Executive Summary

Tackling Economic Inequality, Boosting Opportunity: A Blueprint for Business

A Report by the Committee for Economic Development of The Conference Board
April 2016
This policy statement is a part of CED’s ongoing project on “sustainable capitalism.” In this project, we undertake research on a series of issues that are part of the controversy surrounding capitalism today, in the aftermath of the recent financial crisis. Many of these issues also echo the vigorous debate at the time of CED’s founding — almost 75 years ago, in 1942, and in the aftermath of the Great Depression — when many contemporary commentators also spoke of a “crisis of capitalism.”

We will complete and release this policy statement, and others, in the nature of working papers — to solicit and provoke comment and discussion. We will use that input to develop each policy statement into a chapter of our forthcoming book, Sustainable Capitalism, which will mark CED’s coming diamond anniversary year of 2017.

We believe that capitalism — perhaps more accurately described as the free-market system — historically has been an enormous success. It has delivered worldwide progress against poverty and has been the foundation of the growth of the greatest nation ever known to man. But capitalism cannot stand totally immutable in a world of rapidly advancing technology and changing social institutions. Capitalism must evolve if it is to continue to serve the needs of the world’s people and economies and if it is to remain “sustainable.”

And perhaps one of the key challenges to capitalism’s ability to sustain itself — one of the most powerful sources of the controversy surrounding capitalism today — has been the perception and the reality of the growth of inequality over recent decades, and especially since the financial crisis.

To some Americans, economic inequality has become a matter of intense concern. President Obama has called it “the defining challenge of our time.” It has been the subject of numerous books, articles, and symposia.

There has been an equally impassioned pushback to this concern — not so much on the recent growth of inequality as on its significance, potential ill effects, and possible remedies. And with the rising intensity of the debate, the noise has tended to overwhelm the information on a topic that was already highly complex. Different measures of economic well-being — income versus wealth, and numerous variations of each — have been confused and conflated. Weaknesses in the available data often have been ignored.

Inequality touches on so much of our nation’s economic policy that decisions in this space can have a profound impact on our collective well-being. So our nation needs a meeting of the minds, thoughtfully but urgently. We need to establish the facts, consider our options in an accurate and dispassionate way, and decide on a course of action.

True business statesmen are uniquely situated to begin such a national conversation. Government is paralyzed by partisanship, and most outside advocacy groups are guided by political orientation. CED has a history of almost three-quarters of a century of pursuing the public interest rather than trying to score partisan or ideological points. We call issues as we see them. We understand that all of society is in the same boat and that our nation can prosper best if we prosper together. We seek to communicate why business must be a key part of a resumption of growth of economic prosperity for all Americans, just as business has been a driver throughout the history of our nation’s rising prosperity, including the immediate post-World War II era that many remember and wish to re-create today.

The inequality debate thus far has been highly polarized and polarizing. Although we come from a perspective that emphasizes the historical achievements of free markets, we see merit on both sides of the debate. We believe that our
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society will advance when each side recognizes the wisdom in the other’s position and joins an open dialogue to find the common ground that holds the principles and concerns that we all share. We counsel patience as we hear each other out, in full. We believe that our discussion below is a sound first attempt at a synthesis of what each competing perspective on this issue has to offer — ideally, a presentation of what every responsible voice both already believes and can learn from others.

That was the motivation behind our investigation of economic inequality, and this policy statement shares our findings, which we summarize here.

A Note About The Color Coding

This summary, and the policy statement that follows, present a nonpartisan consensus among our members, who individually come from diverse partisan backgrounds. In producing these documents, our members sought to understand each other’s differing points of view and to find and recognize the value that each brought to the table. They agreed in this summary to try to communicate where they could agree on arguments and recommendations that came from each of the two main partisan perspectives, and where they found ways to combine those perspectives in honorable and productive compromise. Toward that end, some of the text of this summary is printed in color and formatted to convey the balance of the consensus among our members of different persuasions.

• Views and recommendations that might be seen as more characteristic of the conservative point of view are slightly offset to the right and are printed in RED.

• Views and recommendations that might be seen as more characteristic of the liberal point of view are slightly offset to the left and are printed in BLUE.

