The Fraudulence of "Waste, Fraud and Abuse"

PAUL KRUGMAN

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This newsletter will be a lot wonkier than my Times column, and usually wonkier than my old Times newsletter. Definitely snarkier than either. I'll try to stay fairly accessible, but may at times revert to academic-economist mode.

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And with that, let's get going.

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History repeats itself, the first time as farce, the second as clown show

PAUL KRUGMAN

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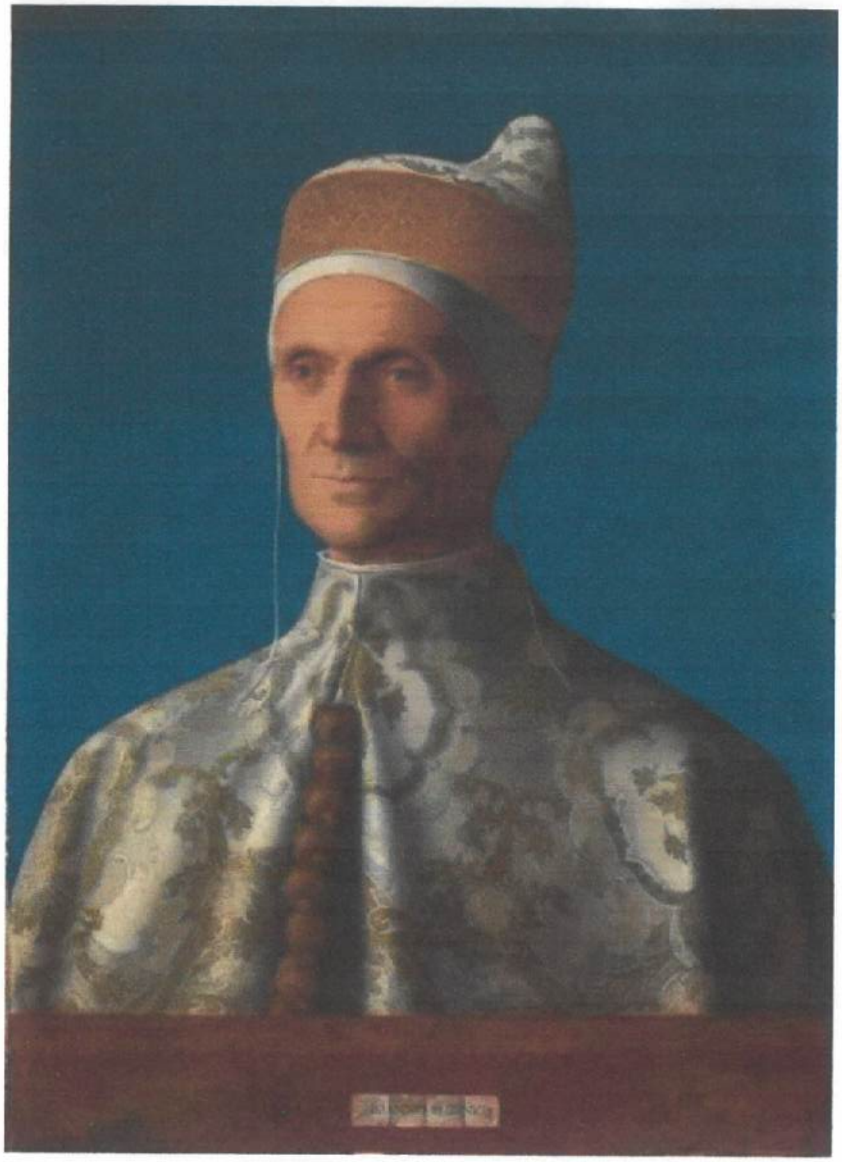


Once upon a time a Republican president, sure that large parts of federal spending were worthless, appointed a commission led by a wealthy businessman to bring a business sensibility to the budget, going through it line by line to identify inefficiency and waste. The commission initially made a big splash, and there were desperate attempts to spin its work as a success. But in the end few people were fooled. Ronald Reagan's venture, the [President's Private Sector Survey on Cost Control] — the so-called "Grace commission," headed by J. Peter Grace — was a flop, making no visible dent in spending.

Why was it a flop? There is, of course, inefficiency and waste in the federal government, as there is in any large organization. But most government spending happens because it delivers something people want, and you can't make significant cuts without hard choices.

Furthermore, the notion that businessmen have skills that readily translate into managing the government is all wrong. Business and government serve different purposes and require different mindsets.

In any case, the Grace commission's failure taught everyone serious about the budget, liberal or conservative, an important lesson: Anyone who proposes saving lots of taxpayer money by eliminating "waste, fraud and abuse" should be ignored, because the very use of the phrase shows that they have no idea what they're talking about.

OK, you know where this is going. There's an obvious parallel between the Grace commission and Donald Trump's Department of Government Efficiency, DOGE, led by Elon Musk and Vivek Ramaswamy. (The picture above is Leonardo Loredan, doge of Venice from 1501 to 1521, painted by Bellini.) But there are differences too: Muskaswamy bring a level of arrogant ignorance and clownish amateurishness that Grace never came close to emulating.

Grace, after all, assembled a staff of nearly 2,000 business executives divided into 36 task forces, who spent 18 months on the job, although they mostly came up empty. So far, at least, Muskaswamy don't seem to be doing anything besides credulously scooping up random posts from social media.

Oh, and putting supervision in the hands of [Marjorie Taylor Greene] won't help.

That said, there's a pattern in their pronouncements so far, which I'd describe as Willi Sutton (the man who robbed banks because "that's where the money is") in reverse: going where the money isn't.

