

From the Politics of Illusion to the High Cost of Regulation
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John Maynard Keynes, without doubt the most prominent economist of the 20th century, wrote in 1936 “practical men are usually the slaves of some defunct economist.” Many people have debated what Keynes meant and the significance of his claim. What is clear in any case is that there are many instances where the writings of some defunct economist cast strong illumination on practical affairs.

One such defunct economist is the Italian Amilcare Puviani, who in 1903 published *The Theory of Fiscal Illusion*. While this book has never been translated into English, its teachings are on display throughout the world of practical politics. Puviani asked a simple question: how can a politician best use his powers of the purse to promote his political projects?

The success of a politician’s activities and projects will depend on the skill with which he uses his budgetary tools. With respect to public spending, Puviani explained that the ambitious politician should seek to magnify the public’s perception of benefits. He should strive to take credit whenever possible, regardless of the merits of his claim. For instance, if crime rates go down he should take credit. He should do this even if the fall in crime was a natural result of the population’s getting older, and had nothing to do with the politician’s own policies and programs.

Puviani gave most of his attention to taxation. It is here where the term fiscal illusion derives its meaning. The politician should make taxes appear to be less of a burden than they really are. Through fiscal illusion, the real burden of a

tax is made to seem lighter than it truly is. As a result, taxpayers will put up with larger budgets than otherwise, and will support a politician whom otherwise they might have opposed.

The most direct and truthful way of taxing people is to send them monthly bills, much as we pay for our utilities. Politicians never do this. We don't get a monthly bill for government. Income taxes are withheld even before we receive our paychecks. Moreover, we don't pay one tax. We pay dozens of individually smaller taxes, and in many different ways. We pay income taxes, social security taxes, medicare taxes, death taxes, business taxes, tobacco taxes, sales taxes, and excise taxes, just to name some of the more prominent categories. The only tax that is paid in similar fashion to a utility bill is the real property tax, and many people pay this tax through an escrow account. That the property tax generally ranks low in popularity is an observation that Puviani would have understood.

One place where the politics of illusion works particularly strongly is in supporting the high cost of regulation. Regulations and their costs are spread over thousands of products and activities. There are regulations about the amount of gasoline cars can use, which makes cars more costly and increases accident damage. The Department of Energy has announced regulations that will increase the cost of washing machines by about 50 percent and the cost of home air conditioners and heat pumps by several hundreds of dollars per unit. The ergonomics rules that the Occupational Health and Safety Administration recently postponed would increase business costs by many billions of dollars per year.

The Competitive Enterprise Institute <www.cei.org> estimates that federal regulations cost around \$700 billion per year. This is about \$2,500 per American. The problem is that we are no more presented with a single regulatory measure whose cost we must bear than we are presented with a single tax for which we must write a check. Regulations and their costs are spread over thousands of products and activities. Regulations are like many small excise taxes, and are an excellent application of Puviani's approach to fiscal illusion. The bill for regulation is not presented directly in one lump sum. It is presented indirectly and in hidden fashion, and is presented in many small pieces.

Yet we should never forget that regulation is just another form of taxation. Anything that can be accomplished through taxation can be accomplished through regulation, and vice versa. For instance, a school district could reduce its taxes simply by requiring parents to send their children to approved schools. The net effect, however, would be pretty much the same, whether schools are financed by taxes and provided free of direct charge, or whether parents are required to send their children to approved schools. As a first approximation, taxation and regulation are simply different means for accomplishing the same thing: government control over the use of resources in society. Our true tax burden is really a compound of taxes plus regulations.