young men and women are about one-third less likely to graduate from college when they come from non-intact families.<sup>8</sup> These patterns help explain why children from intact, married families are more likely to realize the American dream, understood in terms of enjoying increased economic mobility or the same relative economic status as their parents.<sup>9</sup>

## Conservatives have stressed the importance of changes in culture and public policy while liberals have stressed the importance of changes in the economy.<sup>12</sup> And both are right.

Equally important, new research from Harvard economist Raj Chetty and his colleagues suggests that family structure also plays a major role in determining which communities are most likely to foster the American dream. In looking at a range of variables that predicted rags-to-riches mobility in different regions across the nation, Chetty and his colleagues found that when it comes to mobility, “the strongest and most robust predictor is the fraction of children with single parents.”<sup>10</sup> In other words, children from both two-parent and single-parent families are more likely to experience economic mobility when they hail from communities with a lot of two-parent families. This growing body of research has led many scholars, including Ron Haskins, co-director of Brookings’ Center on Children and Families, to conclude, as he told the *Washington Post*, that “We are not going to have an effective solution to the growing inequality and poverty in the U.S. unless we can do something about family structure.”<sup>11</sup>

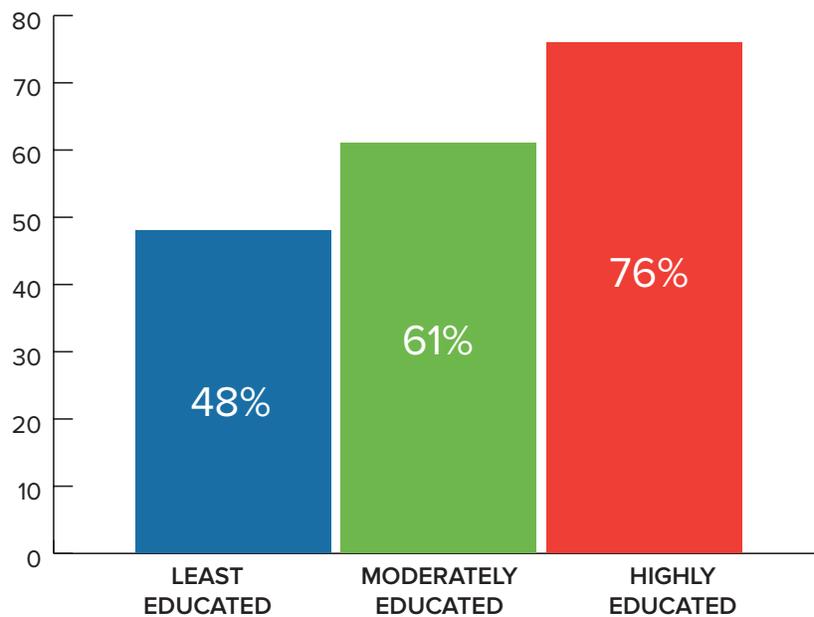
### **Why is Marriage in Retreat?**

In seeking to explain why marriage is in retreat, conservatives have stressed the importance of changes in culture and public policy while liberals have stressed the importance of changes in the economy.<sup>12</sup> And both are right.

When it comes to culture, marriage still remains the ideal for the vast majority of Americans. Most Americans are married or aspire to marriage. A recent report, *Knot Yet: The Benefits and Costs of Marriage in America*, found that more than 80 percent of young adults deemed marriage “important” for their life plans.<sup>13</sup> But beneath the near universal support for marriage in the abstract lurk important educational differences in attitudes toward teenage childbearing, divorce, and single parenthood: all behaviors that depart from the ideal of lifelong marriage that ordinary Americans continue to hold. Now, less-educated Americans—including Middle Americans—are less likely to identify with many of the marriage-minded norms that help steer adolescents, young adults, and middle-aged adults from highly educated homes in the direction of marriage, and away from divorce and nonmarital childbearing.<sup>14</sup>

Take, for instance, teenage views of nonmarital childbearing. As Figure 5 indicates, adolescents from moderately and the least-educated homes are much less likely to report that they would be “embarrassed” if they got (or got someone) pregnant. Specifically, 76 percent of adolescents from college-educated homes indicate that they would be embarrassed by having a teenage pregnancy, compared to just 61 percent of adolescents from moderately educated households and 48 percent of adolescents from the least educated homes. Divergent orientations toward childbearing, divorce, and single parenthood may help explain why the retreat from marriage is more pronounced in Middle America and in poor communities.

