One World

Economics for the Citizen
Part 3: RX for the US

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RX for the US

Note: this section includes an accurate but simplified synopsis of information covered in Parts 1 & 2. For full background and details please refer to those sections or read them first.

The United States is only one country, but as one of the richest per person, and with the largest economy in the world, it has an outsized influence. The US economy overall is a powerhouse of growth and has made us, as a country, very rich with an average gross national income of $81,000 for every man, woman, and child. That said, in our survey of economic data in Part 2 we found that the growth of the US economy is not benefiting everyone in equal measure. There are many in the US who feel left behind, and plenty of data to confirm that this perception has a basis. Income inequality has grown, wealth concentration is literally off the charts, the homeless population has increased, economic mobility has declined for the poor and near poor, we have a persistently high trade deficit, and the budget deficit continues to grow. On top of that, humanity now faces the limits of what the earth can sustainably support. We almost all realize that human-caused climate change if left to continue will cause huge irreversible economic, environmental, and social damage. In reality, if not in perception, that is the most urgent issue we face and will require major investment and cooperation with the other countries of the world. That is only one of several critical issues we face from the explosion of the human population beyond 8 billion.

None of these economic and sustainability issues are beyond our ability to address. The incredible rise in productivity over the last 100 years means we have the resources and technology required to address them while making life better for all of us. History has clearly shown, however, that while market capitalism is an incredibly powerful driver of productivity and innovation, left on its own it also drives income and wealth inequality and has no incentive to address "externalities" such as climate change. Only broader society can address such issues and the mechanism for doing so is government. In a democracy in particular, we the people decide what our society should look like economically, and our priorities for addressing the issues that we face. Early in the 20th century we in the US undertook to tame unfettered capitalism to make it work more broadly for the country as a whole, resulting in an explosion of the middle class. Later in the century we took up environmental and social issues. But there has been pushback on both, and, as we've seen, inequality which fell in the years following the New Deal and Second World war, started rising again around 1980. What happened? As we saw in Part 2 it wasn't that real incomes fell so much as the gains of productivity went more and more to the top. Mostly to the very top. While we've looked at the effects of productivity, trade, migration, deregulation, and de-unionization on incomes and wealth, and will review those findings again later, we haven't discussed US government taxes and spending and how that has affected the distribution of income and wealth. We'll look at that now and then put everything together.

US Government Spending

The US has a federal system, and states and localities raise and spend roughly as much as the Federal government. Actually, states and localities together spend more than the Federal government but raise less because the Federal government transfers a lot of money to them. The graphic below shows 2017 government spending. The yellow area is transfers of revenue from the Federal government to states and localities.

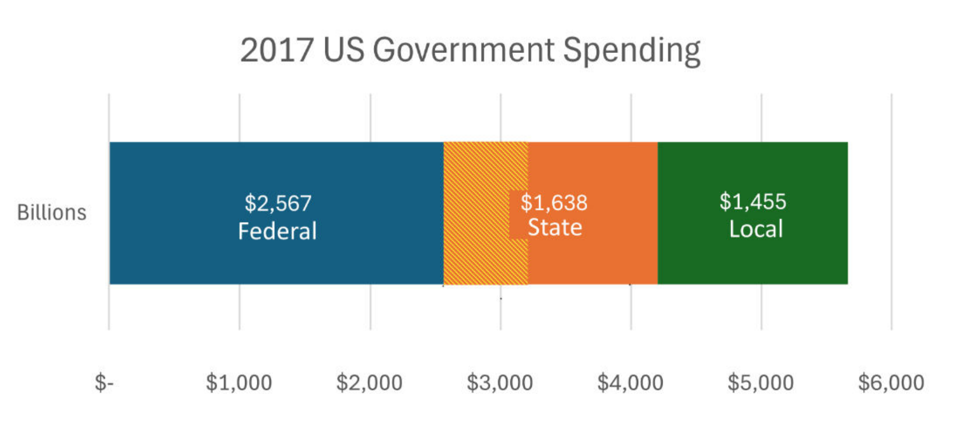

Figure 1 2017 US Government Spending. Yellow area is Federal transfers to state and local governments. Source see note [1] ww133

Governments get most of their money from taxes, so "spending" by government at any level is really about buying stuff on behalf of taxpayers. We give up some of our purchasing power, say to add another cable channel to our lineup, to the government, say to help pay for a school or an aircraft carrier. Unfortunately, people, including many of the already immensely rich, don't like giving up purchasing power even for things they understand we need, so there are and will always be endless squabbles over who pays and what we buy through governments. It is important to keep in mind that our tax dollars aren't loaded into a rocket and sent off into space. All of the money the government collects and spends goes to people or businesses, it is spending that drives the economy just like consumer spending does. In fact, much of it comes back to us, we pay Social Security taxes now so that we can spend our Social Security incomes later. Even foreign aid, military or otherwise, is often directed to purchases from US suppliers. In short government is an integral part of the economy, as any lobbyist knows[2]. In 2017 about 29% of US Gross Domestic Product (GDP, the total output of the country) flowed through our Federal, state, and local governments[3]. Here's how we spent the money in 2022.

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[1] : https://federalism.us/federalism-101/an-overview-of-federal-state-and-local-expenditures/#:~:text=Of%20the%20total%20amount%20of,30%20percent)%20in%20public%20spending and https://www.whitehouse.gov/wp-content/uploads/2024/03/hist12z1_fy2025.xlsx

[2] A great tool for exploring US spending which lets one drill down within each spending category is provided by the Treasury at https://www.usaspending.gov/explorer/budget_function

[3] National income is total income earned

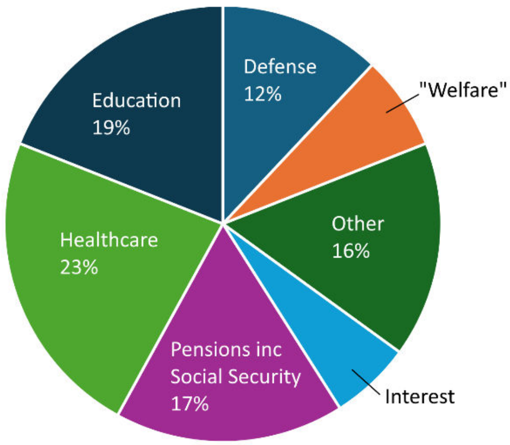

Figure 2 2022 Federal, state and local spending by function. "Welfare" includes food stamps, unemployment benefits, workers compensation, housing, cash welfare, earned income credit above tax liability and others but excludes health care (Medicaid). "Other" includes transportation, protection (police, fire etc.) and general government. "Spending through the tax code" not included. Source: see note[4]. WW134

Looking at it this way, spending 30% of our income on healthcare, pensions, education, defense, plus everything else governments do, like roads and police, might not seem like a bad deal. As we have seen in Part 2, education and infrastructure are keys to having an advanced economy and few of us want to give up our pensions or do without healthcare.

Budgets are contentious at all levels of government (I've attended Town Meeting for 25 years in my hometown), and certainly lobbying and special interests often get their way (ditto), but we can't possibly deal here with 52 states and innumerable local budgets. Let us look at the roughly one half of government spending that flows through the Federal government and the taxes that are collected to fund it.

Here is the Federal budget from fiscal year 2023.

[4] Percentages are approximate given the way the Census collects data. These numbers are taken from a Wikipedia entry in turn based on https://www.usgovernmentspending.com/year_spending_2022USbt_25bs2n whose author must be commended for his effort and transparency.

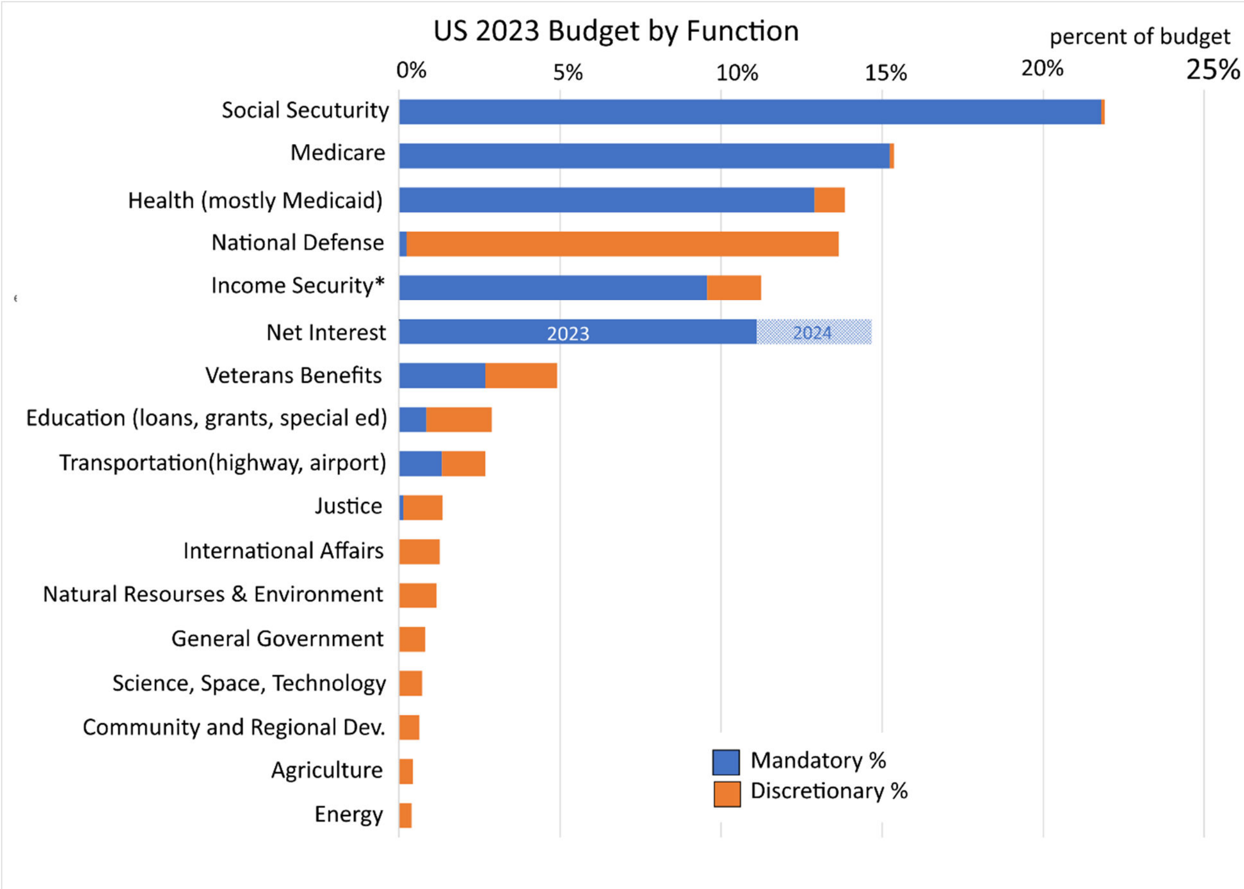

Figure 3 US Federal 2023 Budget. Source: https://www.govinfo.gov/app/collection/budget/2023/BUDGET-2023-PER except for actual net interest from treasury data WW128
** Income Security includes Federal employee retirement, earned income refundable credit, food stamps and other programs.*

We can see a number of interesting things about the budget from the chart. First, most of it is "mandatory," meaning Congress set up programs such as the Social Security Act where the legislation, until amended, provides a formula for making payments. Congress could, if it wanted, abolish Social Security, or lower or raise payments, but unless it does so, the formula used to calculate benefits "entitles" people to certain payments which have to be included in the budget. If you subtract mandatory and defense spending, you are left with 15% of the budget for everything else.

As noted above, a lot of the federal budget transfers money, it isn't spent directly by the government. This includes the mandatory spending on the social insurance programs of Social Security and Medicare. Most of us pay, or paid, into the Social Security Trust Fund through our payroll taxes and when we retire our payments come from that fund. Until recently Social Security ran a surplus. In 2022 the trust fund had a positive balance of around $2.7 trillion. Medicare also involves a pair of trust funds, but payroll taxes are inadequate to cover costs, and general tax revenue provided 43% of required funding in 2023. Medicaid is a joint state/federal program with the federal government providing about 70% of the funding from general revenues.

Income security mandatory items include the earned income tax credit which was signed into law by President Ford and substantially expanded by President Reagan. The earned income tax credit is “partially refundable” meaning that poor families can get up to $1,600 per child in cash if the credit exceeds their income and payroll tax liability. About 20% of the mandatory income security line item in the chart is the earned income tax credit and child tax credit. A similar amount is for retirement benefits for government employees, with slightly smaller amounts going to military retirement and food stamps.

Interest payments are of course mandatory. Interest on the $34 trillion national debt was $658 billion in 2023. Those payments are tied to interest rates and the hatched area in Figure 3 shows that as interest rates have risen recently the payments on the debt have also and are now about the size of defense spending[5]. About 1/3 of our national debt is held by foreign governments and entities, those payments dwarf foreign aid. If we don’t want to “send money overseas” we should reduce our deficit and borrowing.

How has federal spending changed over the years? Here the breakdown since 1940:

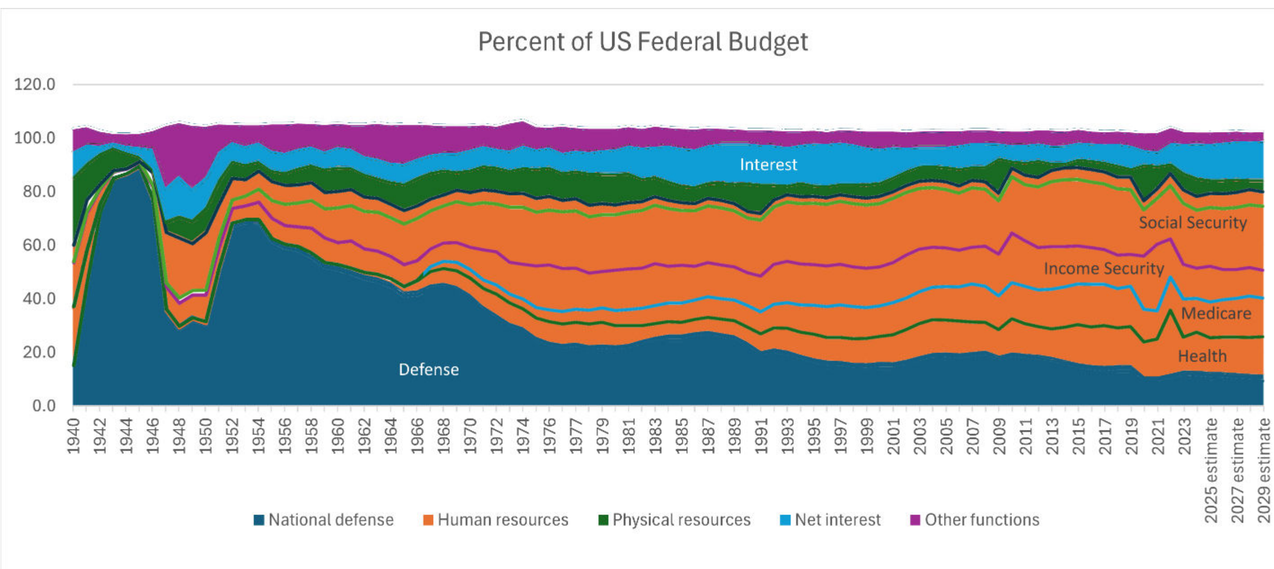

Figure 4 US Federal Budget by Major Function. “Income security” includes Federal employee retirement, unemployment, housing and food assistance. “Physical resources” includes energy, natural resources, housing, transportation, and commerce. In addition to health-related spending, “Human resources” includes the subitems shown as well as education & training and veterans benefits and services not counting health. “Health” includes all health related other than Medicare (Medicaid, Veterans medical care, research, etc.) Source: https://www.whitehouse.gov/omb/budget/historical-tables/ Table 3.1. The chart omits offsetting receipts (less than 1%) which explains the slight deviations from 100%. WW132

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5 The chart shows budget authorization for 2023 but actual spending expected in 2024. Actual net interest payments in 2023 were 10.7% of the budget in 2023. https://www.whitehouse.gov/omb/budget/historical-tables/ Table 3.1

As we will see, the overall Federal budget hasn't changed much as a percent of GDP since 1975 but Medicare and Medicaid have gone up from a combined 8% of the budget to 28% in that time. In Part 2 we looked at how much of an outlier US medical costs are, those costs are passed on to both private insurance and taxpayers. The fix is to reduce the costs, around 17% of GDP, to be in line with other rich countries, at 12% of GDP for universal coverage, a task in progress. Even then, though, health care costs are not going down to historical levels because there is simply more and better medicine now and the population is getting older.

