1

Equality

Beyond Tax-and-Spend

FOR TWO DECADES ECONOMISTS concerned with inequality have debated the precise role global competition, changing technologies, sectoral balances, and other strictly economic factors have played in generating the worsening trends. Whatever the final resolution of the technical debate over how much weight to assign different forces, the important truth, as Barry Bluestone points out, is that none shows "the least sign of weakening."[1]

Accordingly, what is of truly fundamental concern for those who care about equality has been the collapse of the *political*-economic strategies it once was hoped might counter the deepening trends.

And the central question is whether there are any other ways forward, even in theory.

The evolving progressive reassessment begins with a cold appraisal of the reasons traditional approaches no longer work. There is very little doubt about what has happened to undermine liberal redistributive strategies.

First and foremost has been the radical decline of America's labor unions. Always weak in comparison with other advanced nations, peacetime U.S. union membership peaked at 34.7 percent of the labor force in the mid-1950s; it was a mere 12.9 percent in 2003 (8.2 percent in the private sector). The downward trend is all but certain to continue; responsible estimates suggest union membership in the private sector may sink below 5 percent by 2020.[2]

The decline obviously weakens union bargaining power over wages. Far more important, however, is that historically labor's political power has played a central role in the passage of social legislation and redistributive programs. "The political consequences of high levels of unionization are . . . straightforward," political scientist Michael Wallerstein observes. "[O]ther things being equal, union movements representing a large share of voters are better able to influence policy."[3] Throughout the Western world, many studies show, greater unionization has been one of the best predictors of greater equality.[4]

Labor has been the most important countervailing force (partly) offsetting conservative political power throughout much of the twentieth century. As labor has continued to decline, the way has been opened to a series of aggressive corporate and other campaigns that have challenged redistributive programs of all kinds—first by the Reagan administration, then by the Gingrich Congress, now by the Bush administration.[5]

The globalization of economic activity also has played a role, and it has increased the already enormous power of the large corporation economically and politically. Globalization brings with it ever expanding opportunities for relocation to other countries—and this adds to corporate leverage and the capacity to threaten departure unless demands are met. Business in turn has used its increased bargaining power to win concessions from labor.[6]

Worldwide competition for investment has added to the pressures, forcing government to reduce business tax rates, shifting more of the burden to low- and moderate-income earners. Globalization thereby also implicitly reduces the capacity of governments to spend on redistributive social programs. In 1945 corporate income taxes amounted to 35.4 percent of federal receipts. By 2003—as labor's political power decreased, as corporate power increased, and as globalization proceeded—such taxes had fallen to 7.4 percent of federal receipts. More than three-fifths of U.S. corporations paid no federal taxes at all in each of the years between 1996 and 2000![7]

The post–World War II social, economic, and cultural concentration of suburban political power and the urban exodus of the post-1960s decades have brought additional difficulties. Increasingly the largely white suburban middle class is simply no longer willing to pay for a progressive political agenda it believes will mainly benefit the black and Hispanic poor. At the same time, racial and ethnic divisions have weakened the capacity of the majority to unite behind redistributive measures.

Thomas and Mary Edsall document the radical implications in their book *Chain Reaction:* "Just as race was used, between 1880 and 1964, by the planter-textile-banking elite of the South to rupture class solidarity at the bottom of the income ladder . . . race as a national issue over the past twenty-five years [broke] the Democratic New Deal 'bottom-up' coalition. . . . The fracturing of the Democrats' 'bottom-up' coalition permitted, in turn, those at the top of the 'top-down' conservative coalition to encourage and to nurture . . . what may well have been the most accelerated upwards redistribution of income in the nation's history."[8]

Finally, we may add the rise of the post-1970s Republican South—a change that has added force to each of the key factors and to conservative politics in general. By 1994—for the first time in modern history—Republicans constituted a majority of the Southern delegation in both the Senate and the House of Representatives. The new form of racialized Southern politics, political scientist Augustus B. Cochran III points out, inevitably produced "policies that favor political and economic elites to the disadvantage of the vast majority of average citizens."*[9]

* Michael Lind goes further: George W. Bush's Texas "is a toxic by-product of the hierarchical plantation society of the American South, a cruel caste society in which the white, brown, and black majority labor for inadequate rewards while a cultivated but callous oligarchy of rich white families and their hirelings in the professions

Taking the various factors together, in fact, provides only a minimal estimate of the unfavorable prospects for traditional strategies aimed at reversing growing inequality—for several additional reasons.