Figure 5. Percentage of adolescents who would be embarrassed if they got (or got someone) pregnant



Source: National Longitudinal Study of Adolescent Health, Wave 1 (1994-95).

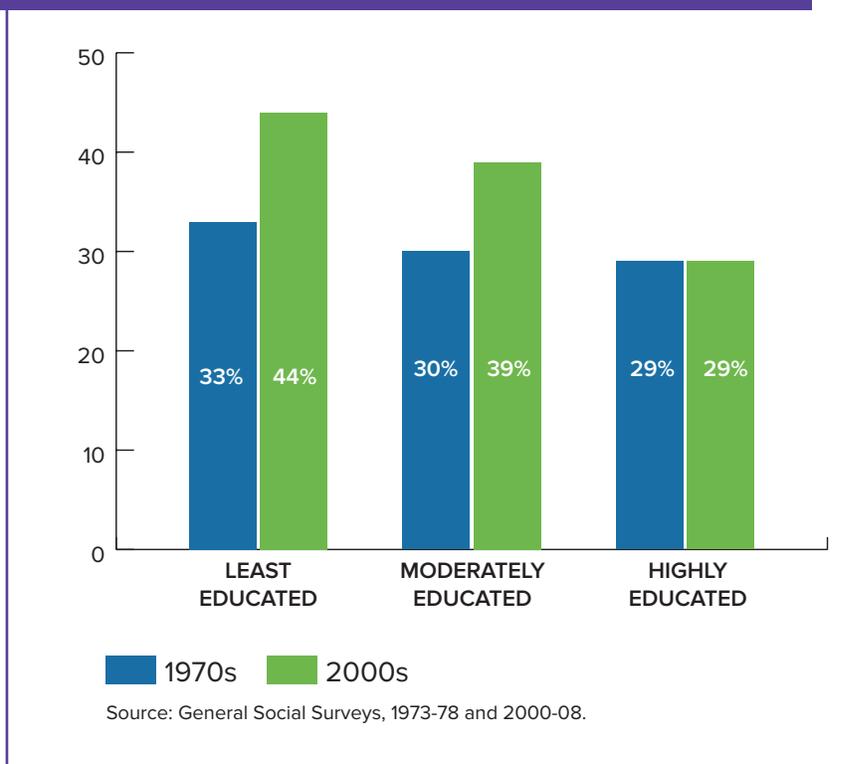
Poorly designed public policies have also had a hand in the uneven retreat from marriage in the United States. Although scholars disagree about the extent to which welfare policy has undercut marriage, many scholars would acknowledge that welfare benefits that have penalized marriage or made single parenthood more affordable or acceptable have played at least some role in fueling increases in nonmarital childbearing and single parenthood among the poor.<sup>15</sup> Some studies find that adolescent girls who grew up in a household supported by welfare are more likely to have a child outside of wedlock.<sup>16</sup> Research also suggests that the generosity of welfare benefits is linked to higher rates of nonmarital childbearing, especially in more recent years.<sup>17</sup> The broader lesson here is that public policies that reward single par-

enthood or penalize marriage—as do many means-tested tax and transfer policies, including the Affordable Care Act, that now touch many lower-income and Middle Americans<sup>18</sup>—may have played and may continue to play a role in accounting for the growing marriage divide in America between the college-educated and everyone else, especially the poor.

