**WHAT TO DO ABOUT THE**

**GROWING U.S. INCOME GAP BETWEEN THE RICH AND EVERYONE ELSE**

Philip Kotler

Revolutions occur when the income and wealth gap between the rich, the middle class and the poor reaches a boiling point. We may be near the boiling point. This gap launched the Russian Revolution of 1917. Social injustice led to Castro’s takeover of Cuba and Mao Tse Tung’s takeover of China. The picture of Karl Marx continues to hang on many walls in homes in Venezuela, Bolivia, and in many Asian and African countries. A scholar on income distribution recently exclaimed: “We need a new Karl Marx!”

There is still time to avert a political revolution. Just like we are threatened by a growing climate crisis, most of us know that measures exist, if taken now, that could protect our atmosphere and planet from further desolation.

Several questions need attention. How extreme is the concentration of income and wealth? What does wealth concentration cost in human terms? What is the attitude of the wealthy toward taxation and transfer payments? What measures can we take now to contain or reverse the growing income gap?

**How to Measure Growing Economic Inequality**

There are different measures describing the growing inequality of income and wealth.

**The Gini Coefficient**

The Gini coefficient is the main measure of economic inequality. In 1912, the Italian sociologist Corrado Gini proposed this measure. The Gini coefficient is a number between 0 and 1, where 0 corresponds with perfect equality (where everyone has the same income or wealth) and 1 corresponds with perfect inequality (where one person has all the income or wealth - and everyone else has zero income or wealth).

In 1990, the U.S. Gini coefficient for household income was 0.43. Twenty seven years later, by2017, **the Gini coefficient rose to 0.48.** Unless certain actions are taken, the Gini coefficient will move still higher. This is one of the highest country Gini’s, considering that Denmark, Norway and Sweden Gini coefficient ranged between 0.24-0.26.

When income inequality is excessively high, it can be reduced by taxation and transfer payments. Germany’s Gini index before any redistribution was 0.55. But Germany chose a strong redistribution program and the Gini index for Germany fell to 0.30. By contrast, the U.S. at that time had a lower Gini index of 0.47 before redistribution. But the U.S. chose a weaker redistribution program, reducing its Gini index to 0.37.

The average U.S. worker’s real wages have not increased in the last thirty years. This is in spite of the strong and continuous rise in the U.S. Gross Domestic Product (GDP). About 90 percent of the rising income in the GDP went to the rich. All the time the rich claimed that workers would benefit from the rising GDP. They named it the “trickle down” effect, that all boats would rise. Not only did this not happen but the reverse happened. **Income trickle up to the wealthy** occurred, rather than trickle down to the workers.

**Wealth Concentration of the Rich Exceeds Income Concentration**

Wealth is even much more highly concentrated than income. Wealth concentration at the top has risen since the 1980s. Wealth rises from innovation, globalization, digital technology, oligopolization, and other causes. The result is the creation of new billionaires as we witnessed with the founders of Apple, Facebook, Google, Amazon, Alibaba and other hi-tech businesses. But even innovation in low tech businesses work. Consider this earlier explosion of wealth:

In 2007, the six Walton family members on the Forbes 400 had a net worth equal to the bottom 30 percent of all Americans.[[1]](#endnote-1)

These are six persons lucky enough to be born into the right family. They didn’t do anything to create their wealth. They are the beneficiaries of the brilliance of Sam Walton. We ask: Should Sam Walton have been taxed at a much higher rate to prevent this great wealth from accumulating? Would Sam Walton still have worked this hard at the higher tax rate? These are tough questions.

Wealth concentration is a self-feeding process. Those who hold wealth have the means to invest in newly created sources and structures of wealth to leverage their wealth, and are thus the beneficiaries of even greater wealth.

Today, in the USA, the richest 1 percent own 40 per cent of the wealth. Notice how much this wealth concentration contrasts with Sweden where the richest 1 percent own 24 percent or in Canada where the richest 1 percent own 15 percent.[[2]](#endnote-2)

The richest 10 percent of U.S. households own 70 per cent of the wealth. This heavy concentration is matched by India 73.8%, Indonesia 75.0%, and South Africa 74.8%. The **United States is now the most unequal of all advanced economies**. It is in the league of corrupt underdeveloped countries, no longer in the league of the developed nations.

The richest 10 percent start with those U.S. citizens earning $200,000 or more a year and having over $1 million. The richest 10 percent are all “millionaires” in the literary sense.

At the same time, the wealth of the median household in 2013 was $56,335. One can see that a major illness can easily wipe out the $56,335 wealth of a median American household.[[3]](#endnote-3)

**CEO Pay Levels**

Another factor feeding into wealth concentration is the extremely high pay levels of CEOs. In 2017, America’s CEOs averaged **361 times** that of nonsupervisory workers. This ratio is so much higher than it was in earlier times. **20 to 1** was a more normal ratio. Management expert Peter Drucker thought 20 to 1 was a socially appropriate pay level for CEOs.

Here are the four top paid CEOs in 2017:

* Hock E. Tan, Broadcom Ltd, $103.2 million
* Frank J. Bisignano First Data Corp, $102.2 million
* Peter P. Gassner Veeva Systems $88.1million
* Michael Rapino Live Nation Entertainment $70.6 million

The latest CEO pay of the S&P 500 rose by 6.4 percent while the pay of production and nonsupervisory workers grew only by 2.6 percent.

CEOs are not the only high paid group in the U.S. Many entertainers who hit the big time draw huge pay. Note also that the highest paid hedge fund managers earn even much more than CEOs. Here are the 2011 incomes of the three top hedge firm managers:[[4]](#endnote-4)

1. Ray Dalio Bridgewater Associates $3.9 billion

2. Carl Icahn Icahn Capital Management $2.5 billion

3. James Simons Renaissance Technologies $2.1 billion

Any major bank president would undoubtedly prefer to run a hedge fund! And we are not counting the pay of mafia and others engaged in illegal activities.

Also observe CEO severance pay packages. G.E.’s Jack Welch received a $417 million farewell package from G.E.’s Board upon retirement. William McGuire left United Health Group in the midst of a stock option scandal with a $286 million severance package.

Public companies are also generous in compensating their board directors. I remember receiving many years ago about $25,000 to attend each board meeting, usually four board meeting a year. The average annual total compensation per director (excluding the independent chairman) today is $245,842 consisting of stock grants (52%), option grants (6%), cash fees (19%), and other compensation (3%).[[5]](#endnote-5)

Fortunately, not every CEO is greedy. Several CEOs managing top companies are satisfied in receiving total annual compensation under $6 million. Edward S. Lampert of Sears ($4.6 million), Tim Cook of Apple ($4.2 million), Alan Lafley of P&G ($2 million), and Steven Ballmer of Microsoft ($1.2 million).[[6]](#endnote-6) Given that these executives have the skills to manage huge companies, why are the other executives receiving such high pay?