First, there is very little evidence that inequality-related trends have ever been significantly altered because of progressive political strategies per se—that is, efforts to enact reforms in normal, noncrisis times. Inequality has been significantly reduced in the twentieth century mainly as a result of major crises like the Great Depression (which spurred unusual political and policy change), and in the context of war-related conditions that produced a special policy environment, tight labor markets, and a compressed wage structure (especially World War II but also, in other ways, the boom years of the Cold War, including the Korea and Vietnam wars). Even in the best of times, the capacity of traditional political strategies to achieve major impact on their own in "normal" circumstances has been far weaker than many commonly acknowledge.[10]

Second, a close examination of traditional conventional measures makes it obvious that on its current path, *real* inequality will continue to worsen, no matter what. Most academic discussions of inequality are based on relative assessments. While useful for many purposes, such measures mask important relationships—especially of absolute political-economic power, and of cultural and social differences. If you have $1,000 and I have $50,000 this year, and next year you have $2,000 and I have $100,000, the relative measures widely used in conventional reporting will indicate that there has been no increase in inequality because the ratio of 1-to-50 is unchanged. However, absolute inequality—the real-world difference between us—obviously has gone from $49,000 to $98,000.

dominate the economy, politics and the rarefied air of academic and museum culture." Michael Lind, *Made in Texas: George W. Bush and the Southern Takeover of American Politics* (New York: Basic Books, 2003), p. 160.

The *absolute* income gap between the top 5 percent and the bottom 20 percent exploded from $191,800 in 1979 to $419,700 in 2000 (in 2000 dollars).[11]

Contributing to both the relative and absolute trends during much of the final quarter of the twentieth century was the fact that hourly wages of the bottom 60 percent did not rise as fast as inflation—with the result that the real income each person earned, hour by hour, was actually lower in 1995 than in 1973. For very large numbers of Americans, the only reason total family income rose—very modestly—was that people worked longer hours and/or spouses (mainly wives) went to work in increasing numbers.[12]

Put another way: unless they worked more hours or someone else in the family went to work during these years, many would have been better off if the economy had simply stood still at the 1973 level. Economic growth not only did not increase the real pay that an hour of work earned, it brought with it price increases that reduced real income.[13]

We also appear to be reaching a limit of those who can add to family income. The percent of wives working rose from 28.5 percent in 1955 to 42.3 percent in 1973 to 61 percent in 2002. Though spouses will provide a continuing contribution to family income, nothing like the qualitative shift that occurred during the second half of the twentieth century is ever likely to occur again.[14]

Traditional redistributive political strategies which aim to deal with inequality are based on what are sometimes called "after-the-fact" methods. It is accepted that capitalist economic systems as a matter of course produce highly unequal distributions of income. It is hoped that "after the fact"—after the basic income flows have been generated—progressive taxation, combined with various social programs, can alter the underlying patterns.

No one would deny the possibility of some future tax changes, but there has long been little expectation that significant after-the-fact approaches for dealing with inequality can be revived—even before the administration of George W. Bush added to the difficulties. Galbraith's summary judgment of the well-understood realities is trenchant: "The only effective design for diminishing the income inequality inherent in capitalism is the progressive income tax. . . . That taxes should now be used to reduce inequality is, however, clearly outside the realm of comfortable thought."[15]

Another Harvard economist, Richard Freeman, minces few words about the dead end that has been reached: "[C]urrent 'strategies' run the gamut from inadequate to sham."[16]

Some liberals continue to hope against hope that somehow a revival of progressive politics can one day reverse the decaying trend. But clearly, if serious after-the-fact redistributive measures are no longer viable, something much more fundamental is needed.

In recent years those who have confronted the issue squarely have increasingly come to the judgment that if change is ever to occur, an assault must ultimately be made on the underlying relationships that have produced the inequality trends in the first place—especially those involving ownership and control of the nation's wealth.