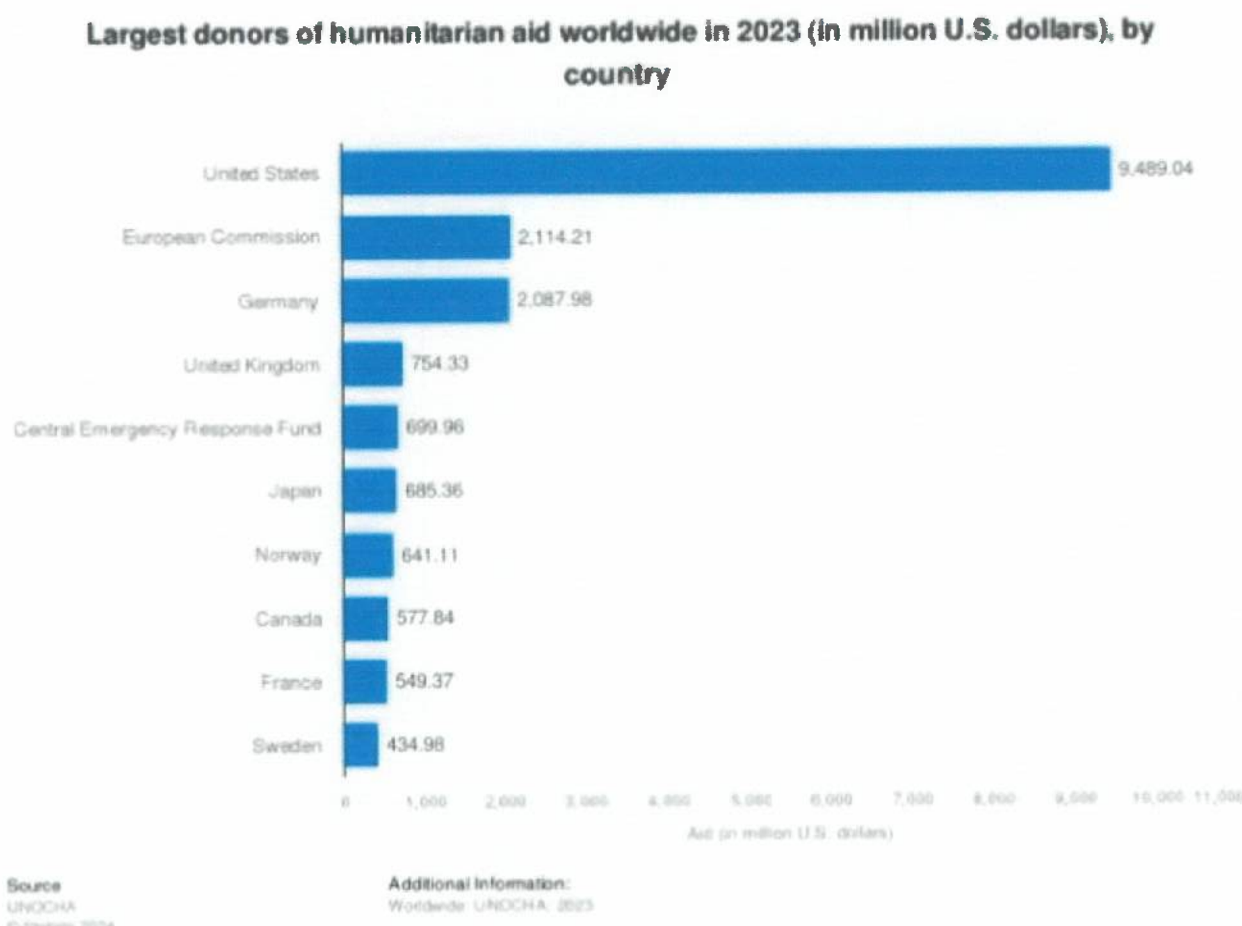
One of the first posts on DOGE's Twitter account (of course it has a Twitter account) makes a classic, maybe *the* classic rookie error when talking about the federal budget, imagining that foreign aid is a significant expense:

Department of Government Effi...
@DOGE

Follow

The United States gives more in aid to foreign countries than the next 9 countries combined.

Where exactly is that money going and how is it being spent?