One explanation of excessive CEO pay is the addiction to greed. These CEOs can acquire any material possession that they desire – personal airplane, yacht, or several mansions. Sam Polk, who had accumulated a huge income, wrote how one day that he regained his life by overcoming his wealth addiction. His manic drive for “more” no longer made any sense.[[7]](#endnote-7)

Let’s ask a simple question. Suppose Larry Ellison, CEO of Oracle, suddenly feels overpaid about that year’s income of $78.4 million. He decides that he could live on $4 million and give his Oracle employees higher pay so that they can pay down debt on their credit cards. The average worker carried a credit card debt of $15,799 in 2012. Ellison decides to give a one-time gift of $10,000 to 7,800 of his employees. Larry Ellison has made 7,800 families happier without sacrificing hardly anything in his own family’s life style. Readers could ask Ellison why not distribute his excessive income to shareholders in dividends. He might answer that the shareholders would object and pay him less in the future.

If companies paid less to excessively paid CEOs, would that cause the companies to underperform? The French economist Piketty’s answer: “It is possible to find hard-working managers who are willing to be paid 20 times the average wage in their company rather than 100 to 200 times.”

Today, with not only newspapers, radio and TV but also with Google, Facebook and You Tube, more people are learning about the vast differences in the earnings of the median American household ($51,000) and the superrich. The income of these highest-earning Americans has recovered completely from a fall after the financial crisis, compared with the 8 percent decline for the median American household.[[8]](#endnote-8)

This much can be said:

1. Economic inequality is very high in the U.S.
2. Economic inequality has been increasing and is very likely to increase even more in the absence of positive measures to constrain or reduce economic inequality

**Why is There So Much Wealth and Income Inequality?**

We need to acknowledge that much of income inequality comes from the forces of *globalization* and *technology* and differences in *education*, none of which we can do much about except through changing government tax policy. Globalization means that companies will move their production to lower labor cost countries. Technology helps companies replace labor with capital when labor becomes too expensive. And educational differences go a long way to explain the great difference in earnings within a country.

We would not expect everyone in a country to earn about the same. First, people have different levels of talent. Talent is not distributed equally. Second, people vary greatly in how much energy they have and how much hard work they will do. Thirdly, people grow up with different levels of advantage coming from parents, location, race and ethnicity. Those who have received a high level of education are likely to earn more. Studies show that the chance of poor persons becoming rich is closer to zero.

**What Are the Human Costs of Extreme Income Inequality?**

The first human cost of economic inequality is poverty and hunger. In 2016, 40 million Americans, or 12.7 percent of our population, lived below the poverty line. This is astonishing in a rich country such as the U.S.

We are living at a time when the extreme income gap is making daily headlines in our news media. Many think that middle class stagnation and the growing number of the poor is the most important civil issue facing the nation. Yet the U.S. Congress is thinking of reducing the food stamp program that benefits for about 45 million people. We hear of single mothers with children who were receiving food stamps now may have to go to soup kitchens to feed their family.

Richard Wilkinson and Kate Pickett, in their book *The Spirit Level,* found negative correlations between inequality, on the one hand, and physical health, mental health, education, child well-being, social mobility, and trust and community life. They found positive correlations between inequality and drug abuse, imprisonment, obesity, violence, and teenage pregnancies. Inequality creates these adverse outcomes through psycho-social stresses and deprivations generated in a highly unequal society.

**Are Capitalism and Democracy Compatible Systems?**

Capitalism promises a high level of freedom and good economic growth. But the economic growth is highly unevenly distributed. Those with high wealth and property have the ability to leverage their wealth further. Those without wealth or property are totally dependent on wage labor, except for transfer payments. If there were no safety net, workers would be described as totally dependent “wage slaves.”

The wealthy have a disproportionate amount of power and influence in political affairs. We have seen how the Koch brothers could spend millions of dollars to support their preferred political candidates. Ever since the Supreme Court passed the 5 to 4 decision in the Citizens United Case (2010) declaring that businesses are persons, growing millions of dollars are spent on elections. Every political candidate needs at least one million dollars to even think of running for office. Most candidates can attract many millions from donors and in turn they support their donors’ political interests. The elected politicians pay as much attention to the wishes of their donors as they do to the citizens in their voting districts. Elected politicians also pay great attention to the wishes of lobbyists who can further their careers.

The result is that members of Congress are corrupted. They are not men and women who see the interests of their voters and the country paramount. Many are lackies of their political party, donors and certain industries such as guns, pharmaceuticals, and defense. The basic principles of American democracy are corrupted by the flood of donor money flowing out of our Capitalist system and ruining our “one citizen, one vote” system. We need to fundamentally reform how our elections are financed to eliminate this corrupting influence.

**What Are The Attitudes of the Wealthy?**

Citizens clearly carry different attitudes toward the rightness or wrongness of extremely large differences in income and wealth. Here are some opinions heard on the street.

1. “I am only concerned with whether I have equal opportunity and not with income differences.”
2. “There will always be extreme differences in income. It is the survival of the fittest.”
3. “High incomes are mostly the result of differences in ability that lead to differences in income.”
4. “High incomes come from having the right parents. If you are born in a wealthy family, you will be brought up with more advantages and go to the right schools and get excellent jobs, partly through your parent’s connections.”
5. “The super-rich have rigged the system to get us complacent through feeding us the ‘candy’ of television and cell phones and other distractions so that we don’t notice their thievery.”
6. “From a social justice point of view, I think that the rich should be taxed proportionately higher than the average income earner.”

I personally can imagine one system of income distribution that would be worse than today’s. The worst would be if everyone was limited to getting the exact same income, regardless of age, family size, ability, effort and other factors. There would be no incentive to work or innovate.

The system that we have today of extreme income and wealth disparity has existed through most of history. Territories were run by tribal leaders or a king or queen who along with all the court and courtiers would amass great wealth. There was hardly a middle class. There was a huge peasant or working class, and most of the laborers were serfs or slaves living on a bare subsistence level.

**How Do the Rich Feel about their Wealth?**

Most wealthy people feel good about their wealth. Many feel that they were especially clever or talented and deserve their wealth. Those who were wealthy through inheritance at least feel lucky in their choice of parents. They may have some ambivalence because they didn’t create wealth, perhaps only hoping to be good at preserving or growing their wealth.

The wealthy don’t like taxes. Many would advocate paying a single low rate, say 10% of their income. This is the idea of the *flat tax*. The wealthy recognize that a flat tax means they pay more in dollars but they prefer this to paying a higher percentage of their income than lower income citizens pay. They tend to resent a *progressive tax system*.

Part of the resentment is that many rich persons and families are generous and philanthropic. They give large donations to their church and their college. They may give large donations to medical causes such as cancer, heart disease, and others. They will give more money when there are generous tax advantages in giving money to charities. They prefer deciding who should get their money over letting the government tax them and decide where to distribute their money. In some cases, they believe that the government will distribute their money to “lazy, poor people who don’t want to work.”

