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Cato Policy Report

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Deficits, Debt, and Debasement

BY SCOTT A. BEAULIER AND PETER J. BOETTKE

“Those of us who manage the public’s dollars will be held to account, to spend wisely, reform bad habits, and do our business in the light of day, because only then can we restore the vital trust between a people and their government.”

—BARACK OBAMA
Inaugural Address, January 20, 2009

In recent years policymakers have pushed the economy ever closer to the brink of fiscal catastrophe. Federal spending rose substantially under President George W. Bush, with the deficit reaching \$460 billion in his last full year. In President Barack Obama’s first two years in office, it soared to \$1.4 trillion in 2009 and \$1.29 trillion in 2010. Deficits are on track to remain at unprecedented levels in 2011, and President Obama’s promise to halve the deficit by 2012 turned out to be the same “politics as usual” that he denounced during his campaign. Even if he made good on that promise, deficits would still be twice as high as ever before.

To be fair, the gloomy budgetary picture is not entirely Obama’s fault. His is just the

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latest administration unwilling to tackle serious fiscal challenges. While bailouts and stimulus programs compounded the problem, its source is the big three transfer programs—Social Security, Medicare, and Medicaid. Together, these programs consume approximately 10 percent of U.S. gross domestic product. By 2052 they will

reach 18.2 percent of GDP and, assuming tax collections remain at their long-term levels, will absorb all federal tax revenue collected by the government. In other words, no discretionary spending and no defense spending will be possible by 2052 unless tax revenue increases or the government

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At a Cato Institute Conference in April, **SEN. MIKE LEE (R-UT)** called for a balanced budget amendment to address the burden of federal spending in Washington. Lee also attended a private breakfast held at Cato in June, where he talked with Cato analysts about several policy issues. **PAGE 14**



BY DAVID BOAZ

Editorial

This Is the Business You Have Chosen

In *The Godfather, Part II*, the gangster Hyman Roth recalls the killing of a colleague and says there's no point in complaining about it because "This is the business we've chosen." Murders are just part of mob business.

Government has its standard practices, too. Government programs in a mixed-economy democracy are typically shaped by lobbying and marked by waste.

One recent Sunday (May 15), the entire *Washington Post* seemed to remind readers of that fact. Leading the paper was a big investigative story titled "Million-Dollar Wasteland." Reporters Debbie Cenziper and Jonathan Mummolo wrote:

The federal government's largest housing construction program for the poor has squandered hundreds of millions of dollars on stalled or abandoned projects and routinely failed to crack down on derelict developers or the local housing agencies that funded them . . . The result is a trail of failed developments in every corner of the country. Fields where apartment complexes were promised are empty and neglected. Houses that were supposed to be renovated are boarded up and crumbling, eyesores in decaying neighborhoods. . . The *Post* found breakdowns at every level.

And on and on for three full pages.

Then, in the Metro section, columnist Robert McCartney wrote about the D.C. Council hearings on the hiring scandals in the administration of newly elected mayor Vincent Gray:

The main thing learned in the hearings so far is that Gray showed bad judgment in allowing [three close advisers] to guide so much of the hiring for patronage jobs just below the cabinet rank. Although all three advisers were longtime personnel executives, they blundered repeatedly by overpaying people, doing inadequate vetting and hiring children of officials [including their own].

And an article on Amtrak's annual billion-dollar deficits included this gem: "Critics in Congress also have questioned Amtrak's management, asking, for example, how an employee with a \$21,000 salary earned \$149,000 in overtime last fiscal year."

Those articles reminded me of another investigative tour de force in the *Post* two months earlier, bannered as "A D.C. lawyer and her associates secured \$500 million in federal contracts to benefit Alaska native corporations. Less than one percent made it

back to Alaska." That article too had been prominently displayed in the Sunday paper but had not generated much online comment, and I asked at the time on the Cato blog: "Are we so jaded that a full-page investigation of self-dealing and corruption involving affirmative action, small business, defense contracting, and complicated financial maneuvers just doesn't get our juices flowing?" But surely I was wrong. Outrage ensued, right? Angry editorials, congressional hearings? No, not so much.

Newspapers are full of stories about serious people and clowns running for president, about who's up and who's down in political maneuvering, about Charlie Sheen and Lindsay Lohan. All fine topics indeed. But if journalists spent even 10 percent of their time digging into how the federal government is spending \$3,600,000,000,000 this year, who knows how many stories of waste and deadweight loss we'd find? If one diligent reporter could find that much fraud by one well-connected contractor, how much could a hundred reporters find?

I generally don't think that "waste, fraud, and abuse" is the key to cutting federal spending; you have to go after the big programs, like transfer payments and military spending. But as Everett Dirksen almost said, \$500 million here, \$500 million there, pretty soon you're talking real money.

There are reasons that government programs are often characterized by waste, fraud, and abuse. Politicians tend to respond to interest groups that stand to receive benefits from any particular program rather than to the average citizen who will pay very little for each program. Policymakers have less incentive to control costs and improve efficiency than do people in the private sector with their own money (or their boss's money) at risk. As government gets bigger, it becomes less and less possible to have meaningful oversight and transparency—though we can hope that new technologies may help somewhat on the transparency side.

Realistically, if you want the federal government to tax and borrow and transfer \$3.6 trillion a year, if you want it to build housing for the poor and give special benefits to Alaska Natives, if you want it to supply Americans with health care and school lunches and retirement security and local bike paths, then you have to accept that such programs come with incentive problems, politicization, corruption, and waste.

For those who like such expansive government: This is the business you have chosen.

“If you want the federal government to tax and borrow and transfer \$3.6 trillion a year, then you have to accept that such programs come with incentive problems, politicization, corruption, and waste.”

Safety, debt crises, and altruism in the Cato Journal

The Virtues of Free Markets

In the Spring/Summer 2011 issue of the *Cato Journal*, Mark Zupan, dean and professor of economics and public policy at the University of Rochester, examines “The Virtues of Free Markets.” He argues that entrepreneurs’ interest in maintaining long-run relations with their customers gives them an incentive to cooperate and honor their word—or face the loss of business to those who are more ethical. Private property, freedom of contract, and the rule of law—the institutions upon which free markets rest—motivate individuals to take account of the impact of their current decisions on future values, and in so doing foster cooperation and integrity over time.

French social philosopher Anthony de Jasay examines several cases in which it appears that an individual sacrifices self-interest for the good of the group. Upon deeper reflection, and with some realistic assumptions, he finds that what initially looks like “selfless” behavior turns out to be “selflessly self-ish.” Thus, the self-interest postulate behind rational economic man (*homo economicus*) can be broadly applied.

Economists Daniel Gropper, Robert Lawson, and Jere Thorne Jr. present evidence from more than 100 countries that economic freedom and happiness go hand in hand. Economic freedom expands individual choices and increases real per capita income, making people better off and happier. Carrie Kerekes of Florida Gulf Coast University, in a cross-country study, finds that when property rights in land and water are more secure, there is a positive impact on environmental quality.

Paul Rubin, professor of economics at Emory University, examines the role of markets, tort law, and regulation in achieving safety. He finds that free markets are often the most important mechanism to achieve safety and that tort law and regulation may “overreach”—doing more harm than good.

Other contributors include Jerome Stein on “The Diversity of Debt Crises in Europe,” Matthew Carr on “The Impact of Ohio’s EdChoice on Traditional Public School Performance,” Dean Stansel on “Why Some Cities Are Growing and Others Shrinking,” Joseph Noko on “Dollarization: The Case of Zimbabwe,” and Jerry Tempelman on “Why Do Federal Funds Trade at the FOMC’s Target Rate?” ■

All of these articles, as well as the five book reviews in this issue of *Cato Journal*, are available online at www.cato.org.



Cato News Notes

PREBLE NAMED VICE PRESIDENT



Christopher Preble has been named vice president for defense and foreign policy studies at the Cato Institute, succeeding Ted Galen Carpenter effective July 1. Carpenter will retire from management and from Washington but will continue writing and lecturing as a senior fellow.

Carpenter, who joined Cato in 1985, is the author of 8 and the editor of 10

books on international affairs, including *Smart Power: Toward a Prudent Foreign Policy for America*, *Bad Neighbor Policy: Washington's Futile War on Drugs in Latin America*, *The Captive Press: Foreign Policy Crises and the First Amendment*, *Beyond NATO: Staying Out of Europe's Wars*, and *A Search for Enemies: America's Alliances after the Cold War*. He is currently completing two new books. He has written for all the major foreign policy journals and major newspapers. Carpenter received his PhD in U.S. diplomatic history from the University of Texas and will move back to Austin.

Preble has been Cato's director of foreign policy studies since 2003. He is the author of three books including *The Power Problem: How American Military Dominance Makes Us Less Safe, Less Prosperous, and Less Free* (Cornell University Press, 2009), which documents the enormous costs of America's military power and proposes a new grand strategy to advance U.S. security. Preble is also the lead author of *Exiting Iraq: How the U.S. Must End the Occupation and Renew the War against Al Qaeda*, and he co-edited, with Jim Harper and Benjamin Friedman, *Terrorizing Ourselves: Why U.S. Counterterrorism Policy Is Failing and How to Fix It*. His resume also includes a Cato internship, four years as a naval officer, and a PhD in history from Temple University.