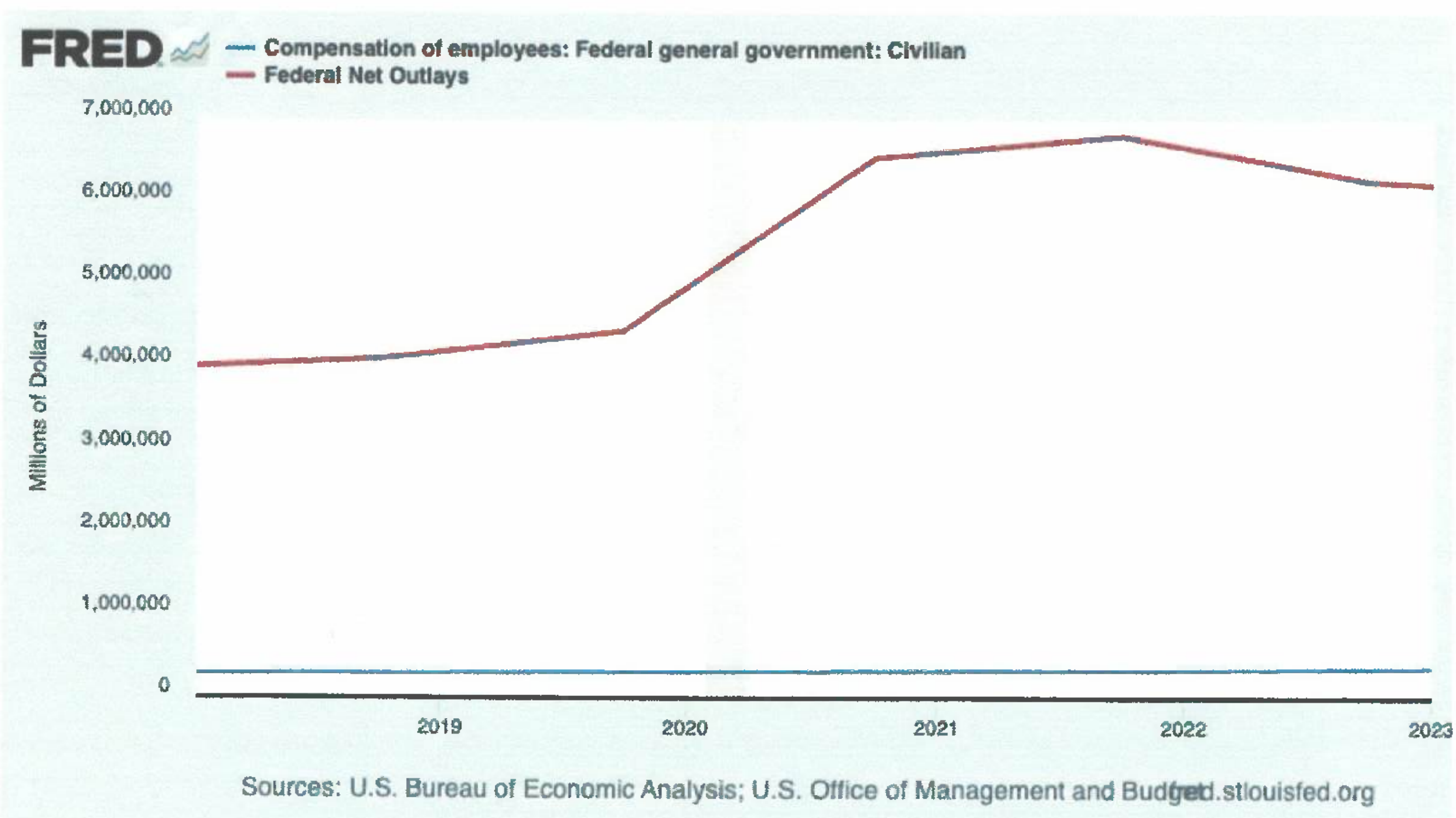


12:26 PM · 12/7/24 · **281K** Views

Surveys consistently show that the public believes that foreign aid is around 25 percen of federal spending. But self-proclaimed budget experts should be aware that this is completely wrong; the true number is actually less than 1 percent.

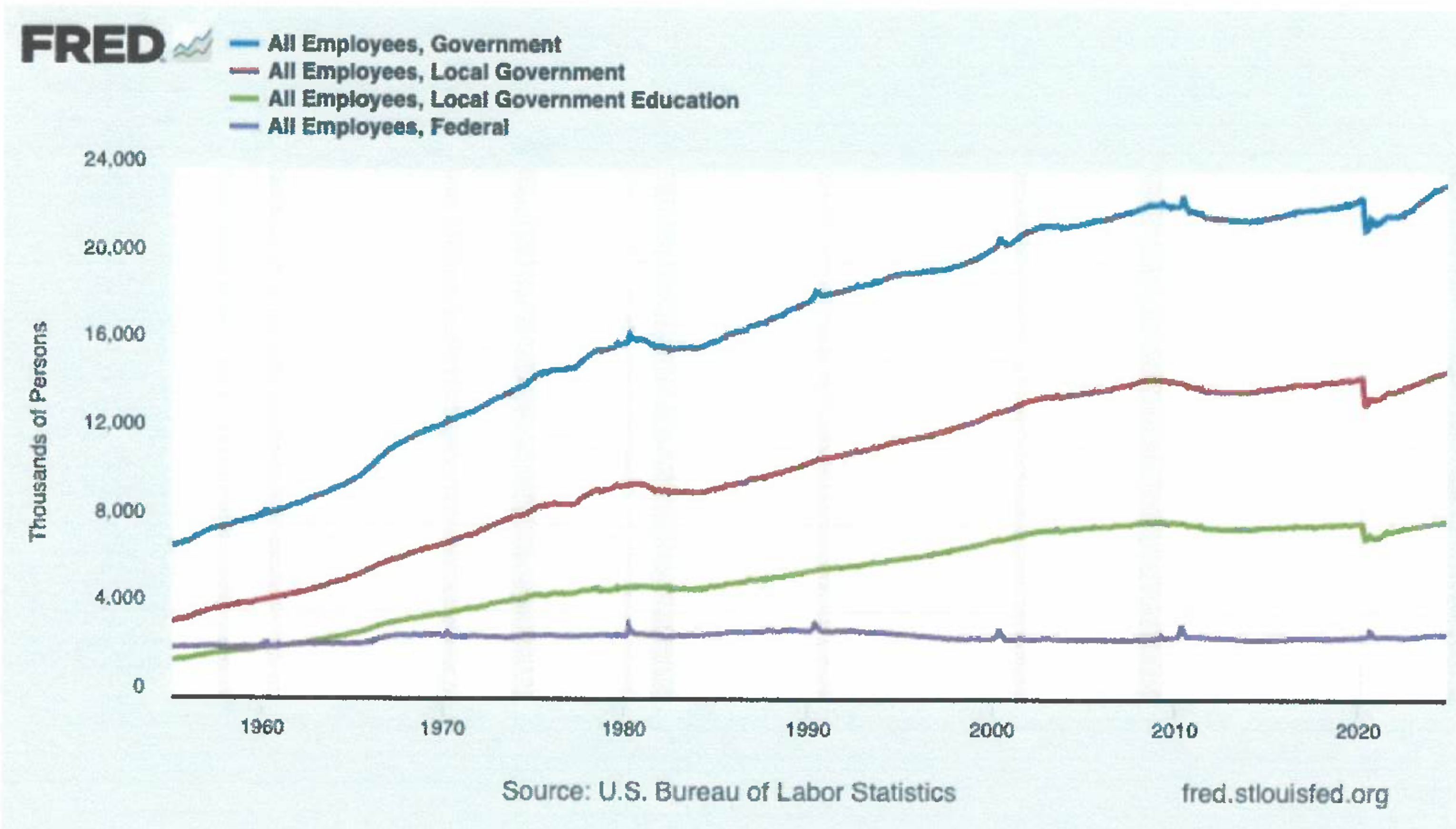
Furthermore, whoever posted that chart didn't bother to read the label. It's not a chart of total foreign aid, just humanitarian aid — which is about *one-sixth of one percent* of federal spending. Overall, by the way, America spends a smaller percentage of GDP or foreign aid than the average advanced nation.