The wealthy greatly affect the kinds of goods and services that are produced in a society. The larger the wealthy class, the more that will be spent on mansions, private airplanes and yachts, private swimming pools, expensive clothing and jewelry, and expensive travel. All of this provides employment but there is a downside for the less fortunate. New York City, San Francisco and other cities of the wealthy build many luxurious apartments and homes leaving few affordable housing in areas where workers work. Workers often have to drive long distances to and from work to carry on the company’s business.

The wealthy tend to think highly of their self-importance in creating a growing economy. Workers will look at the life styles of the rich and famous and want to emulate them. Workers will put out more effort to get a chance at the good life. Were there no group to emulate, many workers would be less ambitious and GDP growth will suffer. So goes the story.

Wealthier families main problem is how to handle their children. Their children may want to live off their wealth, gamble and not create anything. Warren Buffett, one of the world’s wealthiest men, sagely observes that “ a very rich person should be able to leave his kids enough to do anything but not enough to do nothing.” This captures the spirit of what should be passed on to one’s heirs.

Fortunately there are some very wealthy individuals and families that care greatly for improving the lives of workers and the poor. They want to make the world a better place for more people. Here are some of them.

*Bill Gates*. He deserves great credit for deciding to use his wealth to fight major diseases and to raise education levels here and abroad. Gates didn’t do this by sitting in an office. He left Microsoft and with his wife Melinda spends much time in the field in all parts of the world.

*Warren Buffett*. He is regarded as one of the sharpest financial thinkers in the world. Over 30,000 people flock to his annual Berkshire Hathaway meeting. Warren heads many foundations and he has given half of his wealth to Bill Gates to manage in Bill Gates work. Warren and Bill Gates initiated the Giving Pledge that has convinced 182 billionaires to part with more than half of their lifetime wealth by giving their money to good causes.

*Sir Richard Branson.* Branson started the Virgin franchise that led to many innovative branded products and services. He has always supported liberal causes to help economies grow and workers to do better.

*Marc Beniot*. Marc is the CEO of SalesForce, a major tech company. He cares greatly about the poor. San Francisco now has a major homeless population who cannot afford the high rents of the city. He wants San Francisco to put a tax on its large companies to raise enough money to double the budget that helps the city’s homeless people.

*Nick Hanauer*. Nick is a venture capitalist and civic activist operating in Seattle, Washington. He co-founded The True Patriot Network, a progressive think tank “which focuses on public education and the environment, and additionally supports a variety of progressive causes locally and nationally." In June 2014 Hanauer wrote an op-ed for [*Politico*](https://en.wikipedia.org/wiki/Politico) magazine in which he foresaw [*pitchforks*](https://en.wikipedia.org/wiki/Pitchfork) coming for his "fellow .01%ers" if they did not address the issue of increasing [*wealth inequality*](https://en.wikipedia.org/wiki/Wealth_inequality). He noted how it would result in the destruction of the [*middle class*](https://en.wikipedia.org/wiki/Middle_class)and damage to the wealthy class.

*The B Team.* Several leading executives of business and civil organizations have joined to fight corruption and lack of transparency in business. They want businesses to operate with the highest ethical standards. They believe in reporting accurate, timely and useful information to key stakeholders around the world. They aim to develop a new framework for approaching tax with a set of responsible tax principles. The group includes Paul Polman, Indra Nooyi, Muhammad Yunus, Ratan Tata, and several other high ranking executives.

Some wealthy individuals remind us of the 19th century “robber barons.” They opened up new industries that advanced the standard of living. John D. Rockerfeller entered the oil industry, built refineries, and in turn enabled the rapid development of the railroad and automobile industry. Rockerfeller’s near monopolization of the oil industry led to the growth of anti-trust work against huge firms. In retiring, Rockerfeller became one of the more respected philanthropists in history. His money helped pay for the creation of the University of Chicago (1892), to which he gave more than $80 million before his death. He also helped found the Rockefeller Institute for Medical Research (later named Rockefeller University) in New York and the Rockefeller Foundation. In total he gave away more than $530 million to various causes. His oldest son continued his father’s legacy of giving, in this case to establishing the United Service Organization (USO), the United Nations headquarters in NYC, the Lincoln Center for the Performing Arts, and the restoration of Colonial Williamsburg, Virginia and funding for the Museum of Modern Art. All these contributions carried out the spirit of elevating the Common Good, improving the living conditions of the greatest number of people.

Andrew Carnegie, the world’s richest man in 1901 at the age of 66, retired after building up the American steel industry. It was steel that enabled the further growth of the railroad and auto industry and the construction of skyscrapers. He decided in 1901 to become a philanthropist carrying out the “Gospel of Wealth” believing that wealthy people were morally obligated to give their money back to others in society. In 1902 he founded the Carnegie Institution to fund scientific research and established a pension fund for teachers with a $10 million donation. Carnegie believed greatly in education and reading and gave his money to towns and cities to build more than 2,000 free public libraries. He also gave $125 million to a foundation called the Carnegie Corporation to aid colleges and other schools. Carnegie also believed in world peace and he established the Carnegie Endowment for International Peace and funded the building of the Hague Palace of Peace, which houses the World Court, in the Netherlands. By 1911, Carnegie had given away a huge amount of money -- 90 percent of his fortune.

I cite these contributions of the robber barons as an example of how today’s millionaires and billionaires can think about what they want to leave as their legacy. They have three possible paths. One is to center their lives on rich living and living with the rich. Another is to use their money to rant against progressive causes and do everything to protect the interests of the wealthy. The third path is the follow the examples of John D. Rockefeller and Andrew Carnegie to distribute their money to bring a higher level of health, education and happiness to their fellow citizens.

**What are the Main Tools to Constrain or Reduce**

**Income and Wealth Inequality?**

There are a wide range of measures that would constrain or reduce economic inequality. The hope is that these measures don’t also hurt economic growth. That question should always be asked as we discuss these measures.

1. **Raise Wages and Other Benefits**

One measure to improve the life of the working class is to raise the minimum wage. There is mounting pressure to raise the national minimum wage that had stayed too long at $7.25. A large number of states have already raised their state’s minimum wage. The Democratic Party advocated raising the hourly minimum wage to $10.10 and thereafter indexing the minimum wage to inflation. This has already happened in other countries. Germany and Britain raised their minimum wage to $11.30 an hour. Denmark is at $20.30 an hour. Switzerland wanted to reset it at $25 an hour but it was voted down. All of this makes the U.S. minimum a disgrace.

Those opposed cite two possible undesirable consequences. First, some small businesses that hardly make a profit paying $7.25 are likely to close shop at a higher minimum wage. Second, employers will search for other ways to replace labor with capital. Labor saving devices would have the effect of reducing the number of jobs but paying more to those who are still employed.