Justin Logan, who has written studies on such topics as nation-building and grand strategy over the past seven years, has been promoted to director of foreign policy studies.

THE FIRST THING WE DO, LET'S READ ABOUT THE LAWYERS

Cato senior fellow Walter Olson has received significant media attention for his latest book, *Schools for Misrule: Legal Academia and an Overlawyered America*. Law professor John O. McGinnis reviewed the book in the *Wall Street Journal*, calling it “Excellent... A fine dissection of these strangely powerful institutions.” Other favorable reviews have appeared in the *Weekly Standard*, *Yale Alumni Magazine*, and the *Washington Times*. Olson has made eight law school appearances, and has spoken at the Heritage Foundation, the Manhattan Institute, and the Heartland Institute, as well as the Cato Institute. His book was featured on C-SPAN2's popular “BookTV,” and the episode can currently be found on the “BookTV” website.



In May, former Minnesota governor TIM PAWLENTY held a press conference outside the Cato Institute’s headquarters on Massachusetts Avenue after his address at a Cato Policy Forum, during which he discussed his vision for reducing the size of the federal government. The occasion marked Pawlenty’s first appearance in Washington, D.C., after announcing his presidential bid two days earlier.



At a Capitol Hill Briefing in May, Cato legal policy analyst DAVID RITTGERS (left) joined forces with ACLU senior policy counsel MIKE GERMAN to reexamine the Patriot Act and its impending renewal. German focused on the “exceedingly broad” nature of the law, while Rittgers stressed the need for vigilance. “Terrorism, contrary to what we’ve been told, is not an existential threat to our liberty,” Rittgers said. “But our own counterterrorism efforts can be.”



Cato senior fellow JOHAN NORBERG introduced his film *Free or Equal: A Personal View* at a private screening in April. In the documentary, to be seen on PBS stations this summer, Norberg retraces Milton Friedman’s steps in his path-breaking *Free to Choose* and offers updated conclusions.



Sen. JOE MANCHIN (D-WV) visited the Cato Institute for a private breakfast in April. He touched on a wide range of issues, including energy and the environment, health care, and foreign policy. In Cato's 2010 "Fiscal Policy Report Card on America's Governors," Manchin received an A.



DANIEL GRISWOLD, director of the Cato Institute's Herbert A. Stiefel Center for Trade Policy Studies, spoke at the Carnegie Endowment for International Peace in May. He talked about the lessons learned from protectionism during the Great Depression and how post-war trade institutions helped limit protectionism in the recent crisis.



At a Cato Policy Forum in April, KELIANG ZHU, an attorney at Landesa, reviewed the development institute's recent findings from their large-scale survey on land rights in China. Zhu joined Roy Prosterman, Landesa's founder, and Xiaibi Zhang, senior research fellow at the International Food Policy Research Institute, in exploring the conditions of Chinese farmers. Citing the importance of land documentation, Zhu highlighted advances in the protection of these rights.



In April, Cato's government affairs department held a series of lectures for House freshmen. ROGER PILON, vice president for legal affairs at the Cato Institute, discussed constitutional issues at one session.

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slashes benefits to these three programs.

BREAD AND CIRCUSES

An inevitable crisis seems the almost certain outcome of America's deficits and debts. The massive increases in transfer spending, coupled with steady growth in discretionary and defense spending, mean that large deficits will haunt America for the foreseeable future. Deficits occur when government expenditures exceed tax revenues, leading to higher interest rates and crowding out private investment. They generate unpredictability in policy, as they herald rising taxes. Since deficits cannot be left unpaid, governments normally finance them by issuing bonds that promise to repay the principal (with interest) over a period of time.

Most troubling, deficits add to our already high federal debt. Publicly held debt currently stands near 60 percent of GDP and, according to the Congressional Budget Office, will rise to 90 percent by 2021. As debt rises, interest rates rise, taxes on future generations rise, and politicians inflate the currency to hide their profligate spending. To pay off this debt, the government must run surpluses, which occur when tax revenues exceed spending. If the government is unable to generate surpluses, a third and far more dangerous option can be employed to eliminate long-term debt: debasing the currency.

Debasement is the "pretend payment" of debt that occurs when governments inflate their currency by printing money. It's a problem of nearly every government, from the "bread and circuses" of ancient times through today. In the 18th century, governments debased their currencies by trimming metal coins and recirculating them. By making a coin worth less in real terms, governments throughout Europe were able to spend beyond their means. "The honour of a state is surely very poorly provided for," Adam Smith wrote in 1776, "when in order to cover the disgrace of real bankruptcy, it has recourse to a juggling trick of this kind."

Today, paper money limits governments' ability to physically trim the edges of metal coins. But by printing money to pay off debts, governments debase the currency and

“Debasement is the ‘pretend payment’ of debt that occurs when governments inflate their currency by printing money.”

ultimately erode its purchasing power. Simply put, they are using a slight variation of the same “juggling trick” to achieve their ends: by pushing the debt problem into the future, they hide the full cost of repayment to the public.

As a result, the symptoms of debasement are not always easy to recognize. Yet several recent indicators have been revealing. The Federal Reserve's balance sheet, for instance, has expanded from its long-established level of \$8 trillion to \$23 trillion. This expansion in the money supply helped fuel a bond market rally that resulted in artificially low Treasury yields. The Fed's direct interventions into the mortgage-backed security market have held mortgage rates at record lows as well. By purchasing toxic assets private investors weren't interested in, the Fed artificially expanded the money supply. As more money entered the system, prices rose and each dollar lost some of its value.

Inflation is always and everywhere the result of monetary expansions, and its pernicious effects are becoming palpable. Commodity prices are all nearly twice as high as they were in 2008. Prices for education and health care continue to rise rapidly. Consumer price increases, when food and energy are included, are well above levels a central bank would normally be comfortable with. And prices for technologies like cell phones, personal computers, and televisions are not falling as rapidly as they should be.

The distortions in these prices indicate that debasement is already taking place—and it stems from problems that economists have been warning about for decades.

Historically, the public accepted deficits and debts only in response to major wars and huge economic crises. During World

War II, for example, public debt increased to nearly 109 percent of GDP. Yet after the war, the government made a concerted effort to pay down the debt, reducing it to 50 percent of GDP by 1956 and 24 percent by 1974. The experience of the last 30 years, however, shows that deficit spending is no longer an emergency response to catastrophe. In 1980, America's total national debt stood at \$1 trillion. Over the next three decades, it grew 14-fold—without a major depression or world war. Deficit spending has become business as usual, and we're quickly approaching the point where repayment is impossible.

HOLDING A TIGER BY THE TAIL

Politicians are unable to address our current fiscal challenges in part because they rely on flawed Keynesian arguments to justify their spending. Simplistic Keynesianism argues for greater government spending when the economy softens, followed by spending cuts when the economy returns to growth. But this rests on the crucial assumption that politicians act benevolently, in the interest of the overall economy. It assumes politicians will exercise fiscal restraint.

The historical record since Lyndon B. Johnson's "Great Society" suggests otherwise: politicians, regardless of party, do not follow Keynesian assumptions. Instead, they spend during the bad times and during the good times. There are, of course, good public choice reasons why politicians cling to Keynes: he offers an economic justification for promising everyone everything! Politicians therefore achieve success through a simple mantra: "Spend 'em if you got 'em, and spend 'em if you don't."

Government officials don't want to lose popularity by raising taxes and cutting spending. Instead, they employ juggling tricks to give the illusion of paying their bills. The Treasury finances government expenditures by floating bonds to the public, and the Federal Reserve steps in as buyer whenever the Treasury is unhappy with the market interest rate. The process is referred to as monetization, but really it's debasement, and it stems in part from the fact that it is difficult to keep the Fed and the Treasury separate.

In fact, some have said that the idea of a

separate Fed and Treasury is utopian, that the two offices within government will remain forever entangled. The 1974 Nobel Prize winner in economics, F. A. Hayek, called the monetary and fiscal policy dance an exercise in “holding a tiger by the tail.” In 1969, while discussing the broad, inflation-borne prosperity affecting Venezuela and much of the Western world, Hayek said:

How long can this inflation continue? If the tiger [of inflation] is freed, he will eat us up; yet if he runs faster and faster while we desperately hold on, we are still finished!

Hayek’s message was that inflation leads to a misallocation of resources. During inflationary periods, the structure of production gets distorted and higher-order, capital-intensive goods like housing get overproduced. At some point during the inflationary cycle, central bankers face a choice of either inflating more or contracting the money supply. When the money supply is contracted, the capital-intensive “boom” finally “busts.” According to Hayek, any attempt by policymakers to address the misallocation through deficit spending—letting the tiger run faster—creates further distortions and a greater misallocation. By keeping prices and interest rates away from their natural levels, fiscal and monetary interventions simply prolong the inflationary cycle and prevent a return to normal, long-run conditions. Two decades after his death, Hayek’s “tiger by the tail” critique of Keynesian policies remains as relevant as ever.