Moving on: In what I guess we should consider their opening manifesto, published in the Wall Street Journal, Muskaswamy call for "mass head-count reductions across the federal bureaucracy." This suggests that they believe that bloated payrolls are a major budget issue. But how big a factor is employee compensation in federal spending? This big:



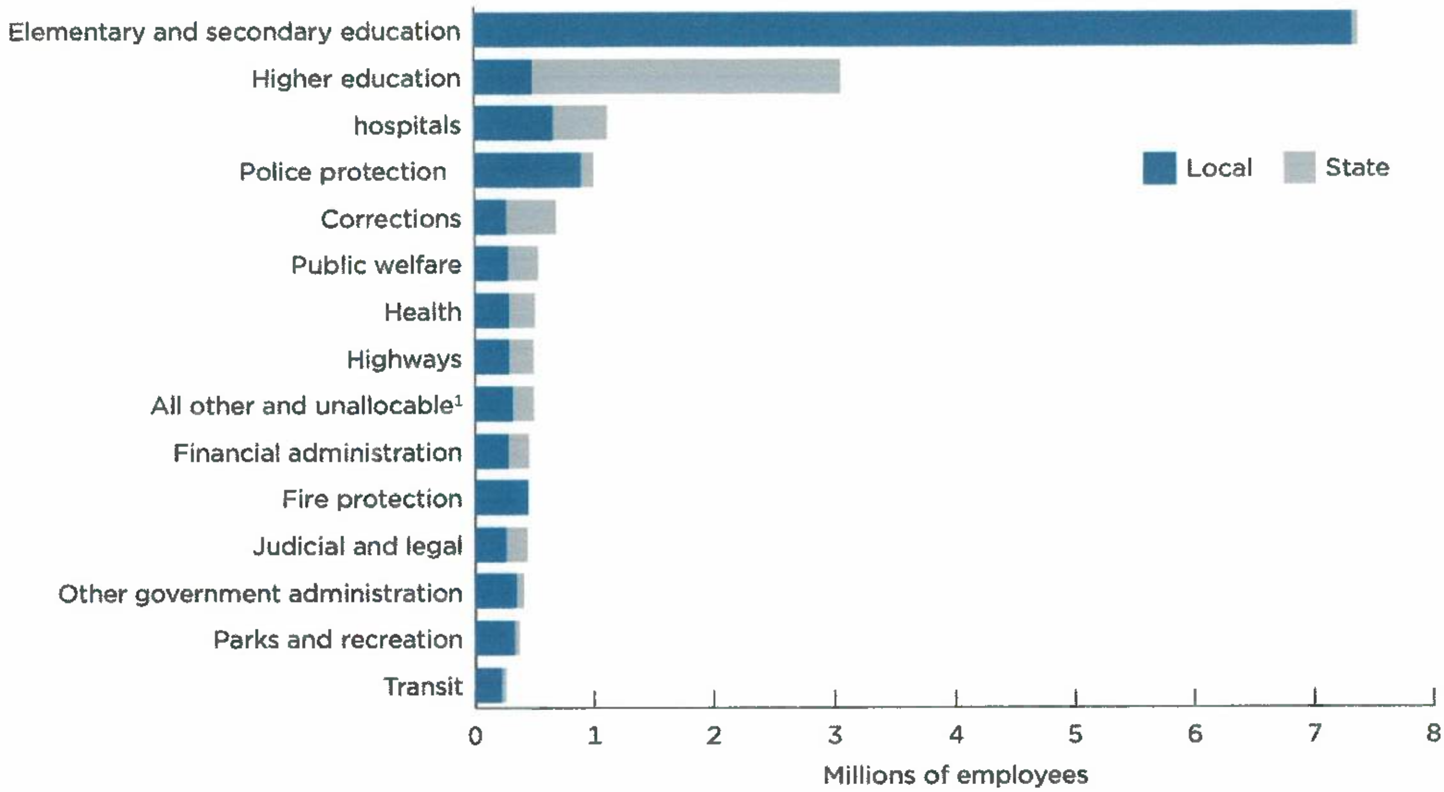
Again, going where the money isn't.

But wait: aren't there tens of millions of Americans employed by the government? Yes there are — but they overwhelmingly work for state and especially local governments, not the federal government DOGE is supposed to be tackling. In fact, federal employment is about the same now as it was in the 1950s:



What are all those state and local workers doing? The Census offers a very useful chart:

Figure 1.
Top 15 Functions: Total Government Employment



The lion's share of state and local employment is in education. Much of the rest is either in hospitals and other health care or in law enforcement. So when someone says "government worker" you shouldn't imagine a paper-pusher in a cubicle — I mean, the government, like the private sector, does have lots of guys in cubicles, but they aren't the typical employee. You should instead picture a schoolteacher, or maybe a nurse or a police officer.

But if the federal government doesn't employ all that many people, why does it spend so much money? The answer — which, again, anyone who has paid the least attention to the subject knows, but Muskaswamy apparently don't — is that the federal government is basically an insurance company with an army. Nondefense spending is dominated by Medicare, Medicaid and Social Security, with relatively small additional amounts for other safety-net programs like food stamps and health insurance subsidies.

Are these programs efficient? In the case of Social Security, the answer is a flat yes: it simply sends out checks, with very low overhead and very little fraud. (Not zero fraud: a few years ago someone managed to impersonate me and collect checks for a few months. But the Social Security employees who helped me resolve this were incredulous, because this almost never happens.)

