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The Philanthropic Illusion

"He Has a Thousand Dollars!"

The financial system of modern government is staggeringly complicated. It imposes scores of taxes that create direct and indirect burdens on hundreds of millions of taxpaying individuals and organizations, and it has thousands of different kinds of benefits that it gives to those same hundreds of millions. If anyone were to attempt to draw up a chart of all the connections in government's tax-and-spend arrangements he would need a sheet of paper larger than an Idaho county, and he would not finish drafting even a corner of this chart in his lifetime.

Because we cannot grasp government's financial system in all its complexity, we reach for analogies or simplifications based on obvious features. The first feature one is apt to notice about government is that it has money—lots of it. Government seems to be a fabulously wealthy entity that can—if its heart is in the right place—shower wealth on worthy causes and needy individuals. Years ago, when my daughter Ellen was five and just beginning to grasp the meaning of the word *money,* I asked her, "Ellen, should the government give money to poor people who don't have any?"

She thought very hard about this as she tried to fit novel concepts together. Her eyes finally lit up as an answer clicked into place. "Yes," she exclaimed, "because he has a thousand dollars!"

She saw government as a fabulously wealthy person ($1,000 was the largest sum she could imagine), and, applying the principle of sharing that she had been taught, she reasoned that "he" should therefore share his excess wealth with the less fortunate. Ellen was a victim of the *philanthropic illusion: the idea that government has money of its own.* Those who accept this premise will consider government payments to nice-seeming causes helpful. If you ask them whether government should promote the arts or help education or support science, their answer will be an unhesitating "yes."

The problem is that government does not have any money of its own. Any money that it has to spend has first to be taken away from a nation's citizens, and this process of taking injures the people and the activities forced to give up the funds. Government taxation takes money away from the arts, away from education, and away from science. Once you realize that government's giving has to be counterbalanced by taking, you become much less enthusiastic about government spending programs.

I believe that when most young people first contemplate the political realm, they begin with Ellen's perspective of government as a generous philanthropist capable of helping good causes and needy individuals. As they mature, this perspective becomes overlain by more sophisticated ideas. They notice that government raises money through taxes, and they become aware that they pay taxes. For many people, however, the philanthropic illusion is not fully overcome and consciously discarded. It remains lodged in their thinking, giving them a falsely positive view of government spending programs.

A number of complexities and confusions concerning government finance keep many people from clearly grasping the connection between government's nice-seeming giving and its harmful taking. One problem is that most people are not aware of the full burden of taxation as it falls on them and on causes they consider worthy. There are many different taxes, and most of them are paid in small and often unnoticeable ways. The telephone tax, for example, just seems to be a part of the phone bill. A gasoline tax is part of the cost of filling up. A sales tax on purchases is either unnoticed or seems small in most instances. The wage tax (Social Security and Medicare) is made to seem half as large as it actually is by having employers appear to pay half of it. Also, the use of the tax withholding system reduces the awareness of income tax payments.

Furthermore, much of the burden of taxes is born indirectly: it is passed on to someone else in the form of a higher price. For example, when a business pays the telephone tax, that amount simply becomes an expense to be passed along to consumers in higher prices. The property tax is shifted into rents. A person who does not own property still pays the property tax: it enters as a cost factored into his rent payment.

Corporation taxes, imposed by both the federal government and state governments, are perhaps the most poorly understood levies. The public believes that they are being paid by distant, impersonal entities and therefore assumes that these taxes do no harm to ordinary people. In fact, a corporation is a legal fiction, and all taxes levied on it must be borne by the human beings connected with the corporation. The burden of the corporation tax is shifted to its customers in the form of higher prices for the product the corporation produces, to its workers in the form of lower wages than they would otherwise have, and to its stockholders in the form of lower returns than would otherwise occur.

Because of the complexity and obscurity of taxes, most people do not have a clear idea of the total amount of money government is taking away from them. When they get a check from the government, they believe they have benefited and praise government for its intelligent generosity. They are not aware that in a thousand unnoticed ways they may have sent ten times that amount to the government in taxes. The situation is not unlike a stealthy cat burglar who sneaks into your bedroom and extracts bills from your wallet. He is careful not to take so much that you clearly notice the loss, and on the first Sunday of each month he comes to your door and gives some of the money back to you. You thank him for his generosity, and tell your neighbors that the world would be a better place if there were more people like him.