In 1977 James Buchanan and Richard Wagner warned about the political legacy of Keynesian economics. “Sober assessment suggests that, politically, Keynesianism may represent a substantial disease,” the two wrote in *Democracy in Deficit*, “one that can, over the long run prove fatal for a functioning democracy.” If economic policies are not somehow constrained by rules and supermajorities, deficits are the predictable outcome of democracy. “The bottom line: political capitalism is not laissez faire capitalism,” they write. “To continue down our current path is to reinforce the perverse fol-

“The honour of a state is surely very poorly provided for,’ Adam Smith wrote in 1776, ‘when in order to cover the disgrace of real bankruptcy, it has recourse to a juggling trick of this kind.’”

ly of politics that has threatened the viability of the current economic system.”

TYING THE JUGGLER’S HANDS

There are several ways we can constrain the juggler in an attempt to reverse our current course. The first involves tying the juggler’s hands. The federal government could adopt a balanced-budget amendment, for instance—one similar to those constraining many states. This would limit the government’s fiscal authority through constitutional mechanisms, with the goal of confining levels of taxation and balancing the budget. Such an amendment would be quite popular with voters, though obviously less so with elected officials, and it could choke off the fuel needed for deficits, debts, and debasement.

To provide a further safeguard against this cycle, legislative steps could be taken to separate the Fed from the Treasury. The two currently work as “partners,” but by any measure they are dangerous bedfellows. Reform that better defines the roles of the organizations could greatly reduce the threat of debasement. One such step would be to limit the kinds of bonds the Fed can purchase from the Treasury. For example, the second round of quantitative easing (QE2) would not have been possible had there been a rule saying the Fed cannot buy long-term bonds from the Treasury. A vast literature in monetary economics has consistently found that more independent central banks outperform ones where the fiscal and monetary

authorities are closely aligned. Other rules—along the lines of antitrust restrictions—that limit Fed and Treasury interaction would also be worth considering.

Because it is difficult to imagine members of Congress taking actions that tie their own hands, these steps would ideally be augmented with more radical fiscal reform. Reverse revenue sharing would get the federal government out of the business of taxation and would instead allow for 50 different experiments in optimal taxation across the different states. Unlike the Articles of Confederation, which encouraged free-riding by states, each state could be required to contribute a certain amount to the federal government. But, rather than be hampered by one-size-fits all federal taxes, individuals could choose from different tax regimes in various states. Reverse revenue sharing reduces many of the problems of our current federal system—special-interest groups become less relevant and centralization declines.

LIMITING THE JUGGLER’S TRICKS

We fully recognize that we’re a long way from a world where federal balanced budget amendments and reverse revenue sharing programs are the preferred policy options. But we firmly believe we are a long way down the bankruptcy path, and any kind of turnaround requires far more drastic action than typical policy measures. To ensure the juggler has fewer tricks at his disposal, goods and services provided by government must be shifted to the market and privatization must be embarked on.

Our current entitlement programs, for instance, are unsustainable. The plan to reform Medicare being advanced by Rep. Paul Ryan is an acknowledgement that we are on an unsustainable entitlement path, and his commitment to rein in spending is commendable. But these reforms still fall short because they leave power in the hands of the juggler. What is really needed is reform that fully shifts medical coverage for the elderly and the poor from the public sector to the market. Reforms that fall short of full privatization still leave the juggler with tricks on hand.

Even more fundamental than privatizing

entitlements would be to strip the government of its control of the money supply through a return to the gold standard, a monetary rule, or “free banking.” Reforming the Fed and chasing after the “separate Fed and Treasury” ghost has proven futile, and it may be time to acknowledge that our central banking system has failed. While there would certainly be transitional costs to work through and consider in the short-term with a move to free banking, a decentralized monetary regime would help to check and constrain any particular bank aiming to overexpand the money supply.

ENDING THE CYCLE

Many of the policy recommendations we are making ask politicians to fall on their own swords for the sake of financial solvency. While these reforms are admittedly radical, the alternative is undoubtedly more extreme. To see why, it is worth expanding on Adam Smith’s juggling metaphor from earlier. In the final chapter of *The Wealth of Nations*, Smith observed:

When national debts have once been accumulated to a certain degree, there is scarce, I believe, a single instance of their having been fairly and completely paid. . . . Pub-

“We are currently faced with a problem of unprecedented magnitude, one that should justify giving unconventional reforms a seat at the table.”

lick bankruptcy has been disguised under the appearance of a pretend payment. . . . When it becomes necessary for a state to declare itself bankrupt, in the same manner as when it becomes necessary for an individual to do so, a fair, open, and avowed bankruptcy is always the measure which is both least dishonorable to the debtor and least hurtful to the creditor. The honour of a state is surely very poorly provided for, when in order to cover the disgrace of real bankruptcy, it has recourse to a juggling trick of this kind. . . . Almost all states, however, ancient as well as modern, when reduced to this necessity, have upon some occasions, played this very juggling trick.

Federal bankruptcy—whether it occurs through debt repudiation or a more orderly process of restructuring—would serve as a sobering wake-up call. The municipal bankruptcies some cities and counties have faced in recent years, along with the state budget crises afflicting most states, are grim portraits of what bankruptcy at the federal level would look like. People promised benefits would see their expectations dashed. Taxes across the board would rise. Interest rates on future debt issuance would soar. The long-term consequences of renegeing on our promises would be difficult to estimate in full. As such, we are currently faced with a problem of unprecedented magnitude, one that should justify giving unconventional reforms a seat at the table.

After vowing “to spend wisely, reform bad habits, and do . . . business in the light of day,” President Obama instead accelerated the country down the path of overspending, made unsustainable promises, and used the Fed to conceal the full cost of government profligacy. Perhaps our best hope now is to consider measures that fundamentally challenge the system, and finally break free from the cycle of deficits, debt, and debasement. ■

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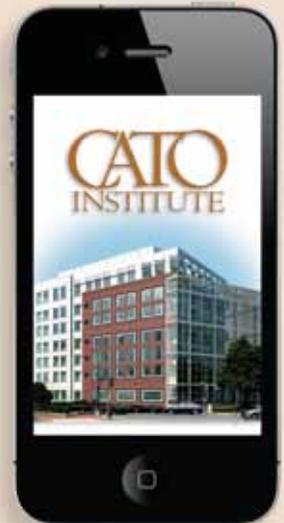
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The Case for Marriage Equality: *Perry v. Schwarzenegger*

The 1967 Supreme Court case *Loving v. Virginia* ended state bans on interracial marriage in the 16 states that still had such laws. Now, 44 years later, the courts are once again grappling with denial of equal marriage rights. Two California couples have filed suit against Proposition 8, the 2008 initiative that limited marriage to opposite-sex couples. The plaintiffs in *Perry v. Schwarzenegger* won in federal district court, and the case is now on appeal. At a Cato Policy Forum held in May, co-counsels Theodore B. Olson, former U.S. solicitor general, and David Boies, chairman of Boies, Schiller & Flexner, discussed their progress with the case. As co-chairs of the American Foundation for Equal Rights advisory board, Robert A. Levy, chairman of the Cato Institute, and John Podesta, president of the Center for American Progress, also spoke on how the principle of equality transcends the left-right divide.

THEODORE B. OLSON: David Boies and I have been involved in this case for two years, as of this month. We represent two couples: two gay men who live in southern California and a lesbian couple in Berkeley. They have both been in long-term relationships, and they have wanted to be married. We went to trial in January of 2010 and had closing arguments in June. In August, the judge rendered a decision—a 134-page explanation of findings of fact and conclusions of law—that struck down Proposition 8.

When we tried the case, the judge decided that this was an important question affecting hundreds of thousands of Californians and millions of Americans. It was a constitutional challenge—going to the very core of what the Fourteenth Amendment Due Process and Equal Protection Clauses mean. The trial itself went 12 days, and it was a remarkable education. As many of you know, it was once against the law in many places to serve alcoholic beverages in public to a person who was gay—*against the law*. Both the server and the drinker could go to jail. President Eisenhower once announced that someone who was gay could not hold a federal position. In our arguments, we presented evidence on the history of marriage, and how race was once used as a basis to deny people the right to marry.

The district court very thoughtfully



“Fourteen times, the U.S. Supreme Court has announced that marriage is a fundamental right under the Constitution.”

reviewed our evidence and rendered a decision that Proposition 8 denied individuals the fundamental right to marry. Fourteen times, the U.S. Supreme Court has announced that marriage is a fundamental right under the Constitution. It is a compo-

ment of liberty, privacy, association, the right to identify oneself spiritually—and it is currently being denied to a large segment of American society.