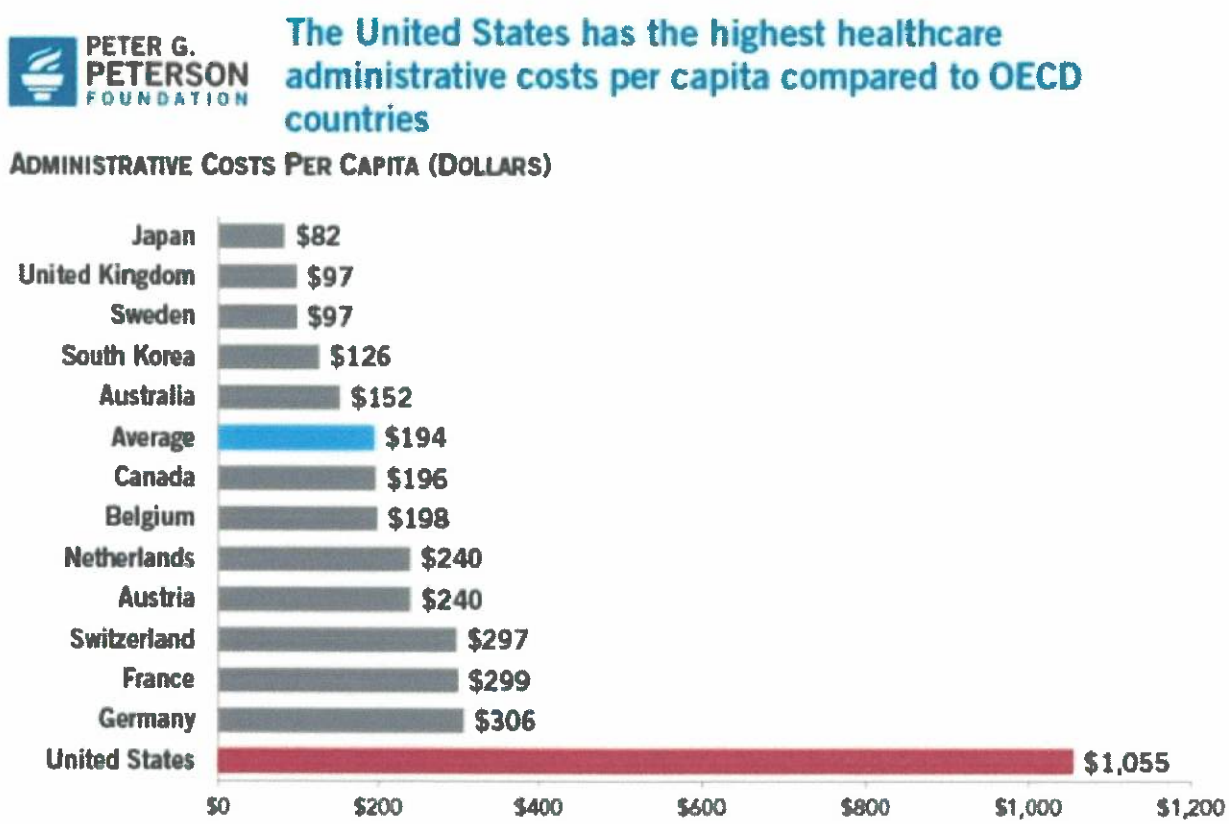
Health care is a more complicated story; there are some real inefficiencies in our system. But Musk seems to have the nature of these inefficiencies completely backwards:

Elon Musk @elonmusk · Follow

Shouldn't the American people be getting getting their money's worth?

The Rabbit Hole @TheRabbitHole84

The United States has the highest healthcare admin costs (per capita) compared to OECD countries.



Yes, American health care has uniquely high administrative costs. But Musk pretty clearly imagines that these costs reflect *government* inefficiency, when the real reason health care in America involves so much bureaucracy is the exceptional degree to which we rely on private insurance companies. Comparing administrative expenses fo public and private insurance is tricky, but there's no question that they're much highe in the private sector.