Finally, when it comes to the economy, declines in male labor-force participation, which have been concentrated among less-educated men, also appear to have played a role in fueling the retreat from marriage in Middle America and among the poor. Since the 1970s, spells of unemployment and underemployment have been much more common among men without college degrees than they have been for men

with college degrees. Figure 6 indicates, for instance, that spells of unemployment rose from the 1970s to the 2000s (before the Great Recession) for men without college degrees, but not for men with college degrees. When it comes to marriage, this matters because men who are not stably employed are much less likely to get married and to remain married.<sup>19</sup> Thus, shifts in the economy since the 1970s, which have increased employment instability and unemployment among less-educated men, also may have played some role in driving the retreat from marriage among Middle Americans and the poor.

**Figure 6. Percentage of 25–60-year-old men unemployed at some point over the last 10 years, by education and decade**



Shifts since the 1970s in culture, public policy, and the economy have therefore all to weaken the normative, legal, and economic foundations of married life in the United States. Moreover, these shifts had to operate in tandem to have the stratified effects they are now having. It's no accident, for instance, that the Great Depression did not have a big impact on family stability during the 1930s: There was no normative acceptance of wide-

spread divorce or nonmarital childbearing during that era that would have allowed family instability to trend sharply upwards. At the same time, it's no accident that the retreat from marriage has hit the poor and Middle Americans hardest since the 1970s: These two groups have been affected much more by the recent changes in public policy, work, and—possibly—the culture that have undercut marriage.

## Considering the checkered role that public policy has recently played vis-à-vis marriage, one paramount rule for crafting new public policy solutions should be: “first, do no harm” to marriage and the family.

### **First, Do No Harm**

Given the varied roots of the marriage problem in America, no one public policy is likely to make a decisive difference in renewing the health of marriage and family life in America. There is no silver bullet here; instead, public policies should target the range of economic, legal, and cultural forces now eroding marriage and family life in the United States. Moreover, considering the checkered role that public policy has recently played vis-à-vis marriage, one paramount rule for crafting new public policy solutions should be: “first, do no harm” to marriage and the family.

Therefore, the first step policymakers should take is to end the marriage penalty often associated with means-tested public benefits. Many of the nation’s tax and transfer policies—from Medicaid to food stamps—end up penalizing marriage, albeit often unintentionally. Because the tax and transfer system in the United States is means-tested, lower-income families with children can see their benefits reduced or eliminated when another earner, including the father of the child or children, is officially brought into the household through marriage.<sup>21</sup> Three options for reform would go a substantial way to eliminating some of the marriage penalties associated with the nation’s social welfare system.

First, the Earned Income Tax Credit (EITC) program could be transformed. Instead of depending on household size and household earnings—which creates the poten-

tial for a marriage penalty—it could become a wage subsidy for individual low earners. Someone making a low wage could then marry someone with children (or expecting a child) without incurring a major income penalty.<sup>22</sup> The subsidy would also reinforce the norm that work should be rewarded, an important goal given recent declines in male labor force participation and, hence, male marriageability.

Second, for other means-tested tax and transfer policies targeting low- and moderate-income families, couples could receive a refundable tax credit for the amount of money that they lose by marrying. This credit could be limited to the first five years of marriage to reduce its public cost. The Administration for Children and Families at the Department of Health and Human Services and the Urban Institute has developed a “Marriage Calculator” that could be used for this purpose.<sup>23</sup> This credit would be costly, but its costs would be offset to some extent if it fostered stable married families, which are much less costly to federal and state governments than are single-parent families.<sup>24</sup>

Third, the marriage penalty associated with Medicaid should be eliminated. Today, a majority of nonmarital births are to cohabiting couples, most of whom are lower-income. Because most of these couples rely upon Medicaid to cover the costs of childbirth, Medicaid eligibility rules may play an important role in their deci-

sion making about marriage.<sup>25</sup> We need more research to determine if Medicaid is playing a major negative role in decisions about marriage among lower-income couples. If there is evidence that Medicaid is discouraging marriage among substantial numbers of lower-income families, the federal government should move quickly to end any Medicaid-related marriage penalty.