Freeman, for instance, urges, "If we were to start democratic capitalism with a blank slate, we would naturally divide the ownership of existing physical assets equally among the population. . . . Our main strategy—be we left or right—for fighting income inequality under capitalism, should be to assure a fair initial distribution of physical and human capital themselves." Freeman states the essential principle of such an approach in this way: "Equality of income obtained in the first instance via greater equality in those assets, rather than as an after-the-fact (of earning or luck) state redistribution of income from rich to poor, would enable us to better square the circle of market efficiency and egalitarian aspiration."[17]

Former secretary of labor Robert Reich also urges a similar, wealth-related, shift in focus: "The asset elevator has been lifting America's wealthy to ever-higher vistas, without their moving a muscle (except, perhaps, to speed-dial their brokers). Current tax law is lifting them, and their children, even higher. Hence the case for allowing the rest of America on the elevator, too."[18]

And former chief counsel to the U.S. Senate Finance Committee Jeff Gates holds: "[A]bsent an accompanying ownership-participation element, unbridled free enterprise is destined to throw both the social and economic system badly out of balance."[19]

The emphasis on wealth (rather than simply income) by these writers and others involved in the quietly growing reassessment has brought with it a related emphasis on underlying institutions (rather than simply policies). One specific line of development stresses the possibility that workers might own their own companies, a straightforward idea that if extended and applied across the board implies a political-economic system quite different from both traditional socialism and corporate capitalism.[20]

Radical economists Samuel Bowles and Herbert Gintis also begin their analysis by agreeing that political progressives need to reconsider failing traditional approaches: "[E]galitarian strategies should abandon what has hitherto been an exaggerated emphasis on . . . tax and transfer policies." Not only is this a political dead end, but asset-based redistribution, they urge, "can use markets to discipline economic actors." Indeed, they hold that worker-owned firms ultimately may prove to be "more efficient than the capitalist firm, in the technical sense that the democratic firm uses less of at least one input to produce the same output."[21]

"Workers frequently have access at low cost to information concerning the work activities of fellow workers," Bowles and Gintis point out, "and in the democratic firm each worker as a residual claimant on the income of the firm has an interest in the effort levels of other workers." The ordinary firm must spend a good deal of money monitoring work activity. Quite apart from the equities involved, this is a drain on economic resources.[22]

Jeff Gates, drawing on his experience in the Senate, stresses the political possibilities of worker-ownership strategies: "The political potential in this area became obvious to me when, over the span of a two-week period . . . I was asked to provide speech material for both Republican Senator Jesse Helms and Democratic presidential candidate Jesse Jackson." Gates and others have produced long lists of those endorsing the principle of employee-owned firms ranging from Ronald Reagan and George Will on the right, to Robert Kuttner and Robert Reich on the left.[23]

Worker ownership clearly is not the only wealth or "asset-based" approach that flows from the argument that a new strategic principle beyond after-the-fact taxing and spending is necessary. Another major strategy begins with the observation of Washington University expert Michael Sherraden that the federal government already provides very large indirect tax subsidies to encourage asset ownership by middle- and upper-income Americans. The most obvious of these are the tax deductibility of home-ownership mortgage interest, tax, and other payments; and of savings contributions to Keogh, IRA, and 401(k) plans. In fiscal year 2004, public subsidies of $98 billion were projected to go to home-owners and another $113.8 billion to those who saved through any one of the plans; taxpayer costs for 2004–2008 were estimated to be more than $1 trillion.[24]

Sherraden suggests that if such huge subsidies can be given to middle- and upper-income groups to encourage savings, incentives also should be used to develop asset holding among the poor. He proposes a system of Individual Development Accounts (IDAs) through which the government would directly match the savings of the poor—thus doubling their efforts and allowing low-income individuals to benefit from the ownership of capital: "Instead of focusing welfare policy on income and consumption, as we have done in the past, we should focus more on savings, investment, and asset accumulation. This idea might be summarized by the term *stakeholding*. . . . A stake in the system means, in one form or another, holding assets."[25]

Although not as striking in their institutional implications as worker-ownership ideas, over the decade of the 1990s a stream of related asset-based wealth-holding and wealth-building proposals has expanded on Sherraden's theme—and on the general principle that wealth should benefit much broader groups directly. Most of the specific plans also emphasize the obvious point that any capital investment started early enough and held long enough ultimately will pay off handsomely.