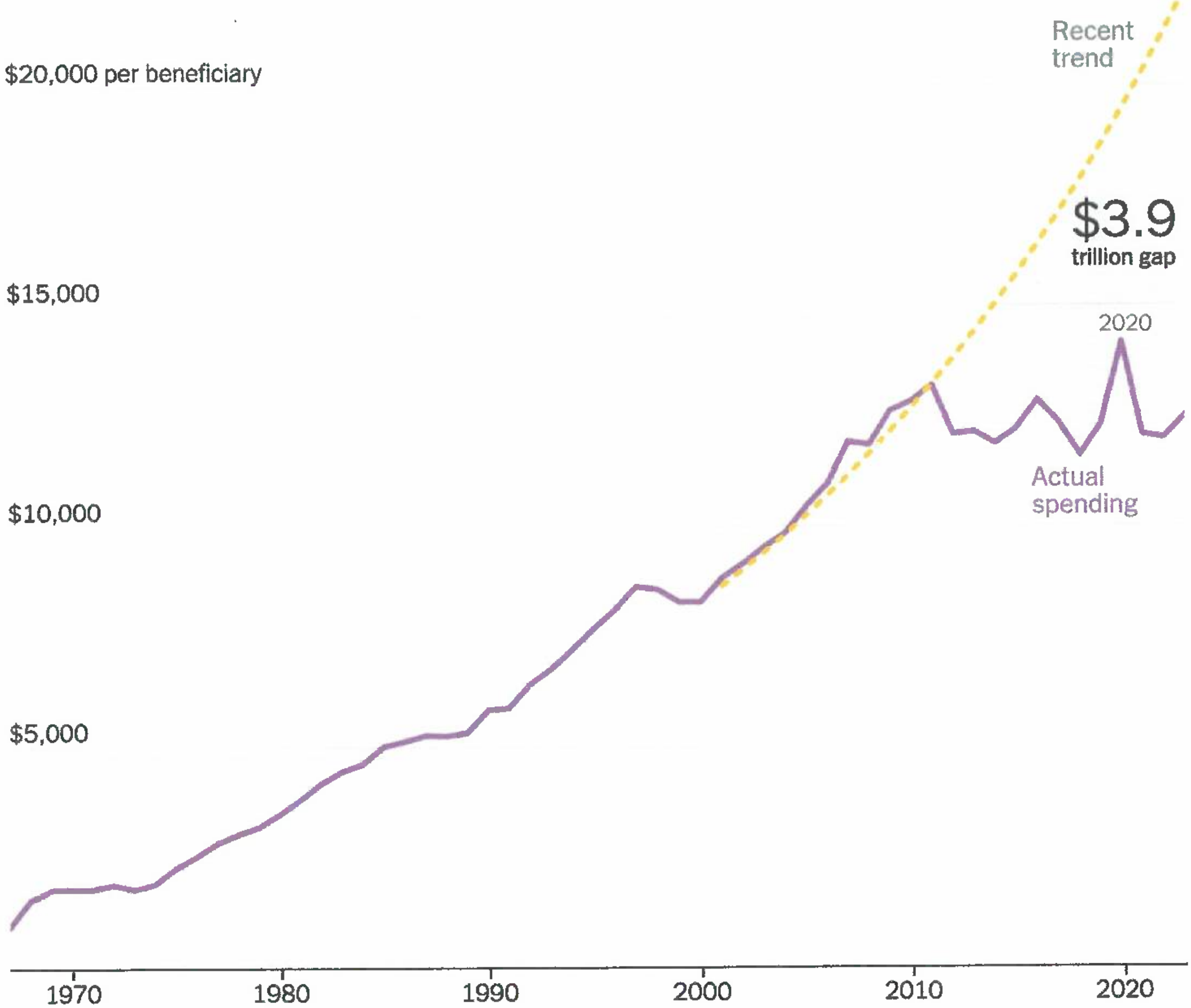
This comes back to the point that running the government isn't at all the same as running a business. The purpose of Medicare and Medicaid is to pay for peoples' health care. The purpose of health insurance companies is to collect premiums; paying for care is a cost — the industry actually calls the share of premiums that end up paying medical bills the "medical loss ratio" — and they devote considerable resources to finding ways to avoid covering medical expenses.

Obligatory disclaimer given recent events: No, I'm not offering a justification for killing health-industry executives. Murder is evil, and in this case it's also stupid. The problem with the U.S. health insurance industry isn't that it's run by bad people, it's the antisocial incentives created by the system.

Some readers may ask why, if I believe that private health insurance is so problematic, I didn't support Bernie Sanders's call for a single-payer system. The answer is political realism; it wasn't going to happen, while an enhanced Affordable Care Act could and did (and now we'll see if it survives.)

Back to government-financed health care: Am I saying that all is well with Medicare? No. True, in recent years the program has had remarkable, unheralded success in controlling costs, on a scale orders of magnitude larger than anything Muskaswamy are likely to achieve:

If the spending trajectory had continued



And the Biden administration finally — finally! — gave Medicare the ability to negotiate over drug prices, which is a serious cost saving.

But the program faces a threat of rising costs due to, you guessed it, privatization: a growing number of seniors have bought Medicare Advantage plans, which funnel taxpayer money through private insurance companies, and there's growing evidence that these plans have become a major source of, well, waste, fraud and abuse. The Wall Street Journal reports $50 billion in outlays for diseases doctors no longer treat. Some estimates suggest that overbilling by Medicare Advantage plans may cost taxpayers more than $100 billion a year; United Healthcare lost a big lawsuit over that practice.

Somehow, though, I very much doubt that DOGE will recommend rolling back Medicare privatization.

Now, in the end none of this may matter. The real purpose of DOGE is, arguably, to give Elon Musk an opportunity to strut around, feeling important. And while it's a clown show, these clowns — unlike some of the other people Trump may put in office — won't be in a position to inflict major damage on national security, public health and more.

But it *is* a clown show, and everyone should treat it as such.

MUSICAL CODA

The Times recently had a piece on Lauren Mayberry of Chvrches. Here's a clip from their first live performance in 2012; the lyrics seem alarmingly appropriate for this moment:

Mother Jones

TAXES DECEMBER 10, 2024

Here's Trillions in Federal Waste the DOGE Bros Could Actually Target

Because what's more wasteful than giant tax breaks for people who don't need them?

MICHAEL MECHANIC

Mother Jones illustration; Grzegorz Wajda / SOPA Images/Sipa USA/AP, Alex Brandon/AP

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As you may know, our felonious president-elect put mega-billionaire Elon Musk and mere billionaire Vivek Ramaswamy in charge of a commission—though not an *actual* government department, because only Congress can create those—named for the same silly dog meme as Musk's favorite "shitcoin." But even in an advisory role, the so-called Department of Government Efficiency could cause significant upheaval if Congress and agency chiefs follow its lead, or if Donald Trump launches a flurry of executive orders—and then lawsuits are filed and everything is messy and chaotic and journalists are all in a tizzy, just as Trump likes it.

DOGE's supposed goal is to identify $2 trillion in savings and reduce the size of government—and the deficit—by slashing federal waste and redundancy. (It's been tried before, with limited success.) Based on their activities and statements, Musk and Ramaswamy would accomplish this by gutting the federal workforce, eliminating certain agencies, slashing regulations, ending selected entitlements, and, as a corollary, privatizing as much as possible as quickly as possible.

7 Ways to Cut TRILLIONS in Wasteful Government Spending

For starters, the DOGE bros have proposed killing veteran's health benefits, Pell grants, Head Start, and the Bureau of Prisons—which simply means the government would spend its "savings" on contracts with private prison companies, and what could go wrong? They also seek to eliminate the National Institutes of Health, which would be a disaster for US leadership and innovation in science, because the NIH funds most basic biomedical research—work that brings about lifesaving drugs and procedures and vaccines, which, whatever you may think of them, have saved millions of Americans from gruesome deaths.