Beyond eliminating marriage penalties, policymakers should also lift the unique economic burdens placed on parents by some tax and spending policies. The existing child tax credit, dependent exemption, and childcare deduction should be consolidated and expanded to \$4,000, as economist Robert Stein argues elsewhere in this volume.<sup>26</sup> This credit should be applied to both income and payroll taxes so as not to discriminate against low- and moderate-income families with minimal or no federal income tax burden. It would also replace the current Child and Dependent Care Tax Credit, which serves families where both parents work outside of the home, thereby discriminating against families with a stay-at-home parent. A \$4,000 per-child tax credit would provide real financial relief to Middle American families struggling to make ends meet. Such a credit would also serve as a vehicle for expanding families' to care for their children as they see fit.

Policymakers should also think differently about job training. The federal government devotes substantial resources and attention to four-year colleges and universities.<sup>27</sup> Yet most Americans do not receive a four-year college degree. When it comes to education, federal and state governments should focus more attention and financing on vocational education and apprenticeships that prepare young

(and middle-aged) adults for careers in information technology, health services, and other promising fields. South Carolina, for instance, has done an excellent job in establishing an apprenticeship program that connects young adults with its burgeoning manufacturing sector.<sup>28</sup> And career academies, which provide vocational education in high schools across the United States in partnership with local employers, have achieved substantial success in boosting the income and marriage rates of youth from lower-income communities.<sup>29</sup> As economist Robert Lerman has noted, approaches like these seem to be particularly attractive to young men who do not find academic classrooms appealing, and could be easily expanded at a fraction of the amount of money now spent on college loans by the federal government.<sup>30</sup> Educational efforts like these could play a major role in strengthening the marriageability of men from poor and Middle American communities across the United States, and in renewing the economic foundations of family life in Middle America.

Finally, public policy could go some distance toward promoting healthy choices. As Ron Haskins and Isabel Sawhill of the Brookings Institution have noted, any change in public policy is not likely to have a dramatic effect on marriage “unless there is also a change in the wider culture.”<sup>31</sup> To that end, they propose that Congress help to fund a social marketing campaign that would encourage “the success sequence” among young adults. This sequence runs as follows: “finish school, get a job, marry, and have children—in that order.” Haskins and Sawhill point out that young adults who follow this sequence are highly unlikely to fall into poverty,

and likely to make it into the middle class or higher. They also note that a substantial body of research suggests that public campaigns like this—on topics ranging from smoking to drunken driving—have proven to be successful in changing behavior in the public at large.<sup>32</sup> Such efforts should also help convey to the general public that children are most likely to thrive when they are raised in an intact, healthy marriage.<sup>33</sup> A campaign of this nature, which would also attract a lot of free publicity from the press, could play some role in shoring up the cultural foundations of marriage and family life in Middle American and poor communities across the nation.

The cultural, economic, and policy challenges facing marriage in America—especially in low- and middle-income communities—are substantial. None of

the policies mentioned above are likely to inaugurate a dramatic reversal of the retreat from marriage that has marked American life over the last 40 years. But if they could help to halt this retreat, both by strengthening the economic foundations of family life in Middle America, and by helping to turn the culture in a different direction, that would be a major achievement. The alternative is passive acceptance of the growing marriage divide in American life, a divide that threatens to make a majority of men, women, and children in this great nation alienated from one of the key pillars of the American dream, liberty, and the pursuit of happiness: namely, a stable and happy family life. That alternative should be unacceptable to all who seek to sustain the exceptional American experiment in ordered liberty.



W. Bradford Wilcox, a professor of sociology at the University of Virginia, directs the Home Economics Project at the American Enterprise Institute and the Institute for Family Studies. Portions of this essay are adapted from W. Bradford Wilcox, *When Marriage Disappears: The Retreat from Marriage in Middle America* (Charlottesville, VA: National Marriage Project and Institute for American Values, 2010).

CONSERVATISM SHOULD BE  
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*Ramesh Pennuru*

CONCLUSION

# RECOVERING THE WISDOM OF THE CONSTITUTION

RAMESH PONNURU



The plunge in Americans' confidence in their government over the last few decades is one of those social facts so large that it must have many causes.<sup>1</sup> Surely one of them is that our government so often seems to have grown unwieldy, ineffective, and unaccountable.