Defense spending has declined as a percent of the budget and US GDP. It is currently around 3.5% of GDP.

The fact the budget hasn't grown much as a percent of GDP despite the large run-up in medical costs is truly amazing. But what has grown is the deficit as a percent of GDP and along with it the national debt. The chart below shows expenditures and deficit as a percent of GDP. The spike in expenditures around 2020 is associated with emergency COVID spending together with a dip in GDP. The spike in 2008 marks the sub-prime mortgage credit crises which Obama inherited at the beginning of his term.

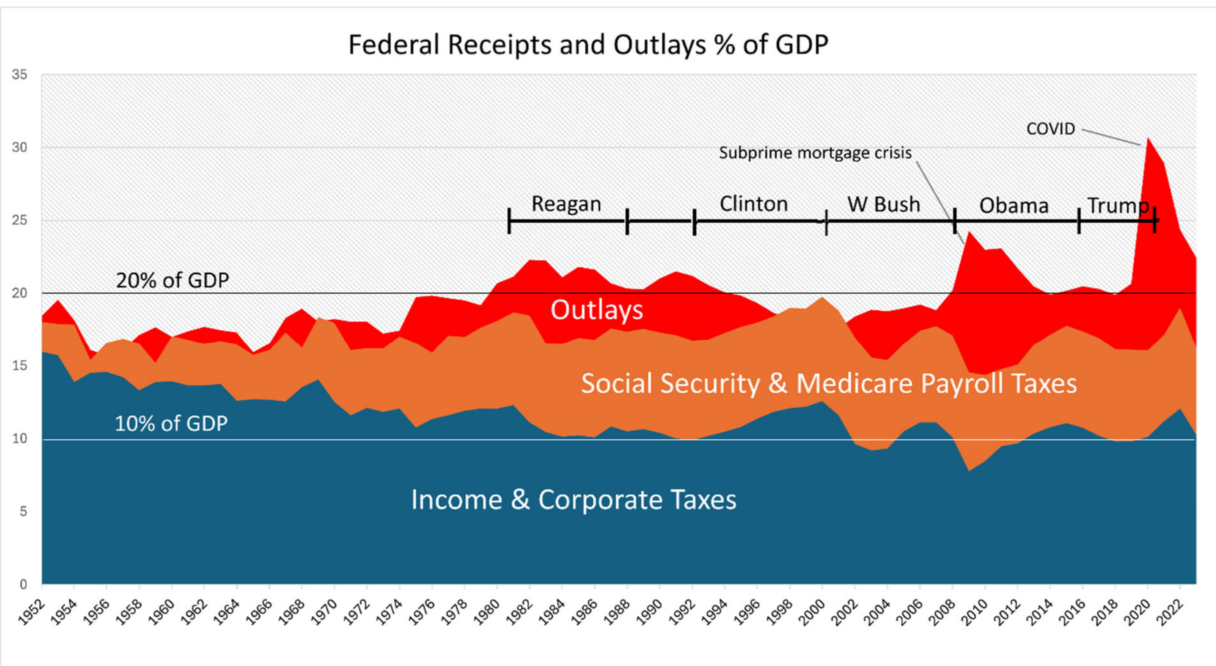

Figure 5 Federal Current Expenditures and Taxes as a Percent of GDP by Year. The spike around 2020 was COVID spending combined with a dip in GDP. Source: BEA, OMB via the Fed data interface, FRED. WW135

As the graph shows, income tax revenue has fallen from 15% to 10% as a percentage of the country's total income, GDP, while outlays have gone up somewhat, resulting in more borrowing and larger deficits. The red area in the chart is deficit spending. The deficit increased dramatically as a result of the Reagan era income tax cuts and increased spending. Under the Clinton administration, the Tax Reform Act of 1993 modestly raised taxes on the wealthy and corporations and cut spending. By 1998 it allowed Clinton's administration to run the first budget surplus in three decades and the last one to date. Under the GW Bush administration these tax increases were quickly reversed. It is estimated that the top 1% saw a tax cut of $50,000 per year[6]. Deregulation, which was a mantra under Reagan and Bush, resulted in the subprime mortgage meltdown in 2008 which required a mountain of red ink to fix. Most recently COVID, a natural disaster, also required huge deficit spending to keep the economy from tanking.

The chart below shows how this deficit spending adds up over time.

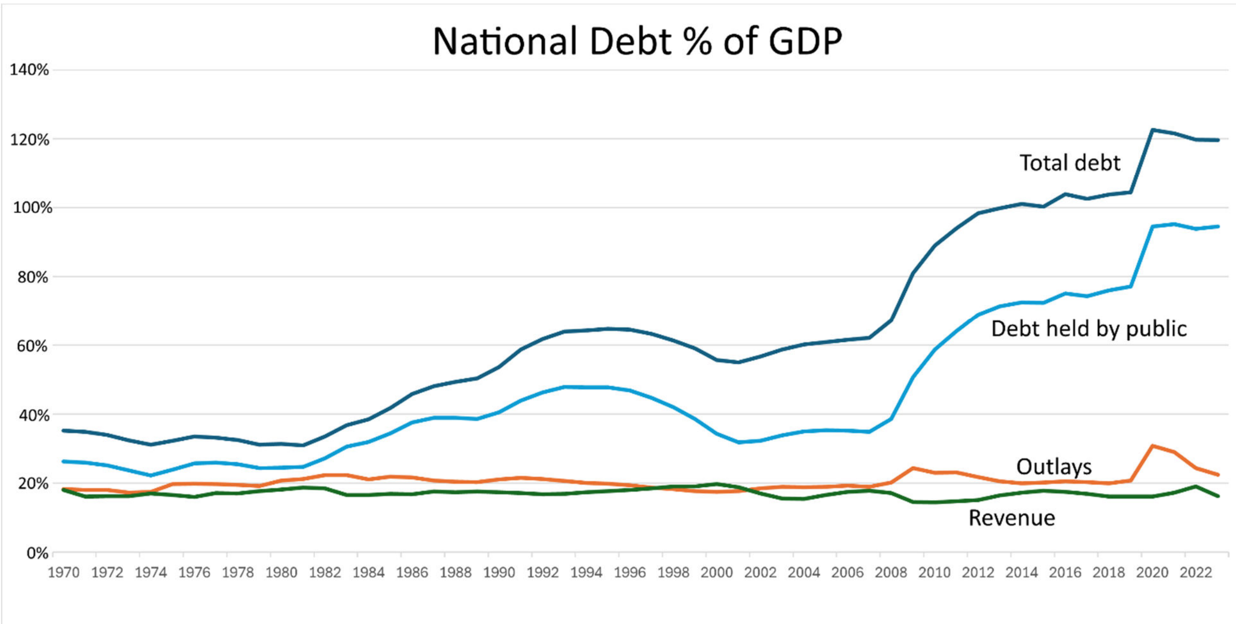

Figure 6 National Debt as a percent of GDP. Source: FRED WW140

In the chart, there are two lines shown for debt: debt held by the public and total debt. Why? Because a lot of debt is "intragovernmental" loans. Social Security ran a surplus for many years and accumulated $2.7 trillion in the Social Security Trust Fund by 2022. That money was "invested" in special Treasury bonds, which then reduced the amount of public borrowing the Treasury had to do to close the deficit. In the chart above, total debt includes intragovernmental borrowing, while the "debt held by the public" line is the amount of actual public borrowing the Treasury had to do. The difference between the two lines is the amount our right pocket borrowed from our left one. Of course, we'll have to pay that money back to ourselves if we're going to collect full social security benefits. In effect, we borrowed Social Security surpluses to partly finance income and corporate tax decreases which benefited the wealthy most (as do any broad tax cuts.) To make matters worse, when the Treasury borrows money, it does so by selling bonds which are interest bearing IOUs. When interest rates go up, the cost of this borrowing increases, and as we saw interest payments are now about the size of the defense budget. Of course, if interest rates drop so will interest on the national debt.

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6 https://www.cbpp.org/research/the-legacy-of-the-2001-and-2003-bush-tax-cuts

US Taxes

As we saw in Figure 5, income tax collections as a percent of GDP have come down, while Social Security and Medicare taxes (also called payroll or FICA taxes) have stayed pretty constant. Payroll taxes are predominantly paid by the middle class and poor as a fixed percentage of income with a cap. A middle-class household pays 15.3% of their income in payroll taxes while a household in the top one percent paid an average 2.2 % in 2020[7]. On the other hand, most income tax is of course paid by those with the most income even in the absence of progressive tax rates. The five percent of GDP decline in income and corporate taxes between 1952 and 2022 shown in Figure 5 equals about $1.36 trillion per year in lower revenue now, most of that going to the wealthy. So, there has been a shift in the tax burden when total revenue is considered.

Table 1 shows the highest marginal tax rates and number of brackets for some years. A tax bracket is a range of income. For example, in 2000, income below $43,850 was taxed at a 15% rate, any income above that and below $105,950 was taxed at 31% rate. As can be seen, during the boom times following WWII there were many brackets and the top marginal rate was over 90%. The wealthy now pay a maximum rate of 37% on income above $693,750. Corporate income tax rates have also come down, but Social Security and Medicare taxes have gone up.

Table 1 Tax Rates/Brackets for married filing jointly. Sources: https://www.whitehouse.gov/omb/budget/historical-tables/ historical income tax rates, https://www.ssa.gov/oact/progdata/taxRates.html, https://taxfoundation.org/data/all/federal/historical-corporate-tax-rates-brackets/

Year	Highest Marginal Personal Income Tax rate	Number of Brackets	FICA rate (Payroll Tax)	Highest Corporate Income Tax rate	Capital Gains rate
1960	91%	25	6%	52%	25%
1975	70%	33	11.70%	48%	35%
2000	40%	5	15.30%	35%	20%
2023	37%	6	15.30%	21%	20%

The chart below shows a snapshot of how the Federal Government paid for outlays in 2023. Most Federal revenue came from individual income taxes (53%), Social Security and Medicare (FICA) payroll taxes were one third, corporate income tax contributed a bit less than 10% and everything else was around 5%. Estate and gift taxes contributed less than 1%. To make up for the budget deficit, we borrowed more than payroll taxes bring in!

[7] Effective tax rates, CBO, as complied at https://www.taxpolicycenter.org/statistics/historical-average-federal-tax-rates-all-households

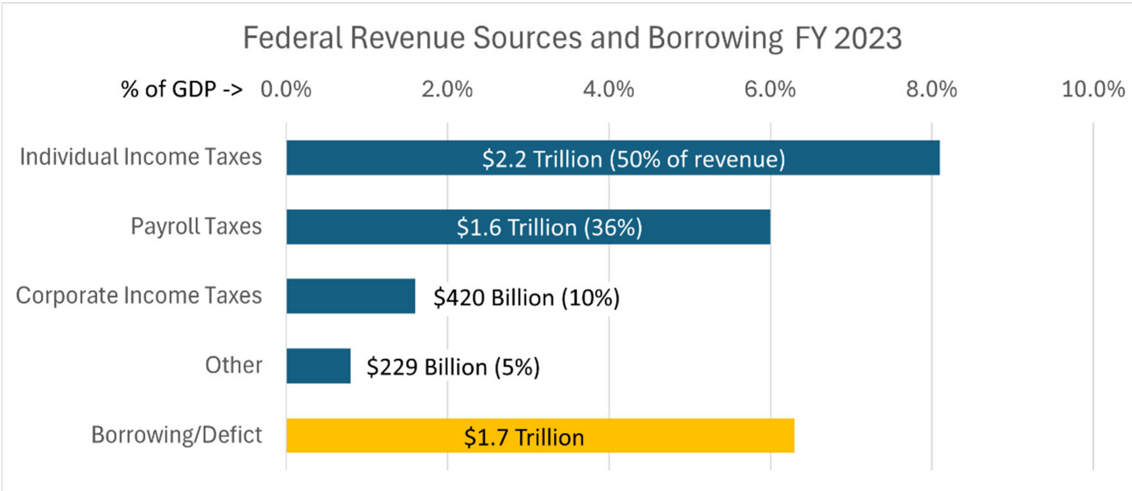

Figure 7 Federal Revenue Sources and Borrowing 2023 as a percent of GDP. Source: https://www.cbo.gov/publication/59727 WW131

Let us look at these sources in a bit more detail.

Payroll Taxes

The payroll or FICA tax is the simplest of the taxes. Payroll taxes include the Social Security tax and the Medicare tax. Social Security taxes are pretty high: 6.2% of wages paid by the employer and 6.2% paid by the employee for a combined 12.4%[8]. But that is up to a wage limit of $160,200 in 2023. Someone earning $10 million a year in wages paid the same $19,865 in Social Security contributions as someone earning $160,200. There is no lower limit on the wages taxed. The Medicare tax rate is 1.45% for both employer and employee and there is no cap. Payroll taxes are only paid on wage or salary income. They are shown in orange in Figure 5.

Income Taxes

Individual income taxes are paid on total income which includes wages, realized capital gains, dividends, and pass-through business income. But the *rates* on each of these types of income are different.

We all understand the tax on **wage income**. It's taken out of our paychecks. The rate is from 10% to 37% currently depending on your wage or salary.

Realized capital gain income is what you make from selling an asset such as a stock or house over what you paid for it. Until the asset is sold, there is no "realized capital gain" for tax purposes. In 2018, Jeff Bezos the Amazon CEO had salary of $81,840. His total compensation

[8] Self-employed pay both parts, currently 15.3%. The split between employer and employee is cute but employers figure the cost of labor based on all costs including taxes and benefits. So, the entire amount really is "paid for" by employees in the form of lower after-tax wages. In exchange we get guaranteed, inflation-protected, life-long income with survivor benefits.

package came to $1,681,840. But since he owned roughly 16% of Amazon, the value of his stock went up about $27 billion. None of that unrealized $27 billion in appreciation counted as income for tax purposes. This allows great wealth to be built essentially untaxed. When you do sell, the tax rate on capital gains is 20% (or lower if your income is below $492,300). That rate is much lower than the tax on wages would be for the same amount, and there is no payroll tax.

Dividend income is income you receive often from owning a stock which pays out profits to stockholders. They were taxed at the same rate as wages until the George W Bush tax bill of 2003. They are now taxed at the same rate as realized capital gains (20% or lower)[9]. Dividends like capital gains go disproportionately to the wealth since they own a lot of stock. No payroll tax is paid on dividends.

Pass-through business income is profit from a privately owned business, such as an S-Corp, which is "passed through" to the business owners. Pass through income is taxed like wage income, except no payroll tax is assessed. In the Trump administration tax bill of 2017, which lowered the top income tax rate, a 20% deduction for pass through business income was created. The pass-through rate is currently 20% lower than for wage income. As we saw in Part 2, some very large privately owned US corporations, such as Mars Inc., the candy company, are organized as pass through businesses.

Corporate Income Tax

The corporate income tax is a tax on the profits of companies organized as "C Corps" for tax purposes. The 2017 tax bill lowered the corporate income taxes rate from a maximum of 35% down to 21%. To be fair, a lot of large profitable US companies were able to pay no or minimal corporate income tax before 2017 by utilizing various loopholes. The 2017 bill, the Tax Cuts and Jobs Act or TCJA, was designed to reduce the incentive for multinational US companies to "book" profits through subsidiaries in low tax countries among other things. The jury is out on whether that has happened, but one effect has been to reduce corporate taxes collected by 40 percent[10].