A proposal by former Senator Bob Kerrey of Nebraska, for instance, would establish "KidSave Accounts" to which the government would contribute $1,000 at birth for every child, and $500 per year thereafter for the next five years. The funds would be invested and allowed to grow until the individual reaches age twenty-one—at which time roughly $20,000 would be available for investment in education or for other purposes.[26]

Significantly, the KidSave proposal was cosponsored not only by liberals, but by centrist and conservative senators Joseph Lieberman of Connecticut and John Breaux of Louisiana as well. A related proposal by Robert Kuttner aims to provide each child with a $5,000 capital grant at birth and up to $1,000 a year thereafter until age eighteen. Kuttner estimates that if conservatively invested, such an amount will produce a capital fund of roughly $50,000 per individual at maturity.[*27]

* In a related proposal the Clinton administration put forward the idea of Universal Savings Accounts as a supplement to Social Security. In such IDA-like accounts the savings of the poor would be supplemented by up to $1,300 per year. The Blair government in Britain introduced a "baby bond" proposal based on similar asset-based ideas in early 2003. See Robert B. Reich, "To Lift All Boats," *Washington Post,* May 16, 1999, p. B1; Will Hutton, "A Chance for a Robin Hood Budget," *The Observer* (London), April 6, 2003, p. 30.

"Imagine if instead of being promised at birth that you will get a Social Security pension decades in the future . . . you were given a trust fund based on bonds or stocks whose returns would constitute your social transfer," comments Richard Freeman. "The incompetent poor would then be more like the incompetent rich: they would have income from assets that would let them live at some basic level, without depending on income transfers."[28]

Yale professors Bruce Ackerman and Anne Alstott take such wealth-holding ideas a step further by proposing that every individual be given a "capital stake" of $80,000 on reaching adulthood—to be used for any purpose they chose. The Ackerman-Alstott program also adds an important new dimension to asset-based strategic thinking: They urge that the program be initially financed by a 2 percent wealth tax, thus linking the principle of broadening wealth ownership to much larger publics, on the one hand, to a strategy that challenges the extreme concentration of existing wealth ownership in the hands of tiny elites, on the other.[29]

Several writers have pushed the basic principles underlying wealth-holding proposals forward to their logical—and much more far-reaching—system-wide institutional conclusions. Yale economist John Roemer, for instance, proposes a very radical long-term strategy he calls "coupon socialism," which in theory would ultimately totally "change the system" and pass on the benefits of *all* major stock ownership to the citizenry at large.

Under the Roemer proposal, taxation would first transfer ownership of capital to the government. Every adult would then receive an equal endowment of voucher-like coupons—nontransferable dollars—which could only be used to purchase stock through a new form of mutual fund. The resulting profits would be distributed to such investors—that is, to all adults—thereby ultimately providing an income stream from the now widely distributed ownership of capital.[30]

An important feature of Roemer's approach is that although the ownership of wealth would be revolutionized, the management and functioning of firms would not be disturbed. Since individuals could choose where to invest their coupons, competition for the funds they represent would continue to discipline market behavior.

A similar, equally radical, long-term system-wide asset-changing proposal is that of political scientist Leland Stauber. In this approach, too, the management and competitive situation of firms is not altered, and mechanisms of market discipline are maintained. Instead of individuals benefiting directly from the change in asset ownership, however, municipalities—as representatives of the public—are the ultimate recipients of dividends from the ownership of capital.[31]

A midrange position that also develops the full institution-changing logic of wealth-holding ideas is that of the Nobel laureate British economist, the late James Meade. Under Meade's approach, taxation of large-scale wealth produces funds to be used, first, to pay off the national debt, and second to accumulate surplus public capital. The surplus, in turn, is invested in corporate stock by investment trusts and other private financial institutions. The "beneficial ownership" of roughly half the nation's capital in this proposal is ultimately passed on to the public in the form of a "social dividend," distributed "free of tax to every citizen . . . which depends solely upon the age of the citizen, a distinction being drawn between the payment to a child or to an adult of working age or to a pensioner."*[32]