Joint federal-state programs grow seemingly inexorably, unable to be reformed no matter how disappointing their results. The federal government inserts itself into every nook and cranny of American life, with no decision too local, or trivial, to escape its attention. Federal courts micromanage institutions—schools, prisons—and make policy judgments traditionally confined to legislatures on issue after issue. Companies face multiple and sometimes conflicting regulators in an atmosphere of pervasive uncertainty. Presidential orders revise laws without a vote of Congress. Agencies combine judicial, legislative, and executive powers while staying far removed from the control of voters.

The result of all of this is nothing so coherent as socialism, as constitutional scholar Michael Greve has remarked: Socialism implies a plan.<sup>2</sup> Instead

much of government becomes a series of shakedowns, special-interest deals, and programs that continue from inertia. This type of government can weaken the economy and civil society, but it cannot reach the lofty ambitions politicians set for it. And it is a far cry from the limited, deliberative government of divided powers that the Founders envisioned.

Take, for expensive example, the growth of Medicaid, a program that has repeatedly brought about fiscal crises for state governments without yielding much in the way of health benefits for its poor recipients. Medicaid allows state governments, within limits, to add people and services to the program, with the federal government picking up at least half the cost. In good times state officials can offer their voters two or more dollars of benefits for a dollar of taxes. In lean years the program is hard to pare back because state officials have to take away two or more dollars of benefits to save a dollar.

So the program expands: States exploit one another's taxpayers, who end up paying for more spending than they would if either the federal government or the states had full responsibility for

## The federal courts have an important role in defending constitutional norms. The Supreme Court was right, for example, to set an outer limit to federal power by holding that Congress cannot simply make it illegal to refuse to purchase health insurance.

funding and running the program. And federal and state officials blame each other for the frustrating results. We get more government, and worse government.

There can be no going back to the “original Constitution,” as some conservatives carelessly say, and we should not want to do that: the Reconstruction Amendments added to the document’s excellence and remedied its defects, and we should honor them. Nor should we insist on returning to the policies of some year of the distant past. Our Constitution would not deserve much respect if it were so impractical as to prevent government from adapting to changing circumstances. But we can avoid these mistakes while still appreciating the considerable wisdom in the Founders’ design, and particularly in the structural limits it placed on governmental power. Recovering that wisdom is no mere exercise in nostalgia, but would yield practical benefits.

The political culture of recent decades has encouraged us to look to the courts to effect that recovery. Conservatives have invested a lot of hope in the courts: in the idea that appointing the right justices and making the right legal arguments will reset our constitutional trajectory. They are right, to a point: The federal courts have an important

role in defending constitutional norms. The Supreme Court was right, for example, to set an outer limit to federal power by holding that Congress cannot simply make it illegal to refuse to purchase health insurance.

The task of recovery is too large to be plausibly entrusted in its entirety to the courts. They cannot set right all that is awry with contemporary government. They cannot do that for reasons of politics, of prudence, of institutional capacity, and of judicial restraint. The courts, for example, rightly treat the balance of power between the executive and legislative branches on matters of war and peace as a political question. Because our political culture thinks of the courts as the arbiters of all things constitutional, unfortunately, it tends to treat any governmental practice that the courts have left in place as constitutionally legitimate.

The rise of the Tea Party movement has in recent years begun to counteract this tendency. That movement is in part a revival of popular interest in constitutionalism. Instead of treating the Constitution as the property of lawyers and judges, it proposes that legislators, and even citizen-activists, have an independent duty to evaluate the constitutionality of legislation. Moved by this senti-

**The task of recovery is too large to be plausibly entrusted in its entirety to the courts.**

ment, the U.S. House of Representatives now requires legislation to identify its constitutional basis.