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Other Revenue Sources

There are other smaller sources of revenue for the Federal Government such as excise taxes. The estate tax brings in less than 1% of revenue.

Spending Through the Tax Code

[9] There are further details omitted for simplicity that don't materially change the effect
[10] https://www.pgpf.org/blog/2024/05/how-did-the-tcja-affect-corporate-tax-revenues#:~:text=The%20changes%20to%20corporate%20taxation,the%20law%20was%20in%20effect.

One can download the Internal Revenue Code, Title 26 of the laws of the US, from a congressional site. The Federal tax code is 7,058 pages long. By comparison, Title 24 - Hospitals and Asylums, is 89 pages. Clearly it is a life's work to get a handle on the tax code and keep up to date with changes. All recent Presidents have decried the complexity of the tax code and promised to try to simplify it and eliminate "loopholes". The Mercatus Center, often described as a conservative think tank, said of the 2017 Trump administration tax reform effort "If recent history is a guide, and if special interests are able to dictate the terms of the debate on Capitol Hill, an attempt to de-rig the tax code will turn into a re-rigging."[11] The liberal Center for American Progress' analysis of the resulting legislation suggests that indeed re-rigging occurred just as it has in the past[12]. Economists from across the conservative/liberal spectrum agree on the need for tax reform, as they do on a surprising number of economic issues.

The tax code is long and complex for many reasons, including the accumulation of provisions over the years, frequent amendment, the need to provide detailed instructions for the many types of entities and transactions covered, and special tax breaks which are referred to as "spending through the tax code".

While tax breaks are often ostensibly enacted to serve some desirable end, it is estimated that "spending through the tax code" cost over $1.6 trillion in 2023. Here are some of the biggest breaks for individuals:

Table 2 Federal Tax Expenditures[13]. Note that in this table, Earned Income Credit outlays, not just tax credits, are shown. Those are also shown in the table on Federal Outlays above.

Row	**Expenditure**	**Annual Cost (Billions)**
1	Reduced Rates of Tax on Dividends and Long-Term Capital Gains	$238.80
2	Defined Contribution Plans	$193.40
3	Exclusion of Employer Contributions for Health Care, Health Insurance Premiums, and Long-Term Care Insurance Premiums	$187.40
4	Credit for Children and Other Dependents (includes Earned Income Tax Credit)	$184.70
5	Defined Benefit Plans	$94.70
	Total (All 165+ Expenditures)	**$1,721.20**

[11] https://www.mercatus.org/economic-insights/expert-commentary/tax-reform-will-trump-really-stand-special-interests
[12] https://www.americanprogress.org/article/broken-promises-special-interest-breaks-loopholes-new-tax-law/
[13] The source for this table is the Tax Foundation https://taxfoundation.org/blog/largest-tax-expenditures-saving-investment-tax/ which is based on a Joint Committee on Taxation report. The Treasury also has data on all tax expenditures at https://home.treasury.gov/policy-issues/tax-policy/tax-expenditures.

The total is about the same as all discretionary spending in the budget. What purposes do these tax breaks serve?

Capital gains tax rates (row 1) have long been lower than income tax rates. One reason given is the need to account for inflation in figuring gains. If you hold a stock worth $10,000 and inflation runs 3% a year, in twenty years your stock would have to be worth $18,061 to have kept up with inflation. So, it would be unfair to have to pay a tax on the $8,061, you would have been better off spending the $10,000 in the first place[14]. Stock dividends are corporate profits distributed to shareholders. In 2003, the tax on those distributions was lowered for several stated reasons, one being that corporate profits were already taxed, and taxing the distributions was double taxation. As we will see, actual taxation of corporate profits is spotty at best.

Defined contribution and benefit plans (rows 2 and 5) allow the employee and employer to contribute pre-tax money to retirement plans such as IRAs and 401Ks. This reduces income taxes and is designed to encourage individual retirement saving. Employer contributions are usually linked to income: the higher the income, the higher the matching and allowed contributions.

Credit for children and, as of 2017, other dependents (row 4) are partially refundable tax credits of up to $2,000 per child or $500 per dependent. You can get this credit in full against your taxes if your jointly filing income is below $400,000. When enacted in 1997, it primarily benefitted middle- and upper-middle-income families since poor families could only claim a credit against any income tax they owed[15]. The credit is now partially refundable, meaning poor families can get a check of up to $1,600 annually per child even if no taxes are owed, subject to some conditions and limitations.

Row 4 also shows Earned Income payments, both tax credits and the much larger amount that is refunded (i.e. payments when no further income tax is due). These are also shown in the line on spending for income security in Figure 3. Earned Income Tax Credit (EITC) refunds are primarily directed to low income working households with children. This program is the US's main antipoverty program. EITC payments have kept many poorer families just above the poverty line.

While each of the above tax expenditures has a stated purpose or purposes, more than half the benefits go to the top twenty percent of households[16].

There are also "tax spending" breaks for corporations and certain industries such as oil and mineral extraction and agriculture that that are included in the trillion and half dollar total.

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[14] Some have suggested indexing capital gains to account for inflation.

[15] https://crsreports.congress.gov/product/pdf/R/R45124/4#:~:text=The%20child%20tax%20credit%20was%20created%20in%201997%20by%20the,incur%20when%20they%20have%20children.

[16] https://www.taxpolicycenter.org/publications/distributional-effects-individual-income-tax-expenditures-after-2017-tax-cuts-and-jobs/full. This data is charted at Policy Basics: Federal Tax Expenditures | Center on Budget and Policy Priorities (cbpp.org)

Corporate Tax Avoidance

In addition to spending through the tax code, there are enormous losses of tax income through legal tax avoidance and illegal tax evasion. We will look first at corporate tax avoidance.

Between 2018 and 2020 a few of the US companies with income in the billions that paid zero in corporate income taxes include Archer Daniels Midland, Edison International, FedEx, Principal Financial, Salesforce.com and T-Mobile[17]. How is that possible? Simply put, these companies, and many others like them, report billions in profits to their shareholders but use tax provisions and dodges to report lower or no profits to the IRS. Between 2018 and 2020 in particular, the tax reform act of 2017, the "Tax Cuts and Jobs Act" or TCJA, allowed companies to write off capital investment immediately for tax purposes instead of depreciating it over a useful lifetime as is usual in accounting.

A different, long-standing, way to avoid US taxes for US corporations is to "book" profits through foreign countries with ultra-low corporate tax rates. We have seen these tax havens before in Part 2 when we looked at tiny countries such as the Cayman Islands that "own" several trillions in US assets. Booking profits through a tax haven can be accomplished via a "corporate inversion" in which a company forms a corporate entity or buys a company in the tax shelter country and makes that company the corporate owner with the US company a subsidiary. A more popular gimmick is to use "transfer payments" along with intellectual property (e.g., patents or trademarks such as the Nike "Swoosh" which "belongs" to a paper subsidiary in Bermuda)[18]. How does this work? For tax purposes, companies can assign earnings to different subsidiaries around the world. For example, if a US based pharmaceutical company makes pills at a Puerto Rico subsidiary, it can assign or "sell" the patent for that drug to the subsidiary and pay monopoly pricing for the "imported" pills. The pills can then be sold in the US for minimal markup over the already inflated price resulting in most of the profit being assigned to the Puerto Rican subsidiary where corporate taxes are much lower. The big pharmaceutical companies are avid users of this tax strategy, reporting 75 percent of their taxable income in foreign subsidiaries while notoriously charging their highest prices and making most of their sales in the US[19]. The IRS recently billed Amgen $11 billion in back taxes and penalties for just one of these transfer payment schemes.

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[17] https://itep.org/corporate-tax-avoidance-under-the-tax-cuts-and-jobs-act/?gad_source=1&gclid=Cj0KCQjw6PGxBhCVARIsAIumnWZnXISBtQLAZ_T9qEAYliR-p49ts3WvOGeJXE5f3OWamzI3dJI1F0gaAthfEALw_wcB .
[18] https://www.icij.org/investigations/paradise-papers/swoosh-owner-nike-stays-ahead-of-the-regulator-icij/
[19] https://www.finance.senate.gov/chairmans-news/wyden-releases-new-findings-in-ongoing-pharma-tax-investigation

Apple is a notoriously profitable company and has in the past been a poster child for tax avoidance. Wikipedia's account is almost funny for those of us not familiar with the world of international tax gaming:

> ASI is an Irish-registered subsidiary of Apple Operations Europe ("AOE"). Both AOE and ASI are parties to an Irish advanced pricing agreement which took place in 1991. ASI is the vehicle through which Apple routed €110.8 billion in non–US profits from 2004 to 2014, inclusive. ASI's 2014 structure was an adaptation of a Double Irish scheme, an Irish IP–based BEPS tool used by many US multinationals. Under the Double Irish structure, one Irish subsidiary (IRL1) is an Irish registered company selling products to non–US locations from Ireland. The other Irish subsidiary (IRL2) is "registered" in Ireland, but "managed and controlled" from a tax haven such as Bermuda. The Irish tax code considers IRL2 a Bermuda company (using the "managed and controlled" test), but the US tax code considers IRL2 an Irish company (using the registration test). Neither country taxes it[20].

While in this case the sales occurred outside the US, at that time Apple would have been liable for US corporate taxes on these profits. By leaving the profits overseas Apple was able to avoid taxes until the money was brought back to the US. The 2017 tax reform included a tax break on bringing back money accumulated overseas, and Apple is making use of that to repatriate around $250 billion of accumulated cash at a lower tax rate[21]. American Fortune 500 companies held an estimated $2.6 trillion offshore in 2017, presumably as a result of tax avoidance schemes such as these[22].

Not all US companies can move profits around like this and so the corporate tax burden is unevenly distributed and favors large international companies, especially ones with a lot of intellectual property. In 2022, corporations overall paid total income taxes of 16% ($425 billion) on domestic profits of $2,736 trillion which, given the corporate tax rate of 21%, leaves 5% or $136 billion uncollected for one reason or another[23]. To make collections fairer, the Inflation Reduction Act of 2022 included a minimum corporate tax applicable to large companies of 15% of the profits they declare to shareholders.

Individual Tax Avoidance

20
https://en.wikipedia.org/wiki/Apple%27s_EU_tax_dispute#:~:text=ASI%20is%20an%20Irish%2Dregistered,from%202004%20to%202014%2C%20inclusive see also Apple Sidesteps Billions in Taxes and Profits at Apple's subsidiary in Ireland rise to $69bn

21 https://www.forbes.com/sites/kellyphillipserb/2018/01/17/apple-says-it-will-bring-cash-back-to-us-pay-38-billion-in-repatriation-tax/?sh=34f293002222

22 https://www.imf.org/en/Publications/fandd/issues/2019/09/tackling-global-tax-havens-shaxon

23 Profits source: Corporate profits with inventory valuation and capital consumption adjustments from U.S. Bureau of Economic Analysis, "Table 6.16D. Corporate Profits by Industry" (accessed Tuesday, June 4, 2024). Taxes paid source: US Treasury Dept https://fiscaldata.treasury.gov/americas-finance-guide/government-revenue/

In 2021 ProPublica reported some findings on a trove of IRS data it had received. The article starts as follows:

> In 2007, Jeff Bezos, then a multibillionaire and now the world's richest man, did not pay a penny in federal income taxes. He achieved the feat again in 2011. In 2018, Tesla founder Elon Musk, the second-richest person in the world, also paid no federal income taxes[24].

How is it possible for multibillionaires to pay little or nothing in taxes in a year when their wealth increases by billions? As we've seen, the trick is to have unrealized capital gains but low or no net income. If the value of Bezos' Amazon stock goes up by $27 billion in a year but he does not sell any of it, he doesn't have to pay any taxes on that unrealized capital gain. So said the Supreme Court in 1920. Ever since that time, the rich have been able to use a tax avoidance strategy called "buy, borrow, die" which works like this: (1) buy or build assets such as a company, (2) instead of paying yourself a salary or selling stock, borrow money using your assets as collateral, (3) never sell your assets and pass them on to your heirs or favorite charities when you die. Repeat.

It may not be immediately obvious why borrowing money would be a better idea than selling stock or earning a high income. Consider, if the maximum tax bracket is 37%, you would have to pay roughly that rate if you took a million dollars a year in salary. Or you could sell assets such as stocks and pay a 20% capital gains tax on the appreciation. But if you borrow a million dollars instead, using your stock as collateral, you only pay, say, 5% interest annually. Meanwhile, your stocks or other assets often grow at much higher rates, so you are effectively making money by borrowing on your wealth. There is no tax on borrowed money, and in fact if you use the money to buy investment property, the interest is tax deductible. Unlike the interest on a credit card.

What happens when you die? Federal estate taxes only applies to estates worth over $13 million net of debt and charitable bequests. Surviving spouses are exempt. What is more all estates get what is called "stepped up basis" meaning that the stock, business, real estate, or other assets you inherit are immediately assigned their value as of the date of inheritance. If you subsequently sell the asset, you only pay capital gains tax (maximum 20%) on the gain since you inherited it, not on the entire gain since the asset was first bought.

What about estates larger than $13 million? To quote Investopedia, "The portion of the estate that's above this $12.92 million limit in 2023 will be taxed at the top federal statutory estate tax rate of 40%. In practice, various discounts, deductions, and loopholes allow skilled tax accountants to reduce the effective rate of taxation to well below that level."[25]

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[24] https://www.propublica.org/article/the-secret-irs-files-trove-of-never-before-seen-records-reveal-how-the-wealthiest-avoid-income-tax
[25] https://www.investopedia.com/articles/personal-finance/120715/estate-taxes-who-pays-what-and-how-much.asp

These techniques and others allow the rich to build wealth while avoiding income and capital gains taxes. Depending on the size of the estate, most or all of that wealth can be passed on to heirs on a stepped-up basis thus permanently avoiding even capital gains taxes on the increase. This kind of tax avoidance is less effective for those earning most of their income as wages, which includes everybody right up to the 99th percentile as we saw in Part 2.

Tax Evasion

Above we looked at legal ways corporations and individuals *avoid* taxes. Tax *evasion* refers to illegal methods of reducing taxes. Estimates of the annual loss just for US Federal taxes run as high as $1 trillion per year, although the official IRS "tax gap" between what it collects and what it estimates is due was $688 billion in 2023[26]. That means that about 85% of taxes due are paid eventually, leaving about one dollar in six unpaid. Most tax evasion is simply understating income in a way that is easy for auditors to detect, but wealthy individuals can use shell companies and accounts in tax haven countries to hide money in ways that are difficult to untangle. High value tax audits take considerable resources and, until recently, the IRS was starved of resources despite the fact that each dollar spent on investigating complicated tax returns yields about six dollars in taxes and fines[27].

US Economic Issues

Now that we've looked at how the US Federal Government raises and spends money, we can look at some of the economic issues we face and how they relate to these changes in government taxation and spending. Remembering that in a democracy, the government is us, we can then look at how we could address some of these issues.

Growing Income Inequality

Productivity has continued to grow in the US, which means that every year we produce more goods and services per hour of work than the year before. In the past, median wages and salaries grew in sync with productivity. That is the expected result of productivity increases: if labor on average produces more per hour of work, then workers, on average, will get paid more per hour of work. After all, the value of all the goods and services produced in a country is its gross income and that goes up per worker when productivity increases. As many authors have noted, though, for the last 50 years inflation-adjusted incomes for most workers have not risen along with productivity increases in the US. The chart below shows this relationship. "Net domestic product per worker" is the value of output per worker with depreciation of machinery,

[26] https://www.budget.senate.gov/chairman/newsroom/press/whitehouse-offshore-tax-evasion-by-big-corporations-the-wealthy-cheats-american-people#:~:text=The%20IRS%20estimates%20tax%20cheats,gap%20could%20be%20%241%20trillion.
[27] https://www.cnbc.com/2024/02/22/tax-evasion-by-wealthiest-americans-tops-150-billion-a-year-irs.html

infrastructure, housing, and other capital goods taken out. It is the amount of money every worker could be paid if national income was distributed evenly.