• Findings and recommendations that might be seen to meld those partisan perspectives are centered and are printed in PURPLE.
Our economy always has generated some measure of inequality — although no more than, and quite possibly less than, historical alternatives. That is not surprising. Individuals inevitably differ in their innate skills and their other endowments. And free enterprise encourages people to take risks to innovate and invest. Investments that are successful generate the jobs and incomes that the American people need and can earn substantial incomes for the innovators and investors. But investments can meet with less success — for their initiators, investors, and employees (who often invest through stock options and pension plans). The American people at large would not have it any other way; they want innovation and investment, and if they succeed they want to be rewarded. Thus, economic systems that are most conducive to economic growth because they allow market forces to reward success tend to have some measure of inequality. And on the other hand, trying to enforce equality of outcomes can be expected to reduce economic growth and incomes because it will deter investments that will not seem worth the risk and the effort without a reward for success. That is why many alternative economic systems, including socialism and communism, have failed: they have not produced growth and widespread prosperity, and as much as they have promised utopian equality, they have generated their own inequality and waste through economic manipulation and corruption as well.

There are many reasons to choose to do business in the United States, the world’s largest market. For Americans, patriotism is among them; for non-Americans, it is often our open free-enterprise system as well as our robust consumer market. But if innovators and investors conclude that too much of the return to their efforts will be denied to them in a search for equality of outcomes, they will not pursue their ideas, concluding that it is not worth the hard work and risk. Or, in today’s open global economy — and especially if the innovators are non-American — they will pursue their ideas elsewhere.

But over the past several decades in the United States, inequality (by any measure) has been increasing significantly. After the transformative events of World War II, our economy enjoyed more than two decades of extraordinary growth and a general narrowing of inequality. Since the early 1970s, however, growth has generally been slower, and inequality has generally grown. This has been true of all measures of economic well-being: market incomes, after-tax, after-transfer incomes, and wealth. And this finding is consistent across most developed countries in multiple databases constructed by multiple researchers, even though they disagree on many narrower details and on their policy conclusions. Although there are numerous sources of data and analysis, we see as particularly persuasive the findings of the Congressional Budget Office, which has focused on a consistent methodology using the same data sources since
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1979, under organizational leadership appointed by both political parties. Their findings show consistent increases in inequality using several alternative measures of income. Some analyses suggest that the current degree of inequality is at or near its level of 1930, which was the highest in modern times. This raises concerns about economic stability and popular reactions that might lead to hasty and counterproductive policy making.

The finding that there has been a consistent trend toward both income and wealth inequality over the last several decades provides definitive conclusions about neither causation nor what policy steps, if any, should be taken in response. Answering those questions requires deeper analysis.

Some, but not all, of the increasing inequality of the last four decades has resulted from spectacular returns to highly successful innovations and investments. We are not troubled by this phenomenon. The highly successful enterprises of recent years by definition provided substantial value to a large number of people; had they not, they would not have been so successful. Many of the individuals who profited so spectacularly from those innovations were line employees with stock options, not executive decision makers. Such rewards were examples of the opportunity made possible by free enterprise.

Thus, we see no ground to attempt to undo such success. At the most important level, every American wants access to the American dream, which is driven by innovation. Innovation provides us with new and better products and services at lower prices. It raises our standards of living and provides prosperity, even as it sometimes provides large returns that can expand measured inequality. We must take care that in pursuing other goals we do not pay a disproportionate price in terms of innovation, growth, and living standards.

Some, but not all, of the greater inequality that we observe has resulted from lagging real income growth for a large number of working Americans. We find that reduced income growth exceedingly troubling. CED’s mission has always included income growth broadly shared among the American people. This is the essence of the promise of the free-enterprise system that we have supported from our founding. Any erosion of that American dream is unacceptable and will reduce the quality of life for even the successful.

Some have alleged that the loss of income growth is a sign of a loss of ambition or will on the part of the American people. This is false. The enormous
drop in employment since 2007 was not caused by a synchronized collapse of interest in prosperity on the part of vast numbers of American workers. We owe our fellow citizens more respect than to suggest as much.

Some also have alleged that the spectacular returns enjoyed by some have come directly and causally at the expense of those who have suffered lower income growth. We find this belief to be unfounded. Many of the conspicuous innovations that have been richly rewarded have no possible connection to broad wage trends. They have come from the development of new products and services that have been built from the ground up, with newly employed labor and new resources.