The Tea Party has also implicitly resisted the modern tendency to treat the rights protections spelled out in the Constitution's amendments, rather than the structural provisions in its main body, as the most important element of our constitutional system. The individual mandate to buy health insurance ran into trouble not because it violated some specific prohibition in the Bill of Rights, but because it could not be justified as "necessary and proper" to execute the Article I powers of Congress.<sup>3</sup> We can infer from the few and limited instances in which the Constitution authorizes Congress to commandeer individuals that such commandeering outside those contexts is presumptively improper.

The constitutionalist turn in conservative politics is so new—and politics so busy and distracting an enterprise—that its philosophical and practical implications remain to be worked through. A few of those implications, however, are clear enough.

*This constitutionalism should be political rather than legal.* Constitutional advocacy in the courts is tightly bound up with Supreme Court precedents. The Court gives those precedents great weight because of concerns about both legal stability and institutional authority. A legislative argument about the Constitution need not be constrained to the same degree. A conscientious legislator will give precedents some weight, certainly: He will want to take into account the likelihood that a bill he is considering supporting will be struck down by the courts; he should have a healthy regard

for stability; and he should be willing to be persuaded by the Supreme Court's analysis of a constitutional question.<sup>4</sup>

He may from time to time, however, decide that the Court has gotten it wrong. He may decide, for example, to oppose a bill that he expects the courts would uphold, on the ground that it does not accord with his own understanding of the Constitution. Many conservative legislators have taken exactly this tack with respect to gun regulations: For decades they called some of these regulations unconstitutional, even before the Supreme Court finally concluded that the Second Amendment does indeed protect an individual right.<sup>5</sup>

The conscientious legislator may even act on constitutional reasons that he does not wish to move the courts. Let's say a legislator were considering a health-care bill along the lines of Obamacare, but a version that lacked a specific objectionable provision such as the individual mandate. The legislator might oppose it because he thought it too expensive, or unlikely to work, or other reasons of that nature. He might also, though, oppose it for exceeding the legitimate powers of the federal government.

The argument would be that the Constitution establishes a presumption against federal activity that can be defeated only by strong considerations. The federal government is defined as one of limited powers, and the Tenth Amendment reiterates that the states and the people retain all others. To judge a proposal for a federal program against the Constitution will therefore require answering such questions as whether the states and the people could serve the purpose of that program

## In rejecting a judicial monopoly on constitutional interpretation, the constitutionalist also gives up the fantasy that any particular institutional arrangement can guarantee perfect fidelity to the Constitution.

without federal involvement. In some cases it may be that federal overreach is so gross that the courts should step in. In other cases, though, the question will turn on quintessentially legislative determinations: Is the law necessary? Are its means well proportioned to its ends? Are there better ways of achieving those ends?

*Political constitutionalism therefore involves a less restrictive form of reasoning than legal constitutionalism does.* The constitutionalist legislator, or citizen, will not always need to find a clearly articulable rule to decide that this proposal goes too far while that one is appropriate as a constitutional matter—the sort of legal rule we would want the courts to apply in striking down legislation. He will be able to draw on a wider range of considerations than the justices: He might, for example, decide that our hypothetical health-care law would warp the national character by making the federal government’s decisions too important to citizens’ health.

*A political constitutionalism should be practical and incrementalist rather than apocalyptic.* In rejecting a judicial monopoly on constitutional interpretation, the constitutionalist also gives up the fantasy that any particular institutional arrangement can guarantee perfect fidelity to the Constitution. If he sees laws and programs that do not fit with our constitutional commands and ideals, he will not vainly demand that they

all be abolished straightaway. Instead he will move patiently and intelligently to bring government closer to its proper bounds. If he finds himself unable to abolish a program he thinks a poor fit for our constitutional order, he will try to reform it to render it less obnoxious or destructive.

*A political constitutionalism should be coalition-minded rather than dogmatic.* Different conservatives will reach different judgments about particular laws and programs. Some conservatives will take a more Jeffersonian view, some a more Hamiltonian one, about the proper scope of the federal government. Other disagreements will concern what is achievable in the near term, and how to go about achieving it. Conservatives should not treat the existence of these disagreements as a scandal. Conservatism should be home to everyone who takes seriously the task of strengthening the constitutional structure of a limited, accountable government that serves rather than masters civil society.