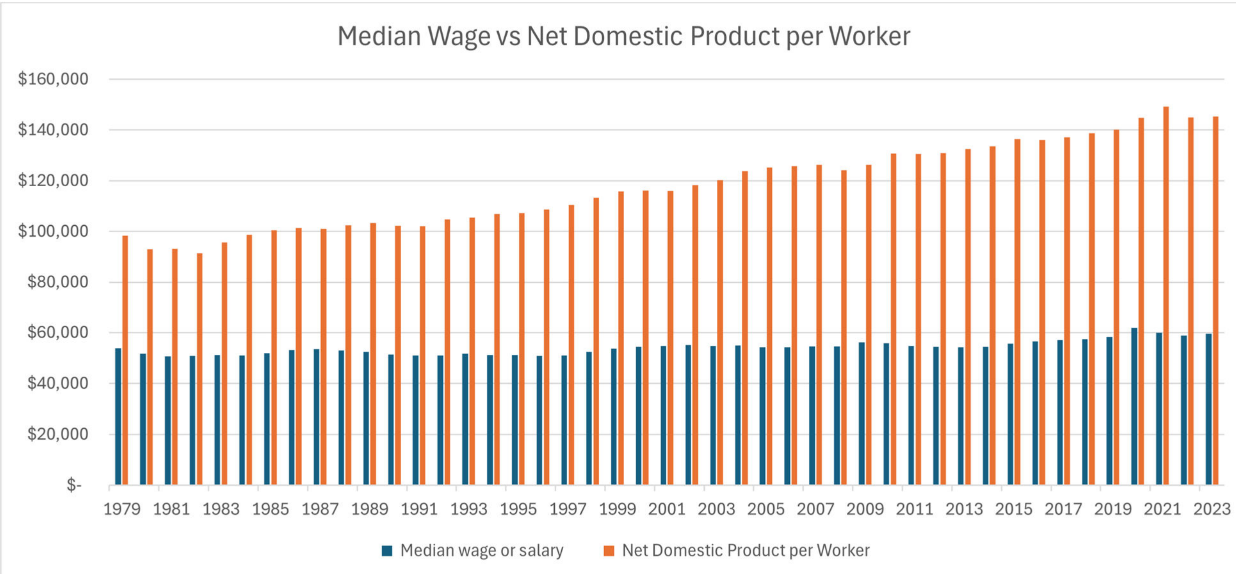

Figure 8 Median Wage vs Net Domestic Product in inflation adjusted 2023 Dollars. Sources: BLS and BEA via FRED[28]

The gap between the blue bars (median wage or salary) and the orange bars (how much on average workers could make if all net national income was distributed to workers) represents a huge amount of moola. It is also clear that in 2023 this gap was much larger than in 1979. Where has all this money gone? The answer is that income inequality has risen. Income at the top of the income spectrum has risen while the median wage income hasn't risen at all in purchasing power over the last 45 years.

We should note that "income" has varying definitions. In the chart above we are looking at how "national income", which is the value of everything the economy produces in a year, is distributed. National income doesn't include capital gains because selling an asset doesn't increase output, it just transfers ownership. This is unlike the definition of income for tax purposes which includes capital gains. Inequality researchers generally focus on national income when looking at the distribution of income. Ownership of capital comes into play when looking at wealth inequality.

The charts below shed more light on how national income distribution has changed over the last century.

[28] Inflation adjusted by CPI. Other inflation indexes such as the PCI might show higher growth but the ration between the two lines would stay the same. Net Domestic Product is the total value of output for final sale less depreciation.

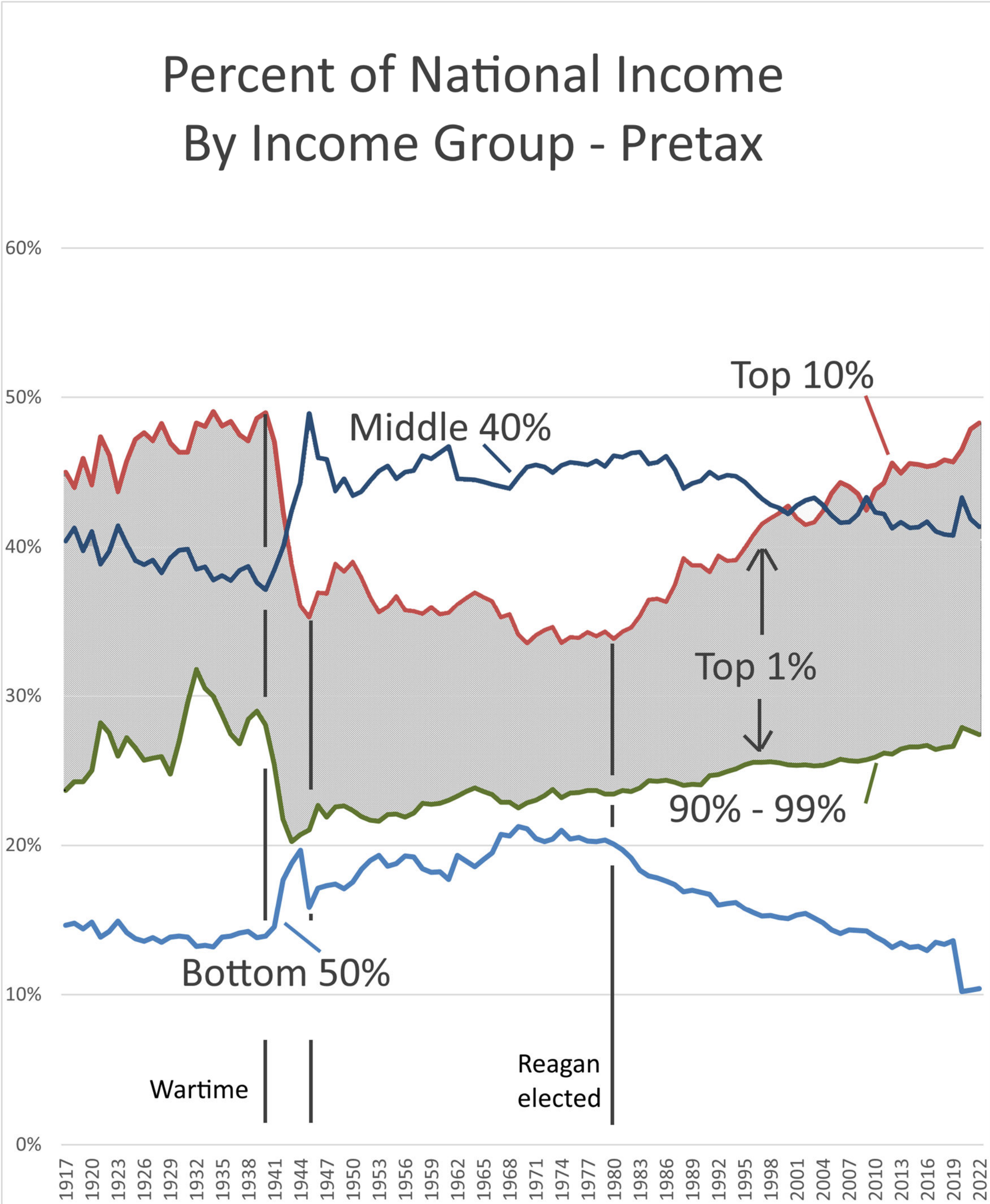

Figure 9 Pretax share of national income by income group. Includes pensions but not capital gains, taxes or transfers other than public pensions. Source: World Inequality Database WW143

Figure 9 shows how national income has been distributed between income groups over the years. The bottom 50% currently has about 15% of national income. The green line is the share of income of the top 10%, not including the top 1%. The grey area is the percent of national income going to the top 1%. During World War II, price and wage controls reduced the top 10% and top 1% share of national income and after the war high marginal tax rates kept a lid on those shares. Meanwhile the middle 40% share increased during the war and stayed there until the late 1970's, while the bottom 50%'s share of income went up over the same period.

Reagan was elected in 1980, and Congress passed his first big tax cut in 1981. Almost immediately the upper one percenters' share of national income started rising and middle- and lower-income group shares fell.

The same chart looks a bit different after taxes and transfers.

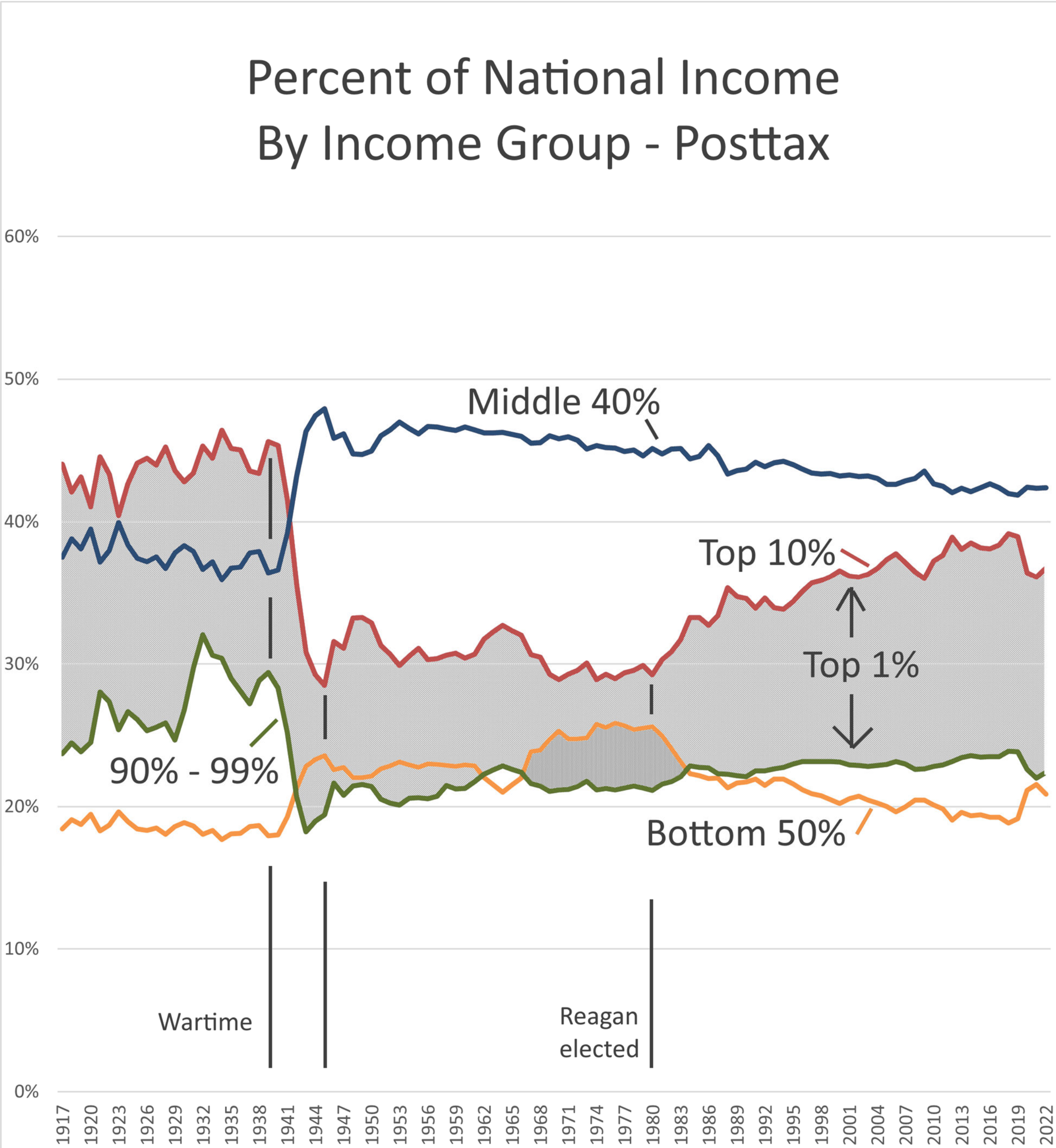

Figure 10 Share of National Income after taxes and transfers. Taxes include Federal State and Local. Source: World Inequality Database WW143

In Figure 10 we see that taxes and transfers have distributed a bit of national income from the top 10% to the bottom 50% but haven't made much of an impression on the top 1%. (The dip in top income share with the matching rise in the bottom 50% after 2019 is a temporary COVID relief bump.) Meanwhile, as we saw in Figure 5 the national debt has ballooned because tax cuts were not matched by spending cuts. In fact, the Reagan tax cuts were across the board and included expanding the Earned Income Tax Credit, so spending went up while tax receipts went down.

These two charts show that share of national income has grown for the very top of the income distribution, the one percenters, and declined for the middle class and lower 50% of the income distribution. The growth in share for the top 10% without the top 1% is modest after taxes. But even within the top 1% growth in income share is skewed. The chart below shows the growth in actual dollar mean (average) income per adult for groups within the top 1%.

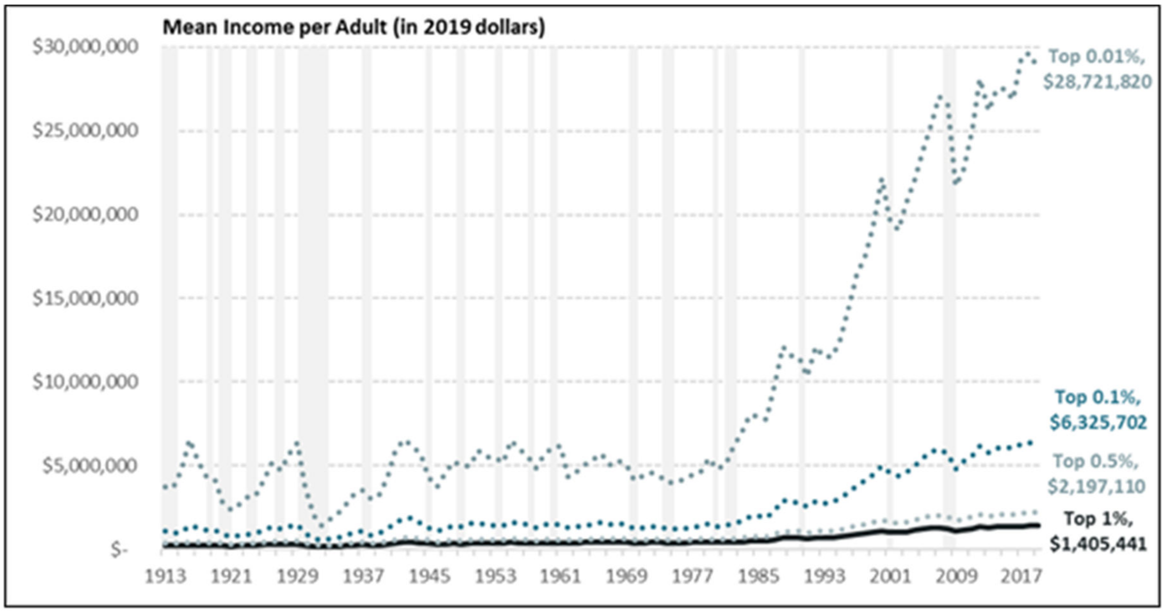

Figure 11: Mean Income Per Adult, Top 1%, 1913 to 2017 - Note that lower income groupings include higher ones (e.g. top 1% includes top .5% and .01%). Source: Sarah A. Donovan, Joseph Dalaker, Marc Labonte, Paul D. Romero. 2021. "The U.S. Income Distribution: Trends and Issues." Congressional Research Service.

