WHO STOLE
the
AMERICAN
DREAM?

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CHAPTER 21

RECLAIMING THE DREAM

A DOMESTIC MARSHALL PLAN:
A TEN-STEP STRATEGY

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—PRESIDENT GEORGE WASHINGTON,
First Annual Message to Congress, January 8, 1790

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—SUSAN HOCKFIELD,
president, Massachusetts Institute of Technology

One key to Germany’s success: “The social contract,
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ers to put aside some of their differences and make
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—KLAUS KLEINFELD,
Alcoa CEO
FOR THREE DECADES, we have pursued the laissez-faire economics of lower taxes, less regulation, and trust in the market to lift all boats, and we have seen the dangerous schisms this has created. Just in the past two years, there has been a dramatic increase in people's sense of a class division and a sharp class conflict in America.

To reverse that trend, to heal our schisms, to restore our sense of community, and to rejuvenate our competitive economic strength, we need a new direction and a new agenda—a new political and economic response, in Toynbee's terms. Changing America's direction will not be easy. It will happen only if there is a populist surge demanding it, a peaceful political revolution at the grass roots, like the mass movements of the 1960s and 1970s.

In the economy, we need to get the virtuous circle working once again to rebuild middle-class prosperity. That challenge requires a positive response from business—a change in the business mind-set: smart CEOs committed to rebuilding productive capacity at home in America and then sharing more of the fruits of higher productivity with average Americans through higher pay. Even if that means lower dividends for Wall Street and for wealthy shareholders in the short run, everyone will profit in the longer run from a vigorous economy where the spoils are shared more evenly.

And in the world at large, we need to step back from Imperial Overstretch that has exceeded our means and refocus our resources and our energies on regenerating America's economic might and shared prosperity.

A Domestic Marshall Plan

Many good people from different walks of life sense the need for a new direction. Some top corporate executives have joined economists and political moderates and liberals in calling for a national economic strategy that will generate an American industrial renaissance and revive America's global competitiveness. Advocating a come-back for manufacturing in America is one issue that Mitt Romney, Rick Santorum, Newt Gingrich, and other contenders for the Republican presidential nomination shared with President Obama.

One group of top corporate executives, the Horizon Project, advocates a domestic Marshall Plan, evoking the generous American aid that put Western Europe back on its feet after World War II by financing reconstruction of its infrastructure and its war-ravaged industry. In other words, a massive collective effort—a public-private partnership sparked at the outset by government initiatives and investments.

"Job creation must be the number one objective of state economic policy," declares former Intel CEO Andy Grove. "The government plays a strategic role in setting the priorities and arraying the forces and organization necessary to achieve this goal."

It's a mistake, says Grove, for America to count on individual companies, even big ones like Intel, to meet the job and growth needs of the nation without government policies that stimulate them to do so. "Each company, ruggedly individualistic, does its best to expand efficiently and improve its own profitability," says Grove, who ran Intel from 1987 to 1998. "However, our pursuit of our individual businesses, which often involves transferring manufacturing and a great deal of engineering out of the country, has hindered our ability to bring innovations to scale at home. Without scaling (mass production), we don't just lose jobs—we lose our hold on new technologies.... [We] damage our capacity to innovate."

Business Organizations, such as the Alliance for American Manufacturing and the U.S. Business and Industry Council, as well as organized labor, endorse Grove's thinking. So do many economists.

New York University's Michael Spence, a Nobel laureate in economics, explains their logic. Spence has documented how global competition has stunted the growth of the "tradable" sectors of the U.S. economy—the industries that make cars or cellphones or energy equipment and that are directly exposed to foreign competition. Their poor performance, Spence explains, has left nearly 98 percent of America's job growth since 1980 to the lower-paid health care,
service, and public sectors, the so-called nontradable sectors where work has to be done locally. These domestic-oriented sectors have generated 26.7 million of the 27.3 million new jobs in the United States from 1980 to 2008. But those sectors face dim prospects for future growth, Spence asserts, and so America needs “to devote public funding to developing infrastructure and the technological base of the U.S. economy with the specific goal of restoring competitiveness and expanding employment in the tradable sector.”

To the free market thinking that has dominated our politics and our economics for three decades, the Grove-Spence approach is anathema. Market advocates reject the very idea of a national economic strategy as heresy. Government involvement in the economy, they argue, amounts to Washington’s picking winners and losers. That, they contend, is un-American. It goes against the grain of American history.

But that’s not really true.

From George Washington to George W. Bush:
A Government Industrial Policy to Spur America’s Growth

The Founding Fathers, and many other American presidents from both major political parties, have favored what other nations call an “industrial policy.”

Not only did George Washington make a point of wearing an American-made suit for his inauguration, when British tailors were reputedly the world’s best, but he advocated a government plan to promote domestic manufacturing against British imports.

In his first annual address to Congress on January 8, 1790, Washington emphasized in words that resonate today: “A free people ought not only to be armed but disciplined … and their safety and interest require that they should promote such manufactories as tend to render them independent of others for essential, particularly military, supplies.”

Washington’s Treasury secretary, Alexander Hamilton, promoted high tariffs and “buy American” policies, endorsed by Washington. Thomas Jefferson, the Virginia plantation owner who was originally an agrarian foe of merchants, switched to Hamilton’s view after the British sacking of the nation’s capital during the War of 1812. That war, Jefferson wrote to a friend, had showed “that manufactures are now as necessary to our independence as to our comfort.” He argued that American industry needed support, contending that “He, therefore, who is now against domestic manufacture, must be for reducing us either to dependence on that foreign nation, or to be clothed in skins, and to live like wild beasts in dens and caverns.” Presidents James Madison, James Monroe, John Adams, and John Quincy Adams, holding similar views, supported subsidies and tariffs to promote domestic industry.

In fact, American history is replete with examples, from the Erie Canal to the transcontinental railroad to the Apollo moon project to the Internet and the GPS, where the government has backed economic and industrial projects to build the nation’s transportation backbone or to create new technologies to enhance America’s competitiveness and then has handed them off to the private sector.

In 1842, Congress awarded Samuel F. B. Morse a $30,000 appropriation to test the feasibility of an experimental telegraph line, and another $10,000 in 1843 to lay a telegraph line from Washington to New York via Baltimore and Trenton, New Jersey. In 1862, Abraham Lincoln got Congress to pass the Pacific Railroad Act, which made huge land grants to railroads that became the springboard for America’s astonishing economic surge in the late nineteenth century. Nearly a century later, in response to the Soviet Sputnik space shot, Dwight Eisenhower got Congress to vote funds for a nationwide highway network that still serves us today. The nation’s space program, which Eisenhower launched and nine other presidents kept going, generated many of the technologies that led to America’s supremacy in aerospace and computers.
Reagan’s Economic Interventions

Even Ronald Reagan, despite his mocking remark that “government is not the solution; government is the problem,” used governmental power to bolster U.S. industry. When Japanese computer firms threatened American computer chip makers in the early 1980s, the Reagan administration put political pressure on the Japanese government to guarantee U.S. firms a 20 percent share of the Japanese market by initiating an unprecedented trade case against Japan. Reagan persuaded Congress to approve the government’s investment of $1 billion in Sematech, a new public-private partnership with a dozen computer companies, to create “precompetitive” technologies to keep America’s high-tech industry in the vanguard and to prevent the Pentagon from becoming dangerously dependent on foreign suppliers for components of military weapons systems.

Reagan also moved forcefully to protect America’s automakers. When Toyota and Honda made deep inroads into the U.S. car market, Reagan forced a 40 percent devaluation of the dollar, making Japanese imports much more expensive. Then Reagan pressed Tokyo to accept quotas on Japanese auto exports to America and pushed Japanese automakers to set up assembly plants in the United States to generate jobs for American workers.

So there was ample precedent for Barack Obama to extend an $80 billion rescue fund to General Motors and Chrysler during the economic collapse of 2008 with funds that George W. Bush had gotten from Congress to rescue Wall Street banks.

In short, contrary to modern right-wing political rhetoric, presidents of both parties have used government funds and authority to protect American industry and have poured hundreds of billions of dollars into the nation’s transportation, communications, and financial systems. They have fostered the development of new technologies since the dawning of our Republic, though Americans have often remained unaware of the government’s role in what are marketed as private sector innovations.

As CEO of Apple, Steve Jobs won a deserved reputation as the creative and entrepreneurial genius behind many groundbreaking products. But as former Reagan administration trade negotiator Clyde Prestowitz observed, “Virtually everything Jobs has developed—the mouse, Mac/Windows displays, operating systems, touch screens—began in or received support from a government office.”

That is hardly surprising since federal agencies such as NASA, the Departments of Defense, Energy, and Agriculture, the National Institutes of Health, and the National Science Foundation are so large and spend so many hundreds of billions of dollars a year in the economy that there is no such thing as a free market without government influence. Without announcing it, the United States already has a de facto industrial policy—in effect, picking winners—by pouring lifeblood into such huge contractors as Boeing, Lockheed Martin, United Technologies, IBM, Microsoft, Intel, Apple, and hundreds more.