Many companies have freely chosen to raise worker wages above the minimum wage in their city or state. Some companies are sincere in wanting to improve their workers’ lives. The wage rise might also be due to needing to attract workers during labor shortages resulting from full employment.

The real problem is that GNP has continued to grow but labor wages have not grown much. About 90 percent of the income in the GDP growth has gone to the wealthy class. This highlights how weak labor’s voice is in the economy. American labor unions have shrunk in size as a result of conservatives doing their best to handicap workers’ unions. Conservatives passed the “right to work” laws so that workers could get a job without having to join a union. Until unions get their strength back, labor will continue to share less in GDP growth and the wealthy will continue to draw the lion’s share of income.

1. **Make the Income Tax System More Progressive**

We hear new cries for increasing taxes on the rich. Bill de Blasio, New York City’s mayor, said “We will ask the very wealthy to pay a little more in taxes so that we can offer full-day, universal pre-K and after-school programs…Those earning between $500,000 and $1 million…would see their taxes increase by an average of $973 a year. That’s less than three bucks a day—about the cost of a small soy latte at your local Starbucks.” [[9]](#endnote-9)

This leads to the larger idea of a progressive tax system that would establish higher tax rates for higher income brackets. The U.S. tax system does this. Here were the tax rates in 2013:

* 10% on taxable income from $0 to $17,850, plus
* 15% on taxable income over $17,850 to $72,500, plus
* 25% on taxable income over $72,500 to $146,400, plus
* 28% on taxable income over $146,400 to $223,050, plus
* 33% on taxable income over $223,050 to $398,350, plus
* 35% on taxable income over $398,350 to $450,000, plus
* 39.6% on taxable income over $450,000.

The question: Was the maximum tax rate of 39.6% a high enough tax on the rich, given the growing level of income inequality? Consider that in 1939, the U.S. top tax rate was a whopping 75%. It rose to 91% during WWII for incomes over $200,000 that was a high income at that time. In 1964, the highest tax rate was lowered to 70%. Starting in 1981, President Reagan managed to lower the maximum rate from 70% to 50% and subsequently down to 38.5%. Reagan has been praised by the right as a tax cutting President but he actually raised taxes eleven times. In President Clinton’s term 1993-2001, the top marginal rate was raised to 39.6%. Under President George W. Bush, the maximum tax rate was lowered to 35% and his deep tax cuts were scheduled to expire at the end of 2010 but they became permanent. Many believe that the full Bush-era tax cuts were the single biggest contributor to the deficit in the subsequent decade, reducing revenues by about $1.8 trillion between 2002 and 2009. During the 2008-2011 fiscal disaster, the top tax rate was raised back to 39.6%.

In 2018, the Republican-dominated Congress managed to pass the first strong tax reform in 20 years. They could have kept a top tax rate of 39.6% on the rich, and lower substantially the taxes on the middle and lower income class. Instead, they lowered the top tax rate on the rich to 37%, saving rich persons billions of dollars while eaking out small tax reduced rates to the middle and lower class. The lower top tax rate led to a redistribution of money from the poor to the rich! They accomplished this “trickle up” transfer of wealth by adding $1.5 trillion to our deficit. The federal government will have to borrow and pay a growing interest rate on $1.5 trillion instead of getting this as tax money. Conspiracy minded thinkers suggest a Republican strategy of starving the budget so severely that the Republicans will make it up by cutting Social Security and Medicare.

What we need now is a more progressive income tax system. At what income level does the middle class end and the rich class begin? [Bryce Covert](http://www.nytimes.com/2015/12/28/opinion/campaign-stops/250000-a-year-is-not-middle-class.html) claimed that the middle class ends at $206,568. This is the income that defines the start of the top 5% of income earners. The top 5% is the rich class whose incomes grew substantially during this period. The middle and working class had falling real incomes since 1973.

Let’s consider setting the rich class as beginning at an annual income of $200,000. We will acknowledge that earning $200,000 a year in smaller cities or rural areas is a rich class income while in New York City or San Francisco is a middle-class income. But we need some number to start with.

The real question is how to distribute the tax burden between the rich and very rich. This calls for establishing a set of rising brackets where the marginal tax rate rises in each bracket. This is the essence of a progressive tax system. For example, the brackets and marginal tax rates can be:

40% on taxable income from $200,000-$500,000, plus    
42% on taxable income from $500,000-$1,000,000, plus   
44% on taxable income from $1,000,000-$5,000,000, plus   
46% on taxable income from $5,000,000-$10,000,000, plus   
50% on taxable income Over $10,000,000

Note that all these rates are for the rich and superrich and start at 40%, not 37%. The other point is that the rich who (say) pay 50% are not paying 50% on their income. They are paying 50% on the last bracket of their income. A rich person may end up paying about 35% in income tax, although the marginal rate was 50%. Many left-leaning Democrats would like to raise the marginal rate to 70%, knowing that the actual tax will be substantially less than 70%.

Conservatives will raise the following objections:

1. The government is practicing class warfare and this will change the economic behavior of the rich, leading them to work less hard, invest less and move their capital abroad. (But the rich did not object when redistribution flowed from the workers to the rich.)

2. The rich will increase their drive to replace labor with capital and this will seriously reduce the number of jobs. (There is little that can stop the continuing advances in technology).

The spirit behind these higher taxes on the rich is captured in the remark of Oliver Wendell Holmes, Jr., “I like to pay taxes. With them, I buy civilization.”

An entirely different tax philosophy operates in Scandinavian countries where the maximum tax rate is 70% in Sweden and 72% in Denmark. The Scandinavian countries take care of their citizens’ education and health from birth to death. There is little chance of a medical calamity bankrupting a Scandinavian family. And families don’t have to save as much for their future retirement. It is not surprising that Scandinavian countries rank higher in happiness measures than the U.S.

In 2014, France’s President **Francois Hollande** established the highest marginal tax rate of 75% on individuals earning an income of over one million Euros. The implication is that one million Euros a year is a sufficient salary for any person and above that, the State should take 75%. Of course, this has led to outcries from the business community and even France’s soccer teams have threatened to leave France. The measure didn’t pass. I would add two optional features that might have increased the acceptance of this 75% level. One, the tax money collected would be put into a separate government fund to help improve the education of poor students. Or two, the money could go into a non-profit foundation that supports a variety of social causes and each family can even specify which category of causes they want their money to support.

The International Monetary Fund (IMF) has taken aim at income inequality. Christine Lagarde, head of the IMF, considers income inequality in deciding on financing programs for member states. A recent IMF staff paper said “Income inequality can be of macroeconomic concern for country authorities, and the fund should accordingly seek to understand the macroeconomic effects of inequality.”[[10]](#endnote-10)

What would a higher tax rate on the rich do to their incentive to work and earn income? Conservatives warn that talented CEOs, financiers, athletes, and movie stars would work less and the U.S. would suffer from a lower level of talent and output in these sectors. They claim is that if high earners work less, and start fewer businesses, the number of jobs would decrease, unemployment would increase, and average incomes will fall. They add that needed philanthropy would decline and long term investment in infrastructure would dry up. They rail against “class warfare” that would “make everyone poorer.” So why would we put any higher taxes on the rich that 39.6%?