We can get an idea of what this increase in national income share is worth in dollars by noting that at the time Reagan was elected the top one percent share of national income was a bit under 30% and just before COVID in 2019 it was nearly 40%. Ten percent of net national income is around $2.3 trillion dollars per year as of 2023. That works out to over $14,000 per worker in the US. A lot of moola indeed.

What caused this shift of national income from bottom and middle to top? The economy is complex and there are many interrelated factors. In the end though inequality would be significantly reduced if we restored the progressive income tax rates that we had pre-Reagan while trimming tax avoidance. I outline such a program below. It is still worth briefly mentioning the factors that did, and did not, contribute to the rise of the top one percent share of income, and the stagnation of median incomes.

We've already mentioned tax cuts. Reagan's 1981 tax cut slashed Federal revenue by 2.9% of GDP, surpassing even the 2.7% tax cut at the end of World War II. The deficit ballooned so quickly that Reagan agreed to a series of tax hikes to restore about half of that revenue loss.

When Reagan was elected the top marginal rate was 70% and by the time he left office it was 28% and applied to adjusted gross income above around $30,000. The top rate has never recovered[29].

Aside from taxes, technology change, such as the automation of manufacturing, is often mentioned as having disproportionately benefited workers with higher education and specialized skills, leading to increased wages for these workers while wages stagnate for less-skilled workers. But evidence for what is called skill-biased technological change is lacking and, in any case, wouldn't explain the increasing one precent share. It is more likely that technology change was one of several factors that lead to a decline in labor's bargaining power, especially for lower income workers. The same could be said of trade and outsourcing and the union busting techniques that came into vogue around the time of Reagan's election. In addition to these factors, there was a change in corporate culture that prioritized shareholder value over other stakeholders, such as employees, leading to a focus on short-term profits and cost-cutting, including wage suppression. Shareholder primacy in turn led to ballooning CEO compensation, often tied to stock performance, which contributed to the income gap between top executives and average workers. To all these factors we have to add the rise of enormously profitable "superstar" firms in technology and pharmaceuticals and other industries, often relying on intellectual property (patents) and network effects (getting there first, like Facebook). Finally, increased use of capital has slightly reduced the share of national income accruing to labor.

Trying to identify the relative contribution of each of these factors is probably impossible[30]. What labor has lost has in large part flowed through to the top one percent - actually mostly to the top one tenth of one percent - through profits. Corporate profits in the US have increased to about 12% of GDP from a long-term average of around 7% of GDP. These profits are distributed to shareholders and the wealthy get much of their income from these distributions. The chart below shows the increase in corporate profits as a share of GDP.

[29] There were also tax cuts and expanded earned income credits in the bipartisan Reagan era tax bill of 1986 that effectively removed 6 million lower income Americans from the tax rolls. Furthermore, effective tax rates didn't change as much as one would think from the change in marginal rates. The tax code is complex and high-income individuals had many ways to reduce their tax burden before Reagan as well as after.

[30] In Part 2 we saw that both trade and immigration are far less important than technology change in explaining deindustrialization, and both have had positive effects on real incomes.

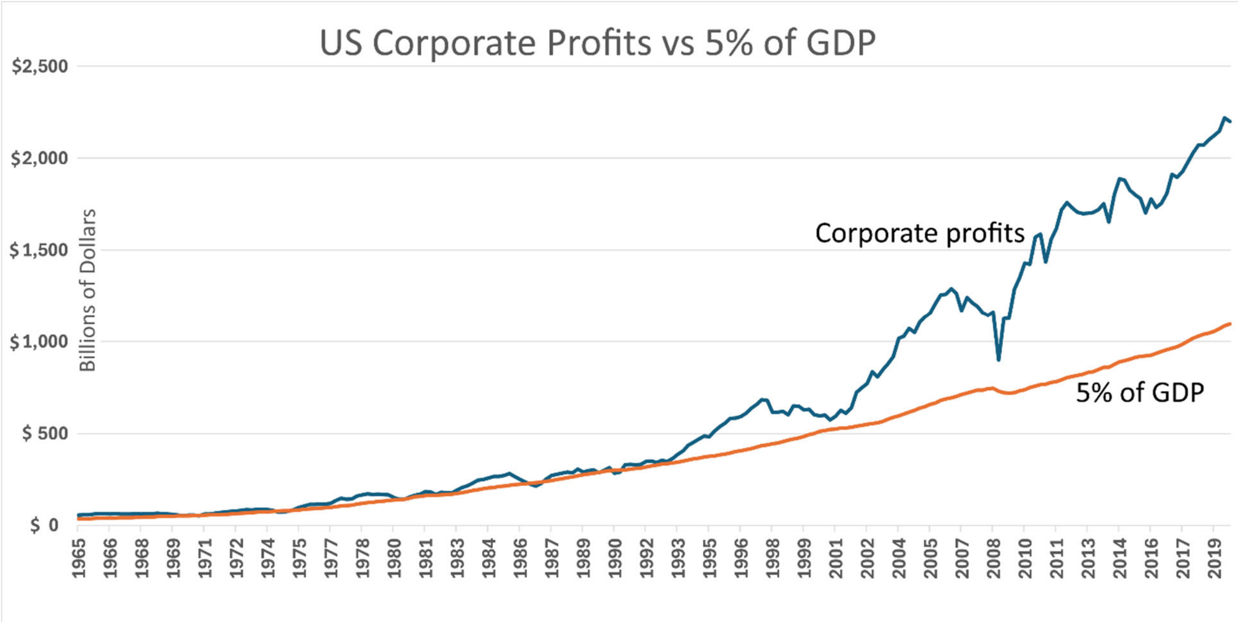

Figure 12: US corporate profits (all corporate types including C, S and REIT but not partnerships) vs 5% of GDP. Corporate profits have risen as a percent of GDP. Source: BEA via FRED (CPATAX series). WW147

Reagan justified his tax cuts for the wealthy by citing a theory called "supply side economics". This theory supposes that the wealthy will invest their tax savings in business which will in turn stimulate productivity and drive down production costs. These lower costs will drive an increase in demand which will increase the size of the economy. That increase in the size of the economy will result in more tax revenue, enough to cover the cost of the tax cut. Supply side theory is often referred to as "trickledown economics" because the tax cuts for the wealthy will supposedly trickle down to the middle class. It runs counter to the widely accepted notion of supply rising and falling to meet demand, and productivity increases being driven by technology change. There is no empirical evidence to support supply side theory and indeed as we've noted, while any tax cut will stimulate the economy by increasing demand (demand side, not supply side), deficits ballooned as a result of these cuts. David Stockman, Reagan's budget director, was quoted as saying that the tax cut "was always a Trojan horse to bring down the top rate.... It's kind of hard to sell 'trickle down.' So the supply-side formula was the only way to get a tax policy that was really 'trickle down.' Supply-side is 'trickle-down' theory." During the presidential primaries, George H.W. Bush referred to Reaganomics as "Voodoo Economics". None the less, tax cuts for the wealthy were enacted during the George W. Bush and Donald Trump administrations. The Trump era tax cut of 2017 lowered the tax on corporate dividends, a major source of income for the top one percent, from the income tax rate (max 37%) down to the capital gains rate of 20%. That tax cut also lowered the corporate income tax rate from a maximum 35% down to 21%. In short, a double tax cut on corporate profits distributed to shareholders. Since spending hasn't been cut we have been borrowing money, including Social Security Trust Fund money, to pay for tax cuts which benefit the wealthy most.

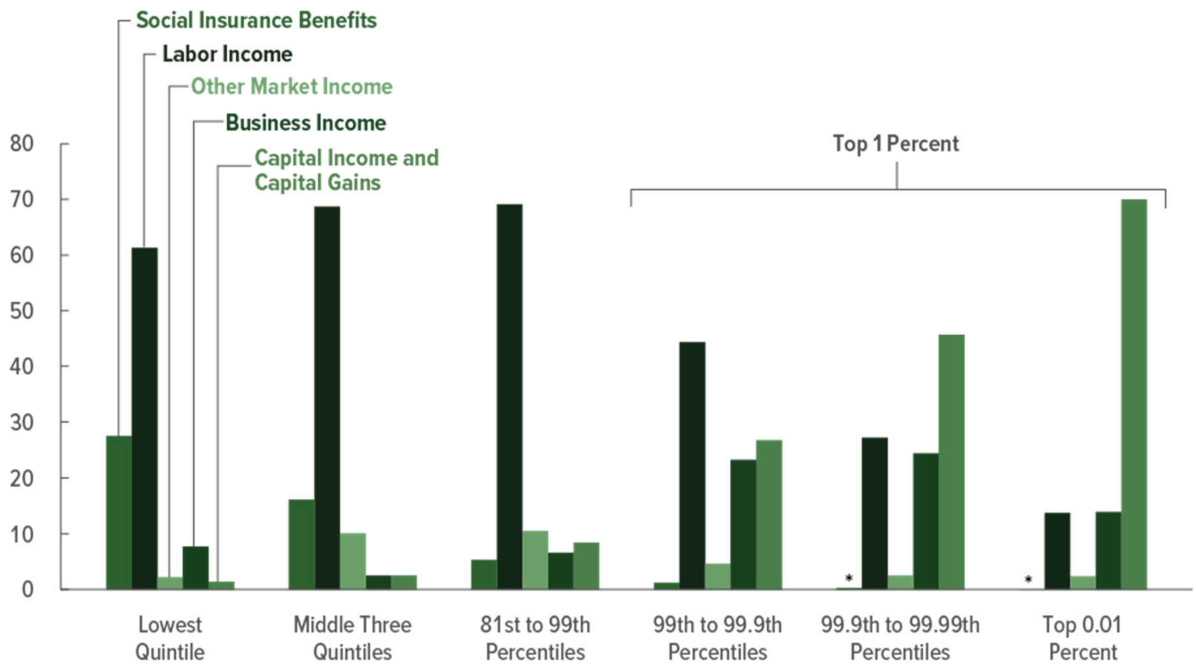

Figure 13: Percent Composition of Income Before Transfers and Taxes, 2019. Source: "The Distribution of Household Income, 2019." Congressional Budget Office. July 29, 2022

Growing Wealth Inequality

So far, we've been looking at how national income has been distributed and found that median wages have stayed essentially flat in purchasing power for the last half century, while the share of national income going to the top one percent has absorbed most of the real growth in the economy, even after taxes and transfers.

Wealth distribution is much more skewed than income distribution. It really is true that 3 men owned more wealth than the bottom 50% of Americans in 2018[31]. Here is the wealth distribution in 2024:

[31] https://www.forbes.com/sites/noahkirsch/2017/11/09/the-3-richest-americans-hold-more-wealth-than-bottom-50-of-country-study-finds/

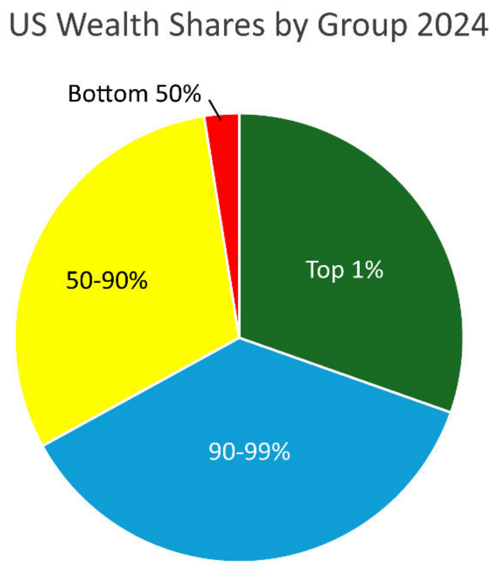

Figure 14: US Wealth Distribution. Source FRED https://fred.stlouisfed.org/graph/?graph_id=1361331 WW145

Most of the wealth held by the middle class is in the form of housing, and as the chart makes clear, the bottom 50% own very little of that. The graph below shows that the percentage of national wealth owned by the top one percent has been climbing since the late 1970's while the middle-class percentage has been falling. The increase in the one percent share represents about $18 trillion.

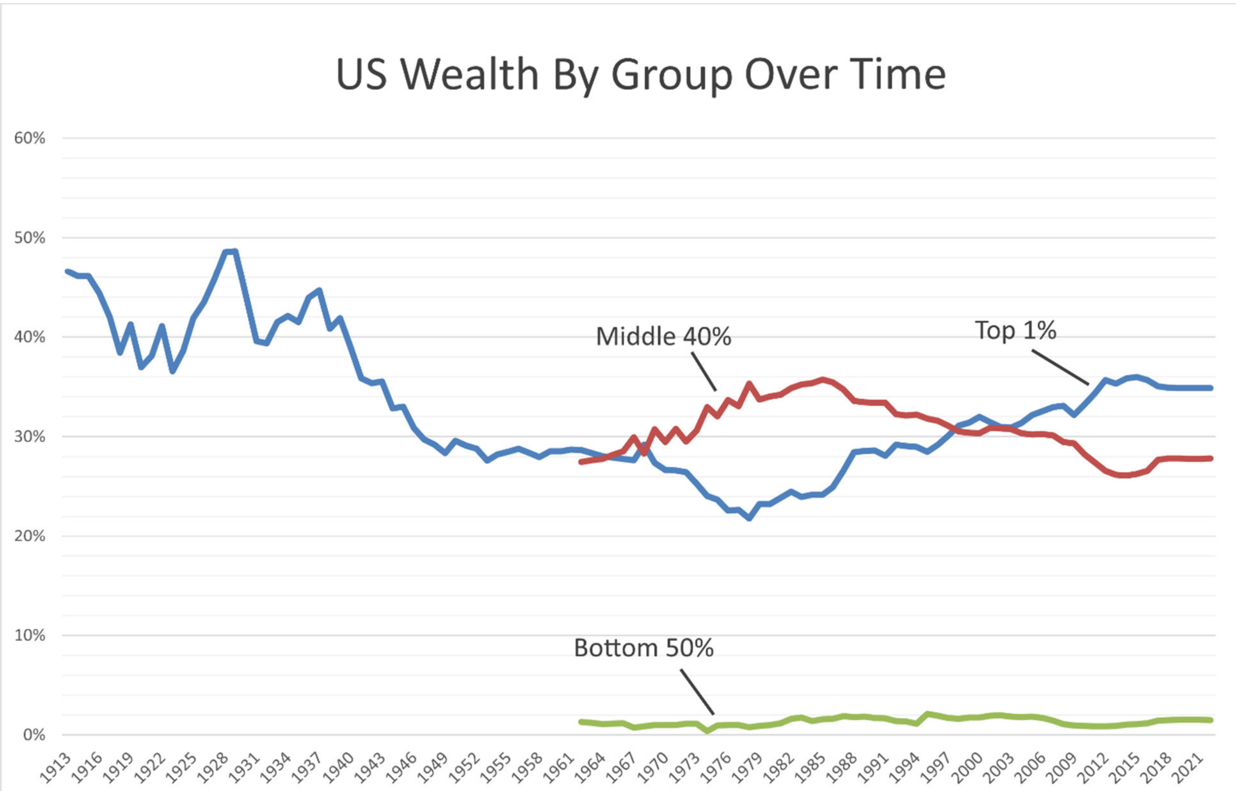

Figure 15: US Wealth by Group over time. Source: World Inequality Database. WW146

Clearly wealth distribution is heavily skewed and it's not getting better.

Declining Economic Mobility

Economic mobility is the ability to get ahead financially. It is the essence of what many mean by the “American Dream”. To be true to our vision of the US as a land of opportunity, someone born to poor parents should have a decent chance of achieving what we think of as a middle-class life. In Part 2 we looked at the data on mobility for countries around the world and found that mobility is similar to our European peers for the middle-class in the US, but that the sons of poor fathers have nearly a fifty percent chance of also being poor as defined by being in the lowest fifth of income. Daughters in the lowest fifth of income do better, about three quarters rise to a higher income group. In short, at both ends of the income spectrum, there is what is called high persistence. Intergenerationally, the poor tend to stay poor, and the well off tend to stay well off. What are the factors that underpin persistent poverty and what can we do about them? We look at that more later.