Reconnecting America’s Genius at Innovation with Production and Job Growth

So the question now is not whether, but how—how should the existing influence of government be used most effectively to help the private sector revitalize our economy, to share the economic gains more widely, to create millions of jobs for average Americans, and to make our nation more globally competitive again?

Corporate CEOs such as Jeffrey Immelt of General Electric, Andrew Liveris of Dow Chemical, and former Intel CEO Andy Grove, as well Nobel Prize–winning economists such as Michael Spence, Joseph Stiglitz of Columbia, and Paul Krugman of Princeton declare that we must urgently restore the nation’s industrial strength.

“The United States became the world’s largest economy because we invented products and then made them with new processes . . . .” asserted MIT president Susan Hockfield. “Today, our most important task is to restart this virtuous cycle of invention and manufac-
turing. . . . We need to create at least 20 million jobs in the next decade to offset the effects of the recession and to address our $500 billion trade deficit in manufactured goods.”

The key, these corporate leaders and economists contend, is to re-establish vital connections in our economy in order to reinforce the crucial ways in which America's genius at innovation translates into economic growth for the nation and job growth for the middle class through large-scale production, which then powers the next generation of innovation, production, and job growth.

The dynamic interaction between innovation, production, and job growth in America was disrupted, they say, when major U.S. multinationals moved overseas the mass production of commodities—from computer and aircraft components to auto parts, appliances, and cellphones—to places like China. “Not only did we lose an untold number of jobs, we broke the chain of experience that is so important in technological evolution,” cautions Andy Grove. “Abandoning today’s ‘commodity’ manufacturing can lock you out of tomorrow’s emerging industry.”

Behind Germany’s Success: A Social Contract for Jobs and Exports

As the United States looks ahead, many economic analysts see valuable lessons in Germany, the linchpin of the euro zone, over the last two decades. Germany’s response to the challenge of globalization and low-cost competition from China and Asia has been different from ours, as we saw earlier, and its outcome has been better.

Since the mid-1990s, the German economy has grown faster than the U.S. economy, and its middle class has shared more of the gains. Since 1985, Germany’s average wage went up nearly 30 percent versus only 6 percent in the United States. In foreign trade, Germany generated $2 trillion in trade surpluses from 2000 to 2010, while the United States racked up $6 trillion in trade deficits. So today, Germany still has twice as many people working in manufacturing as the United States—21 percent of its workforce to 9 percent of ours.

“The German model shows that a developed country can remain competitive even in a world where new economic giants, such as China, India, and others, are emerging,” observes Wall Street investment manager Steve Rattner. One reason is that German consumers import less than half as much, per capita, from China as Americans do, and German industry, with its marque brands and precision machine tools, exports more successfully. BMW, for example, makes 25 percent of its profits selling luxury cars in China.

But what explains Germany’s so-called economic miracle is a social contract that brings together business, labor, and government working for the nation’s benefit. “It isn’t a miracle,” former German economy minister Michael Glos explained. “It’s because we stuck to manufacturing whereas other countries de-industrialized”—moved into services and shifted their production offshore.

Klaus Kleinfeld, former CEO of the German electrical giant Siemens and now CEO of Alcoa, asserts that the key ingredient of Germany’s success is “the social contract, the willingness of business, labor, and political leaders to put aside some of their differences and make agreements in the national interest.”

Trade union leaders sit on the supervisory boards of major firms such as Volkswagen, Daimler, and Siemens, positioned to persuade management to keep the highest value-added work in Germany. As a trade-off, unions have eased demands for pay increases.

“To keep work at home, German unions also agreed to continual productivity and efficiency increases,” noted commentator Harold Meyerson. “They can afford to do this because, as is not the case in the United States, such increases don’t necessarily mean their members will be sacked.”

In fact, during the 2008 economic collapse, big German companies adopted a “short work” policy to spread the pain of recession. Instead of laying off masses of workers, German companies short-
ened everyone’s workweek, saving five hundred thousand jobs, so Germany’s unemployment rate went down during the recession while America’s rose sharply and stayed high.

Ten Steps to Reclaim the Dream

Reclaiming the American Dream will not be quick or simple. We have a long-term structural jobs problem that demands new thinking and an ambitious new economic agenda. Hence the call from the Horizon Project CEOs for a domestic Marshall Plan. What they advocate is a government-led industrial policy focused on generating millions of new jobs, exporting more products, modernizing our infrastructure, making our tax laws smarter and fairer, restoring America’s manufacturing at home, and legally challenging or retaliating against China’s unfair trade practices.

From their thinking and that of others, here are ten steps for reclaiming the American Dream.

Step #1: Infrastructure Jobs to Compete Better

Step #1 is to form a new public-private partnership to modernize America’s outdated transportation networks and create five million jobs—and maybe many more—with major investments over the next decade. Follow the model of President Lincoln, who used government aid to promote and subsidize the transcontinental railway, or President Theodore Roosevelt, who built the inland waterways, or President Dwight Eisenhower, who fathered America’s modern interstate highway network.

Wall Street is reported to be eager to invest in infrastructure projects if the government puts up seed money. That plan wins backing from such traditional political adversaries as the U.S. Chamber of Commerce and the AFL-CIO. It wins bipartisan endorsement from politicians like New York mayor Michael Bloomberg, Texas senator Kay Bailey Hutchison, and former California governor Arnold Schwarzenegger, all Republicans, and Democrats such as Senators John Kerry of Massachusetts and Mark Warner of Virginia and former Pennsylvania governor Ed Rendell.

The U.S. Chamber of Commerce estimates that America’s faltering infrastructure costs the United States $1 trillion in economic growth and hampers U.S. exports. In world rankings of infrastructure, the United States has fallen from No. 1 to No. 15. Not only do we have sixty-nine thousand structurally deficient bridges, but our national rail network has such serious bottlenecks that it takes a freight train longer to get through the city of Chicago than it does to go from Chicago to Los Angeles. In high-speed rail development, China is outspending the United States $300 billion to $100 billion. Our aviation control system is so outdated and overloaded that the Federal Aviation Administration predicts it “will reach total gridlock by 2015” unless it is urgently modernized. Our ports are overloaded. Our highways are clogged. In 2009, Americans wasted 4.8 billion hours and 3.9 billion gallons of fuel sitting in traffic at an estimated cost of $115 billion.

Leaders from both parties as well as business-oriented task forces advocate responding to this challenge with a national infrastructure bank to spark the financing of a ten-year plan to improve our ports, airports, and commercial and commuter rail systems, as well as our bridges and highways. Because of current low interest rates and high unemployment, one economic study pointed out that it will “never be cheaper” for the nation to undertake a major infrastructure push because “capital costs are now at historic lows . . . and labor is in abundant supply . . . .”

The U.S. Chamber of Commerce estimates that $10 billion to $30 billion in government start-up funds could attract up to $600 billion in private investments. Another $1 trillion in private investments could be generated, some economists suggest, from the overseas profits of U.S. multinational corporations, if they were
given attractive terms to bring those funds home and invest them in financing U.S. infrastructure development. They could profit from that investment, while paying U.S. taxes—a win-win for all sides.

As a parallel move, former CEO Leo Hindery, Jr., and United Steelworkers president Leo Gerard have proposed that the government provide funds to put five million young people to work on modest infrastructure projects, especially in urban areas. A youth jobs program, similar to the New Deal Civilian Conservation Corps, they assert, would not only reduce the much higher than average unemployment rates among young people, but reduce the risk of idled youth turning to crime. Hiring young people would have a multiplier effect on the economy, economists explain, because young people are known for spending their earnings fast.

**Step #2: Push Innovation, Science, and High-Tech Research**

Step #2 is a major new national commitment to rebuild America’s capacity to out-invent and out-innovate the world. Despite breakthroughs by companies such as Apple and Google, the United States has slipped in innovation, which has long been America’s bedrock advantage in the world. In 2007, the National Academy of Sciences, joined by leaders in industry and education, reported that a “gathering storm” from foreign competitors was threatening America’s traditional edge in science, high tech, and innovation. In a second major report three years later, the academy issued an even sharper warning of a “rapidly approaching category 5” disaster.

Scientists date the American slide in research from the Reagan administration’s sharp cuts in government funding for basic research in the early 1980s—from nearly $9 billion in 1979 to $1.4 billion in 2006, figures adjusted for inflation. The impact has been disastrous on America’s once invincible lead in research and innovation. From a No. 1 innovation ranking in 2000, the United States fell to No. 4 in 2011, behind Finland, Singapore, and Sweden. Georgia Tech University’s global study of high-tech indicators found that China in 2008 surpassed the United States in overall “technological standing.” The World Economic Forum ranked the United States fifth in global competitiveness in 2011.