Of course, there is no evidence of this. In earlier times, when the U.S. government charged quite high marginal tax rates on the rich, we often had high employment and high incomes. There were more periods of prosperity in the United States under the left leaning Democratic Party than under the right leaning Republican Party. We can’t assume all high income earners behave and react in the same way. I remember meeting a CEO of a large cereal company confiding to me that he was having so much fun running the company that he would have gladly managed his company for $1 a year. Mayor Michael Bloomberg, who over a 12 year period brought New York City to a high level of prosperity, insisted on taking only $1 a year salary because he had all the money that he needed to be satisfied.

I believe that both corporate executives and entrepreneurs are motivated primarily by three things: power; independence; and creativity. I do not believe that increases in the marginal tax rate would have a major downward impact on GDP, but this can be debated. Economic theory suggests one view on this subject. The law of diminishing returns says that further increments of income tend to produce diminishing returns or satisfaction. The law of diminishing returns suggests that making an extra $10,000 will improve the well-being of a worker more than losing $10,000 would reduce the well-being of a millionaire. One study indicates that well-being increases as incomes approach $75,000 a year but beyond that it does not consistently produce higher levels of personal happiness.[[11]](#endnote-11) We are saying that it is easier for a rich person to give up the last $10,000 than a poor person.

Yet raising the tax rate on the rich may be an almost impossible task when we consider that it would have to be passed by Congress. Politicians get in office by being able to raise money. A newly elected Republican official must raise $500,000 a year just to give to the Republican Party, aside from what he or she must raise to run his or her own campaign. Most of the money comes from those who are wealthy rather than from small contributions from the working and middle class. Politicians have little choice but to curry the rich and vote for what the wealthy want. And the wealthy by and large do not want to pay higher taxes. Given that the very rich are getting a growing share of the GDP, this means that less money is available for the poor and even the working class.

The lack of purchasing power in the hands of the average citizen slows down economic growth and leads to further immiseration of the poor. This is partly what led to Occupy Wall Street. The Occupy movement went from some 75 people demonstrating in a small Manhattan park to tens of thousands demonstrating in hundreds of cities in 80 countries, all in one month. One can expect more protest movements and political clashes in the future. In the past the protestors were labeled “socialists” or “communists” and the wealthy managed to have them hounded or imprisoned. I do not see how substantially higher taxes can be passed politically on the rich without evoking another period of Red scare and the Republican charge of the Democrats starting “class warfare.”

1. **Cap the Ratio of Top Executive Pay to Worker Pay**

In 2010, Congress passed a rule requiring public companies to disclose the ratio of the CEO’s pay to the median compensation at the company. The objective was to help shareholders, companies and the public compare pay practices across companies. It wasn’t implemented.

President Obama offered a specific proposal for holding down the high pay of executives. He held that executive pay should be related to the minimum federal wage. At the time, his $400,000 salary was 27 times the minimum federal wage of $7.25. If the minimum wage rose to $10.10, his salary would be 20 times the minimum wage. He suggested that top-paid federal executives of companies that do business with the federal government should not have their top executives paid in excess of 20 to 1. This would mean stopping doing business with Oracle (1,284 to 1), General Electric (491 to 1), and AT&T (339 to 1). Although this was currently impractical, it captures the seed of an idea for limiting excessively high pay in the federal and private sector.[[12]](#endnote-12) The state of Rhode Island is considering not buying from companies that pay the CEO more than 32 times the lowest paid worker. .

The European Commission is actively encouraging member countries to consider pay cap policies. Each public company is advised to take into account the ratio of top executive pay to average employee earnings. Companies should consider the impact of high executive pay on the long-run sustainability of the company. The EU is considering banning banker bonuses of more than twice the level of fixed pay, especially after seeing the hefty bonuses recently given by some of the major European banks.[[13]](#endnote-13)

1. **Raise the Capital Gains Tax Rate**

A person who invests in a security for more than one year and then sells the security was formerly taxed at 15 percent rather than at their normal income tax rate. The capital gains tax rate was recently raised to 20 percent plus another 3.8% temporary, or 23.8%. The purpose of the lower tax rate on long term capital gains is to encourage investors to stay longer in securities that they believe in. Most wealthy people put their money into securities that they hold for over a year and therefore their effective tax rate on capital gains is 20-23.8 percent. Ironically, wage earners are taxed on their income anywhere up to 35 percent. During Romney’s run for President in 2012, it came out that he had earned $13.7 million but his tax rate was only 14.1 percent of his income. And finance expert Warren Buffett said that he was embarrassed to only pay a 15 percent tax on his income that is substantially lower than his secretary’s tax on her income.[[14]](#endnote-14) This loophole is estimated to have cost the U.S. Treasury $457 billion between 2011 and 2015.

1. **Raise the Tax on Carried Interest**.

There is also an effort to end capital gains treatment for “carried interest.” Carried interest is a share of any profits that the general partners of private equity and hedge funds receive as compensation, despite not contributing any initial funds. This method of compensation seeks to motivate the general partner (fund manager) to work toward improving the fund's performance. Traditionally, the amount of carried interest comes to around 20% of the fund's annual profit. While all funds tend to have a small management fee, the management fee is meant to only cover the costs of managing the fund, with the exception of compensating the fund manager. Carried interest is meant to serve as the primary source of income for the general partner.[[15]](#endnote-15)

The criticism is that putting a capital gains tax of only 15 or 20 percent on carried interest is another example of a preferential income tax treatment mostly going to the very rich. The general partner of a hedge fund should pay an ordinary tax on this income because it is a reward for his labor in managing the fund, not for his capital.

1. **Remove or Reduce Home Mortgage Interest Deduction**

Persons buying a home with a mortgage are allowed to deduct the mortgage interest payment from their tax bill. The purpose of this deduction is to encourage more home ownership on the notion that people owning homes (instead of renting) will be more rooted in their communities and care more for their communities. Most other industrialized nations do not offer this deduction and people still buy homes. This is estimated to have cost the U.S. Treasury $464 billion between 2011-2015. It amounts to non-home owners (i.e., renters) subsidizing home owners. Homeowners with an income exceeding $200,000 get an annual tax benefit of more than $2,200. They get another mortgage tax benefit if they own a second home, which primarily benefits wealthy people who are the most likely to own a second home. Furthermore, most of these high income homes are in California and the Northeast, thereby giving a benefit that is geographically disproportionate.

1. **Strengthen the Earned Income Tax Credit.**

The U.S. runs a large cash-transfer program to help the poor that cost $61 billion dollars in 2010. It provides up to $3,305 a year to low-income working families with one child and up to $6,143 for those with three or more children. The program has not been extended to help childless people who have very low incomes. Broadening the tax credit might make it possible to do away with food stamps and a miscellaneous set of other props aiming at providing a decent living for all.