If you're going to deny people that right, what justification exists? In fact, several times during the case, the judge asked, “What harm would it do to people of heterosexual orientation if homosexuals were married?” Our opponents didn't want to answer and tried to avoid the question, but the judge insisted. And one of our opponents, who is a very good lawyer, paused, looked at the judge, and said, “I don't know.”

The institution of marriage and what it means in this country isn't simply a legal thing. It is a social construct. The example I like to use is citizenship: What if you were told by your government that because you came from a certain country, you could be all the things that a citizen could be—you could vote, travel, own property—but you couldn't call yourself a citizen? You wouldn't be a citizen, and if you can't be married in this country, you are being left out of a very important component of what our society reveres. We are telling people that they are different—that they are not entitled to the same respect, the same dignity, the same equality—and they are therefore second-class. That is a state-based license to discriminate, and that is what the Proposition 8 case is all about.

DAVID BOIES: What exactly is going on when a state like California says that they will not permit a certain group of citizens to marry? As a thought experiment, imagine that the state simply got out of the marriage business entirely. You wouldn't have the problems we are having, because issues of equal protection and due process only arise with state action.

In order to attack that state-sponsored discrimination, we wanted to establish three things. One, we wanted to establish that

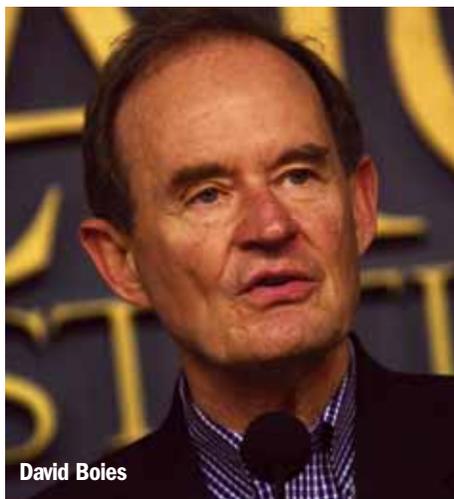
marriage is a fundamental right. Both the plaintiffs and the defendants agreed on this, and they could hardly have said otherwise. The U.S. Supreme Court has repeatedly affirmed that marriage is a fundamental right. In fact, marriage is so important to human dignity—to the rights of privacy, association, and liberty—that even when a significant interest exists, the state cannot prohibit it. Marriage is much more than any of its individual attributes. It has such significance that you cannot even deprive people who are locked away for life from entering into it. So the idea that marriage was a fundamental right was taken, I think, by both sides as a given.

The second thing we set out to prove was that depriving citizens of the right to marry seriously harmed them and their children. Hundreds of thousands of children are being raised today by gay and lesbian couples. And we proved, with a wealth of statistical and analytical data, the harm that forbidding marriage did. Our experts—child psychologists, sociologists, anthropologists, statisticians, economists—proved this, and we didn't stop there. The other side identified a number of expert witnesses, starting with eight, just like us. Six of those experts were dropped after we took their depositions because they admitted that deprivation of this right seriously harmed gay and lesbian couples and their children. In fact, in an interesting argument, our opponents objected to our playing some of the deposition tapes on the grounds that their own witnesses weren't really experts. Our opponents lost that argument.

The third thing we set out to prove was that there was no benefit to preventing gays and lesbians from marrying. The defense started out by saying that they don't really need to marry—they've got civil unions. They lost that argument. Then they fell back on the idea that it will be dangerous—it will harm the institution of heterosexual marriage. Think about that for a minute. I ask those of you who are considering marriage whether it would dissuade you if you learned that a gay or lesbian couple down the street was able to get married. Or for those of you who are married, whether you would decide to get divorced because now

gays and lesbians are able to get married. Again, we brought in a wealth of evidence that there was no harm—and again, on the cross examination, even the defendants' own expert witnesses conceded that they had no evidence of any harm.

Based on that record, the court wrote a decision—which everyone should read because it talks about the development of equality in this country and the important



David Boies

“Our opponents objected to our playing some of the deposition tapes on the grounds that their own witnesses weren't really experts.”

ways in which marriage has changed over time. It talks about the fact that slaves were prohibited from marrying—and how once slavery was abolished, they immediately rushed to get married. This was part of what made their relationship dignified and respectable. It gave them a sense of belonging—a sense of equality. When something is that important to people, I think we have to ask ourselves, as a society, “What are we doing in trying to prevent others from achieving this?”

Californians had an established right to same-sex marriage that was then taken away. They now have this crazy quilt: because they could get married for a period of time, there are currently 18,000 gay and lesbian marriages recognized by the state. So you have a couple that is legally married and, next door, a couple that wants to get married but can't. Indeed, if the couple that is married gets a divorce, they can't remarry. *They can't even remarry each other.* That strikes people instinctively as not being rational.

The fundamental issue is one of civil rights—of individual rights. That is why you see people on this panel who don't necessarily agree on a range of other issues. We all have an interest in protecting individual rights against government discrimination.

JOHN PODESTA: Fifteen years ago, the thought of same-sex couples being allowed to legally marry was hard for most Americans to contemplate. You probably had to work at the Cato Institute to even wrap your head around that idea. No state offered this right. Barely 30 percent of the country thought that it should be offered—and 10 years before, that number was in the low teens. Senators and representatives who today are outright supporters of marriage equality voted for the Defense of Marriage Act in 1996. And of course, the president who signed it has not only changed his views, but is now a vocal supporter of marriage equality.

Yes, today the world looks very different. Just 15 years later, marriage equality for same-sex couples is becoming a fairly mainstream idea—embraced by liberals, conservatives, moderates, and not surprisingly, by libertarians alike. Five states have legalized same-sex marriages. Eight states offer civil unions or domestic partnerships, and three additional states recognize same-sex marriages performed legally in other jurisdictions.

National polls consistently show that a small but growing majority of the country supports marriage rights—including two-thirds of Democrats, almost 60 percent of independents, and more than a third of Republicans. Two-thirds of people under 40 now support marriage equality. The

change in public opinion is not only happening, it's happening quickly. In fact, most of the spike in public support for marriage equality has come in the past few years. In 2004, when marriage equality was a "game-changing" issue at the ballot box, support was only at 34 percent—not much higher than it was in 1996. Today, 53 percent of Americans support marriage for same-sex couples. Despite recent high-profile attacks, marriage equality clearly has a strong and growing momentum.

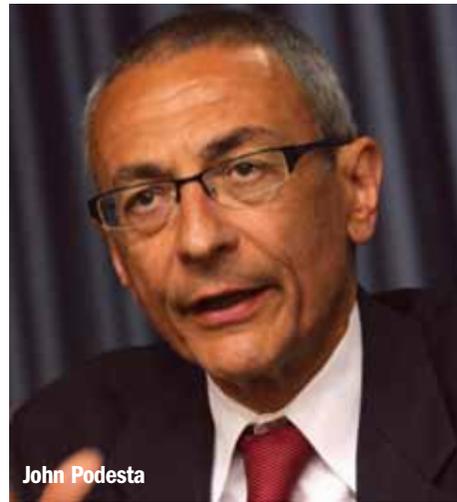
Yet across the political spectrum, it's clear that an appeal to discrimination has not completely lost its potency. We see a number of candidates seeking their party's presidential nomination attacking marriage equality. But these appeals to divide America will ultimately be rejected. What has historically made America great is our promise of freedom and equal opportunity to all of our citizens. We have failed to live up to that promise in times past. But our country is constantly evolving for the better, expanding the circle of opportunity, deepening the meaning of freedom. We're evolving because countless policymakers, activists, and lawyers—including those in this room—keep working tirelessly to root out injustice and expand America's promise to every citizen.

This is another step in our journey to form a more perfect union, and it is something even the Center for American Progress and Cato can agree on. Our partnership shows that we can transcend political labels to focus on basic rights and smart public policy—policy that is rooted in our most enduring founding principles of equality, fairness, and liberty. We both recognize that, at its heart, marriage equality is about treating our fellow citizens with dignity and respect, whether they're gay or straight.

ROBERT A. LEVY: Why do libertarians argue there ought to be a right to same-sex marriage? The purpose of government is to secure individual rights and prevent some persons from harming others. The threshold question, therefore, is this: Whose rights are being violated when two gay people get married? The answer, of course, is nobody's.

In fact, why should government be

involved at all in the marriage business? For most of Western history, marriage was a matter of private contract between two parties. Marriage today could follow that tradition, with little or no government intervention. Some institutions would recognize gay marriages; others would not. Still others would call them "domestic partnerships." No one would have to join any group, and no group would have to adopt a



John Podesta

“National polls consistently show that a small but growing majority of the country supports marriage rights.”

definition that its members found offensive. The rights and responsibilities of the partners would be governed by personally tailored contracts, like those that control most of the interactions among people in a free society.

That's the ideal. Regrettably, however, government has interceded, enacting more than a thousand federal laws dealing with issues like taxes, child custody, and inheritance. Whenever government imposes obligations or dispenses benefits, the Constitution is implicated. The Equal Protection

Clause of the Fourteenth Amendment says that no state may "deny to any person within its jurisdiction the equal protection of the laws." That provision is the relevant constitutional issue here, and that is where conservatives and libertarians sometimes part company. I want to explore that parting of company by looking at two topics: federalism and fundamental rights.