The trends in patents, a key indicator of innovation, are worrisome. After decades of domination by U.S. firms, universities, and individuals, 51 percent of the U.S. patents awarded in 2009 went to non-American companies. In clean energy development and production, the United States was once the undisputed leader but has been surpassed in production by China, Japan, and South Korea. Without large new U.S. investment, the Information Technology and Innovation Foundation predicts that the United States will soon be importing “the overwhelming majority” of its clean energy technologies, jeopardizing the U.S. economic recovery and our balance of trade.

**Business and Science Leaders Look to Government to Take the Lead**

Not only scientists and educators, but corporate leaders such as former CEOs Norman Augustine of Lockheed Martin, Craig Barrett of Intel, and Roy Vagelos of Merck support the National Academy of Sciences finding that it will take dramatically expanded government funding for the United States to bounce back in the R&D race. The private sector and universities will do the work, they say, but they need a big financial shot in the arm from Washington. In 2007, industry leaders urged Congress to appropriate $130 billion over the next decade for government funding of research, innovation, and targeted aid to education, plus tax credits to industry for research and development.

In April 2009, President Obama provided a kick start. He an-
nounced plans to add $42.6 billion to science and technology research over the next decade and he set up a new Advanced Research Projects Agency at the Department of Energy (ARPA-E). It was modeled on the Pentagon’s DARPA (Defense Advanced Research Projects Agency), which has spawned thousands of important new technologies with commercial as well as defense applications. Obama put $400 million in his 2009 stimulus package to launch ARPA-E and to fund more than thirty of the most daring new energy projects. But as we saw from the bankruptcy of the solar energy firm Solyndra after it got more than $500 million in government loan guarantees, the government has to be much smarter in picking the companies it funds and much tougher in overseeing their performance.

**Step #3: Generate a Manufacturing Renaissance**

Step #3 is to generate a manufacturing renaissance in America—perhaps the boldest step of all, and one that will require not only a series of public-private partnerships, but a reset in New Economy thinking.

To those on Wall Street, in Washington, or within academia who say that the United States does not need an industrial base, General Electric’s CEO Jeffrey Immelt and Intel’s Andy Grove retort that this is dangerous nonsense. “Many bought into the idea that America could go from a technology-based, export-oriented powerhouse to a services-led, consumption-based economy—and somehow still expect to prosper,” Immelt told the Detroit Economic Club in 2009. “That idea was flat wrong.”

Richard McCormack, editor of *Manufacturing & Technology News*, points to the slow, jobless U.S. recovery as evidence of the fallacy in that thinking. “Without an industrial base, an increase in consumer spending, which pulled the country out of past recessions, will no: put Americans back to work,” McCormack argues. “Without an industrial base, the nation’s trade deficit will continue to grow. . . . Without an industrial base, the United States will be increasingly dependent on foreign manufacturers even for its key military technology.”

Immelt, too, insists that technology-based manufacturing must be central to reviving the U.S. economy. His goal is to see manufacturing employment double, from 9 to 20 percent of the nation’s workforce—a target endorsed by the Horizon Project, a task force of former CEOs led by Leo Hindery, Jr., who used to run AT&T Broadband. “You cannot survive as a nation of such size and complexity with such a small manufacturing workforce as we have,” Hindery asserts. “If you have only 9 percent making things, the only way you can grow is to have credit bubbles.”

In the decade from 2001 to 2011, U.S. employment in manufacturing fell from 17.2 million to 11.7 million, and more than fifty-nine thousand factories were shut down. The damage was even wider because of the ripple effect. Each job lost in manufacturing cut 2.5 other jobs in the rest of the economy.

“Close a manufacturing plant, and a supply chain of producers disappears with it,” says Richard McCormack. “Dozens of companies get hurt: those supplying computer-aided design and business software; automation and robotics equipment, packaging, office equipment and supplies; telecommunications services; energy and water utilities; research and development, marketing and sales support. . . . The burden spreads to local restaurants, cultural establishments, shopping outlets, and then to the tax base that supports police, firemen, schoolteachers, and libraries.”

Reversing the multiplier effect—to make it work for economic expansion—is essential to America’s economic growth, but it is a tough challenge. Rebuilding our industrial base, Andy Grove points out, means being sharp enough to convert American innovations into American-based production for U.S. jobs, and that requires new government initiatives and public-private partnerships.

Take clean energy. Before the recession, the green energy sector was growing faster than the economy in general, and many forecast great job potential. The consulting firm Booz Allen Hamilton
predicted a jump from 2.4 million jobs in 2008 to 7.9 million jobs in 2013 in construction of green energy projects. More modest job growth in producing clean energy devices was expected—from a few hundred thousand to 1.7 million jobs. But the test is whether the United States can move fast enough to ensure that technologies invented in the United States are produced here and not in Asia.

To do that, the Alliance for American Manufacturing wants help from Washington—federal loan guarantees to help finance new energy infrastructure projects, tax credits for clean energy manufacturing, and tax changes that permit up-front expensing on capital investment in plant and equipment. More broadly, the alliance wants the government to fund a new investment facility to initiate and promote financing for new U.S. energy plants and other domestic manufacturing, and to do it before fragile American start-up firms are driven out of business by government-subsidized competitors in China, Korea, Singapore, and Hong Kong.

Buy American

One other major change in government policy—and in the actions of American consumers—could bolster U.S. manufacturing, and that is to Buy American. Many in business urge that state and federal governments tighten the “Buy American” requirements for government contracts, consistent with U.S. trade agreements.

In two recent high-profile cases, the state of California hired U.S. contractors to help rebuild the San Francisco–Oakland Bay Bridge, but the steel was imported from China. And in Washington, the monument to Martin Luther King, Jr., was designed by a Chinese architect, built by workmen from China, and constructed from marble that came thousands of miles from China.

To prevent such episodes in the future, job-first advocates say that both the federal and state contracts should establish tighter “Buy American” standards that require at least 75 percent domestic content in products and services.

Step #4: Make the U.S. Tax Code Fairer

Step #4 is to rebalance the U.S. income tax code to reduce its heavy tilt in favor of the super-rich. As nonpartisan economists have reported, the large Reagan tax cuts of the 1980s and the even larger George W. Bush tax cuts in 2001 to 2003 contributed greatly to the vast economic inequality in America today by generating more than $1 trillion in tax savings for America’s superclass every decade, with only modest benefits to the middle class.

Large majorities of the public favor taxing the super-rich more by letting the 2001 Bush tax cuts for the wealthy expire. An alternative idea is to let the Bush tax cuts expire for all Americans and then pass a new tax reform to lower tax rates, especially for 90 percent of American families earning less than $138,925 a year—and to simplify the tax code by eliminating loopholes and tax breaks that benefit mainly the wealthy.

Simplifying the tax code will make it easier to enforce. So many exotic tax shelters have been invented by ingenious tax lawyers and accountants to reduce the taxes of the super-rich that former IRS commissioner Charles Rossotti, a Republican businessman, estimated the tax loss to illegitimate tax evasion at $250 billion to $350 billion a year. As a result, Rossotti told me, honest taxpayers have to pay 15 percent more in their taxes.

“Stop Coddling the Super-Rich,” declares Warren Buffett, the famous billionaire investor from Omaha. “I know well many of the mega-rich and, by and large, they are very decent people. They love America and appreciate the opportunity this country has given them. . . . Most wouldn’t mind being told to pay more in taxes as well, particularly when so many of their fellow citizens are truly suffering.”

As Buffett has frequently pointed out, the super-rich make most of their money from the stock market and other investments, which are taxed at the 15 percent capital gains rate, much lower than the
tax rate on most middle-class salaries. As we saw earlier, Buffett paid a rate of 17.4 percent on his multimillion-dollar income in 2010, and that was the lowest tax rate in his office. Buffett advocates not only repealing the Bush tax cuts for the super-rich, but imposing a supertax on income over $1 million a year and a super-super rate on income over $10 million a year. Others propose a special tax on corporate stock options to CEOs and other top executives.

Another important move would be to close the exemption in the payroll tax now enjoyed by the rich. Ordinary employees pay a 7.65 percent payroll tax to fund Social Security and Medicare, but the income from investment gains of CEOs and super-rich investors is exempted from the payroll tax. In fact, multimillionaires pay a much lower payroll tax rate on their salaries and bonuses—as low as 1 percent—because all their income over $106,800, even their salaries and bonuses, is also exempt from the payroll tax. Removing that $106,800 tax cap would not only make everyone pay the same rate, it would go a long way toward solving the funding shortfall for Social Security and Medicare.

But the simplest, broadest tax reform to achieve a more level economic playing field would be to end the special low 15 percent capital gains tax rate and to tax investment gains at the same rate as wages and salaries (35 percent). Exceptions could be made for assets such as a house, a farm, a small business, or even a stock investment owned for a truly long term, say, for twenty years or more—to compensate for long-term inflation.