Increasing Deficit / Spending Pressures

We’ve seen that total Federal spending has remained fairly stable as a percent of GDP except during economic downturns and emergencies. That is actually remarkable given the enormous growth in retirement and medical care pass-throughs in the budget. Meanwhile, tax cuts and “spending through the tax code” have resulted in lower revenues. The result is the large ongoing deficits that started with the Reagan administration. We saw that we are borrowing about one third of our federal budget now. Clearly that can’t continue forever.

At the same time there is a critical need to invest. The 1950’s and 60’s highway infrastructure is crumbling, and we need to make twenty-first century investments in our energy sector which will yield enormous benefits in the future. At the same time the aging population will require continued funding for retirement and medical care. And since the world as a whole is not meeting climate goals, dealing with the effects of climate change will require huge additional infrastructure investments. Think about New Orleans after Katrina.

Clearly, we have better uses for money than corporate buybacks. In the section below, we look at how we can address all these issues.

Towards a More Perfect Union

Principles

I’ve repeatedly mentioned that the US is a rich country. It is also a country founded on the Enlightenment ideals of individual freedom, equality and opportunity. The government is there to serve the people by “promoting the general welfare”, not the other way around. Individuals are “born equal” and have “inalienable rights”. These principles, baked into the Declaration of Independence and Constitution, are the guiding lights of our democracy. Obviously forming “a more perfect union" was and is an ongoing project. Slaves had to be freed, and women had to get the right to vote. It has not been smooth sailing, but great progress has been made. If we keep these basic principles in mind, it is actually quite easy to see what makes for a more perfect union. Of course, everyone has their own interests. Plantation owners were made rich by the labor of their slaves, and it took a civil war to outlaw slavery. Religious zealots have at times not been happy with the separation of church and state. The progress that has been made is a testament to our belief in, and commitment to, these principles over many generations.

Many of us, me included, see a managed capitalist market economy as complimentary to the Enlightenment belief in freedom of the individual. This preference is not just based on market economics' proven ability to deliver, but also on the implicit concept of us humans as economic free actors. We can start a business, choose a career, change jobs, and buy and sell whatever we want within the limits of the law (if we obey it). However, a capitalist market economy, if left to its own devices, certainly does not promote equality of opportunity or general welfare. Basic market economic theory assumes that "labor" and "capital" will find their "best" uses, but if there is inequality of opportunity, the efficiency of the market is undermined. A capable child who misses out on education will probably not be as productive as they could be. That is a waste of human capital and lowers overall productivity. Put simply, it is good economically as well as in line with our core principle of equality that opportunity be widespread.

I'm going to outline my proposals for how we can address the US economic issues of growing income and wealth inequality, low mobility for those born poor, and an increasing deficit, and do so in a way that is consistent with our core principles and a managed capitalist market economy. But we must address one last philosophic problem. Some claim that taxation infringes on the individual and economic freedoms I espoused above. Nothing could be further from the truth. There is nothing in non-onerous progressive taxation that impacts personal or market freedom. In fact, progressive taxation is designed precisely to make sure that the tax load isn't onerous. Someone earning a million dollars a year can afford to pay a lot more taxes than someone earning twenty-five thousand without hurting. On the flip side economic deprivation certainly can impact both individual and economic freedom. The US had to come to grips with the effects of unfettered capitalism and the concentration of income and wealth in the first half of the twentieth century, and the result was the New Deal. I can do no better than quote from Teddy Roosevelt who set the stage. Here is a quote from a speech he gave in Osawatomie, Kansas in 1910[32].

"In every wise struggle for human betterment one of the main objects, and often the only object, has been to achieve in large measure equality of opportunity. In the struggle for this great end, nations rise from barbarism to civilization, and through it people press forward from one stage of enlightenment to the next. One of the chief factors in progress is the destruction of special

[32] This historic speech is well worth reading in its entirety. It can be found at https://obamawhitehouse.archives.gov/blog/2011/12/06/archives-president-teddy-roosevelts-new-nationalism-speech. For background see https://www.kshs.org/p/kansas-historical-quarterly-theodore-roosevelt-s-osawatomie-speech/13176

privilege. The essence of any struggle for healthy liberty has always been, and must always be, to take from some one man or class of men the right to enjoy power, or wealth, or position, or immunity, which has not been earned by service to his or their fellows."

"At many stages in the advance of humanity, this conflict between the men who possess more than they have earned and the men who have earned more than they possess is the central condition of progress. In our day it appears as the struggle of freemen to gain and hold the right of self-government as against the special interests, who twist the methods of free government into machinery for defeating the popular will. At every stage, and under all circumstances, the essence of the struggle is to equalize opportunity, destroy privilege, and give to the life and citizenship of every individual the highest possible value both to himself and to the commonwealth. That is nothing new."

"I stand for the square deal. But when I say that I am for the square deal, I mean not merely that I stand for fair play under the present rules of the game, but that I stand for having those rules changed so as to work for a more substantial equality of opportunity and of reward for equally good service. One word of warning, which, I think, is hardly necessary in Kansas. When I say I want a square deal for the poor man, I do not mean that I want a square deal for the man who remains poor because he has not got the energy to work for himself. If a man who has had a chance will not make good, then he has got to quit."

"The Constitution guarantees protection to property, and we must make that promise good. But it does not give the right of suffrage to any corporation…. There can be no effective control of corporations while their political activity remains. To put an end to it will be neither a short nor an easy task, but it can be done…Corporate expenditures for political purposes, and especially such expenditures by public-service corporations, have supplied one of the principal sources of corruption in our political affairs."

This speech outlined a progressive Republican platform (how things have changed!) that called for a national health service, an inheritance tax, a constitutional amendment to allow a federal income tax, an eight-hour workday, farm relief, workers' compensation for work-related injuries, and social insurance to provide for the elderly, the unemployed, and the disabled. The 26th Amendment allowing Congress to assess taxes on income was adopted in 1913, some other parts of the program were adopted during the presidency of Franklin Roosevelt. In any case, the balance between "property rights" and what is best for the country and the "general welfare" was debated extensively over the first half of the 20th century. To quote the Osawatomie speech one last time:

I believe in shaping the ends of government to protect property as well as human welfare. Normally, and in the long run, the ends are the same; but whenever the alternative must be faced, I am for men and not for property…

Teddy makes clear that there is a balance. But he was certainly on to something when he says, "in the long run, the ends are the same." As the president of General Motors remarked in 1953, he thought that what was good for the country was good for General Motors, and vice versa. Opponents of the reforms put in place during the first half of the twentieth century predicted dire consequences for business. Instead, these reforms ushered in the fastest productivity and widespread income growth in US history. While called “socialist” the reforms did not call for government ownership of the means of production, the economic system remained capitalist. What did change a bit were the rules by which business had to play, along with higher income tax rates for the rich. This turned out to be good not just for the country, but for business as well.

As we’ve seen, since Reagan there has been a considerable reversion to lower tax rates on high incomes, and a weakening of general labor’s market power due to a number of factors. The result has been the growth in income and wealth inequality we’ve discussed.

As the above history shows, the US has wrestled with the issue of taxation and regulation versus an extreme version of property rights that would call into question something as basic as progressive taxation. Precisely where the line is drawn has shifted over time, but the history of the 20th Century tends to support the contention that what is good for labor is good for the country and is good for business as well.

A thought experiment may help clarify the issue. One of the main causes of the loss of market power by general labor has been the automation of manufacturing. It simply takes far fewer workers to produce as many manufactured goods now as 50 years ago. Let us imagine that artificial intelligence likewise automates service jobs. Trucks drive themselves. AI largely automates the work of lawyers and accountants. Even writing is largely automated. All of this is great news for productivity: it takes far less labor to make and do these things. But labor loses market power (there is decreased demand for labor) while wealth and income inequality rise further. In an extreme version of this vision, machines manufacture the goods we make, and AI largely provides the services we consume. Labor and capital are no longer complimentary but competitive. Clearly, for the good of us all including business, we need to figure out how everyone can share in the wealth we produce. Below I suggest a program that extends the New Deal to account for the realities of our current world. Of course, such a program, like the New Deal will have to be driven from below, it will certainly not be handed to us on a platter.

Raising Revenues

We’ve looked at spending and found that while government spending has risen very modestly as a fraction of the economy, government tax revenues have fallen. We’re running an enormous deficit that can only be closed by raising revenue or decreasing spending. Spending cuts would have to come out of the programs that have somewhat lessened growing income and wealth inequality in the US, programs such as Social Security and Medicare and the Affordable Care Act. The growth in deficits has been fueled by reductions in taxes primarily benefiting the wealthy since Reagan’s time. Since cutting spending on social programs would have been unpopular, Republican administrations simply increased deficit spending, financed in part by “borrowing” the Social Security Trust Fund. It is time to reverse this trend. Income and wealth inequality have grown enormously. As during the gilded age, tax increases are necessary to somewhat flatten the income and wealth distribution. Democracy itself is distorted and threatened by such concentrations of income and wealth. The wealthy do not need trillions to live on, they can get by quite comfortably on a few million a year. As it is now, we're saddling our kids with debt to finance tax cuts that benefit the wealthy most while maintaining social spending.

We need the money. We have seen that about half the US population struggles to make a basic living. To quote a recent Brookings article:

Prior to COVID-19, almost half of the American workforce (44 percent or 54 million workers) earned low wages, with a median annual salary below $18,000. About half of low-wage workers had a high school diploma or less, with only 14 percent holding a bachelor's degree. Moreover, our research has shown that most low-wage workers churn through low-wage jobs, struggling to move up in a labor market with declining and uneven access to development and advancement opportunities[33]

With the advance of technology, there is simply less demand for labor. Since it is far from apparent that this situation will be changing any time soon if ever, other methods of apportioning the benefits of all this productivity have to be found.

On top of that, we need to invest money. To quote the Brookings article again

Public spending on physical infrastructure has persistently failed to keep up with economic growth; the U.S. spends only 2.3 percent of GDP on infrastructure, while European countries spend 5 percent on average and China spends about 8 percent. Just to meet basic national needs by 2025, the U.S. faces an estimated funding shortfall of more than $2 trillion. Several more trillions in spending on clean energy and climate change adaptation and mitigation will be needed to achieve carbon neutrality by 2050.

Climate change and sustainability due to human population growth and consumption are crisis as real as an advancing army. As during times of war, more revenue must be raised. There is a difference though. Investments in climate change and sustainability often yield returns far in excess of their costs. Sun and wind are free once you build the infrastructure to harvest their energy. If we don't invest in these technologies, we cede the field to those who do, most notably the Chinese.

As I have said many times already and will do again, the US is a very rich country. There is plenty of money (output, productivity) to go around. Everyone in the US could live a comfortable middle-class lifestyle based on current GDP if labor was paid more equally. There are many ways to accomplish that with a bit of imagination and will. Most economic programs start by

[33] Gandhi, Dhruv, Marcela Escobari, and Sebastian Strauss. 2021. "How Federal Infrastructure Investment Can Put America to Work." Brookings. March 17, 2021. https://www.brookings.edu/articles/how-federal-infrastructure-investment-can-put-america-to-work/.

listing all the great things they are going to do and either skip the part about how to pay for them or put it at the end. Let's do it the other way around. Here's the income distribution by percentage of households from earlier.

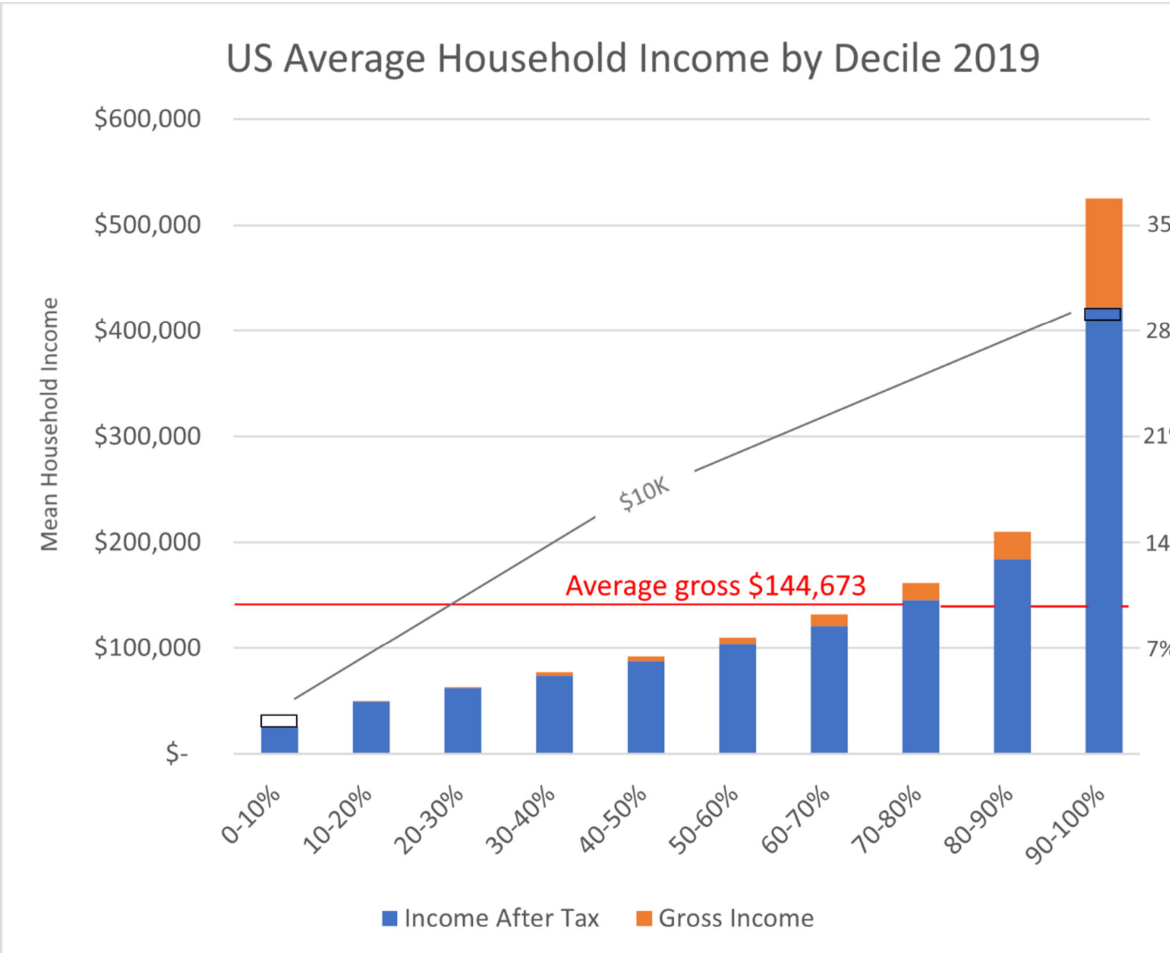

Figure 16 US mean (average) household income by decile group. Note that since the groups include the same number of households, this also shows the distribution of income: the 0-10% group has 1.8% of the total income while the 90-100% group has 36.6% pre-tax. The small black rectangles on the first and last bars are $10,000. The red line shows the income all households would have if personal income was evenly distributed. Personal income does not include capital gains. Data source: https://www.bea.gov/data/special-topics/distribution-of-personal-income WW126

Pretty clear why the upper 10% pay more income taxes than other groups, they make more. As we've seen within the top 10% income is even more skewed. Note that this accounting of income does not include capital gains, realized or not. It is not Elon Musk's or Jeff Bezos' untold billions that inflate this number, this is actual income received in a year. It also does not include all the money that is used to run a business such as depreciation and capital investment. In short, even if somehow all households participated equally in national income, the owners of capital and businesses would retain their wealth and could grow that. The capitalist engine that is so productive would continue to chug along unaffected by income redistribution. Jeff Bezos as we've seen, took a very modest wage at Amazon. That didn't prevent the company, and his net worth from growing exponentially.