With respect to federalism: Why don't we simply leave the same-sex marriage question up to each state? At the time of the framing, the Constitution only applied to the federal government. But we later learned that the states can be every bit as tyrannical as the Feds, slavery being the case in point. After the Civil War, however, the Fourteenth Amendment effectively made the Bill of Rights and other provisions of the Constitution applicable against the states. For the first time, the federal government could intervene if the states violated our rights. That significantly altered the balance between the national and state governments. Federalism surely allows some states to recognize heterosexual and gay marriages on an equal basis while other states opt to privatize all marriages. Still others can call all marriages "domestic partnerships." But the states may not discriminate between same-sex and opposite-sex unions, without justification, and none has been shown.

Next, consider the issue of fundamental rights. Since the New Deal, the courts have rigorously reviewed government regulations only if they infringe on a fundamental right—meaning one that is either implicit in the concept of ordered liberty, or deeply rooted in our nation's traditions and culture. How that right is defined—narrowly or broadly—makes all the difference, and can even dictate the outcome of a case. Some conservatives argue that the right to same-sex marriage doesn't meet the criteria for a fundamental right and therefore the courts should defer to the legislature.

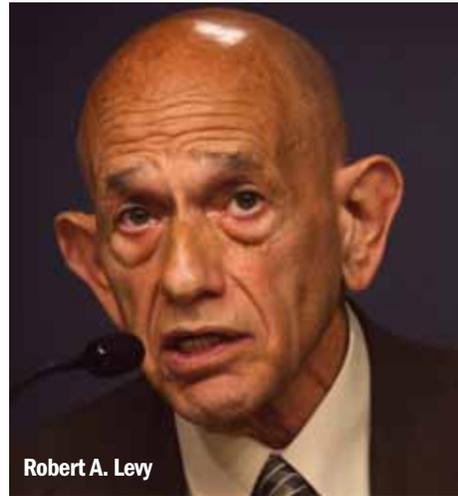
Consider the case of *Gonzales v. Raich*. A sick person with a doctor's note claimed a fundamental right to use medical marijuana in California, where it is legal. The court of appeals characterized the right as "the

use of narcotics for medical purposes.” Ms. Raich lost because medical marijuana, said the court, is not required for ordered liberty, nor is it deeply rooted in our nation’s traditions. If the court had adopted Ms. Raich’s characterization of the right—the liberty to pursue a less painful life without infringing on the rights of anyone else—she would have won that case. Which characterization is correct? Both of them are correct.

Raich was indeed trying to live with less pain; she was also using medical marijuana. Similarly, Kristin Perry’s right in *Perry v. Schwarzenegger* could be characterized as “the right to marry another woman,” which might not be considered deeply rooted in our traditions. Or it could be characterized as “choosing a spouse and forming a household,” which would be deeply rooted. So sometimes courts can rule on the basis of how they describe the right, and that is the foolishness of bifurcating our rights. All rights—enumerated, unenumerated, fundamental, nonfundamental—should be rigorously protected by the courts. That’s the view of most libertarians. Too often, it is not the view of many conservatives.

From liberals, with all due respect to Mr. Podesta, we sometimes get too much government—an enlargement of state power. From conservatives, with all due respect to Mr. Olson, we sometimes get too few freedoms—protection of some, but not all, of our constitutionally secured rights. The left and the right are selectively indignant about the proper role of government. Libertarians,

by contrast, have a consistent, minimalist view. We want government out of our wallets and out of our bedrooms. We view the



“From liberals, we sometimes get too much government. From conservatives, we sometimes get too few freedoms.”

powers of government very narrowly and the rights of individuals very broadly—and that was precisely the vision of the Framers.

THEODORE B. OLSON: Next month is the

44th anniversary of *Loving v. Virginia*, which struck down as unconstitutional Virginia’s law prohibiting interracial marriage. The Supreme Court decided it unanimously—but that case, if it had been decided the other way, would have prevented our president’s mother and father from getting married. These days, it’s inconceivable that such a law could exist in the United States.

The polling numbers confirm this: the swing in public opinion has been 10 percent in most polls in favor of recognizing the rights of individuals to marry, irrespective of their sexual orientation. That’s in two years, since *Perry v. Schwarzenegger* was filed. That matters, because court decisions are made in the atmosphere of public opinion. When we win this case, if we do, we want people to react and say, “It’s about time.”

The American Foundation for Equal Rights has supported us very strongly, and put us out there—this so-called odd couple, which we’ve heard a thousand times now (but at least no one’s said “strange bedfellows” here). It helps us attract attention so that people will say, “How did you two get together?” It gives us a chance to talk to the American people—on radio, on television, in newspapers. We’re finding that it resonates. Little by little—actually it’s really quite fast—the American public is changing. So when this case comes out the way it should, we believe the American people are going to say, “Thank God that terrible vestige of discrimination is gone.” ■

IN CELEBRATION OF CONSTITUTION DAY 2011

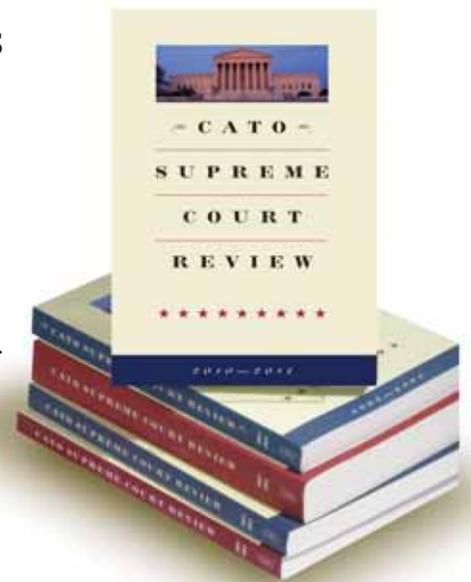
THE CATO INSTITUTE’S CENTER FOR CONSTITUTIONAL STUDIES
presents the 10th Annual Constitution Day Conference

**THE SUPREME COURT: PAST AND PROLOGUE—A LOOK AT
THE OCTOBER 2010 AND OCTOBER 2011 TERMS**

Thursday, September 15 • 10:30 a.m.–7:00 p.m.

One of the premier programs we present each year, Cato’s Constitution Day Conference is a comprehensive critique of the Supreme Court’s just-concluded term, plus a look at the term ahead.

For details, plus information on the *Cato Supreme Court Review: 2010-2011*, available after September 15, go to www.cato.org/constitutionday.



Ted Galen Carpenter

Ted Galen Carpenter is a senior fellow in defense and foreign policy studies at the Cato Institute. He is the author of 8 and the editor of 10 books on international affairs, including, most recently, *Smart Power: Toward a Prudent Foreign Policy for America*.

Carpenter is contributing editor to the *National Interest* and serves on the editorial boards of *Mediterranean Quarterly* and the *Journal of Strategic Studies*. He is the author of more than 400 policy studies and articles, which have appeared in the *New York Times*, the *Washington Post*, the *Wall Street Journal*, the *Los Angeles Times*, the *Financial Times*, *Foreign Affairs*, *Foreign Policy*, the *National Interest*, *World Policy Journal*, and many other publications. He is a frequent guest on radio and television programs in the United States, Latin America, Europe, East Asia, and other regions.

Carpenter joined Cato in 1985. He has just stepped down from his longtime position as vice president for defense and foreign policy studies at the Institute.

My upbringing did not offer a hint that I would become a committed libertarian. My parents were staunch liberal Democrats who admired the socialist heritage of Milwaukee, where I grew up. My father believed that the greatest U.S. president was not George Washington or Abraham Lincoln, but Franklin Delano Roosevelt. It was an unpleasant shock to him that his youngest child became an enthusiastic high school volunteer for Barry Goldwater's presidential campaign.

My political apostasy was not just a case of youthful rebellion, though. I had read Goldwater's *Conscience of a Conservative*, and it bothered me how large and intrusive government had become. But I was not a conventional conservative on every issue. It seemed to me that conservatives were hypocritical when they criticized oppressive government but were enthusiastic advocates of censorship laws and statutes that prohibited drug use or certain types of sexual behavior.

Meeting my future wife, Barbara, at the University of Wisconsin-Milwaukee decisively shaped my ideological education. She introduced me to *Atlas Shrugged* and the other writings of Ayn Rand, which intensified both my suspicion of government and my commitment to individual liberty.

I started out as a foreign policy hawk, but two developments transformed my outlook.

One was the increasingly evident failure of the Vietnam War and the lies from military and civilian leaders that accompanied that debacle. The other was my exposure to the writings of the founders, especially Washington and Jefferson, regarding foreign policy. I began to conclude that promiscuous military interventions were inherently destructive of limited government and individual liberty.