A majority of Americans favor raising capital gains taxes to 35 percent or higher, according to a New York Times poll taken in January 2012, when the political controversy broke out over Republican presidential candidate Mitt Romney’s 13.9 percent tax rate in 2010 on his $27 million income. Romney is fairly typical of the super-rich since virtually all of his income came as capital gains, which are by far the main source of income for the richest Americans. Those gains are heavily concentrated at the top. The tiny sliver at the peak of our economy—the top 0.1 percent of all income earners—captures almost half of all the capital gains in America.

All these tax reforms taken together—on capital gains, on payroll taxes, on closing loopholes, and on a special tax on executive stock options—would make the U.S. tax code much fairer, plus it could cut the national debt by $1 trillion over a decade.

Step #5: Fix the Corporate Tax Code to Promote Job Creation at Home

Step #5 is to fix the corporate tax code by lowering the rate and closing loopholes, because that would make the United States more globally competitive by enacting reforms that would discourage U.S. firms from offshoring jobs and reward those that hire at home.

American business leaders complain that they are hurt competitively by the U.S. corporate tax rate, and it is true that the U.S. corporate tax rate is one of the highest in the world. But in practice, most U.S. multinationals pay far less than the official 35 percent rate. When Citizens for Tax Justice examined the records of 280 major firms, it found that from 2008 to 2010, their true federal tax rate averaged 18.5 percent. What's more, the rate varied widely. Some companies paid the full 35 percent rate or close to it. Others cashed in heavily on loopholes and tax breaks that corporate lobbyists and pro-business members of Congress have written into the tax code—loopholes that were worth $1.2 trillion in reduced business taxes over a decade, according to the Treasury Department.

The multinationals that have been most successful in avoiding U.S. federal taxes include Boeing, DuPont, ExxonMobil, General Electric, IBM, Merck, United Technologies, and Wells Fargo, according to Citizens for Tax Justice, because the way they do business qualifies them for large tax credits. General Electric, for example, made nearly $10.5 billion in profits from 2008 through 2010, and instead of paying taxes, GE got a federal tax rebate of $4.7 billion by using loopholes and claiming tax credits. Companies that pay roughly 35 percent in taxes include retailers such as CVS Caremark, Home Depot, Target, and Wal-Mart; domestic-oriented insurance
companies such as Aetna and Humana; trucking companies; and
electric utilities, food processors, restaurants, and hotels—mostly
firms that do the bulk of their business inside the United States.

In terms of the tax code’s impact on jobs in America, what counts
most is that U.S. multinationals that have large overseas operations
often pay very low U.S. taxes or none at all. Many of them are
high-tech firms that qualify for tax credits for spending on research
and development or on new plants and equipment, but often their
biggest loophole is paying no taxes at all on their overseas profits—
unless and until they transfer their foreign earnings back to the
United States.

Apple: Shifting Profits to Avoid Taxes

High-tech companies such as Apple have big moneymaking prod-
ucts like iPads and iPhones made overseas, often in China. They can
allocate their profits on lucrative patents on iPads and iPhones to
their overseas operations or they can sell software applications from
low-tax countries overseas, shifting around tens of billions in income
from country to country with legal but cleverly devised bookkeeping
to avoid taxes in the United States and in other countries, too. Earlier
this year, The New York Times reported that Apple had pioneered
an accounting technique known as the “Double Irish with a Dutch
Sandwich,” which cut Apple’s taxes drastically by routing profits
through Irish subsidiaries to the Netherlands and then to the Carib-
bean. Today, hundreds of other U.S. corporations have copied tactics
invented by Apple, which, in 2011, paid only $3.3 billion in taxes on
$34.2 billion in profits.

Under current tax law, U.S. multinationals are allowed to write
off all their overseas costs immediately, even though they don’t pay
tax on those overseas profits until the money is repatriated. One big
loophole, created inadvertently by the U.S. Treasury and worth bil-
lions in tax reductions for multinationals, allows them to “Check the
Box” on IRS form 8832 to identify their subsidiaries as doing busi-
ness overseas, not subject to U.S. taxes. This is an automatic process,
rarely given close IRS scrutiny. On paper, U.S. companies can work
accounting rules to their advantage by shifting profits realized in
America (for products sold in the United States) to the financial
books of overseas subsidiaries (where the products were made).

In this way, U.S. multinationals periodically accumulate $1 tril-
lion or more in foreign earnings over several years, and then, as a
group, they lobby Congress for “a tax holiday”—a very low tax rate
on foreign profits repatriated to the United States. In 2005, the Bush
administration pushed through a low 5.25 percent tax rate on repa-
triated profits and gave 843 of America’s largest corporations a $265
billion windfall gain.

All sides agree on the need to rewrite the corporate tax code.
Pro-business conservatives want to lower the maximum corporate
tax rate from 35 to 25 percent. In terms of job creation in the United
States, that would leave more capital in the hands of companies that
operate inside America, enabling them to expand and hire. To bal-
ance such a tax reduction, pro-jobs progressives want to close the
$1.2 trillion in corporate tax loopholes—above all, the tax exemp-
tion on overseas profits. Economists estimate that if overseas corpo-
rate profits were fully taxed, it would generate $100 billion a year in
new corporate tax revenues—$1 trillion over a decade. What’s more,
they argue, taxing corporate profits at the full rate would curb ques-
tionable corporate accounting stratagems used to avoid U.S. taxes. It
might even persuade U.S. multinationals to keep more production at
home and bring jobs back from China and India.

Policy makers within both parties agree in principle on giving
businesses tax credits for research, innovation, and new facilities, to
stimulate more job creation at home. But jobs advocates such as Leo
Hindery Jr., want tax reform to require proof from employers that
their tax credits are actually being used to expand their U.S.-based
workforce. They also want to tie tax breaks to job creation at home
to apply to companies repatriating profits from overseas. When U.S.
multinationals were given a special 5.25 percent tax rate on repa-
trated profits in 2005, they said the money would create jobs, but
economists tracked those funds and found out that 92 percent of that money went to investors and corporate executives through dividends and stock buybacks and only 8 percent went for job creation. This time, jobs advocates want ironclad provisions to make sure the multinationals actually create more jobs in the United States.

Step #6: Push China to Live up to Fair Trade to Generate Four Million Jobs in the United States

Step #6 is strong action by the United States and other countries to combat China’s unfair trade practices and to rebalance global trade. Economists estimate it would generate four million jobs in America and significantly cut the U.S. trade and budget deficits if world currencies were revalued and if China was required to live up to the fair trade rules of the World Trade Organization.

The American economy and American workers are being hurt in three major ways by Chinese trade practices, experts say. First, they contend, China manipulates the value of its currency by fixing a low rate of exchange between the Chinese yuan and the U.S. dollar. A low exchange rate boosts Chinese exports by making them very cheap, and it cuts down U.S. exports to China by making them very expensive. Economists say the yuan would be priced 25 to 50 percent higher if it were allowed to float freely, letting trade flows and the global market determine the value of the yuan relative to the U.S. dollar. It is not just the Chinese yuan that poses a problem for the United States and Western European countries. Other Asian currencies in Hong Kong, Singapore, Taiwan, and Malaysia are pegged to the Chinese yuan, and their low currency values also hurt the U.S. trade balance with Asia.

Second, American businesses accuse the Chinese of widespread intellectual piracy—stealing copyrighted intellectual property, patents, and inventions and illegally copying foreign-made products, from Microsoft software to General Motors cars. A major national intelligence report to Congress on economic theft and espionage stated bluntly in late 2011 that “Chinese actors are the world’s most active and persistent perpetrators of economic espionage” and went on to cite several cases where American companies had lost patented material through cyberespionage.

Finally, Americans accuse the Chinese government of regularly violating rules of the World Trade Organization by dumping products on the world market at below the cost of production and giving illegal subsidies, land grants, and other cost-saving advantages to both Chinese and foreign firms. In fact, American CEOs say they save more on their investments in China through Chinese subsidies and tax breaks than from cheap labor.

Correcting those problems would have a major impact on the U.S. job market. The United States would gain 2.25 million jobs if China let its currency (and others linked to it) rise 25 percent, according to Robert Scott, a China trade specialist at the Economic Policy Institute. If this happened, Scott says, the U.S. unemployment rate would fall by 1 percent and the government’s budget deficit would be cut by at least $621 billion and perhaps by as much as $857 billion over a decade.

The United States would gain another 2.1 million full-time jobs if the Chinese stopped violating international copyright laws and intellectual property protection, according to the U.S. International Trade Commission.

Congress is ready to take a tougher line toward China. “China’s currency manipulation is like a boot on the throat of our economic recovery,” asserted New York Democratic senator Charles Schumer. “There is no bigger step we can take to promote U.S. job creation, particularly in the manufacturing sector, than to confront China’s currency manipulation.” Republicans such as Senator Lindsey Graham of South Carolina have shown a willingness to co-sponsor legislation with Democrats to impose stiff tariffs on Chinese goods unless China raises its currency value. The last time Congress threatened action, China allowed its currency value to rise a fraction but pressures have been building again for action by Congress.