Some people disguise the philanthropic illusion through subjective perceptions of government's burdens. Because government's direct and indirect financial burdens are so difficult to grasp, the confusion allows observers to assume that government takes money only from people who don't need it or who don't deserve it. Some years ago, I interviewed a number of congressmen about fiscal policy, asking each one whether he was aware that the taxation to raise money for the spending programs he favored might be harming the very citizens he was trying to help. Not one of them could face this possibility. Congressman Joe Skeen, Republican from New Mexico, gave a typical answer:

> Q: How do you answer the point that even in the case of worthwhile programs, the money for them is being taken away from other people who had other uses for it?
> CONGRESSMAN SKEEN: Who are they?
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> Q: Maybe they even wanted to feed their families, you could say? *(Congressman looks puzzled)* I mean, as taxpayers?
> CONGRESSMAN SKEEN: *(Flustered)* The effective level of removal from that area . . . there is nothing . . . if it were threatening the food, the clothing, the shelter areas, I would say that *any* government expenditure would be under serious scrutiny. But it doesn't affect that level.

Skeen had apparently never seriously considered that the taxation to pay for spending programs might do significant harm. When presented with this idea, he rejected it on the entirely subjective assumption that needy people don't bear any of the burden of taxation. This assumption is silly. It is a mathematical certainty that people deemed in need of food, clothing, and shelter are having money taken away from them through the direct and indirect operation of the tax system to the tune of thousands of dollars a year. What Skeen ought to have said is, "Yes, I know we're taking money away from them, but I hope we're giving them back more than we are taking away."

It is wrong, therefore, to view government services, payments, and subsidies as simple benefits that make a country a better place. One has to factor in the harm inflicted by raising the funds to pay for those benefits. Taxes drain resources from idealistic charities, innovative companies, educational institutions, art galleries, book publishers, and practically every other worthwhile human activity. Government takes money away from the poor it claims to feel sorry for. A study of minimum-wage workers in Portland, Oregon, found that the direct and indirect burden of taxes on these workers was $3,905 per year, or 40 percent of their total effective income.

Painter Donald Baechler is a prosperous, highly regarded artist who sells several hundred thousand dollars of his art around the world each year. In 1989, government officials decided he deserved a $15,000 subsidy from the National Endowment for the Arts (NEA), the idea being to "help" art. Unfortunately, this money didn't come from the sky. Baechler commented to the *Wall Street Journal,* "I paid about a quarter of my taxes with my NEA grant." So, with one hand government helped Baechler with its arts subsidy, and then with the other it turned around and took four times as much money away.

Commentators in the media reinforce the philanthropic illusion by the way they report on government spending programs. Reporters seldom connect the presumed good of a spending program with the actual harm inflicted by taking money away from people to pay for it. The politician who urges more spending on social programs is called "compassionate," whereas the politician who opposes this spending is called "heartless." A reporter who transcends the philanthropic illusion could point out that the lawmaker who opposed the subsidy is defending all the artists, poor people, homeowners, and so on who would be forced to pay taxes for the program.

Fairy tales about kings and queens encourage the illusion of free government wealth. Consider King Wenceslas, the "good" king in the popular Christmas carol who "looked out on the feast of Stephen" and saw an impoverished peasant. Wenceslas and his page took food to the peasant, and for his benevolence, the king acquired such a heated aura of saintliness that his footsteps melted snow! It is eloquent testimony to the strength of the philanthropic illusion that no one asks the critical question about King Wenceslas: Where did he get what he gave away? Everyone seems content to assume that he gave away his personal property.

If the king had been an ordinary person, working as a farmer or a woodcutter to earn his money, then giving alms would indeed have been an act of generosity. But kings do not get their wealth by selling something of value. What supports a monarch and his castles, stables, banquets, and page boys is taxes. Kings send their soldiers around to farms to force the peasants to give up chickens, corn, and cattle. Indeed, the peasant whom the king saw that night had probably been impoverished by the king's own taxation! So Wenceslas was just giving back a portion of what he had already taken away. Yet our culture immortalizes him in a holiday song that makes him a saint of compassion.

Faulty Economic Theories

Two of the most commonly heard arguments in support of government spending programs are outgrowths of the philanthropic illusion: that spending "puts money in circulation" and that it "creates jobs." Both are fallacious because they assume a source of wealth outside the economy. Whatever money the government