Those views were reinforced during the pursuit of my PhD in history at the University of Texas during the mid and late 1970s. As I read the works of realist writers such as George Kennan and Walter Lippmann, and so-called isolationist figures such as William Henry Chamberlin and Charles Callan Tansill, it became apparent to me that U.S. foreign policy was badly off course.

As I became more active in the libertarian movement at the end of the decade, including joining the Texas Libertarian Party and working on Ed Clark's presidential

campaign, I decided to focus even more on foreign policy issues. There was already an impressive array of libertarian scholars and pundits on most domestic policy issues, but with the exception of Earl Ravenal and one or two others, the ranks of good libertarian foreign policy experts seemed rather thin.

Since my three-year post-doctoral research post with Lyndon Johnson's national security adviser, Walt W. Rostow (an interesting adventure), was coming to an end, I approached the Cato Institute about future plans, including a grant to write a book on how an interventionist foreign policy erodes domestic liberty. It is somewhat ironic that although I've published 18 books as a Cato scholar, I have yet to write the book that I originally proposed. It is a project to which I hope to return in the next few years.



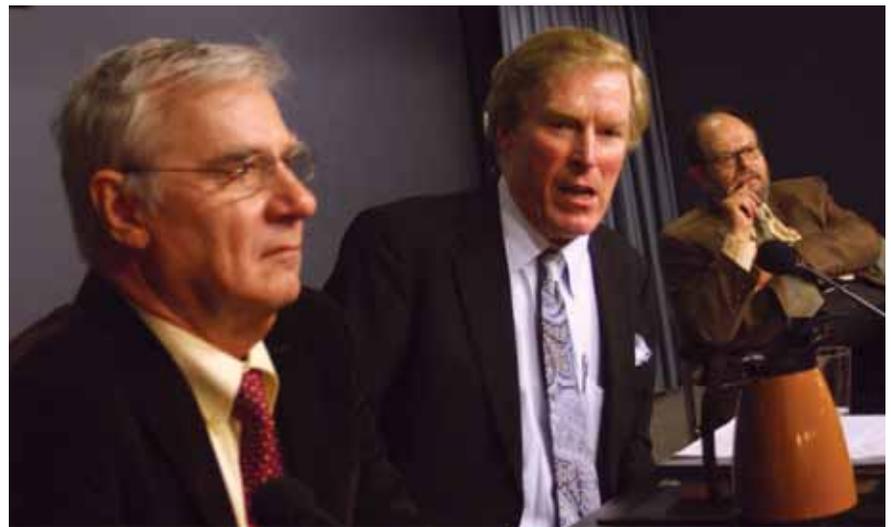
The bulk of my work now focuses on such topics as policy toward Iran and North Korea, relations with China, and the disastrous consequences of the international war on drugs. My latest book, which will appear in 2012, examines the alarming drug-related violence next door in Mexico.

My proudest achievement during the 26 years that I've worked for Cato is building a defense and foreign policy department that

achieves the highest standards for both quantity and quality of scholarship. Cato is now a major and highly respected participant in the debate about America's role in the world. Our Institute is also the brightest hope to create a foreign policy for the 21st century that is consistent with a constitutional system based on limited government and individual liberty. ■



At a Cato Institute conference in April, “The Economic Impact of Government Spending,” PHIL GRAMM (left), former senator from Texas and author of Gramm-Rudman-Hollings, was part of a distinguished lineup of legislators and policy experts. Gramm predicted a stalemate on budget talks, citing the fact that neither party is willing to deal with the problem. Sen. BOB CORKER (R-TN) (center) joined Cato senior fellow DANIEL MITCHELL (right) in diagnosing the looming fiscal crisis in more detail.



At a May 5 Cato Policy Forum ZAINAB AL-SUWAJ, executive director of the American Islamic Congress, offered observations from her recent visit to the Middle East in the wake of that region’s uprisings. “The wall of fear has been broken,” she said. “But the challenge is how to make sure it stays broken.”

Following the publication of *Climate Coup: Global Warming’s Invasion of Our Government and Our Lives*, Cato hosted a forum moderated by PATRICK J. MICHAELS (left), senior fellow at the Institute and editor of the book. BOB RYAN (center), meteorologist for WJLA/ABC 7 News and former president of the American Meteorological Society, and RICHARD LINDZEN (right), professor of meteorology at MIT, examined how climate scientists communicate with the public.



During a three-day conference for students in April, elcato.org hosted more than 60 participants from 12 Latin American countries. Held in Buenos Aires, the event was co-organized with Argentina's Fundación Libertad. Among the high-profile speakers were Peruvian scholar ALVARO VARGAS LOSA (left); Cato adjunct scholar ALBERTO BENEGAS LYNCH, JR., from Argentina (above right); and El Salvador's former finance minister MANUEL HINDS (below right).

APRIL 5: The War in Libya: What Is the Role of Congress?

APRIL 7: The Economic Impact of Government Spending

APRIL 8: Cato Institute Policy Perspectives 2011 (New York)

APRIL 13: Cato Club Naples—ObamaCare: What a Difference a Year Makes

APRIL 14: ObamaCare: What a Difference a Year Makes (Palm Beach)

APRIL 15: America's Transportation Future

APRIL 18: Civil Resistance and Revolution in the Arab World

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

APRIL 21: *The False Promise of Green Energy*

APRIL 28: *The Constitution of Liberty: The Definitive Edition*

APRIL 29: The Future of Chinese Land Rights

APRIL 29: *Free or Equal: A Personal View*

MAY 2: *Rehabilitating Lochner: Defending Individual Rights against Progressive Reform*

MAY 4: *Climate Coup: Global Warming's Invasion of Our Government and Our Lives*

MAY 5: The Arab Awakening and Its Implications

MAY 9: The Moral Implications of Deficits, Debt, and the Budget Battles Ahead

Cato Calendar

CATO UNIVERSITY SUMMER SEMINAR

Annapolis, Md. • Loews Hotel

July 24–29, 2011

Speakers include Rob McDonald, Don Boudreaux, Robert Levy, Edward H. Crane, David Boaz, Tom G. Palmer, and Lynne Kiesling.

CONSTITUTION DAY

Washington • Undercroft Theatre

September 15, 2011

Speakers include Alex Kozinski, Gregory G. Garre, Tom Goldstein, Adam Liptak, David Post, Orin S. Kerr, and Roger Pilon.

CATO CLUB 200 RETREAT

Newberg, Ore. • Allison Inn and Spa • September 22–25, 2011

MONETARY REFORM IN THE WAKE OF CRISIS

29th Annual Monetary Conference

Washington • National Housing Center

November 16, 2011

Speakers include Allan H. Meltzer, James Grant, John A. Allison, Lawrence H. White, Roger Garrison, Richard H. Timberlake, Judy Shelton, and Jeffrey Lacker.

24TH ANNUAL BENEFACTOR SUMMIT

Palm Beach • The Breakers • February 23–26, 2012

MILTON FRIEDMAN PRIZE PRESENTATION DINNER AND GRAND OPENING WEEKEND

Washington • May 4, 2012

MAY 10: *America's Allies and War: Kosovo, Afghanistan, and Iraq*

MAY 13: Why Are We at War in Libya?

MAY 16: Leashing the Surveillance State: How to Renew and Reform Patriot Act Surveillance Authorities

MAY 17: *Peddling Protectionism: Smoot-Hawley and the Great Depression*

MAY 18: The Case for Marriage Equality: *Perry v. Schwarzenegger*

MAY 20: Answering the Critics of Comprehensive Immigration Reform

MAY 25: Limiting Government: What Washington Can Learn from Minnesota

MAY 25: *Selfish Reasons to Have More Kids*

Robust debates on neoconservatism, corporations vs. the market, and more

Online Magazine Cato Unbound Features Leading Scholars

This spring the Pew Research Center released its eighth annual report on the state of American journalism. “In some ways, new media and old, slowly and sometimes grudgingly, are coming to resemble each other,” the study says. The traditional platforms of the Fourth Estate are changing, and last year, online news consumption outstripped print media for the first time in terms of both advertising revenue and readership. The tipping point has arrived. The trend line is clear. And the Cato Institute, it seems, has been ahead of the curve.

Since 2005 Cato Unbound has given readers access to a state-of-the-art virtual trading floor in the intellectual marketplace. A unique online magazine, it reflects an appreciation of the way ideas are exchanged in the digital age. Every month one of the world’s leading thinkers presents an essay on a topical issue. A panel of distinguished experts responds, each offering his case before challenging and refining the arguments in an ongoing conversation. Readers are then encouraged to join the dialogue by offering their own thoughts through websites, blogs, and letters to the editor. These contributions are pulled together into an easily accessible forum, creating a media product that is virtually distinct within the digital realm.

Yet Cato Unbound is also designed to avoid the pitfalls of its platform. For starters, the site revolves around the value of debate. All too often, the sheer availability of personalized news today allows readers to give in to confirmation bias—to seek out only the information that reinforces their existing beliefs. The internet, by any measure, caters to the obstinate. At Cato Unbound, however, contributors are forced to confront their critics, and the tendency to selectively ignore the opposition is mitigated.