Confronting China is not easy. Foreign policy experts urge collec-
tive action rather than unilateral U.S. moves. Western European and Latin American countries such as Brazil and Mexico are also hurt by China’s cheap currency and restrictive trade policies. International economists suggest that the best way to move China and other Asian countries on the currency issue is through global negotiations on rebalancing world trade. On China’s unfair trade policies, economists point to the success of the case brought by several Western nations that accused China of violating free trade rules through export controls on certain industrial minerals that are essential components for producing sophisticated electronics. The World Trade Organization ruled against China in early 2012 and ordered Beijing to end those policies, a ruling that offers precedent for future cases.

In the meantime, it is essential for Congress to fund the retraining of Americans thrown out of work when trade with China and other low-cost countries wipes out their jobs. Under the Trade Adjustment Assistance program, which started in the 1960s, the government spent close to $1 billion in 2008 to give aid to plants shut down by import competition and to provide career retraining for displaced American workers. But in 2011, Tea Party budget deficit hawks blocked all funding for this retraining program. House Republican leaders finally relented after the Obama administration refused to send Congress Washington’s new trade agreements with South Korea, Panama, and Colombia until the worker benefits were guaranteed. Corporate America wanted the trade agreements, so Republican leaders agreed to restore modest funds for worker retraining. Now this vital worker safety net needs to be expanded.

**Step #7: Save on War and Weapons**

Step #7 is to cut spending on wars overseas and to reduce the Pentagon budget by $1 trillion over the next decade—savings that would generate funds for a domestic Marshall Plan and underwrite a middle-class agenda.

The Obama administration began in 2012 by announcing $450 billion in projected defense cuts, plans for a leaner army and marines, and moves to bring home troops from Europe and reorient U.S. defense strategy. Another $500 billion in cuts would be imposed in January 2013 under the 2011 congressional debt reduction agreement—unless Congress comes up with an alternative.

Military advocates from the Joint Chiefs of Staff and Defense Secretary Leon Panetta to defense hawks in Congress oppose a $1 trillion overall cutback, protesting that it would endanger the nation. But former Pentagon officials such as Assistant Defense Secretary Lawrence Korb and other experienced defense experts disagree. They assert that $1 trillion can be cut from projected defense spending over ten years without jeopardizing national security. Former Pentagon officials point out that defense spending now runs $200 billion a year higher than at the peak of the Cold War, adjusted for inflation, and the United States faces no comparable strategic nuclear threat today. Moreover, cutting $1 trillion in military spending over ten years, says longtime congressional defense analyst Winslow Wheeler, would still leave defense spending at the very high 2007 level of $470 billion a year. That level would still enable the Pentagon to spend more than the defense budgets of the next largest-spending seventeen nations combined.

Defense spending cuts are long overdue. This is not just because the United States is pulling back from the wars in Iraq and Afghanistan, wars that will ultimately cost the nation more than $3.5 trillion in deficit spending. It is also because the basic Pentagon budget has been given unprecedented increases for thirteen years in a row.

A cutback of $1 trillion over the next decade would fit past precedents. After the Korean War, President Dwight Eisenhower reduced defense spending by 27 percent. After the Vietnam War, President Richard Nixon reduced Pentagon spending by 29 percent. As the Cold War ended, President Reagan scaled back military spending, too, and so did his successors George Herbert Walker Bush and Bill Clinton. But then it shot back up again after 2001, under President George W. Bush.

What is more, Pentagon critics contend that the U.S. military
establishment has become grossly inefficient and wasteful in buying new weapons and needs to be more strictly controlled. Even such defense advocates as Senator John McCain and Vice Admiral Norb Ryan, Jr., president of the Military Officers Association, have chastised the Pentagon for weapons programs that keep escalating in cost far beyond original estimates and that are so out of control that the Defense Department cannot pass an outside audit.

In November 2011, Admiral Ryan decried the “gross mismanagement and cost overruns in expensive weapons programs, few of which have any relevance to the wars our troops are fighting today.” In a Senate floor speech, McCain issued a savage critique of one weapons system after another, pointing at “spectacular, shameful failure” and accusing the Pentagon of “a shocking lack of any accountability” for cost overruns or matching new weapons to actual combat needs.

It was Dwight Eisenhower, the Republican president who had commanded Allied forces in Europe against Nazi Germany during World War II, who warned against the danger of overspending on the military and, in the process, sapping the nation’s economic strength—America’s primary source of national security.

Better than anyone, this West Point–trained five-star general understood the trade-offs. “Every gun that is made, every warship launched, every rocket fired signifies, in the final sense, a theft from those who hunger and are not fed, those who are cold and are not clothed,” Ike declared. “This world in arms is not spending money alone. It is spending the sweat of its laborers, the genius of its scientists, the hopes of its children.”

In 2008, candidate Barack Obama opposed the war in Iraq and promised a peace dividend: “Instead of fighting this war, we could be fighting to rebuild our roads and bridges. I’ve proposed a fund that . . . would generate nearly two million new jobs. . . .”

Now, four years later, the time has come to cash in that peace dividend. With the Afghan war costing more than $100 billion a year, a faster draw-down of U.S. forces could free tens of billions for programs to revive our domestic economy. Untold billions more could be saved by bringing home some of our eighty thousand troops still stationed in Western Europe nearly twenty-five years after the end of the Cold War. Billions more could be saved by eliminating wasteful and irrelevant weapons—and still leave America with the largest, most modern military force in the world.

There is bipartisan support for reducing military spending. In 2010, the bipartisan deficit commission headed by former Republican senator Alan Simpson and former Clinton White House chief of staff Erskine Bowles proposed $750 billion in defense cuts over the next decade. Sentiment for deeper cuts has grown since that report. In today’s sharply divided Congress, cutting defense is one issue on which Tea Party Republicans and liberal Democrats agree.

Step #8: Fix Housing and Protect the Safety Net

Step #8 is to fix the housing market by arranging massive refinancing of millions of homes now “under water” to help get the economy moving and to strengthen the nation’s safety net programs, especially Social Security and Medicare.

The housing market today is both symptom and symbol of the nation’s economic quagmire and its gross inequalities. Wall Street’s megabanks, which fueled the housing bubble and bust, have been bailed out with more than $700 billion of taxpayer money and are back to multibillion-dollar profits, while six million average families have been foreclosed out of their homes and twenty-two million more families are trapped in homes that are “under water”—worth less than their mortgages. Not only have those families been hurt, but the dead housing market has put a damper on a strong economic recovery.

For those twenty-two million homeowners—mostly creditworthy borrowers who are paying their mortgages regularly—it’s a catch-22. Most can’t afford to sell their homes and take a loss. Many would like to benefit from today’s low interest rates (around 4 percent) and shed their old 7 to 10 percent bubble-era rates. That would give them more cash to spend and to fuel the economics of the virtuous circle.
and lift the economy. But they are trapped. Banks won’t approve
loans for more than the value of the house, and government-backed
enterprises such as Fannie Mae and Freddie Mac have balked at writ-
ing down loans they have guaranteed in the past, because on their
books they would lose some money.

One modest improvement was the agreement in February 2012
by the main Wall Street banks, under pressure from state attorneys
general and the Obama administration, to commit $26 billion to
reduce the principal or interest on the mortgages of a million home-
owners with loans that exceed the market value of their homes. The
banks agreed to spend $1.5 billion on small ($1,500 to $2,000) pay-
ments to about 75,000 people who lost their homes in wrongful
foreclosures. But the deal was only a partial step forward. It did not
cover mortgages insured by Fannie Mae and Freddie Mac (roughly
half of all mortgages), it gave the banks three years to take these
actions, and it fell far short of fully compensating people who were
foreclosed improperly. While hailing the agreement as a step for-
ward, President Obama commented: “No compensation, no amount
of money, no measure of justice is enough to make it right for a fam-
ily who’s had their piece of the American dream wrongly taken from
them.”

Waiting for the market to correct itself is no solution. Establish-
ment bankers such as William C. Dudley, president of the Federal
Reserve Bank of New York, assert that “the infrastructure of the
residential mortgage market is wholly inadequate to deal” with the
massive debt overhang and with getting real upward movement in
home sales. Unless the government takes action, Dudley said, the
housing market will “destroy much more value in housing than is
necessary.”