*A political constitutionalism must seek to appeal to the public.* It must do this in two senses. First, it must involve the public in constitutional deliberation. It is a deep public commitment to the Constitution, more than any institutional arrangement, that is its chief guarantor. We had a more modest federal government for most of our history for many reasons, but it may be safely said that a political culture skeptical of federal

power was a more important factor than the exertions of the Supreme Court.

At key moments political leaders have made arguments to rally the people to the defense of our founding ideals. Abraham Lincoln explained that the logic of the Constitution and Declaration of Independence was incompatible with slavery. Closer to our own day, Ronald Reagan revived the language of constitutionalism, referring to the Founders more than his six predecessors combined. In our time, conservatives have to make the case to the public that our constitutional structure has eroded, that its erosion has baleful effects, and that we can do something about it.

Part of making that case is drawing out the constitutional dimension of everyday policy disputes. The REINS Act, requiring Congress to vote on major regulations before they can take effect, is not just a way to promote economic growth, although it is that; it is a way of reviving the separation of powers. Replacing much of Medicaid with tax credits that enable beneficiaries to join the regular health-insurance market is sound health policy, but also sound federalism policy. Reforming Medicare so that it no longer attempts to set prices throughout the medical sector is a way to make American health care less expensive and more efficient, but it is also a step toward the modest federal role envisioned by the constitutional design.

Conservatives should not see the making of public arguments about the Constitution as a last resort to deploy only when institutional safeguards have failed. No less an authority on the purpose of the Constitution than James Madison suggested that such argument would be one of the chief means of making it effectual. Speaking in favor of the Bill of Rights, Madison conceded that “[i]t may be thought all paper barriers against the power of the community are too weak to be worthy of attention.” His answer to that objection: “[Y]et, as they have a tendency to impress some degree of respect for them, to establish the public opinion in their favor, and rouse the attention of the whole community, it may be one mean to control the majority from those acts to which they might be otherwise inclined.”<sup>6</sup>

Confronted by presidential lawlessness, some conservatives are tempted to throw up their hands. They conclude there does not seem to be much conservatives can do about it besides such extreme, and for that reason impractical, measures as impeachment. But there is something we can do about it: We can make the case that the president must be bound by the laws and that executive dereliction of duty is a threat to national well-being. By making such arguments, we could try to reestablish a political norm by raising the cost of violations of it and increasing the odds that future presidents will feel bound by it.

**Conservatism should be home to everyone who takes seriously the task of strengthening the constitutional structure of a limited, accountable government that serves rather than masters civil society.**

The second sense in which political constitutionalism must appeal to the public is that it must make itself attractive. Our constitutional order was worth adopting, and remains worth preserving, because it protects our liberty and promotes the general welfare. That's what the Founders had to demonstrate, and what we must demonstrate anew. We have to show that our most vexing problems need not be entrusted to the care of a distant elite of micromanagers, but can instead be addressed (sometimes even solved) by free markets and self-government.

We have to show that we can have wider access to health care, an affordable safety net, opportunities to learn, and the like, without granting ever more power to government. Sometimes we will be able to make progress by ending ill-considered government policies,

sometimes by replacing them with ones more respectful of human nature, economic incentives, federalism, and individual rights. A constitutionalist orientation is not enough to make this showing possible: A detailed understanding of particular policy controversies will also be necessary, and so will political judgment. That orientation should, however, be the starting point for political reflection and choice.