Even if the political will were there, realistically we wouldn't be able to flatten the income curve completely, but we certainly can do better than the current one. The rich might have to limp along on a pre-Reagan share of national income, but they would still have incomes in the millions and unlimited wealth. There is no reason that half the US population has to struggle along on low incomes and no wealth. The money is there. How do we go about flattening the curve?

One obvious first step is to go back to New Deal thinking and tax the rich again. We need to raise marginal rates and brackets back to those that were in place during the boom times following WWII. Most of the benefits of the tax cuts have gone to high income households. As we saw on page 21, the shift in income to just the top 1% since Reagan's time amounts to $2.3 trillion a year, and the rich were hardly starving before then.

We also badly need tax reform: the 7,000-page tax code needs weeding and the elimination of special interest tax breaks to reduce or eliminate "spending through the tax code". That spending currently costs $1.7 trillion a year.

Tax evasion amounts to another $1 trillion lost a year, mostly from the wealthy. Beefing up enforcement would bring in much of that.

Increase the inheritance tax on large fortunes. It might be fair to allow entrepreneurs to amass huge fortunes during their lifetimes, but it is not fair to allow generations of their offspring to inherit huge fortunes. Small ones are enough.

The above measures could generate over $4 trillion a year in additional revenue, which was roughly the size of the entire Federal budget in 2019.

Let me mention a couple of taxes I'm not for. I'm not for a high corporate tax rate because that would put a tax on business, and in particular US businesses. While I'm against a higher corporate income tax rate, I'm for the elimination of tax shelters, which can only be done at the international level. Let's go for a low but uniform corporate tax rate that all companies pay.

Another tax I'm not for is a tax on wealth. This may seem surprising given that wealth is even more concentrated than income. The top one percent of the income distribution in the US holds more wealth than the bottom 80 percent[34]. But there is no need for a wealth tax to address wealth inequality, a properly designed, progressive, income and inheritance tax is sufficient, and there are a lot of difficulties in trying to implement a wealth tax. It's pretty easy to move wealth around or hide it, and valuation is difficult. Furthermore, I'm just fine with Jeff Bezos being extremely wealthy, I don't begrudge him his superyacht. Bezos came from a middle-class

[34] Six facts about wealth in the United States | Brookings

background, as did many of the wealthiest, and built a business that significantly increased productivity in a number of areas. Whatever one might think of some of the tactics involved, the Carnegies, Fords, Morgans, Gates', Musk's, and Bezos' of the world move the productivity needle. But what about their heirs? Here we run into one of my prime Enlightenment principles: equality of opportunity. It is also amusingly somewhat Nietzschean, and certainly free market: if we assume that human talent is widely distributed, then to maximize productivity, everyone should have an equal chance to make their contribution and earn their economic and other rewards. Realistically, if you can pass on a few million dollars to each of your kids, great. But beyond that, no. As Bill Gates has said "It's not a favor to kids to have them have huge sums of wealth. It distorts anything they might do, creating their own path."[35] And it certainly isn't fair to the homeless kid. High marginal income tax rates and inheritance taxes could be designed to ensure that vast wealth is not passed on from generation to generation.

Addressing Income and Wealth Inequality

Like Robin Hood, the above revenue measures would take from the bloated rich. How do we "give" that money to those who are at the other end of the income and wealth scale? Clearly Robin Hood would be called a Communist today, especially by the wealthy, but he really wasn't. He didn't have the legal power to confiscate lands, which were the primary source of income and wealth in his day. He just redistributed some of the income. We have proposed exactly that. But throwing around bags of gold coins is a recipe for drunken revels, not a serious way to address ongoing income and wealth inequality. Here are some suggestions which focus on increasing opportunity in particular.

Opportunity

Only a fool or a eugenicist would argue that there is no relationship between the economic circumstances of your birth and your opportunity in life. In the US, those born well off tend to stay that way, and those born poor tend to stay poor. The US was founded on the ideal of equality, and by that was meant equality of opportunity and before the law. The "American Dream" to most of us implies that if you work hard, you'll get ahead, in other words everyone has an opportunity to rise economically.

Clearly that is not always the case. During the Great Depression you were lucky to find work at all. It is also true now that in many occupations you can work your butt off and not "get ahead". And by "get ahead" we mean not just a rising income but also the ability to accumulate some wealth. As we saw in Figure 14 about half of us Americans have essentially no wealth.

One of the main findings of this book has been that general labor in advanced economies has had its bargaining position eroded, primarily by continued automation. We also looked at trade and immigration and other factors that are often blamed, but all the evidence points to automation as responsible for most of the loss in labor's bargaining position. It is simply a fact

[35] Mick Jagger Bill Gates May Not Leave Massive Inheritance

that less labor is needed to produce goods and many services. So, opportunity to “get ahead” for many has declined while the country as a whole has gotten richer. A plague or kicking out immigrants would improve general labor’s position as we found after COVID, but that is temporary. We simply must come to terms with the reality that redistribution of income now, as during the New Deal era, is both necessary and economically beneficial. Back in 1936 Franklin Roosevelt noted that “*man’s inventive genius released new forces in our land which reordered the lives of our people. The age of machinery, of railroads; of steam and electricity; the telegraph and the radio; mass production, mass distribution—all of these combined to bring forward a new civilization and with it a new problem for those who sought to remain free.”*[36]

The New Deal was a response not just to the Great Depression but also the realities of the industrial age. Programs such as Social Security, a guaranteed right to unionize, and a 40-hour work week, helped the industrial work force achieve a middle-class lifestyle. But as we’ve seen, 80% of us now work in “services”. We’re “postindustrial” and have to come to terms with what that means. Economists, from the left and right and center (everyone these days seems to be classified as either left or right, but in fact there is considerable consensus in professional economics) are concerned about the effects of deindustrialization on labor. The statistics we’ve seen on income and wealth are quite compelling but even more so are the accounts of widespread homelessness. How do we deal with the fact that the country keeps getting richer, but the middle class remains stuck, and the poor get less and less as a share? We suggest several ideas below. These ideas are complimentary and are designed to redistribute income while increasing opportunity and help those with no wealth to finally acquire a stake in the country. None of these ideas touch our capitalist economic engine, in fact it is essentially guaranteed that increased opportunity will translate into growth that will benefit our businesses and economy as a whole.

Poverty, Mobility and the Universal Basic Income in the US

The US is a country based on the concept of equality. But “born equal” doesn’t really work if, for example, you’re born a slave. Or poor in a country where opportunity is highly dependent on your circumstances at birth. Providing a good education for a poor child does not deprive a richer child of a good education, but it does increase opportunity for the poor child. Children grow up to be more productive, and both they and society richer, when education levels are higher as we saw in the section on developing economies in Part 2. But education by itself is not enough give poor children the same opportunities as better off ones.

Note that equality of opportunity does not imply equality of outcome. But the economic circumstances of a child’s parents do affect the child. That doesn’t mean we should strive for absolute economic equality, but it does mean that measures designed to help families achieve the basics of a stable life are helpful in the quest for greater equality of opportunity. A homeless

[36] Roosevelt, Franklin Delano. n.d. “FDR at Franklin Field_ A Rendezvous with Destiny _ University of Pennsylvania Almanac.”

child is obviously disadvantaged, and most certainly not “responsible” for that lack of opportunity. Again, from an economic perspective, lower productivity makes us all poorer and greater productivity makes us all richer.

In the discussion of mobility in Part 2, we found that US intergenerational income mobility is similar to other rich countries for the middle class, even the Scandinavian ones, but lousy for the poor. In short, we have a persistent economic “underclass” of people who find it hard to work their way out of poverty: if you’re born to poor parents your chance of rising in the income ranks is relatively low. Is there anything we can do about this that is in accordance with US ideals and a managed capitalist economy?

Of course there is. Some ideas include universal free preschool the way we already have universal free primary and secondary education. For younger children, free childcare is also an option. Studies show that *quality* programs of this type increase mobility substantially and have a net positive payback: returns for every $1 spent on such programs has been calculated as ranging from $2 for the short term to $17 when the child is followed through adulthood. Fewer grade repeats, special-ed classes, incarcerations, and higher lifetime earnings translate into these returns on investment for both the individual and society[37].

Many economists, including conservative ones, have suggested looking at a universal basic income or guaranteed basic income to reduce poverty and improve economic mobility[38]. These programs give all of us a fixed amount of money every month. A universal basic income goes to everyone as the name suggests, while a guaranteed basic income provides regular fixed amounts to poor families. The name “basic income” suggests such programs would provide enough to live on, but the numerous pilot programs that have been run only provide $500 to $1,000 per month. Still, they have been highly successful. Such small contributions to income paradoxically increase employment. They lead to higher rates of business formation, and they lead to large improvements in life satisfaction. In some cases, they lead people to work fewer hours, but they spend more time taking care of children or elderly parents. And of course, they lead to lower rates of poverty and reduce or eliminate the money required for means-tested poverty programs. In short, it has been repeatedly shown that a universal basic income works[39].

We can easily afford a universal basic income (UBI). In Figure 16 we saw that if personal income were evenly distributed, every family would have an income of $144,000 (in 2019, more now) which is several times more than recent proposals for a UBI. The universal basic income is entirely a transfer from the top of the income scale to the lower end, it is in no sense “government spending”. The same amount of income is produced in the country, at least the

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[37] https://learningpolicyinstitute.org/product/untangling-evidence-preschool-effectiveness-brief?gad_source=1&gclid=Cj0KCQjw_-GxBhC1ARIsADGgDjvRaThMKiAJ5_PiSlXCT0lzC0e_4IDScZnrA911I83KUxB2pFIKYawaAp0cEALw_wcB

[38] Conservative economists like Milton Friedman and Greg Mankiw among many. See this interview with Mankiw Harvard Conservative Economist Backs UBI | Greg Mankiw

[39] An experiment to inform universal basic income | McKinsey and Universal basic income has been tested repeatedly. It works. Will America ever embrace it? - The Washington Post

same amount of personal spending is done, and business is not affected. A universal basic income would almost certainly increase demand which would drive up total output and hence income for the country and per capita[40]. You may be wondering why people in middle- and upper-income brackets should get the same universal basic income as poorer people. Because life is uncertain and a UBI, like Social Security or Medicare, is an entitlement you get for being a citizen of the US. A productivity royalty so to speak, like the payments you get for renting out the mineral rights on your land if you are lucky enough to own a ranch on oil land in Oklahoma. For the upper middle of the income distribution, the UBI would probably be just about balanced by a tax increase so nothing would change. But if you lose your job or are unemployed for a period of time, you'd have your UBI to help. And if you work a low wage job, you wouldn't need a pandora's box of demeaning means tested "programs" (mostly administered by states) to make ends meet. In fact, one of the reasons some conservative economists ("conservative" does not imply Republican in 2024) favor a UBI is precisely because it is free market and requires minimal bureaucracy.[41] Andrew Yang deserves credit for proposing a universal basic income of around $1,000 per adult per month, although I dislike his idea of funding it with a value added tax.[42]

There is historical precedent for a universal basic income. In 58 BC the Roman Tribune, Publius Clodius established an allotment of free grain for all Roman citizens to help deal with economic dislocations. That system lasted for about five hundred years and gave rise to the saying "bread and circuses". In America Thomas Paine suggested UBI as a way to compensate people who lost their right to hunt, fish, or farm on frontier lands as that land was sold to private owners. The US was a land of opportunity, at least for European immigrants, because of its frontier. Nixon proposed a negative income tax for the poor in the 1970's. The state of Alaska distributes a "dividend" on oil production from public lands of between $1,000 and $2,000 annually to all residents. Recently, as we mentioned, local experiments with universal basic incomes have had good outcomes.

Other Ways to Expand Opportunity

In the graph above and in the section on income and wealth inequality we saw that both income and wealth are exponentially unequal and growing more so in the US, as well as the world in general. Such extremes of income and wealth are not really in line with democracy and the egalitarian values of the Enlightenment. Back in the days of the Revolution, discussions of how to organize a state both in principle and as a pragmatic matter were widely pursued. The abuses of the industrial revolution, the trusts, and the great depression in the US more or less forced the government to act to create a balance between unfettered capitalism and widespread misery.

[40] As is often noted, consumer spending drives the economy, and a UBI would likely increase demand

[41] For a conservative view of UBI see https://www.gainesville.com/story/opinion/2020/10/08/guest-columnist-conservative-look-universal-basic-income/3594284001/

[42] You can find Yang's 2020 proposals at https://2020.yang2020.com/policies/the-freedom-dividend/ . I much prefer an income tax to a VAT for a variety of reasons, not just repressiveness. Some models show that a VAT has a much larger negative effect on GDP growth than a personal income tax, it requires another complicated tax and the US has outperformed the many countries that use a VAT.

It is high time for us to again have an explicit discussion about how we organize our economy. Along with science and engineering, market capitalism is the engine that is largely responsible for the economic gains of the last two centuries. It's not going anywhere, nor should it. But it is unacceptable that a country as rich as the US should have tens of millions of people living in poverty even to the extent of being homeless. A universal basic income can help solve this problem through market means: the added income would allow people to find their own housing and buy their own food without government subsidies. I would argue that a universal basic income should be sized to a supplement a working income, Andrew Yang's proposal for a $1,000 per adult per month basic income does that nicely. It is enough to make life more tolerable for someone working a full-time minimum wage job, but not enough to replace a working income.

A universal basic income is not the only way for us to more widely benefit from the enormous gains in productivity that we've seen but many (actually most) of us haven't felt.

Healthcare is free and by right in most of the other advanced economies. Forget the forms, the paperwork, the 15% to 30% of healthcare spending that goes to administrative overhead, including insurance[43]. And why should US businesses be saddled with the costs of healthcare when foreign ones aren't? In the section on healthcare in Part 2, we discussed the reasons why free market conditions don't exist in healthcare, and why it is so much more expensive in the US than in other countries.

Other uses for our "productivity dividend" should include lower cost or free higher education, universal high-quality daycare and preschool, better maintained and additional infrastructure, and public amenities such as the national and local parks. Much of this redirection of national income would yield higher productivity and eliminate or lower the costs of programs that subsidize low-paying, low productivity work[44].

Investment for the Future

A majority of Americans support prioritizing the development of renewable energy sources. Two-thirds of U.S. adults say the country should prioritize developing renewable energy sources, such as wind and solar, over expanding the production of oil, coal and natural gas, according to a survey conducted in June 2023.[45] President Carter put solar panels on the roof of

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https://www.healthaffairs.org/do/10.1377/hpb20220909.830296/#:~:text=Administrative%20spending%20accounts%20for%2015,of%20administrative%20spending%20is%20wasteful.

[44] Workers and Walmart and McDonalds make so little that their employees often qualify and use public assistance such as food stamps. This is effectively a subsidy for low paying work.

[45] Blazina, Carrie. 2023. "What the Data Says about Americans' Views of Climate Change." Pew Research Center. August 9, 2023. https://www.pewresearch.org/short-reads/2023/08/09/what-the-data-says-about-americans-views-of-climate-change/.

the Whitehouse in 1979. President Reagan removed them. While these panels were used to heat water, the US failed to pursue investment in solar and wind, ceding these technologies primarily to China which, seeing the future, provided ample funding for their industry to develop these technologies at scale. Labor, even in the US, only accounts for about 5-10% of the cost of producing solar panels, since, like the rest of manufacturing, it is largely automated. The US could pursue industrial policies to support US manufacturing of these products. The Chinese created demand for their own products: they have one third of the world's installed solar capacity (albeit still a tiny fraction of their overall energy generation). Wind and solar power generation are now among the cheapest ways to produce power, even without considering climate change.