Smart economists have suggested multiple ways to break the
housing logjam. Glenn Hubbard, former chief economic adviser to
President George W. Bush, has urged Fannie Mae and Freddie Mac
to reduce loan balances on some of the homes now “under water” and
to rewrite their rules so that up to ten million homeowners can quali-
ify for refinancing their mortgages at lower rates. Economists Nouri-
el Roubini of New York University, Robert Hockett of Cornell
University, and Daniel Alpert of Westwood Capital have proposed
that the federal government buy up near worthless second mortgages
and home equity loans whose holders are blocking first-mortgage
lenders from refinancing their loans. William Dudley has proposed
easing red tape and long delays both at banks and at government
agencies to grant new credit to homeowners and temporary bridge
loans for homeowners thrown out of work. To reduce the massive
backlog of foreclosed homes that are still empty, Dudley has sug-
gested that the banks be pushed by regulators to convert many of
these homes into rentals. Other economists advocate having the Fed-
eral Housing Administration offer loan guarantees to banks to in-
duce them to refinance millions of home loans at lower interest rates,
a move adopted in early 2012 by the Obama administration. Finally,
bankruptcy judges should be given the legal power to alter the terms
of mortgages, just as judges now help troubled companies rewrite
their contracts with labor unions, creditors, and suppliers.

Social Security and Medicare

Equally important are steps to protect and strengthen Social Security
and Medicare, something overwhelmingly supported by Republi-
can, Democratic, and independent voters. Privatizing them or alter-
ing their basic structures, as some in Congress propose, would spell
financial disaster for millions of average Americans, and people know
that. Whenever politicians have moved to privatize or radically alter
these safety net programs, as Speaker Newt Gingrich did in 1995, as
President Bush did in 2005, and as the Republican-led House did in
2011, voters have objected vehemently.

Conservatives are right that some adjustments and cost controls
are needed to prevent health care inflation and our longer life span
from undermining the financial viability of Social Security and
Medicare. One suggestion is to readjust the formula for the annual
cost-of-living increases in Social Security payments so as not to exag-
gerate inflation. The 2010 health care law included measures to slow Medicare cost growth, partly by curbing overpayments to private health insurance plans that cost more than Medicare and by rewarding health providers for quality of care rather than volume.

But the easiest way to put Social Security and Medicare on more solid financial footing is to remove the income cap on the payroll tax. Economists have estimated that taxing now exempt incomes over $106,800 would entirely eliminate the anticipated Social Security shortfall over the next seventy-five years. Added revenue could be raised by increasing Medicare premiums for the top 10 percent of income earners (income over $138,925) or by applying a means test for Medicare's low-cost health coverage.

Without these safety net programs, retirement security for average Americans is in serious peril. As we have already seen, roughly 50 percent of U.S. workers already face long-term poverty in their senior years. To prevent that, we may need to expand retirement protection with new laws requiring all companies with one hundred or more employees to provide some retirement program and to contribute a minimum of 4 percent of each employee's salary. Where 401(k) plans are offered, people need help—both a guaranteed employer contribution and the option of joining a pool of professionally managed funds with low fees.

Finally, as long as we claim to be a "land of opportunity," the United States must keep open the economic ladder upward for the sixty million in America's "aspiring middle class"—the hardworking poor. They depend on such safety net programs as college student loans, Medicaid, food stamps, child care support, housing assistance, and the earned income tax credit. Without those programs, the chances for rising into the middle class would almost disappear. Certainly poverty would be far more severe. Opinion polls show that majorities of Americans favor such programs, and the country can afford them. Over the next thirty years, our economy is projected to grow by 60 percent. That's another $8 trillion to $9 trillion. Steps #4, #5, and #7 suggest ways to generate funds for these programs through tax reform, defense cutbacks, and long-term savings on entitlements.

The Role of Politics

Thirty or forty years ago, in the era of middle-class power, a broad political consensus supported the kind of middle-class agenda outlined in this chapter. But in today's harsh partisan climate with the Senate often immobilized by filibuster tactics, the opposition will be formidable and Washington gridlock will be hard to overcome.

An authentic populist agenda won't be achieved without altering the power equation in Washington, so the political challenge (steps #9 and #10) is to revive middle-class power and to reduce polarized gridlock in our government by returning more power to the political center, the terrain inhabited by moderates and independents.
CHAPTER 22

POLITICS: A GRASSROOTS RESPONSE

REVIVING THE MODERATE CENTER AND MIDDLE-CLASS POWER

There is a disconnection between the people and their leaders. Citizens do not trust their government. And a variety of polls indicate that the distrust extends to corporations and the media. People do not feel that they have much control over their lives, and the sense of impotence grows like a great life-endangering tumor.

—JOHN W. GARDNER, cabinet secretary to President Lyndon Johnson

Either democracy must be renewed, with politics brought back to life, or wealth is likely to cement a new and less democratic regime—plutocracy by some other name.

—KEVIN PHILLIPS, Wealth and Democracy

CHANGING THE POWER EQUATION in Washington will take a mass movement at the grass roots to force the White House and Con-

gress to listen to average Americans and to put a middle-class agenda into law. It will also require reforms in our political system to increase the influence of political moderates and independent voters by reducing the built-in advantages now enjoyed by partisan extremists.

Voting is critical, of course, but experience teaches that voting is not enough. Even when voters elect a middle-class-friendly president and Congress, the hard grit of policy is chiseled out between elections, when voters have turned their backs on politics. That is when the influence game in Washington goes to work and undoes much of what voters thought they had voted for. The public may vent its frustration to pollsters, but as we have seen, Congress doesn’t listen to polls.

Congress—and presidents, too—listen to money. The business of members is getting reelected. As the costs of political campaigns have soared, the power of political money has grown to the point where we have a government responsive largely to the superclass, what economist Joseph Stiglitz called government “of the 1%, by the 1%, for the 1%.” Or as Senator John McCain, the conservative Republican presidential nominee in 2008, put it, the flow of money into lobbying and into election campaigns is “nothing less than an elaborate influence-peddling scheme in which both parties conspire to stay in office by selling the country to the highest bidder.”

Action to Counter the Influence of Money

To counteract the influence of money in the New Power Game, average Americans need to exercise their unique political leverage—direct personal engagement in politics. As John Gardner, longtime head of Common Cause, the nonpartisan public advocacy group, observed, “The sad, hard truth is that at this juncture the American people themselves are part of the problem.” Average Americans have become disenchanted and politically disengaged and, as a consequence, disenfranchised.
If we genuinely want government of the people, by the people, and for the people to fix the deep problems that plague our country, then millions of average Americans will have to become directly involved once again in citizen action—making their presence felt, taking to the streets, just as millions did in the 1960 and 1970s—to restore the vital link between Washington and the people.

There is ample tinder to fire a new populist rebellion. Public discontent over the gaping economic inequalities in America today is at a new high. Two-thirds of Americans now say there are “strong” conflicts between rich and poor—up roughly 20 percent from just two years ago. And this is not the view just of liberals. The perception of class conflict has risen sharply among white people, middle-income earners, political independents—even among a majority of Republicans (55 percent).

Confidence in government, especially in Congress, has plunged to historic lows. The popular sense of alienation is acute. Americans are fed up with the mean-spirited partisan warfare in a Congress that fails to do the people's business. In the summer of 2011, 70 percent told a CBS News poll that special interests have too much influence in Washington, and 85 percent said that ordinary people have too little influence. Voters in focus groups told Democratic pollster Stanley Greenberg: “There’s just such a control of government by the wealthy. . . . We don’t have a representative government anymore.”

Hard facts support this conclusion. Political scientists have documented in detail that without active grassroots pressure, Washington ignores large majorities of Americans. When Larry Bartels of Princeton University analyzed a host of congressional votes in the 1980s and 1990s, he found that senators were “vastly more responsive to affluent constituents” than to middle-class and poorer voters.

In 2005, Martin Gilens, another Princeton political scientist, made a detailed comparison of the policies that voters preferred with the policies Washington adopted and concluded that politicians had disregarded the views of middle-class voters. “Influence over actual policy outcomes,” wrote Gilens, “appears to be reserved almost exclusively for those at the top of the income distribution.”

Correcting the obvious inequalities in our democracy, as well as in our economy, will require political reforms—pushed from the bottom up.

**Step #9: Rebuild the Political Center**

Step #9 is to regenerate the centrist core of American politics both by rejecting extremist candidates in both parties and by opening up our political process in every state to give more influence to moderate and independent voters.

Historically, when there has been mass disenchantment with both major political parties, public anger has spawned third party movements. In the 1992 presidential election, Texas billionaire Ross Perot ran for president and won nearly 20 percent of the popular vote running as an independent.

At that time, 39 percent of the voters voiced dissatisfaction with how government was being run. Today, dissatisfaction with both parties in Washington is far higher—81 percent—and it has once again spurred an urge to reach beyond party lines and revive the political center. The 2012 political year has seen a wave of new political movements such as Americans Elect, Votocracy, Third Way, and No Labels. “There is just so much unrest out there that something is going to explode,” commented Democratic pollster Peter Hart.

Americans Elect is the most ambitious effort to promote a bipartisan middle ground in the presidential election. Capitalizing on the Internet, Republican strategist Kahlil Byrd and wealthy philanthropist Peter Ackerman have been promoting what Byrd calls a “widespread draft movement for presidential candidates,” with strong appeal to moderate and independent voters. Their idea is to bypass the Republican and Democratic nominating conventions with more direct democracy: Offer registered voters a forum to nominate their own presidential candidate via the Internet, with the proviso that whoever is chosen as presidential nominee must select a running mate from the opposite party. By early 2012, Americans Elect ac-
accomplished a major goal—getting the organization listed on the ballot in all fifty states.