* Progressive taxation recoups some of the income flowing to the well-to-do. A second strategy offered by Meade involves new forms of enterprise characterized by labor-capital partnerships that also implicitly change the beneficiary ownership of wealth—an idea echoed in Martin Weitzman's 1984 book, *The Share Economy,* which advocates changing the labor contract from a wage (dollars per hour) to a share of revenues (each worker would receive two-thirds of company revenue per worker). Martin L. Weitzman, *The Share Economy* (Cambridge, Mass.: Harvard University Press, 1984), pp. 3–5.

If Roemer, Stauber, and Meade come to their system-wide extensions of asset-based, wealth-holding concepts from the left, others have come to related ideas from a very different direction: Norman Kurland, Robert Ashford, and Stewart Speiser have picked up on the earlier writings of corporate lawyer and investment banker, the late Louis Kelso, to urge far-reaching programs of "universal capitalism" that draw heavily on Kelso's 1958 *The Capitalist Manifesto* (written with philosopher Mortimer Adler).

Kelso realized from his professional experience that one of the main—and strikingly obvious!—reasons his rich clients were able to multiply their ownership of stocks and bonds was that their existing wealth provided them with collateral that allowed them to borrow money for further investment. They could also hire experts to manage that investment. If the poor had access to collateral and experts, Kelso reasoned, why could they not also make money by investing borrowed funds?

Drawing on the precedent of federal programs that insure home mortgages, Kelso proposed that a new Capital Diffusion Insurance Corporation be established to guarantee loans so as to allow individuals to buy a diversified and professionally managed portfolio of stocks. The portfolio would remain in escrow until dividends repaid the loan, at which time the individual would take full ownership, thereby gaining a "second income" with the help of the government-backed or collateralized ownership of capital.[33]

Although Kelso's proposal would also ultimately result in a major system-changing buildup of wealth among the citizenry, unlike Roemer, Stauber, and Meade, he did not propose taxing away or expropriating existing wealth. Instead, a steady shift in ownership would be slowly accomplished as *new* wealth is created in the normal processes of economic development over long stretches of time.

The key principle involved in all variations on the Kelso approach is that ultimately the stock pays for itself out of the dividends it earns. Speiser puts it this way: "This is a method of acquiring new capital that has been used for centuries by wealthy people and profitable companies. *They simply let it pay for itself.* New factories opened by major successful corporations pay for themselves out of their own output. . . . This is the key to capital accumulation, and it is all based on *long-term* credit, which is not available to the little guy now but is always available to the large corporation or the wealthy person in our society."[34]

William Greider, an important progressive writer, now also urges the essentials of a Kelso-type strategy: "The central mechanism for democratizing ownership . . . is reform of the credit system—enabling people without any wealth of their own to borrow the funds to buy shares of capital ownership, loans that will be paid back by future earnings from the very income-producing assets they have acquired."[35]

Few of those concerned with equality would abandon traditional redistributive strategies entirely (especially those that might still yield some benefits to people at the bottom of the system). The emerging shift, however, points to a longer-term system-wide principle—namely, that ultimately movement toward greater equality requires that the ownership of capital be altered. This in turn requires new institutions.

Clearly, the longer-term system-wide wealth-changing proposals are beyond the range of current political feasibility. But just as clearly, growing disillusionment with traditional after-the-fact policy ideas has set the stage for a much deeper and ongoing reassessment. If the old ways no longer work, is there any other option? New proposals to broaden the ownership of wealth are increasingly commonplace—and given the growing discontent, appear all but certain to continue to grow in number and refinement.

Two obvious questions are: first, whether—even if over very long stretches of time—the emerging principle can ever be significantly embodied in practical institutions; and second, whether it can receive any degree of substantial political backing against the huge odds and interests that stand in the way of major change.

We shall return to these matters in Parts II and IV—and to the question of whether there is any other way to give meaning to values based upon, or even remotely related to, the idea of equality in the new century.