Related to the earned income tax credit is a much broader idea, that of the **Universal Basic Income (UBI).** In the 16th century, Thomas More proposed it in his work *Utopia.* President Nixon even considered it for a short time. In 1967, Martin Luther King, Jr. wrote, “I am now convinced that the simplest approach will prove to be the most effective - the solution to poverty is to abolish it directly by a now widely discussed measure: the guaranteed income.” The celebrated economist, John Kenneth Galbraith, agreed, ‘Everybody should be guaranteed a decent basic income. A rich country...can well afford to keep everybody out of poverty.’ This payment given equally to all citizens would prevent any citizen from ending up with less money.

Universal Basic Income (UBI) would be a fixed, monthly cash grant, given directly to all adult citizens individually, to cover basic living expenses, with no strings attached. Imagine it as a payment of $1,000 a month to all adult citizens. The cost would be $12,000 a year for say 300 million adult citizens, or over $4.2 trillion. This would be an impossible huge transfer payment. The amount could be reduced if limited on only those earning under $200,000 or a lower amount. If we limited it as a payment to only the poor, the cost would be more affordable and pretty much the same as the earned net income tax credit idea.

How would the money be raised for UBI? Many welfare programs will be eliminated. The money spent on these programs will be transferred to the UBI funds. A second source of money can come from raising taxes on the wealthy on the grounds that it will not affect their material living. A third source can be a special tax on companies. Companies destroy jobs by moving abroad and by introducing automation. This company tax will pay those who lost their jobs. A fourth source can be raising consumption taxes (VAT). A fifth source can be a tax on financial transactions. A sixth source might be transferring money from the bloated defense budget to help more people live a better life.

A guaranteed basic income would free people to decide whether they want to work in a permanent job or work part-time or not at all. Today Americans work closer to 50 hours rather than 40 hours a week for 50 of the 52 weeks. Many of them are bored with their jobs and would leave them if they had a choice. Many will exploited by their boss and will want to do something else with their lives and earn money along the ways doing short gigs. Americans work too hard and too long without time to enjoy other aspects of their lives.

Some version of UBI may be necessary in the future, given the speed of automation and the possibility of eliminating many jobs for humans. The U.S. would have to find some way of distributing basic income to the growing ranks of the unemployed.

Versions of UBI have been proposed elsewhere. In 2016, [Swiss](http://www.basicincome2016.org/blog/basic-income-vote-in-5-weeks-sensational-new-polling-results) citizens voted in a referendum on whether to hand out a guaranteed $33,000 to every citizen, regardless of wealth. It was defeated. The Finnish government planned giving each of its 5.4 million citizens $876 tax-free every month ($10,512 a year). In return, it would do away with welfare benefits, unemployment lines, and the other bureaucracy of its extensive social safety net. Denmark gives its poorest citizens roughly $1,800 a month, enough to pull the destitute over the poverty threshold.

Objections are many. People would be paid to be “lazy.” Not having a job means that there would be no building of character or discipline. Many people would not have an incentive to study harder subjects or study much at all. Many will abuse their free time in just watching TV or gambling or turning to drink or drugs when they are no long career-oriented and associating with other career-driven people.

1. **Close Offshore Tax Havens**

Profits earned by U.S. companies were subject to a 35 percent tax rate. This led U.S. companies to keep their foreign earnings abroad rather than bringing them home and paying a 35 percent tax. Companies like Apple, General Electric and many others kept so much money abroad that could otherwise have been invested in the U.S.

Clearly U.S. companies want to reduce their taxes if possible. There are three approaches.

The first is to set up a U.S. company subsidiary in Bermuda, Cayman Islands or Ireland. A U.S. company making a printing machine costing $10,000 in Chicago might sell it to a Miami printing company for $12,000. The U.S. company would have to pay a 35 percent tax on the $2,000 of profit, namely $700. Instead, it could send the printing machine to its own subsidiary in Bermuda. Then its Bermuda subsidiary can sell it to the Miami printing company for $12,000, making a $2,000 profit in Bermuda. But Bermuda doesn’t tax profits (or taxes substantially less than the U.S.). In this way, the U.S. government lost $700 in taxes on this transaction alone. It is estimated that 362 of the Fortune 500 companies operate tax haven subsidiaries. The U.S. government is losing a great amount of corporate tax revenue, requiring either the American public to pay higher taxes or face reducing social welfare, education and health benefits.

The second tax avoidance scheme is called “Inversion.” If an American company can show that some percentage of its shares are owned by another company abroad, it doesn’t have to pay U.S. taxes on this amount. For example, the Walgreens company might buy an Irish drugstore chain and pay for it by issuing more shares of its stock. Walgreens of Ireland would have to pay taxes to Ireland but Ireland’s taxes are considerably lower than U.S. taxes. This is called inversion.

The U.S. government needs to worry about a third possibility where a U.S. corporation starts thinking about moving its headquarters out of the country. The consulting firm Accenture began as a U.S. company, then moved to the Cayman Islands, went public in 2002 and then moved to Ireland and its lower taxes.[[16]](#endnote-16) Eaton Corporation moved its headquarters from Cleveland to Dublin, saving $160 million a year in taxes. So far, some 60 U.S. companies were “never here” or have been using inversion to avoid U.S. taxes. Not only do these companies substantially reduce their taxes but in addition they are less burdened by the endless growth in U.S. government regulations that now cover 169,301 pages.[[17]](#endnote-17)

Gabriel Zucman, an economics professor at the London School of Economics, and a protege of Thomas Piketty, wrote a short book on tax evasion called *The Missing Wealth of Nations*, in which he estimated that $7.6 trillion, or 8 percent of the world’s personal financial wealth, rests in tax havens as hidden money.[[18]](#endnote-18) If this money could be taxed, more than $200 billion a year could be added to tax revenues.

Zucman estimated that 20 percent of all U.S. corporate profits are shifted offshore, with the result that these corporations manage to pay a corporate tax rate of 15 percent rather than the officially correct rate of 30 percent. U.S. corporations have accumulated $1.95 trillion outside of the U.S.[[19]](#endnote-19) U.S. companies don’t pay U.S.taxes on profits earned abroad as long as that money remains abroad, often in Bermuda, Ireland, Luxembourg, the Netherlands and Switzerland. In 2013, Apple held abroad $54.4 billion, IBM $52.3 billion, and Microsoft, $76.4 billion. Proposals have been forthcoming to either lower corporate taxes to 25 percent or less or to change the tax code requiring that these profits be invested in U.S.-located banks.

Zucman recommended that the U.S. and other nations prepare a global registry of personal and corporate wealth (just like there is a global registry of real estate holdings) and go after the banks to disclose their holdings. The U.S. passed the 2010 Foreign Account Tax Compliance Act to enable the Internal Revenue Service to put pressure on foreign banks to disclose accounts held by American residents and corporations. The U.S., in 2012, imposed a $1.9 billion fine on HSBC, a British bank, for poor controls on money laundering. Fines have been set on Barclays, ING and Standard Chartered.