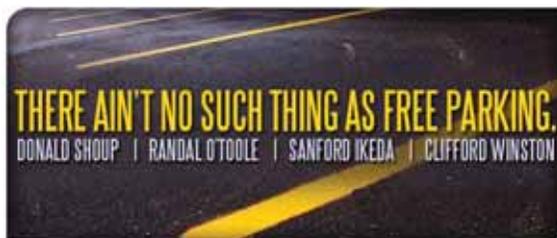
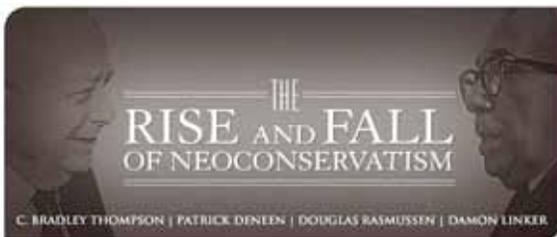
The site also hinges on the importance of perspective. The current news climate is subject to certain kinds of pressure: readers increasingly look for minute-by-minute updates. Many sites therefore suffer from a lack of depth by becoming preoccupied

with instantaneous delivery. Cato Unbound is different. “We try to step back, take a deep breath, and focus on the larger picture,” Jason Kuznicki, the site’s editor, explains.

In the latest issue, “Targeted Killing and the Rule of Law,” the editors ask whether the executive branch can lawfully kill. Lead essayist Ryan Alford, assistant professor at the Ave Maria School of Law, argues that it cannot. In fact, the “presidential death warrant” is so repugnant to our constitutional tradition, he says, that the Founders didn’t even think it necessary to make an explicit statement about the practice. At the time of the Revolution, British kings hadn’t enjoyed such a power for centuries, and it was thought to be the very antithesis of the rule of law. The distinguished panel of legal and historical experts responding to Alford includes John C. Dehn of the U.S. Military Academy at West Point, Gregory McNeal of Pepperdine University, and Carlton Larson of the University of California at Davis.

Other past issues have included

- “The Digital Surveillance State”: After September 11, the growth of the surveillance state was perhaps inevitable. In his lead essay, though, lawyer and columnist Glenn Greenwald argues that it has spiraled out of control. Respondents include law professor John Eastman, Heritage visiting fellow Paul Rosenzweig, and Cato research fellow Julian Sanchez.
- “When Corporations Hate Markets”: The idea that corporations and markets are synonymous is a grave misconception. In his lead essay, philosopher Roderick Long examines the often tangled relationship between business and government. Respon-



Since 2005 Cato Unbound has tackled a variety of issues, from the policy implications of population, to the state of neoconservatism, to the high cost of free parking.

dents include political analyst Matthew Yglesias, economist Steven Horwitz, and economist Dean Baker.

These monthly conversations have received attention from publications like the *New York Times*, the *Washington Post*, and *The Economist*. The site has featured a lineup of prominent contributors, including James M. Buchanan, the Nobel laureate and founder of the public choice school of political economy; Richard H. Thaler, professor of economics and behavioral science at the University of Chicago; James R. Flynn, a pioneer in the study of IQ; Clay Shirky, the renowned social media theorist; and Jorge Castañeda, former foreign minister of Mexico. Over the years, this forum has shown a depth of exchange and an accessible format that few other outlets offer.

An idea can be bound between covers, bound by convention, or bound for the dustbin of history. The ideas of Cato Unbound, we hope, are none of the above. ■

“He’s like Marx, only right.”

Soros, Epstein, and Caldwell Debate the Meaning of Hayek

In 1960, F. A. Hayek published an important book that acted as the positive counterpart to his more famous *The Road to Serfdom*. Whereas the latter fiercely critiqued the very idea of a centrally planned economy, the former provided his view of what should take its place. This spring, a distinguished panel convened in the Cato Institute’s F. A. Hayek Auditorium to discuss the new, definitive edition of that work, *The Constitution of Liberty*, edited by Ronald Hamowy. The panel included Bruce Caldwell, Hayek’s intellectual biographer; Richard Epstein, the brilliant legal scholar; and George Soros, the hedge-fund billionaire and founder of the Open Society Foundations.

Soros opened his talk with his own interpretation of the great economist. “Hayek is generally regarded as the apostle of a brand of economics which holds that the market will assure the optimal allocation of resources as long as the government doesn’t interfere,” Soros said. He went on to describe what he considers the two main pillars of this brand—the efficient market hypothesis and the theory of rational expectations—which, he insisted, place Hayek firmly in the dominant strain of American economics. Most label this breed the Chicago School. “I refer to it as market fundamentalism,” Soros said.

Richard Epstein did not concur. “In some sense, I’m taking exactly the opposite side of George Soros,” he said. While Soros praised Hayek’s warning “against the slavish imitation of natural science” in the social sciences, Epstein thought his ideas weren’t systematic enough. In acknowledging that they were “enormously instructive,” he ultimately concluded that those

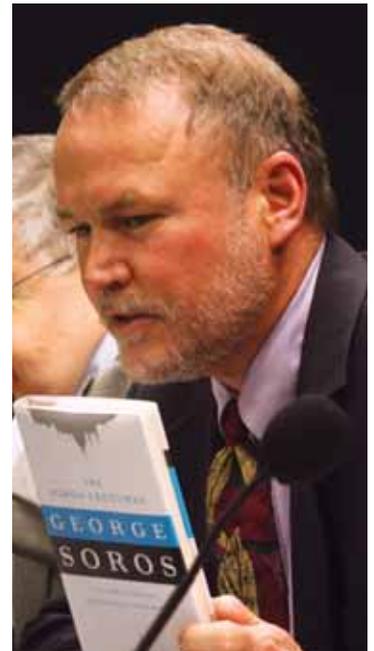
ideas were “incomplete.” Epstein argued furthermore that Hayek’s work points not to unfettered markets but to a “presumption against regulation.”

Giving voice to some of the raised eyebrows in the audience, Bruce Caldwell responded to Soros. “I think that George has a handle on some parts of Hayek, but misunderstands other parts,” he said. With a better grasp of the missing pieces, Caldwell was convinced that Soros “would identify himself, I’ll say it provocatively, as a Hayekian.” He then countered some of the billionaire’s specific claims. Hayek actually rejected the usefulness of the so-called twin pillars in “capturing the workings of the market process,” Caldwell told Soros, demonstrating that “he’s not the sort of mar-

ket fundamentalist that you’re describing. I think a pithy way of putting this is that there’s definitely a difference . . . between Chicago and Vienna.”

Continuing his earlier call for all sides to acknowledge that they only have half of the truth, Soros made some concessions. “Maybe we can find common ground,” he said. “I

Continued on page 19



A Cato Book Forum on April 28 for the new and definitive edition of *The Constitution of Liberty* by F.A. Hayek featured spirited debate among financier **GEORGE SOROS**, legal scholar **RICHARD EPSTEIN**, and *Hayek Collected Works* editor **BRUCE CALDWELL**. The new edition, edited by Cato fellow Ronald Hamowy, is published by the University of Chicago Press.



At the *Constitution of Liberty* event Cato senior fellow **RICHARD RAHN** (right) talked with former Virginia governor **JIM GILMORE**, now president of the Free Congress Foundation.

Immigration Reform: Answering the Objections

“The primary arguments employed against comprehensive immigration reform do not stand up to a review of recent history and predictable social and economic behavior,” writes Stuart Anderson in “**Answering the Critics of Comprehensive Immigration Reform**” (Trade Briefing Paper no. 32). Still, “the best approach for supporters of comprehensive immigration reform is to take seriously the arguments of critics, explain why these arguments are incorrect and, if necessary, adapt legislation to address the concerns raised.” Anderson, an adjunct scholar at the Cato Institute, executive director of the National Foundation for American Policy, and the author of *Immigration* (2010), presents the five main arguments against liberalizing immigration policy and shows that they simply don’t work. Will immigration reform harm taxpayers? No, Anderson writes. Instead, it will raise the wages of once-illegal workers and, thus, tax receipts. Will it burden welfare rolls? Again, no. “The data indicate that immigrants are not over-

whelming users of welfare programs.” Will an amnesty program lead to more like it? Not at all, because legalization is not the same as amnesty. Will more immigrants undermine the English language? No. Anderson notes that “91 percent of second-generation children from Latino immigrant families and 97 percent from the third generation said they speak English very well or pretty well.” Finally, will increased immigration hurt American workers? Anderson addresses this concern by pointing out that “an important reason why immigration is beneficial is that it encourages a more productive use of human capital in the U.S. economy.” He argues that the status quo is not acceptable. Instead, “the best approach is to harness the power of the market to allow workers to fill jobs legally, rather than to rely on human smuggling operations for workers to enter the United States.”