The key, of course, is fielding a high-profile, vote-getting candidate and sustaining the movement. After the 2010 midterm elections, New York’s Republican mayor, Michael Bloomberg, seemed to cast himself as a centrist contender with his broadside blast at both major parties. “Despite what ideologues on the left believe, government cannot tax and spend its way back to prosperity, especially when that spending is driven by pork barrel politics,” Bloomberg declared. “... Despite what ideologues on the right believe, government should not stand aside and wait for the business cycle to run its natural course. That would be intolerable....” But having staked out the political middle, Bloomberg did not throw his hat in the ring. Even when third-party movements have run a potent vote-getter, such as Theodore Roosevelt and the Bull Moose Party in 1912 or Ross Perot in 1992, third parties have never offered a long-term solution to a sharp divide between the two major parties. Perhaps the most important role of Americans Elect in the future may be in state and Congressional races because it has gotten its own ballot line all across the country.

Another sign of rising protest against political extremism—at the state and congressional level—is the birth of No Labels, a group formed by longtime Democratic fund-raiser Nancy Jacobson and Republican Mark McKinnon, a media strategist for the Bush presidential campaigns in 2000 and 2004. No Labels won early blessings from Mayor Bloomberg, Florida’s former Republican governor Charlie Christ, and former Clinton administration official Jonathan Cowan. As Cowan puts it, the goal is to counteract “this kind of hyper-partisanship, my party, right or wrong, damn the consequences” and to pressure politicians in all 435 congressional districts into “setting aside their [party] labels” and moving toward compromises on the nation’s most pressing issues.

But Third Way, a think tank linked to No Labels, has a more focused and practical agenda. Its leaders see parties as the main cause of today’s “pathological polarization” of politics, and they want to break party control over primary elections, the gerrymandering of congressional districts, and party line election of congressional leadership. “Political parties have turned out to be a disaster,” argues former conservative Oklahoma Republican congressman Mickey Edwards. “The problem is the party system itself. And No Labels has on its mission statement to move toward open primaries and to take away party control over districting.”

Reform the Primary System

To revive the political center, Third Way argues, it’s essential to break the iron grip of parties by opening primaries to all voters and turning over the once-a-decade redrawing of congressional district lines to nonpartisan commissions. Such moves, reformers assert, will change the mix of voters and the dynamics of political campaigns. The idea is that open primaries would expand the electorate and therefore push candidates to cater more to moderates, who at 44 percent of the electorate in the presidential election of 2008 outnumbered both conservatives (34 percent) and liberals (22 percent). Third Way argues that open primaries should lead to the election of more moderates, making Congress less polarized and more prone to compromise.

Actual experience is limited, but it supports Third Way’s logic. Twice since the 1970s, California’s legislative redistricting was forced into the courts and carried out by a panel of retired federal judges instead of the legislature. Each time, the parties wound up with less of a lock on legislative districts. Elections swung from Republican to Democrat and vice versa. Voters had more sway.

So far, eleven states have so-called open primaries in the presidential nominating contest for both parties—that is, primaries where each party, running its own candidates, opens the balloting to all voters, whether they are registered in that party or are independents or in the opposite party. Eighteen states follow the same pattern in congressional elections—all voters can take part and vote for that party’s candidates.
So far, only Washington State has taken the next step—running one nonpartisan primary in congressional races, where candidates for both parties run together in a single primary race and voting is open to everyone. The top two vote getters then oppose each other in the general election. Washington State did that in 2010 and the impact was dramatic. The average vote in Washington State’s nine congressional districts tripled the turnout in 2008. That seemed to favor more moderate candidates because higher turnout typically reduces the pull of extremist candidates. California has now decided to follow Washington State in its congressional elections in 2012, and if it works well there, the idea may spread.

**Ways to Boost Voter Turnout**

Since American elections with low turnout usually go to the party that can fire up the political emotions of its most ardent partisan supporters, the most obvious way to increase the influence of moderate and independent voters would be to increase American voter turnout. In 2010, just 37 percent of eligible voters cast ballots. When so many Americans move their residences from year to year, local variations in voter registration pose obstacles to higher turnouts. In the 2008 president election, an estimated 2.2 million Americans were unable to cast ballots because of voter registration problems, according to the Pew Center on the States.

The Pew Center and other groups have urged states to adopt automated online voter registration and computerized voting, to make voting more accessible to people whose jobs are distant from their homes and voting sites. A few states such as Maine, Minnesota, and Wisconsin have instituted election-day voter registration and seen voter turnouts rise. Other countries have gotten better turnouts by putting election days on weekends or holidays to reduce conflicts with work schedules. In America, 25 percent of eligible voters have told pollsters that work and schedule conflicts impede their ability to vote.

To boost turnout, about thirty countries have compulsory voting and some actually penalize voters for failing to exercise their franchise. Australia achieves roughly 95 percent voter turnout by holding elections on Saturdays and fining citizens $A20 for not voting, with the fine escalating each time a voter misses an election. This system changes the dynamics of the campaign and elevates the caliber of debate in Australian elections, according to Norman Ornstein of the American Enterprise Institute.

“The way to gain votes does not come from working your base to fever pitch, it comes from persuading the persuadables, the centrists who are increasingly left out of the American political process,” Ornstein has written. “Appealing to the extremes is a formula for failure. If there were mandatory voting in America, there’s a good chance that the ensuing reduction in extremist discourse would lead to genuine legislative progress.”

**The Corruptive Influence of Money**

The toughest nut in U.S. politics today is how to reduce the influence of money in elections and on legislative policy making. As Arizona’s Republican senator John McCain once admitted, “All of us [politicians] have been corrupted by the process where big money and big influence—and you can include me in that list—where big money has bought access, which has bought influence.”

So far, legislative efforts at reform have repeatedly been undermined. Each time Congress has tried to impose limits on donations to political candidates, either the Supreme Court has voided those measures as unconstitutional limits on free speech or ingenious political operatives have found ways around the laws. In its January 2010 decision on the Citizens United case, the Supreme Court rejected two precedent decisions and ruled that government may not ban campaign spending by corporations on behalf of political candidates. The high court gave the green light to unlimited donations to independent groups, meaning technically independent of candidates...
and parties. That decision, reinforced by the loose rules for independent groups adopted by the Federal Election Commission, has effectively nullified the existing $2,500 limit on personal contributions to political candidates and opened the floodgates to hundreds of millions of campaign dollars flowing from super-rich donors and corporations to theoretically independent Super-PACs.

**The Sudden Surge of Super-Pacs**

Very quickly in the 2012 elections, Super-PACs emerged to play a commanding role, acting as surrogates for the candidates they favored. In Iowa’s Republican caucuses, Restore Our Future, the Super-PAC backing Mitt Romney, demolished Newt Gingrich with a multimillion-dollar television ad blitz. In South Carolina, the pro-Gingrich SuperPAC, Winning Our Future, crippled and defeated Romney. Other candidates, such as former Pennsylvania senator Rick Santorum and Governor Rick Perry of Texas followed suit. “The Super-PACs are plainly an avenue for candidates to evade the law that limits contributions,” Mann and Ornstein commented ruefully.

By late spring, Super-PACs had raised $160 million, bankrolled mainly by a small group of billionaire would-be kingmakers such as Las Vegas casino owner Sheldon Adelson and his wife, Miriam; Harold C. Simmons of Dallas and his chemical and metals conglomerate, Contraan Corporation; Houston home builder Robert J. Perry; PayPal co-founder Peter Thiel; Hollywood producer Jeffrey Katzenberg, CEO of Dreamworks; and hedge fund managers John A. Paulson and Paul Singer of New York. Just three super-donors—the Adelsons, Simmons/Contran, and Perry—contributed close to one fourth of all the Super-PAC cash.

In the 2012 general election campaign, Super-PACs have cast themselves as weapons of political mass destruction. Long before the party conventions actually nominated presidential candidates, runaway campaign fund-raising by Republicans, Democrats, and independent groups was on track to outspend the record-breaking $1.8 billion presidential election of 2008. Charles and David Koch, billionaire owners of Koch Industries, an energy conglomerate headquartered in Wichita, Kansas, pledged $60 million to defeat President Obama and recruited other wealthy conservative super-donors to help raise $100 million. American Crossroads and Crossroads GPS, the Super-PACs masterminded by Karl Rove, longtime political strategist for George W. Bush, set a goal of raising $300 million to blitz Obama. Initially, President Obama had rejected Super-PACs. But facing a Republican Super-PAC offensive, Obama relented and gave the go-ahead for Democratic funders to try to match Republicans, presaging a fierce crossfire of negative attack ads in the fall campaign.