Climate change also calls for investments in other sources of greenhouse gas emissions as we discussed in Part 2. Electric vehicles, and heating homes using heat pumps are two of the biggest. These should be viewed as capital investments and as such are good candidates for long-term financing. Such investment will also generate huge numbers of jobs. Unfortunately, the ongoing tax cutting which does zilch for the poor who don't pay income taxes, is already causing huge, and unsustainable, deficits to pay for basic budget items such as Social Security and Medicaid. We are shooting ourselves in the foot by not investing in these technologies. Technology change is inevitable but inevitably leads to changes in demand which in turn can hurt workers in the effected trades. Locating new industries in areas hurt by transitions can help.

Fortunately, climate change investment can be largely market driven. Maine homeowners are installing heat pumps at such a rate that half of households will use them by 2027[46]. In this case the operational savings are a major factor: most fossil fuel central furnaces in Maine use finicky oil heat which is expensive and has to be delivered. Subsidies for installation help with the upfront costs in Maine.

In general, economists feel it is better to use the market rather than mandates to achieve greenhouse gas reductions. One suggestion is a carbon tax - an idea that appeals to economists because it operates via market mechanisms. The example of Maine we just mentioned shows how effective this can be: the high price of oil makes heat pumps more attractive, and people respond. A tax on carbon could be revenue neutral - the idea is not to increase taxes but to make fossil fuels comparatively more expensive and other sources of energy less so[47]. Simple, market oriented, and effective. A carbon tax incentivizes the most cost-effective CO2 reductions whether by households or industry. Basically, it is not only possible for the US to get to net zero, but doing so would spur our economy and employment, move us out of archaic fossil fuel technology into the present, be good for business overall, and be fun as well. All it would take is a bit of enthusiasm and goodwill and savviness about the forces of disinformation. Think of it as a war effort where nobody gets killed, we build

[46] https://www.nytimes.com/2024/03/02/climate/heat-pumps-maine-electrification.html?unlocked_article_code=1.q00.ZwuT.zEO4dfyc_4YD&smid=url-share. There are 580,000 households in Maine

[47] Revenue neutral means the taxes collected on carbon would be returned in other ways, such as through a reduction in income taxes, the UBI, or subsidies for investment.

plowshares instead of swords, and we all end up richer in the end. Or wallow in expensive, unproductive, “climate mitigation” and wait for temperatures to rise to truly unsustainable levels. And what will our kids do then?

The Need for International Cooperation

The United States is located on planet earth, and while separated from other continents by oceans, those oceans don’t mean much in an era of drastically lower transportation costs, and mean nothing at all, aside from sea level rise, when it comes to climate change. Immigrants stream to our doors and to the doors of other rich countries because of poverty, economic disasters and wars. Money moves instantly to wherever returns can be maximized, and taxes minimized. In short, we can’t pretend we’re an island, we are in fact thoroughly interconnected with the rest of the world, physically, economically and politically.

Following the success of the American Revolution, the individual states of the United States had to cooperate to defend the country, regulate commerce, adopt a basic set of rights, and hammer out how to administer a united government. Federalism doesn’t prevent states from adopting their own laws, as long as they don't conflict with the Constitution, or from maintaining their own cultures. Mississippi is culturally quite different from Massachusetts. As a practical matter, that level of cooperation isn’t going to happen at the world level unless aliens threaten to invade ala “The Day the Earth Stood Still”. But we should strive for stronger international cooperation recognizing that the world is now thoroughly interdependent. To me it is high time that countries no longer feel free to invade their neighbors or continue to snub their noses at international law and agreements for decades.

Just as poverty in the US should be a thing of the past, wars should be a thing of the past in the 21st century. Wars are tremendously costly, destabilizing, and a major driver of migration, to say nothing about the suffering of the victims of war, including soldiers. After the World Wars, Franklin Roosevelt was a major player in the creation of the United Nations which he viewed as a crowning achievement of his political career[48]. In an attempt to ensure “never again”, Eleanore Roosevelt chaired the UN committee that drafted the Universal Declaration of Human Rights which was then adopted with *no dissenting votes* by the nations of the world. It includes the basic concepts of dignity, liberty, equality, right to life, prohibition of slavery and torture, and right to property. The concepts are great, but countries are essentially free to ignore these principles as there is no enforcement mechanism. Individuals who are responsible for crimes against humanity can be prosecuted by the International Criminal Court, which the US has not joined. The UN can organize peace keeping efforts and interventions to try to address humanitarian disasters, but only with the unanimous consent of the Security Council. We should press for more cooperation in the effort to enforce international law, not discredit the existing institutions. And we should also be an example in that effort.

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[48] John Allphin Moore and Jr. Jerry Pubantz. The New United Nations: International Organization in the Twenty-First Century (Upper Saddle River, New Jersey : Pearson Prentice Hall, 2006)

Climate change is another area where cooperation is essential. Global warming is… global. Virtually every country in the world has signed the "United Nations Framework Convention on Climate Change" and the 2015 Paris Agreement, under which each country set voluntary goals for greenhouse gas emissions reductions and other actions[49]. Last year, 2023, a review of progress in meeting these goals showed that there was a large "implementation gap" between the pledged reductions and actual ones. While the rich countries are responsible for most of the accumulated emissions to date, developing countries are now responsible for about two thirds of current emissions. Developing countries require more energy as they grow, but the cost of capital in many of these countries is high[50]. Rich countries such as ours can provide low interest loans to developing countries specifically for greenhouse gas reducing projects such as solar or wind farms. Even if the interest rate on such loans is the same as our domestic loan rates, this would be a big help in ensuring that developing countries pursue greenhouse gas reductions while growing. Low or no interest loans for such projects would be even better. In the past, US companies have benefited mightily from large infrastructure projects in developing countries, some of questionable utility. Currently the US and other G7 countries are pooling funding for infrastructure projects in response to China's Belt and Road development initiative which includes green infrastructure. Climate change investment, with or without the US, will be huge going forward and, as we saw in the chapter on climate change, while much of the technology was developed here, we have let this major market slip through our fingers so far, although Biden era legislation has changed that picture.

The development of the rest of the world is much in our interest for other reasons. The current world population of 8 billion is projected to grow to over 10 billion under current trends. This quite recent explosion of the human population is simply unlike anything the earth has ever seen before, and unsustainable for a host of reasons. We have seen that as countries become richer their birth rate declines so the sooner developing countries get richer, the sooner we reach "peak human". And of course, as we have discussed, as countries get richer and opportunities expand, there is less impetus for migration, and trade becomes more balanced. For our own good, we need to do everything we can to lower human population growth and the only sure way to do that is to help poor countries become wealthier. That is best done through trade and investment, which is good for the earth, our economy, and theirs as well. A win-win-win.

Trade too requires international cooperation. The World Trade Organization (WTO) provides a forum for the negotiation of trade agreements and the resolution of disputes. The large majority of countries, including the US and China and all the countries with the biggest economies are signatories to the agreements at the heart of the WTO. There are in addition, many regional and bilateral trade agreements. The WTO is the "referee" when it comes to violations of trade

[49] Even though the agreement is only voluntary, and signed by every country in the world, the US pulled out of it under one administration in 2020 and back in under another in 2021.
[50] Meaning that these countries pay much higher interest to borrow capital. In 2021 Ecuador's interest rate was over 12 percent while the rate in the US and Europe was under 4%. See https://wedocs.unep.org/bitstream/handle/20.500.11822/43923/EGR2023_ESEN.pdf?sequence=10

agreements, but it has no enforcement powers. Trade in a connected world requires fair and impartial arbitration. Not shoot from the hip ad-hoc tariffs.

Finally, in this list of the benefits and needs for international cooperation is the need to deal with financial malfeasance and tax shelters. As we saw in the section on tax avoidance and evasion in the US, vast amounts of money are secreted in "tax havens" that also serve to park and hide dirty money of all sorts. The sums are enormous, many trillions of dollars. Work has been done on this by groups of countries to share data and impose minimum corporate tax rates, and that effort needs to continue and be expanded.

The Last Word

In 2016, before the primaries, I went canvassing in New Hampshire. I'm not going to say for whom or what I was canvassing, but several people told me that if it came down to Bernie versus Trump, they'd vote for Bernie, but if it came down to Hillary versus Trump, they'd vote for Trump. Bernie was ahead of Trump by 10 points more than Hillary. Clearly these voters were not going to vote for an establishment candidate of either party.

Trump and Bernie both had populist economic platforms. Trump (net worth then low billions, annual income taxes paid $750) blamed immigrants and trade. Bernie (net worth under a million, $35,868 income taxes paid on income of $240,610 in 2015) blamed a shift in income and wealth from the middle class and poor to the rich. Trump's solution was to clamp down on immigration and raise tariffs and lower taxes for the wealthy, Bernie's was to tax the rich and spread the wealth through various means.

The evidence on a shift in income and wealth to the top of the top 10% in the US is crystal clear, we've looked at that in detail in this chapter. Lower taxes, better tax shelters, and higher profits have been the mechanism by which income and wealth have moved from the middle class and poor to the wealthy. Lower taxes were achieved by political means during and after Reagan. Higher profits have been made possible partly by labor's poor bargaining position in the marketplace (supply and demand as always, but also the decline of unions).

To what extent is labor's poor position the result of trade and immigration versus automation and other uses of capital to reduce the demand for labor? This is key to understanding whether Trump's or Bernie's agenda is more likely to raise your income if actually carried out.

We've looked at that question in great detail in this book. Before we recap the general picture, let's look at agriculture. Agriculture historically employed 80% of Americans in 1800, 40% in 1900, and 21% in 1930. It now directly employs less than 2% of workers. This decline was certainly not due to trade or immigration, it was due to immense improvements in the productivity of agriculture. Technology improved and the demand for labor fell. Fortunately for agricultural workers, opportunities to work in manufacturing were expanding. People moved from the country to the city and worked in these new jobs. Of course, this labor was "exploited" (actually just paid what supply and demand dictated under working conditions allowed by the laws of the time), and it took unionization and the legislation of the first half of the 20th century for factory workers to get a decent life and living. Industrialists fought unionization and New Deal legislation tooth and nail, but in the end the economy boomed, the middle class grew, and business expanded along with it.

The picture in the broader economy over the last 50 or so years is similar to the earlier story of agriculture. While a third of workers worked in manufacturing in the 1960's barely 10% do now. Automation and increased capitalization of industry is far and away the biggest cause of that decline. The US is still a manufacturing superpower, just like it's still an agricultural superpower, it just takes fewer workers to do that manufacturing.

Eighty percent of us now work in "services", a huge category, where, as always, supply and demand determine the wages of any type of labor. Automation, capitalization, and technologies such as artificial intelligence continue to reduce the demand for labor, and consequently keep pay in check. Failure of incomes to keep up with growth is not caused by trade or immigrants, nor will it be fixed in the long run by increasing tariffs or removing undocumented migrants. The state in the US with the highest percentage of immigrants is California. California and Texas lost the most jobs due to the expansion of trade with China. Neither comes to mind as an economic basket case. With unemployment at a historic low now in late 2024, one might as well speak of jobs "gained" from trade and immigration. Trade only happens when it brings a lower price, and prices are lower now, in some cases much lower, because of trade. Industrial policy for strategic reasons such as that included in the Inflation Reduction Act make some sense. Tariffs on the other hand increase costs. Immigrants are competitive with certain types of labor, but in the bigger economic picture, they are also consumers, taxpayers and workers. It makes sense to control the flow of in-migration but expelling settled migrants not so much.

The point is that we've been here before. The earlier industrial revolutions simultaneously increased productivity and the country's wealth but at the same time greatly increased inequality. Think of the "Monopoly" guy with his top hat and monocle. The reforms of the New Deal helped increase the bargaining power of labor and spread income and wealth more evenly. But over the last 60 years, inequality has again increased. The country has become incredibly wealthy but at the same time the share of national income earned by the middle class and the bottom 50% has shrunk. It is only after taxes and transfers that the lower half of households has maintained a claim to 20% of national income. Meanwhile the middle-class share has actually declined while the top 1% share has increased accordingly.

Instead of imposing tariffs on trade, which is anti-free market and increases prices, a much easier and more effective method of tackling inequality is to follow the model of the New Deal. Increasing taxes on the rich back to the boom times pre-Reagan immediately reduces inequality. That money can then fund many things such as low-cost health care for everyone, and as I suggest above, a universal basic income to supplement working income.

The New Deal was declared “socialist” by those who opposed it, but in fact it ushered in a period of incredible business growth and a huge expansion of the middle class. Taxing the incomes of the rich does nothing whatever to change the capitalist market system that is one of the key drivers of our wealth. Here is a thought experiment to make this clear:

Right now, as we’ve seen, the rich often get most of their income from owning shares in the US’s huge public companies such as Microsoft or General Motors. Often, they inherit that stock. If the estate tax redistributed those shares at death so that everyone in the US owned them, nothing whatever would change in the running of Microsoft or General Motors. They would not be owned or run by the government, and their managers would be incentivized to increase sales and profits in exactly the same way as now. But the dividend income from the stocks would be distributed more widely. The bottom 50% who own essentially nothing right now, would finally get a share in America in a way that homesteaders once did when land was handed out free to settlers.

A glance at the charts I provided above should reassure the middle class that none of this need come out of your (and my) hide. We’ve seen that if national income, which is income after all expenses of running businesses but before taxes, were distributed evenly, all households would have had $144,000 in income in 2019 and more now. Since realistically the playing field is not going to be anywhere near levelled, if you make less than some arbitrary income like $250,000 before taxes, you would either pay the same in taxes or less. Above that you would pay more in taxes, with the amount increasing as incomes get higher.

The above discussion should have made it clear that if carried out, the direct approach of taxing the rich and using that income to effectively raise the incomes of, say, the lower 50% of earners is simple and effective. We did it before and it worked for everybody, including business. Trump’s agenda includes more tax cuts to add to the ones his party passed during his first term. Those tax cuts greatly increased the deficit as we’ve seen, and about half of it went to the top 5%, increasing inequality as well. He didn’t talk much about these cuts for the wealthy, focusing instead on kicking out undocumented migrants and increasing tariffs, particular on goods from China. If you’re in the middle class or the bottom 50% will that help you? Kicking out undocumented migrants might temporarily raise wages in some low paying jobs, but after that we’re back to the same situation. Tariffs on stuff from China, like a great many things you buy in Walmart, will simply raise prices or force Walmart to buy the products from another low wage country.

It is highly unlikely that Trump’s agenda, if carried out will actually do anything for anyone below the top 10%. Deficit spending may goose the economy further, but that is like putting a shopping spree on your credit card. Live high now and pay for it later. Like with lower Social Security and/or later full retirement benefits. The Trump economic agenda in short, is a fantasy designed to appeal to common misconceptions of the roots of economic inequality in the US, while in fact increasing it. Not particularly surprising for a billionaire with billionaire friends.

As the Eagles sang in Hotel California, “This could be Heaven, this could be Hell”. The US is a very rich country. With a more equal distribution of the fruits of productivity we could all live comfortable lives without working multiple jobs. We have the resources to provide a universal basic income to supplement working incomes. We could have universal preschool and free higher education. Medical care could be free, or almost free, as it is in most advanced economies. Nobody needs to be poor, let alone homeless, in the US. Vast differences in income and wealth are not healthy for any community and a country is a community.

Or we can proceed down the road we’ve been following since Reagan, with more and more unequal distribution of income, three men owning more wealth than the bottom 50%, less and less taxation of the rich, huge deficit spending, and virtually all the increase in national wealth and income going to the top of the top 10%. A national basic income would mean that most of the “means tested” government programs that keep half our country barely afloat could be scrapped along with the bureaucracies, mostly at the state level, necessary to implement them.

The last election, incredibly close in popular vote, was about more than economics of course, and I understand that. I do believe, and polls support this, that a sizeable majority in the US are for policies that will lower the extremes of income and wealth in the country regardless of differences over social issues. Unfortunately, a campaign of “divide and conquer” based on cultural issues has been waged to make possible the vast economic shifts we’ve documented starting with Reagan. Once upon a time in this country, representatives from social conservative areas and those from more socially liberal urban areas could get together to support populist economic programs. It is time for that consensus to reemerge.