The Sun Never Sets on the Patriot Act

“It has become commonplace over the last decade to speak of the need to balance pri-

vacy and security interests,” Cato research fellow Julian Sanchez observes. In the years since the USA Patriot Act was approved, the debate surrounding this tradeoff has been contentious to say the least. However, in “**Leashing the Surveillance State: How to Reform Patriot Act Surveillance Authorities**” (Policy Analysis no. 675),



Sanchez argues that these interests are not inherently in conflict. In fact, the provisions of the Patriot Act he considers “impose heavier burdens on core privacy, speech, and association interests than is necessary to the protection of national security.” In a broad analysis, Sanchez considers several parts of the act—namely, the roving wiretap authority, the “Section 215” orders, and the Lone Wolf provision—exploring their historical precedents and deviations therefrom. He argues for relatively minor adjustments, from

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enforcing sunsets to pressing for additional scrutiny. Most importantly, he calls for the scope of National Security Letters to be narrowed. “There is no legitimate reason to indefinitely retain detailed information about tens of thousands of Americans who are not suspected of involvement in terror or espionage,” he writes. Sanchez acknowledges the climate of fear and uncertainty that vindicated these expanded powers in the first place. “Now, with the benefit of a decade’s experience,” he concludes, “we have the opportunity to do better.”

Development Tax Scams

Politicians often find creative ways to finance their spending habits. In **“Crony Capitalism and Social Engineering: The Case against Tax-Increment Financing”** (Policy Analysis no. 676), Cato Institute senior fellow Randal O’Toole details one increasingly popular method. Tax-increment financing (TIF) is a mechanism that uses taxes generated from new developments to subsidize those same developments. Yet, far from achieving its stated purpose of economic improvement, TIF is often employed to capture scarce tax dollars otherwise intended for schools, libraries, fire departments, and various urban services. Indeed, “most cities can use TIF to increase their rev-

enues at little political cost,” O’Toole writes. Often, this money is then funneled into favored projects, which range from shopping malls to sports stadiums to the



latest fads in urban planning. “No matter how well-intentioned, city officials will always be tempted to use TIF as a vehicle for crony capitalism, providing subsidies to developers who in turn provide campaign funds to politicians,” he writes. O’Toole examines the mechanisms of TIF, tracing the circumstances of its origin and the politics behind its abuse. Ultimately, he concludes, it is little more than an instrument of collusion between market players and an increasingly powerful government—one that should be repealed rather than reformed.

Dumping on Exports

“The president exhorts U.S. exporters to ‘win’ a global race,” writes Daniel Ikenson, associate director of trade policy studies at the Cato Institute, “yet he ignores the fact that the government’s hodgepodge of rules and regulations has tied their shoes together.” In **“Economic Self-Flagella-**

tion: How U.S. Antidumping Policy Subverts the National Export Initiative” (Trade Policy Analysis no. 46), Ikenson identifies a glaring oversight in the centerpiece of this administration’s trade agenda. The National Export Initiative (NEI), which seeks to double exports by 2014, fails to include sensible reforms to the 90-year-old antidumping law. This omission “erodes the competitiveness of U.S. firms.” By restricting access to imports, the law raises the cost of raw materials for many downstream companies, thereby squeezing their profits and elevating foreign competition. The administration, in other words, is undermining its own initiative. “In countless ways, the antidumping status quo subverts the goals of the NEI and is an albatross around the neck of the U.S. economy,” he writes. Ikenson proposes several modest but meaningful reforms, which include granting legal standing for the consuming industries, requiring a public-interest test, and applying a lesser-duty rule. In the end, he raises the curtain on the antidumping regime, revealing how the idealized imagery surrounding the law conceals the real story. Antidumping is often misconstrued as a dispute between patriotic American producers and predatory foreign traders. “The battle is better characterized as ‘we against us,’” he writes. ■

Continued from page 17

think that we would all agree that government regulation is a necessary evil... so if you can avoid regulations, you should.” Many observers picked up on Soros’s criticisms of the less-than-savory political and legislative processes that produced the recent health care and financial-reform bills. In the end, the discussion was both provocative and civil.

The event mirrored a long-standing debate over the great economist’s influence. Last year, Kate Zernike wrote in the *New York Times* that Tea Party activists were resurrecting “long-dormant ideas [found in] once-obscure texts by dead writers.” She was referring, of course, to writers like Hayek. But she may have sold him short.

This is the same man, after all, who won the Nobel Prize in Economics in 1974. Years later, he met with President Reagan at the White House. He also met with Margaret Thatcher, who, in reference to *The Constitution of Liberty*, declared: “This is what we believe.” Hayek was described by Milton Friedman as “the most important social thinker of the 20th century” and by White House economic adviser Lawrence H. Summers as the author of “the single most important thing to learn from an economics course today.” He was the mind behind *The Road to Serfdom*, a book that has never gone out of print and, in fact, sold over 100,000 copies last year alone. Cato is proud to note that, in the last years of his

life, Hayek became a distinguished senior fellow at the Institute.

But even that doesn’t do him justice. “On the biggest issue of all, the vitality of capitalism, he was vindicated to such an extent that it is hardly an exaggeration to refer to the 20th century as the Hayek century,” John Cassidy once wrote in the *New Yorker*. Hayek, however, was much more than an economist. He also published impressive works on political theory and psychology. He embodied the type of intellect that influenced disciplines across the spectrum, remaining relevant long after his own lifetime.

As executive vice president David Boaz wrote on Cato@Liberty, “He’s like Marx, only right.” ■

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“To Be Governed...”

THOSE WHO CAN'T, TEACH

Financial Literacy: The Federal Government's Role in Empowering Americans to Make Sound Financial Choices

—GAO Report, April 12, 2011

ANOTHER BRIGHT IDEA

“The government has no business telling an individual what kind of light bulb to buy,” [Rep. Michele] Bachmann said in a statement last week.

Consumers Union respectfully disagrees, a point we made formally today in a letter to the U.S. Energy and Natural Resources Committee.

—ConsumerReports.org, March 9, 2011

JUST ANOTHER DAY IN THE WASHINGTON NEWS

Critics in Congress also have questioned Amtrak's management, asking, for example, how an employee with a \$21,000 salary earned \$149,000 in overtime last fiscal year.

—Washington Post, May 15, 2011

The federal government's largest housing construction program for the poor has squandered hundreds of millions of dollars on stalled or abandoned projects and routinely failed to crack down on derelict developers or the local housing agencies that funded them.

—Washington Post, May 15, 2011

The main thing learned in the hearings so far is that [D.C. mayor Vincent] Gray showed bad judgment in allowing [three close aides] to guide so much of the hiring for patronage jobs just below the cabinet rank. Although all three advisers were longtime personnel execu-

tives, they blundered repeatedly by overpaying people, doing inadequate vetting and hiring children of officials.

—Robert McCartney, Washington Post, May 15, 2011

HIS ROYAL HIGHNESS PRINCE CHARLES, TO HIS FORMER SUBJECTS WHO ARE EATING TOO WELL

Nobody wants food prices to go up, but if it is the case that the present low price of intensively produced food in developed countries is actually an illusion, only made possible by transferring the cost of cleaning up pollution or dealing with human health problems onto other agencies, then could correcting these anomalies result in a more beneficial arena? . . .

Critically, such a new Washington consensus might embrace the willingness of all aspects of society—the public, private and NGO [nongovernmental organizations] sectors, large corporations and small organizations—to work together to build an economic model built upon resilience and diversity.

—Washington Post, May 10, 2011

POLITICIANS: YOU'VE GOT TO KEEP AN EYE ON THEM EVERY MINUTE

Ohio has launched what appears to be the biggest intervention in the private economy by a state government since at least the Great Depression, according to a USA TODAY review of historical data. The state is preparing new industrial parks and high-tech office buildings; loaning money and giving grants to businesses; and subsidizing clean energy, websites, nanotechnology and warehouses, among other things.

—USA Today, April 26, 2011

EXCEPT MAYBE FOR THOSE SOCIAL CONSERVATIVES WHO GOT A “D” ON CATO'S FISCAL POLICY REPORT CARD

All social conservatives I know are also fiscal conservatives. Not necessarily the other way around.

—Gov. Mike Huckabee, Fox News, May 15, 2011

DEATH BY DECORATOR

Florida is one of only three states that require commercial interior designers to become licensed before they hang a single painting in an office building, school or restaurant. A bill making its way through the state legislature, however, would deregulate the occupation, along with more than a dozen others, including yacht brokers and hair braiders.

That possibility has the state's licensed interior designers ruffled. They've hired Ron Book, one of the state's most influential lobbyists, to fight the bill. And they've stormed legislative hearings to warn of the mayhem that would ensue if the measure passes.

Among the scenarios they've conjured: flammable carpets sparking infernos; porous countertops spreading bacteria; jail furnishings being turned into weapons.

—Wall Street Journal, April 15, 2011

USING TAXPAYERS' MONEY TO LOBBY FOR MORE OF IT

National Public Radio (NPR) is paying the lobbying firm Bracy, Tucker, Brown & Valanzano to defend its taxpayer funding stream in Congress, according to lobbying disclosure forms filed with the Secretary of the Senate.

—Daily Caller, May 5, 2011