The Tax Reform Bill of 2018 finally lowered the corporate tax rate on foreign earnings from 35 percent to 21percent. Some money came back into the U.S. although not much led to building new factories and equipment. Some money went into company stock buybacks, higher bonuses for top officers, and higher dividends for investors. Stock buybacks, management bonuses and investor pay are at an all-time high. Economic disparity is at an all-time high.

1. **Pass a tax on Financial Transactions**

A great amount of money is spent every weekday on buying and selling stock. The mass of securities traded in the United States is in the hundreds of trillions of dollars. The aim of traders is to make a profit through betting on the rise or fall in the price of specific stocks or in the stock market as a whole. At best, this is a form of gambling rather than creating new value. It is a game indulged in largely by persons who have discretionary income. Fifty three percent of Americans have no money in the stock market. Most stock traders have good income or wealth.

Senator Bernie Sanders of Vermont proposed this tax on financial transactions.[[20]](#endnote-20) He proposed a small excise tax, typically a few hundredths of a percent, on trades of stocks, bonds, derivatives and other securities. A one-basis-point tax on $1,000 worth of stock would cost the stock trader a dime. A $100,000 trade would generate a tax of only $10. The nonpartisan Tax Policy Center estimated that a 0.01 percent tax would raise $185 billion over 10 years. That amount could finance an ambitious expansion of prekindergarten programs for 3- and 4-year-olds and restore funding of college assistance for low-income students.

This tax on financial transactions would reduce the amount of high-frequency trading, much of which is automated and used to make windfall profits through taking advantage of small differences in price in milliseconds. This type of trading accounts for over 50 percent of the trades in some exchanges. This kind of trading does nothing for ordinary investors and can destabilize financial markets. If anything, this type of trading may increase the market’s volatility.

The tax would be highly progressive in its impact. The Tax Policy Center estimates that 75 percent of the tax would fall on the top fifth of taxpayers, and 40 percent on the top 1 percent. The tax would fall more heavily on high-volume traders than on long-term investors. The proceeds could be used to reduce inequality and increase mobility.

Transaction taxes of one type or another have been in place in countries with thriving financial markets, including Britain, Hong Kong, Singapore and many others. Eleven countries of the European Union agreed to implement such a tax, in 2013, though pressure from opponents caused the introduction to be postponed. So it simply can’t be the case that they’re unworkable.

1. **Pass a tax on high-value luxury goods**

Most goods and services carry a sales tax or a value-added tax. There is a question whether to add a surtax on luxury goods and services. Luxury goods would include expensive cars, mansions, private airplanes, private boats and yachts, swimming pools, furs and expensive jewelry and clothing. Understand that buyers of these goods already pay more dollars. If the sales tax is 10 percent, then a $100 watch would be taxed at $10 and a $1,000 dollar watch would be taxed at $100. The question is whether to put an additional luxury tax on watches costing $1,000 or more.

The purpose of a luxury tax is to gain revenue from people who have the means and whose life style would not be diminished by that tax. The net result would be to reduce the resources consumed in making luxurious goods and increase the money available to make more affordable housing, city swimming pools, and other socially needed goods. The measure aims at redistribution from the rich to the poor.

In the early nineteen nineties in the United States, a 10% luxury tax was levied on fur, expensive jewelries, airplanes and cars worth $30,000 and above. In the case of cars, the biggest opposition came from European car manufacturers that made some of the most expensive cars in the world. The U.S. motivation was to protect lower price American cars from the competition. But even General Motors and Ford, producing the Cadillac and Lincoln, respectively, objected. Meanwhile European countries themselves were one of the leaders charging luxury taxes on cars. The 10% luxury tax led to a sharp decline in sales of expensive cars and these other items. This caused problems for producers of these items and their retailers, so much so that the law enacting the luxury tax had to be repealed.

In 2014, the Nigerian Government, suffering from declining oil revenues, planned on setting the following luxury goods taxes: • 10% import surcharge on new private jets; • 39% import surcharge on luxury yachts; • 5% import surcharge on luxury cars; • 3% luxury surcharge on champagnes, wines and spirits; and a • 1% mansion tax on residential properties valued above a certain level. These rates were implemented by enforcement faced stiff resistance and was eventually abandoned.[[21]](#endnote-21)

The major question is “What are the specific goods and services that will constitute luxury goods and services?” The answer differs in countries with quite different economic levels and even within these countries. In the UK, chocolate covered biscuits are considered luxury yet somehow biscuits and cakes are considered necessities. In Norway, cars and chocolates are considered luxury items and are liable to luxury taxes. The term “luxury tax” is sometimes mistaken with so-called “sinful items” such as sugary drinks, tobacco and alcohol. Hence the concept of “sin tax”. This could have adverse effects on the affected businesses and by extension the economy.

The idea, however, remains to get the wealthy to contribute a bit more towards easing the deprivations that ordinary families experience.

1. **Adopt Measures to Reduce the Concentration of Wealth**

We need to turn to the great differences in wealth distribution, not just income distribution. As stated earlier, the top 1 percent of U.S. households hold 40 percent of the nation’s wealth. The wealthiest 10 percent of households holds 70 percent of the nation’s wealth.

Why is the very high concentration of wealth a problem? Essentially this goes against the principles of a democratic society. In a democratic society, each qualified person would have one vote. But today, wealthy families have a disproportionate influence on the voting outcome and on public policy. Recognize further that most of today’s wealthiest people are wealthy by inheritance, not by contribution. Yet they are able to supply conservative candidates with a great amount of money for their election campaign. The [Huffington Post reported](http://www.huffingtonpost.com/2012/02/03/koch-brothers-100-million-obama_n_1250828.html) that billionaire Charles Koch pledged to give $40 million to unseat Obama while his brother David Koch has pledged $20 million.[[22]](#endnote-22)

The Supreme Court decided in the Citizen’s United case that a corporation could be called a “person” who under “free speech” could create or give substantial sums of money to new nonprofit organizations to spread conservative views. Wealthy families and wealthy corporations, by giving heavy donations to conservative candidates, have a much greater voice in influencing who become our legislators and how they will vote. Working class families lack personal influence and only can rely on their shrinking unions to exercise some counter influence. The bottom line is that great extremes of income and wealth can diminish or destroy the power of the people to vote for the best candidates.

What can be done to reduce the great concentration of wealth? We have to put heavier taxes on the passage of estates to their heirs. Today, the estate of a superrich person is exempt from a tax on the first $5 million dollars given to each heir. The tax rate on the rest of the estate is 55 percent. This rate can be raised even higher to reduce the concentration of wealth.