But suppose, for a moment, that DOGE's mission is earnest. If they really want to target waste and inefficiency, as Judd Legum pointed out recently, they might start with the Pentagon, which has been failing audits for ages and is notorious for things like $14,000 toilet seats. Defense will eat up nearly half of the $1.8 trillion discretionary budget for fiscal 2025, and Social Security and Medicare will account for most of the $4 trillion mandatory budget—both sacred cows that lawmakers mess with at their peril.

But there's a far richer target that nobody, certainly not the DOGE boys, has been talking about: wasteful tax breaks. These wouldn't be spending cuts, technically speaking, but they amount to the same thing, as evidenced by the fact that the government calls them "tax expenditures." And what is more wasteful, honestly, than giving huge breaks to people who don't need them?

There are myriad examples, but we'll just highlight seven big-ticket items that are costing the Treasury hundreds of billions or trillions of dollars. To be clear, some of these are not all bad, and with the right guardrails can be quite good. The devil is in the details of who gets to take advantage of them, and to what extent.

Musk and Ramaswamy may be even less likely to push for these reforms as they would to target the Pentagon budget. But let's game it out anyway. The cost figures below are five-year estimates, mostly from the congressional Joint Committee on Taxation (JCT) for 2023 through 2027.

Tax breaks for private retirement plans: $2.5 trillion

Some Republican lawmakers are eyeing Social Security reductions to cover the cost of extending the tax cuts for the wealthy that Trump signed into law in December 2017. But if the goal is to eliminate waste, they're barking up the wrong tree. The Social Security Administration estimates it will disburse about $110 billion more in benefits this year than it receives from the taxes that are deducted from our paychecks to fund the program. And that's a fair sum, but the government spends nearly *four times* as much subsidizing private retirement savings, whose benefits flow disproportionately to the affluent.

The US government, and by extension the states, offer tax breaks for contributions to these investment accounts and on the stock profits that accrue in those accounts over the years, benefits that add up to just under $2.5 trillion over five years. But unlike Social Security, private retirement plans are far from universal. Participation varies widely by income. According to the Federal Reserve Board's latest (2022) Survey of Consumer Finances, only 41 percent of families in the lower half of the income spectrum had a private retirement account, whereas 96 percent of families in the top-earning 10 percent have one (or more). And among the participating families, average savings for the lower-income half was $54,700 vs. $913,000 for the top 10 percent.

Encouraging people to save is laudable. The wasteful part is that there's no ceiling. In 2021, the JCT reported that more than 28,000 Americans had IRA (individual retirement account) balances exceeding $5 million, and nearly 500 had holdings of more than $25 million—Peter Thiel, using dubious tactics, even managed to accumulate more than $5 billion in a Roth IRA, a type of account intended for middle-class savers. And that's just IRAs, which a person can own alongside other pensions and 401(k)-type accounts. See my piece "How Congress Made Sure the Rich Retire in Luxury—at Our Expense."

The fix: Once a person amasses a total of $2 million in their combined retirement accounts, remove them from the federal teat. If they need more, they can save without the government's help. (For a preemptive fix, Musk and Ramaswamy might also urge Congress to reject this potentially disastrous Project 2025 proposal, should it ever arise.)

Exclusion of capital gains at death: $309 billion

This aberration, known as the "step-up in basis" rule, resets the value of long-held investment assets as they pass from parent to child or grandchild. Suppose I bought $10,000 worth of Amazon stock way back when and now it's worth $10 million more than I paid. That's a huge capital gain. If I sold the stock, I would owe roughly $2.4 million in federal tax. But if I die and leave it to my kids, the cost basis for taxation "steps up" to the new fair market value of $10,010,000, and neither my kids nor my estate owes the IRS a dime.

The rationale for this giveaway? Well, for estates subject to gift and estate tax (which are now only imposed on inheritances exceeding $13.6 million, or $27.2 million for a couple), the notion is that resetting the value of inherited stock avoids double taxation. But in the real world, most super-wealthy people already deploy strategies to sidestep gift and estate taxes. A second rationale is that it is difficult for heirs (and the IRS) to determine the cost basis of older investments—but that's become far less of an excuse in the digital era.

The fix: Kill the step-up rule. And speaking of tax avoidance...

Grantor Retained Annuity Trusts (GRATs): hundreds of billions*

In the late 1990s, while trying to rein in a type of trust rich people were using for tax avoidance, Congress accidentally opened the door to something far worse: GRATs. Ever since, America's dynasties have widely embraced a variation known as the "Walton GRAT" as a way to channel mind-boggling sums to their offspring without paying any inheritance tax. We're talking hundreds of millions of dollars, or billions in the cases of guys like the late casino magnate Sheldon Adelson and Nvidia head honcho Jensen Huang—who employs additional legal tricks that are now popular among billionaires, and also need to be addressed. "I think the ease with which the ultra-rich can just make their taxes disappear is becoming more visceral to people," an aide to Senate Finance Committee chair Ron Wyden (D-Ore.), told me earlier this year.

*This five-year figure is based on an estimate given to the *New York Times* by Daniel Hemel, a tax expert at New York University.

The fix: Enact limits on GRATs that render them useless for tax avoidance. Sen. Wyden introduced a bill in March to accomplish exactly that. Will it pass? Not on Trump's watch.

Tax deductions for charitable gifts: $379 billion

Okay, now you probably think I'm some sort of Grinch. What's wrong with a deduction for charitable giving? A lot, it turns out.

The Tax Cuts and Jobs Act of 2017 (TCJA) doubled the standard deduction, which about 70 percent of taxpayers had been claiming on their federal returns. As a result of the change, nearly 90 percent of families now claim it. But that means the remaining 10 percent, mostly affluent taxpayers who itemize their deductions, are the only ones who get to subtract the value of charitable gifts from their taxable income. In short, we are all paying to subsidize the charitable inclinations of America's richest. If you are a middle-class taxpayer who donates $500 to a food bank, that's $500 out of your pocket. If billionaire Scrooge McDuck makes the same donation and takes the tax break, it only costs him $315.