Thus, again, we see no reason and much risk in seeking policies that would choke innovation, or risk its relocation overseas, in the cause of reducing inequality. In contrast, our economic system must be geared to increase broadly based income growth to reduce inequality. Increasing growth — really, increasing productivity and innovation — is a monumental task. It is the mystery behind all of economic progress. It is, in essence, seeing into the future. CED’s central mission here is to call business leaders and Americans of all perspectives to unite in the task of seeking prosperity and equality of opportunity to raise all, but not by repressing some.

**Our society’s objective should be equality of opportunity that reduces inequality, not forced equality of outcomes.** It follows from our reasoning above that the economy must lift the bottom, not compress the top. Equality achieved by curtailing opportunity or demonizing success is at best a temporary remedy for any pains of inequality. Forced equality does not raise, and has no prospect of raising, productivity and innovation. It does not raise the achievement of the labor force that it is intended to help. It is a remedy for inequality in only the most superficial, ephemeral sense. In contrast, expanding opportunity will end today’s waste of resources. Expanded opportunity will utilize people’s skills more fully and open up investment opportunities. That is why we must set our economy back on track.

We believe that equality of opportunity is the only ultimate remedy to inequality. Only through raising the capacity of the full US labor force can productivity and incomes be raised on a sustained basis, to the benefit of all of society. We have every confidence that as we approach the goal of equality of opportunity, the resulting rising prosperity will lessen inequality of outcomes, as the incomes of our population rise closer to their potential. As the old saying holds, a truly rising tide will lift all boats.
Although each alternative statistical measure of economic inequality has a valid purpose, we believe that our society’s success should be defined by the growth and distribution of market incomes. We do not believe that our society can target equality of outcomes, nor should it try to force equality of outcomes. But we do believe that from equality of opportunity will follow greater incomes, broadly shared, and with that a lessening of inequality. And in that respect we refer to market income, which we believe is the most meaningful standard.

Dollars of income from different sources are not the same. Dollars earned through labor or as returns on the individual’s own savings represent production, self-sufficiency, and security, in a sense not matched by public transfer payments. If opportunity yields productivity and incomes, individuals achieve greater equality in a more meaningful sense. It is their own stake in the ownership of the economic system. It is that meaning of equality to which our society should aspire, more than some numerical equality that is dependent upon a constancy of future public policy.

Our nation, at this time, does not have equality of opportunity, and past attempts to achieve it, however well-meaning and energetic, have fallen short. Some might take the mere establishment of a goal of equality of opportunity to be an absolution of any and all societal or economic reality. They would say that if one individual has overcome adversity to succeed in our free-market economy, then anyone can. We are free to go on our way.

The sad reality is that too many Americans reach the starting line of a career in the labor force with no realistic chance of success. If we want our nation to remain exceptional, to remain the world’s leader, then we must set opportunity as our primary objective.

In the interim, in the absence of equality of opportunity, we must take responsibility for policies to ease the current inequality of outcomes. What do we do as a society until we have equality of opportunity? Pursuing a long-term goal of equality of opportunity will not directly ease the dislocations caused by recent lagging incomes. The stated intent of current public policy is to assess the cost of government according to ability to pay, and to provide a safety net for those who fail in competition in the free market. However, policy is not fully successful in the pursuit of those objectives. As CED has noted elsewhere, our federal income tax is neither efficient with respect to its effect on the allocation of resources and the maximization of incentives for productive activity, nor fully equitable in terms of the assessment of liabilities. Nor are our cash and in-kind assistance programs on the outlay side of the budget fully effective in achieving
their objectives. Improvement of these policies must be a part of our national agenda as well. With efficient policies — policies that do not waste resources on their own inefficiencies or inequities — we can achieve more of all of our multiple, competing policy objectives.

**Businesses themselves can ease the hostility in the inequality debate.** In our experience, US firms seek to provide rewarding employment for their workers. Businesses see that as in their own and their shareholders' interests, as well as in the interests of their employees. Loyalty and a strong sense of shared purpose yield the best business results. In our work on “sustainable capitalism,” we begin with the perspective of a “multi-stakeholder model” of business — in which lasting value generation is recognized to follow from a cooperative relationship among the management and the board of the firm and their community, employees, customers, owners, and the environment. A mindset that is limited to near-term results at the expense of these stakeholders might lead to temporarily pleasing reported numbers, but not long-term sustainable performance.