Recently Warren Buffett publicly stated that Coca Cola’s recent executive compensation plan “was excessive.” Buffet owns over 9 percent of Coca Cola’s shares and is the largest investor. Another Coca Cola investor had charged that “The Company expects that the 2014 Plan will award a mix of 60% options, 40% full value shares, resulting in the issuance of 340,000,000 Coca-Cola shares” that he estimated would transfer around $13 billion from shareholders to management and he saw this as an “outrageous grab.” Buffett in the past had come out against excessive executive compensation.[[23]](#endnote-23)

Another recent development involved some CEOs declining the bonus to which they were entitled. Virginia Rometty, CEO of IBM, was to collect a bonus of $8 million based on the company’s performance and decided to turn it down. Barclay’s CEO, Antony Jenkins turned down his bonus of $2.8 million for the second year in a row saying “it would not be right.” Similarly Stephen Hester of the Royal Bank of Scotland and Larry Ellison of Oracle turned down their respective annual performance bonuses.[[24]](#endnote-24)

Yet many of the wealthy are bitter about proposals for higher taxes. The billionaire investor Tom Perkins of the venture capital firm of Kleiner Perkins Caufield & Byers lamented public criticism of the “one percent” and compared it to the Nazi attacks on the Jews. Stephen Schwarzman of the Blackstone Group said that eliminating tax loopholes were “like when Hitler invaded Poland in 1939.” These plutocrats react with a mix of paranoia and megalomania rather than thinking deeply about the problem that excessive wealth poses for the economy.[[25]](#endnote-25)

There is a whole industry involved in helping the super wealthy hold on to their wealth beyond the last living member and continue even into their grandchildren’s grandchildren. South Dakota has pioneered “dynasty trusts” to help rich families escape estate taxes forever. In January 2013, Congress allowed families to set up a trust of $5 million that would have iron-clad secrecy. Lawyers have invented more complicated strategies to protect much larger fortunes.[[26]](#endnote-26)

This raises again the question of whether higher estate taxes will lead to more avoidance and also lead talented people to work less hard or threaten to leave the country. I would argue that there are a great many civic-minded talented people waiting to move up the wealth ladder and take their place. The issue, of course, is who would receive the redistributed wealth? Will it ultimately be used by government to increase wages and jobs? Or will it go into more defense spending and more bureaucracies?

We also need to look at other wealth sources and whether they need some trimming. The country may be too generous in its subsidies to those who search for oil. Exxon Mobil took home a net income of $30 billion dollars in 2012. Boards of directors might be too generous in the compensation packages that they set up for CEOs for take home pay. And then consider what has to be paid to the vice-presidents if the top guy gets 300 times. This means that the expense of managing a major American company is top heavy in relation to its foreign competitors. For example, Japanese CEOs take home pay is more in the order 100 times rather than 300 times in the U.S.

The French economist Thomas Piketty holds that wealth inequity keeps growing because in this period “the rate of return on capital…is higher than the economy’s growth rate.”[[27]](#endnote-27) He sees income from capital continuing to exceed income from wages and salaries as a worldwide phenomena. His preferred solution: “a global tax on wealth combined with higher rates of tax on the largest incomes.” Wealth or capital would include real assets - land, houses, natural resources, office buildings, factories, machines, software, patents, stocks and bonds. Households would have to declare their net worth to the tax authorities and pay a levy of one percent for households with a net worth of between one and five million dollars, and two percent for those worth more than five million. Piketty adds that even a steeper progressive tax of 5-10 percent on wealth above one billion euros would help break up such fortunes. In the U.S., this would mean that the 16,000 people (the top hundredth of 1 percent) who have a combined net worth of $6 trillion would pay substantial taxes, and the money would presumably be used to improve the education and health of the U.S. population.

Piketty recognizes problems with his proposal. First, the wealthy would scream that this would reduce incentives and innovation. Piketty doesn’t believe that innovation will be hurt. Second, this proposal would never be proposed, nor passed because politicians are dependent on the wealthy for being reelected. Third, the wealthy would transfer their wealth to other countries where this wealth tax did not exist. They wouldn’t transfer it to Spain which has a wealth tax of 2.5 percent of assets. Piketty would need to advocate that all countries pass such a wealth tax, which he admits is clearly a utopian idea. Piketty is realistic but offers his proposal as a standard against which to judge other proposals for curbing the growth of wealth inequity.

The World Bank economist Branko Milanovic said of Piketty’s book: “We are in the presence of one of the watershed books in economic thinking.” Paul Krugman wrote that it “will be the most important economics book of the year—and maybe of the decade.”[[28]](#endnote-28) Paul Krugman thinks that Piketty’s book has the potential of creating a monumental change in public attitudes toward growing income inequality.[[29]](#endnote-29) The publicity that the book is receiving is making people aware that all great wealth is not the result of meritocracy where great wealth is earned and deserved. Much of the income of the wealthy is not coming to them on the claim that they are “job creators.” Much of their income is coming from the assets they own, “not from their enterprise but from their inheritance.”

Piketty’s book is now worrying the rich because they have not been able to tear down its premises. They rely on name-calling by calling it Marxist or collectivist or Stalinistic. The rich are on the run politically and will use their money to confuse the public as much as possible regarding the real issues. One unsolved mystery is how can it be that so many poor or working class people or even many middle class people identify their interests with the political party whose whole basis is to defend the interests of the superrich.

The real challenge is to convince the superrich that paying higher taxes would benefit them as well as the general public. Arguments can be used that roads and infrastructure will be improved, workers will have more money to spend on the businesses owned by the rich, and the public will think that the tax system is fairer and be willing to comply more readily. If the government can demonstrate that its operations are efficient and that their tax money is going to the right causes, people will be more willing to pay their fair share of taxes. In the end, is it better to move toward a budget calling for preserving tax loopholes and cutting taxes and cutting investments in education, health, and infrastructure or to develop a system that raises more money through a fair and efficient tax system and use the money to improve the lives of people.

**Conclusion**

Clearly a whole set of solutions exist to reduce the sharp differences between the earnings of the superrich and the other groups, solutions that are not likely to damage incentives or productivity. The problem is not one of sound economics. It is one of the ways politics interferes with economics and allows the rich and their publicists to confuse average citizens as to what lies in their true interests and in the country’s long term interest.

We return to our initial question about whether capitalism is intrinsically destined to produce little for the poor, and extreme incomes and wealth for the few. This may well be the tendency of free market or unregulated capitalism. But if so, capitalism could contain the seeds of its own destruction.

Why? Capitalism depends on consumers having enough money to buy the goods and services that the capitalist economic machine produces. Without rising real income in the pockets of the majority of the citizens, the result is overstocks of goods, slowdowns in investment and production, and a rising unemployment rate. The amount of joblessness can reach a point of inspiring an uprising and attack on not only the wealthy but capitalism itself. Ultimately capitalism will be judged on the degree to which it improves the lives of all its citizens. Capitalism has to save itself from Revolution by a fairer tax regime on income and wealth.

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