More broadly, the explosive rise of Super-PACs and their super-donors has overwhelmed the campaign finance reform legislation enacted since 1974 and has thrown America once again into an era of essentially unregulated campaign funding.

Reformers like Senator McCain have warned that unregulated funding corrodes American democracy and corrupts the legitimacy of American elections, and so they have fought to impose limits on donations. Other reformers have advocated large-scale public financing to put political unknowns and challengers on a more equal footing with incumbents and to reduce the lopsided political influence of big corporations and wealthy donors. But decisions by the Supreme Court and the Federal Election Commission have punched large loopholes in those reforms. Fred Wertheimer of Democracy 21 and others have attacked the fictional independence of some Super-PACs from their favored candidates and now call for new laws to ban Super-PACs with any links to candidates, however indirect.

But politicians and their campaign strategists have been so ingenious and adept at getting around laws and regulations that it will almost surely require a constitutional amendment to ban campaign contributions from corporations, labor unions, and other institutions and specifically to empower Congress to impose limits on campaign donations from individuals. But that is a formidable process, sure to be fiercely opposed by entrenched interests. Only a groundswell of grassroots political activism, fueled by public revulsion at the power of Super-PACs and inflated campaign spending by America’s super-rich,
will be able to overcome resistance from politicians, and especially from congressional incumbents who have thrived on the present system.

**Step #10: Mobilize the Middle Class**

The only sure way to alter today’s patently unequal democracy is for average Americans to mobilize politically—to break out of their political inertia and to move forcefully back into the political arena.

Important as it is to open up party primaries, arrange for nonpartisan legislative redistricting, and provide a floor of public financing for elections, the fundamental need of American democracy is the practical exercise of democracy—a rebirth of citizen activism. That requires not only a populist rebellion against the political and economic inequalities of our divided nation, but a hopeful rebirth of American idealism, a revival of the belief that ordinary people can, in fact, make a difference and turn the tide.

At election time, American voters seem flattered and even seduced by the ritualistic declarations of presidential contenders that America’s best years lie ahead and America’s democracy is the greatest in the world. But it is clear from a multitude of opinion polls and reporting that once the inflated rhetoric of campaigns subsides, people don’t really believe that anymore. They doubt their own power.

“The loss of civic faith is an obstacle,” John Gardner remarked in the late 1990s. “One might imagine that the solution would be for government to make itself worthy of our faith. But the plain truth is that the government . . . will not become worthy of trust until citizens take positive action to hold them to account. Citizen involvement comes first.”

Politicians are afraid of mobilized voters. They open their doors when home-state residents flood the corridors of Capitol Hill—evidence that continuing political pressure from the middle class can push Washington to generate what nineteenth-century British philosopher Jeremy Bentham called “the greatest good for the greatest number.”

So the time has come for direct political action by millions of ordinary Americans to use their physical involvement as a countervailing power to Washington influence peddlers.

**You Think Government**

**Doesn’t Work? Take Another Look**

But what’s the point? people say. Government doesn’t work.

Well, take a closer look. Government may not work well for average Americans, but it has been working very well for Wall Street, for multinational corporations, and for the financial superclass. They get the government they want, and they pay handsomely to get it.

During 2009 and 2010, when Congress was writing laws on financial regulation, health care, and taxes, business interests spent $6 billion on lobbying. In “soft money” campaign donations, business outspent labor 97 to 1 in the 2010 elections, and it got a Congress eager to roll back regulations on banks, health insurers, and other businesses and refusing to close corporate tax loopholes or raise taxes on the rich. Over the years, the multinationals have won new trade deals, tax holidays on overseas earnings, and laws that let them import cheaper foreign labor to displace American workers. Some of America’s richest families bankroll anti-tax conservatives like the Tea Party, which has wielded huge influence in two short years, even though it represents only a small fraction of Middle America.

So government can work. You just have to make it work for you.

People are understandably skeptical. Many say they want smaller government, but that may be because they don’t realize how much they already depend on government, like the South Carolina man who in an anti-government tirade told his congressman to “keep your government hands off my Medicare”—not realizing that Medicare was a government program.

In a 2008 survey by Cornell University, people were asked if they had ever benefited from federal policies and government programs. In response, 57 percent said, “No, never.” But when they were questioned more closely, it turned out that 94 percent had actually ben-
focused demands can change the debate and direction of policy in Washington.

Jobs come first. They are the essential economic lever to lift the middle class back to shared prosperity and to jump-start the consumer engine to drive the American economy. The test of whether business leaders are committed to America's growth is whether they invest their $1 trillion or $2 trillion in cash reserves and their overseas profits in creating jobs in America and not primarily in stock options, higher dividends, and buying back their own company's stock.

Practical programs to promote and create jobs are the political litmus test of whether Congress and the White House are committed to a middle-class revival or just to a futile repetition of the failed litany of the lower taxes, less regulation, free market mantra that in the 2000s generated the worst economic performance for most Americans of any decade since World War II.

**Catch-22 for Twenty-Two Million Homeowners**

Fairness is the touchstone for money issues—a test of whether America can return to a more equitable sharing of the nation's economic gains.

As we have seen, the middle class won’t have enough spending power to regenerate “the virtuous circle” in the economy unless a much larger share of America's national income goes to average Americans. Fairness requires rebalancing how business profits are divided between shareholders and employees, and it calls for rebalancing government policies more in favor of average Americans.

Some quick symbolic steps such as closing corporate tax loopholes, raising taxes on the rich, and imposing new fees on Wall Street's stock transactions and executive stock options could help restore government's credibility with ordinary people.

But a more central long-term yardstick of fairness to the middle class is how the Congress and the White House handle housing, since homes are the heart of the American Dream and the corner-

**The Touchstone Issues—Jobs and Fairness**

It would help rekindle public faith in government if political leaders would demonstrate that Washington actually works for average Americans, that the White House and Congress are ready to help out Main Street the same way they bailed out Wall Street.

The test should focus on two touchstone issues—jobs and fairness. Both issues can mobilize the middle class. People have an existential understanding of jobs and fairness, either from their own lives or from the lives of their family, friends, and neighbors.

If enough average Americans mobilize around jobs and fairness and demand action from Congress and the White House, politicians will get the message and respond. As the Tea Party has demonstrated, a highly vocal activist minority with a clear agenda and
stone of middle-class wealth. As Harvard economist Kenneth Rogoff noted, "There is widespread agreement among economists that housing debt is at the heart of the slow recovery, and that finding a way to bring it down faster would accelerate the recovery."

The biggest debt now overhangs twenty-two million families stuck in homes that are "under water." Like the big Wall Street banks, which were bailed out not only with $700 billion in taxpayer funds, but with $7.7 trillion in loans from the Federal Reserve, these creditworthy homeowners desperately need help with rewriting and refinancing their mortgages, and smart economists have spelled out steps to speed massive refinancing—steps that would be a shot in the arm to the whole nation.

A dead housing market hurts everyone. It not only depresses home values, it cuts consumer demand. Even people whose homes are above water cut back their spending when housing prices fall. Economists tell us that the housing collapse from 2006 to 2009 has cost the U.S. economy an estimated $240 billion a year in lost consumer spending.

"Consumer spending is not only the key to economic recovery in the short term," economic historian James Livingston of Rutgers University has written. "It's also necessary for balanced growth in the long term. If our goal is to repair our damaged economy . . . that entails a redistribution of income away from profits toward wages, enabled by tax policy and enforced by government spending."

What's Needed: Armies of Volunteers

Getting help for homeowners and jobs for the roughly twenty-five million unemployed and underemployed Americans will require changing the political dynamics in Washington. The reflexive instinct of most Americans is to ask for a new Lincoln to pull the nation together again and restore a national sense of purpose. But great as he was, Lincoln could not have done it without armies of volunteers—without regiments from New York, Illinois, Ohio, and Pennsylvania, without average Americans prepared to put them-
from Haifa to Beersheba and along fashionable avenues in Tel Aviv to protest against the concentrated wealth of the “tycoons,” as Israel’s richest families are known. They called on the Israeli government to take action to “minimize social inequalities.”

Under pressure from the street, Prime Minister Benjamin Netanyahu and the Israeli cabinet set up an economic commission to study the popular demands, and then, when the commission delivered its findings, the government approved its call for increased taxes on companies and on capital gains and a surtax on the wealthy, as well as its proposals for easing financial burdens on the middle class. “The consumer will feel the government’s decision today in his pocket,” said Netanyahu.

If there can be protests and government action against a lopsided division of the economic spoils in Israel, why not in America?

If there can be an “Arab Spring” among peoples who have never known democracy, why not in the homeland of democracy?

Why not a springtime for American democracy? A jobs-first crusade? A movement to reclaim the American Dream?

We are at a defining moment for America. We cannot allow the slow, poisonous polarization and disintegration of our great democracy to continue. We must come together and take action to rejuvenate our nation and to restore fairness and hope in our way of life. We see the challenge. It is now time: We the People must take action.

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