Philanthropy has its place. Private giving can support bold initiatives that the government won't, which sometimes brings about positive outcomes—though also bad ones and silly ones. But expending billions of public dollars to subsidize unelected philanthropists is profoundly undemocratic, in part because the rich differ so notably from the masses in terms of the things they support. In 2010, a team of political scientists led by Benjamin Page at Northwestern recruited a sample of 1 percenters for interviews—not an easy task—and compared their policy views to the preferences of the broader public, as gleaned from surveys. Fifty-eight percent of his subjects were Republicans. From my book, *Jackpot*:

> Most Americans wanted environmental protections strengthened; the 1 percenters wanted them slashed. Nearly nine in ten public respondents said the government should spend whatever is necessary to ensure high-quality K–12 public schools, versus just 35 percent of Page's subjects—who, after all, could afford private schools and tutors and coaches. Only about half of the wealthy group felt it was the government's responsibility to make sure minorities and whites had educational parity. They also favored less spending on Social Security, health care, food stamps, and jobs programs. The affluent group "tilted toward cutting all the income-redistributive or social insurance programs we asked about," wrote Page et al.

Scrooge McDuck, like Elon Musk, also has a private foundation that he funds (like Musk) with shares of his company stock, which means he not only avoids paying a tax on their gain in value over the years, he also gets to deduct their current value from his taxable income! The McDuck Foundation, like any private foundation, is only required to spend 5 percent of its assets each year on charitable activities, even though its investments are growing by 15 percent annually. And its donations go to nonprofits that are working to eliminate the federal regulations that prevent McDuck Enterprises from polluting rivers and streams. For more, see my piece "Philanthropy in America is Broken." (No more ducks, I promise.)

The fix: Kill the charitable deduction. Replace it with a tax credit available to all, and cap it at $5,000 a head.

Reduced rates on dividends and long-term capital gains: $1.2 trillion

Consider two married couples, each with a combined taxable income of $200,000. (For simplicity, we'll assume they claim the standard deduction.) The first couple's income is entirely from their salaries. The second couple gets all its money from dividends and sales proceeds from one partner's significant stock holdings, inherited from a parent—neither partner is employed. The working couple's effective federal tax rate is a tad over 16 percent. The nonworking couple has an effective rate of 8 percent. Besides being an insult to people who work for a living, this large disparity—for very high earners, the top capital gains tax rate is about 24 percent vs. 37 percent for wage income—encourages lots of tax avoidance schemes. (Carried interest is another notable one.)

The rationales for rewarding passive investment over work don't pass the smell test. Investors will invest regardless, and differing capital gains rates don't appear to have a large effect on economic growth. When the rates are reduced, meanwhile, the windfall goes largely into the hands of people with incomes north of $1 million. Now, you'll hear speculation, and see some research, concluding that higher capital gains taxes discourage entrepreneurial risk-taking. But since when is risk-taking an unvarnished good? There are lots of "innovations" that haven't turned out so great for our society. Think Meta. And Purdue Pharma, maker of OxyContin. Are we really better off for the wasteful innovations of meal kit companies like Blue Apron? Heck, Juul was an innovator—one that got a generation of kids hooked on nicotine. When excess wealth is sloshing around in search of lucrative investments, the consequences can be grim. Consider how an explosion of private equity has hollowed out many industries, as fund managers leverage debt to suck the life out of once-healthy sectors and channel profits to investors and partners at the expense of consumers, tenants, and workers. (See our recent packages “How Private Equity Looted America” and “American Oligarchy.”)

The fix: Treat investment income the same as work income. Boom.

Home mortgage interest deduction: $258 billion

Prior to 2018, a couple could deduct interest on up to $1 million in loans for first and second homes. The Trump tax legislation lowered the limit to $750,000, but because the TCJA also doubled the standard deduction, the mortgage interest deduction shifted further in favor of the rich. In 2023, according to the Congressional Research Service, nearly half of the deduction’s value went to the 14 percent of families with taxable income exceeding $200,000. And the deduction has done little to bolster homeownership: “The economic literature,” the CRS notes, “has generally found that the deduction’s structure…does not address the largest barriers to homeownership—the down payment required by banks, and closing costs.”

The fix: Kill the deduction and replace it with a program to help lower-income homebuyers with down payments and closing costs, limited to first homes only.

Qualified business income deduction: $199 billion

This may sound like a snoozer, but this generous provision of the 2017 Trump tax cuts, enacted at the urging of Republican Sens. Steven Daines of Montana and Ron Johnson of Wisconsin (who stood to gain personally), was a blatant giveaway to the owners of “pass-through” businesses, a category dominated by S corporations and limited liability partnerships, nearly 70 percent of whose profits flow to the wealthiest 1 percent of the population, according to a 2016 Treasury report, while “virtually no” pass-through income goes to people in the lower 80 percent.

As I wrote in my book, pass-throughs include hedge funds and real estate partnerships, private equity and venture capital groups, landlords and professional firms: accounting, consulting, law, medical, dental. Their owners spent hundreds of millions of dollars on political contributions to get their way on the tax bill. Hedge funds more than *quadrupled* their contributions to federal candidates, lawmakers, and PACs during the 2016 and 2018 election cycles relative to earlier cycles. Private equity contributions more than doubled, and venture capital and real estate contributions nearly doubled. Those investments paid off in spades.

The fix: Repeal it.

There’s more, but maybe we’ll just end it here. Your bumper-sticker takeaway: Stop the Plunder, Close the Deficit.

Correction (12/10/2024): My initial estimate for GRATs—$1 trillion over five years—was not the cost to the US Treasury but rather the amount of wealth moving through these and related vehicles the wealthy use for tax avoidance.

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