In America, what conservatism chiefly means is the conservation of our political inheritance from the Founders. That task is no simple or passive one. It entails protecting it from external attack and internal corrosion, interpreting it anew for each generation, and adapting it to meet ever-changing circumstances. The point is not to keep the Constitution in tune with the times; it is to keep the times in tune with the Constitution.<sup>7</sup>



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## The Solution: A conservative governing vision to restore America's promise YUVAL LEVIN

1. So, for instance, Paul Krugman can write: “Start with the proposition that there is a legitimate left-right divide in U.S. politics, built around a real issue: how extensive should we make our social safety net, and (hence) how much do we need to raise in taxes? This is ultimately a values issue, with no right answer.” Like many on the Left, he takes the essential question of our politics to be exactly how much of the Left’s agenda should be adopted. (“The Closing of the Conservative Mind,” *New York Times*, May 25, 2013, <http://krugman.blogs.nytimes.com/2013/05/25/the-closing-of-the-conservative-mind/>.)
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## Health-care reform to lower costs and improve access and quality JAMES C. CAPRETTA

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3. For one, the poverty line is adjusted upward each year to account for the rise in the cost of living in a way that overstates that increase. Today's poverty line is a better standard of living than those of the 1960s. And the definition of income used in the official poverty rate actually excludes benefits from some of the most important anti-poverty policies expanded or established in the past fifty years. Left out are food stamps, Medicaid, Medicare, school breakfast and lunch subsidies, housing assistance, and tax benefits like the Earned Income Tax Credit.
4. One recent paper shows a decline from 26 percent to 16 percent using a poverty line set in 2012 and adjusted for inflation using the Bureau of Labor Statistics's "CPI-U-RS" price index. The paper also used an income definition that includes a range of noncash benefits and accounts for taxes. See Christopher Wimer, Liana Fox, Irv Garfinkel, Neeraj Kaushal, and January Waldfogel, "Trends in Poverty With an Anchored Supplemental Poverty Measure" (2013), working paper, [http://socialwork.columbia.edu/sites/default/files/file\\_manager/pdfs/News/Anchored%20SPM.December7.pdf](http://socialwork.columbia.edu/sites/default/files/file_manager/pdfs/News/Anchored%20SPM.December7.pdf).

The CPI-U-RS shows greater inflation than other indices such as the Bureau of Economic Analysis's "Personal Consumption Expenditures," or PCE, deflator (preferred by the Federal Reserve Board and the Congressional Budget Office) or the "chained CPI" (which, like the PCE, better accounts for consumers' ability to substitute goods and services for one another when relative prices change). To adjust the Wimer et al. poverty rate for 1967, I first compute the odds of being below rather than above the poverty line in 1980 and in 2010 using the Wimer et al. measure, then I compute the ratio of these odds. I do the same using another poverty measure estimated by Bruce Meyer and James Sullivan that relies on a cost-of-living adjustment more similar to the PCE and chained CPI. The odds ratio in the Meyer/Sullivan paper is 1.25 times the odds ratio from the Wimer et al. paper. I then compute the odds ratio for 1967 and 2012 using the Wimer et al. measure, multiply it by 1.25, and multiply that by the odds of being in poverty in 2012 to get the new odds of being in poverty in 1967. Finally, I compute the new percentage from the new odds. See Bruce D. Meyer and James X. Sullivan, "Winning the War: Poverty From the Great Society to the Great Recession," *Brookings Papers on Economic Activity* 45(2) (2012): 133–200.

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### Pro-family policies to strengthen marriage and give kids a better shot at the American dream

W. BRADFORD WILCOX

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### Restoring America's promise by recovering the wisdom of the Constitution RAMESH PONNURU

1. In 1972, 70 percent of Americans told Gallup they had a “great deal” or “fair amount” of “trust and confidence in the federal government when it comes to handling domestic problems”; in 2013, 42 percent did; <http://www.gallup.com/poll/5392/trust-government.aspx> (accessed March 27, 2014).
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3. The Constitution, Article I, Section 1, Clause 8: “The Congress shall have Power ... to make all Laws which shall be necessary and proper for carrying into Execution the foregoing Powers, and all other Powers vested by this Constitution in the Government of the United States, or in any Department or Officer thereof.”
4. This was James Madison’s view. See his letter to C. J. Ingersoll of June 25, 1831.
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7. The oft-cited phrase originates with constitutional scholar Walter Berns.

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