However, businesses, like all other institutions, periodically need to reexamine their relationships with their many stakeholders. And in this day of system-wide economic challenges, that reassessment must encompass inequality and a lack of opportunity, to refresh the "social contract" and restore a broad consensus about the value of our free-enterprise system. For too long, it has been common for business leaders to “keep their heads down in the foxhole” and avoid debate on public issues. That might avoid controversy in the near term, but over time it has cost both trust in business and a full debate on vital public policy.

**In addition, business should advocate sound public policy to enhance and equalize opportunity.** True equality of opportunity for the entire American population and economy will require collective action. Business statesmen can foster a more civil debate and strengthen our economy by advocating sound and thoughtful public policy:

- **Expand access to quality preschool education and child care.** The best evidence indicates that early childhood education has the greatest, surest return among alternative investments in our future workforce. At-risk children, at the very least, need access to high-quality early childhood education if they are to enter the world of work with a solid opportunity for success. Some businesses conceivably can provide their workers' children with adequate day care and early education, but there is little doubt that eventually public and private sources must provide additional financial support for early education for the bulk of the at-risk population. Success requires quality-focused accreditation, qualified teachers,
performance measurement, and accountability for results. Much of the return to early education will come far in the future, but that only emphasizes the necessity of early action.

- **Enhance the K-12 performance with states’ and unions’ cooperation.** Business leaders should work nationally, at the state level, and in their home communities to implement standards for educational achievement that support college and career readiness. Local, hands-on business involvement could help to dispel the fears of supposed outside interference in the setting of standards for the benefit of future workers. CED has researched this issue extensively. Accountability for student success in the classroom is critical. Business should reexamine the potential for partnering with schools in offering job-specific training alongside general academics, and in communicating their skill needs to wide-access, low-cost educational institutions in their areas. Innovations along these lines would help students who enter the workforce out of high school, not only those who plan to move on to college.

- **Broaden postsecondary access and improve performance.** As CED has reported elsewhere, US postsecondary educational attainment is lagging behind our competitor nations around the world. Well-to-do US youth are attending college; our weakness lies among students and families of modest means — even those who are well prepared academically — many of whom have no experience of postsecondary attendance or success. Increasing enrollment and completion by highly qualified students from low-income families could be enormously productive in reducing inequality, and certainly in expanding opportunity. And much can be done. College costs are rising much faster than prices generally — even faster than the widely recognized cost of health care. Our nation must devote its energy and creativity to innovation in postsecondary education. That includes finding less-expensive alternatives to “seat time” while maintaining the verifiable value of a college degree. Business leaders should lend their time and expertise to the wide-access, low-cost undergraduate institutions, as well as to the more prominent, elite graduate and research institutions; it is the wide-access schools that must bear the brunt of extending education to the less affluent underserved segments of our population. At the same time, more scholarships for low-income households and incentives for high-prestige universities to prepare and admit low-income students could help. Businesses should specify and explain the skills that they need, so that postsecondary institutions can develop curricula that impart those skills. Government aid should be tied to defined student outcomes and preset cost-containment goals. And we should improve both secondary education and community college training for those students for whom a four-year degree is not the best choice.
And finally, business should develop and advocate public policies to compensate for the current inequality of opportunity. There are other policy imperatives whose primary effect would be to ease some of the ill effects of the current limited opportunity for many millions of Americans, although these ideas would also enhance incomes and economic growth in the long run:

- Reform the US health care system. The cost of providing quality health care to any family or individual does not vary with household income. However, the cost of health care is much higher as a percentage of income for lower-wage workers. Even after the Patient Protection and Affordable Care Act (ACA), however, our nation still reflexively conceives of health care as a financial obligation of the employer. For that reason, employers must think of the cost of health care as a part of the cost of hiring a low-wage worker. Over time, that crowds out cash wages, and may have contributed substantially to slow wage growth for many workers, and to a perception of growing inequality. CED has recommended substantial changes to US health care finance and delivery that would both reduce the impact of the inverse linkage between the cost of care and employee cash wages, and in the long term slow the rate of growth of health care costs while improving the quality of care. Health care system reform would therefore be one of the most important steps that the nation could take to reduce income inequality.

- Reform the US tax system. The US tax system should also be an important part of attaining equal opportunity, by encouraging growth and assuring that tax liabilities are distributed fairly. Instead, it falls far short. Polling suggests that the American people support a progressive income tax but that they are sensitive to the level of the highest tax rates imposed. This is broadly in keeping with John Rawls’ A Theory of Justice, in which he posits that people should choose public systems that they would want whether their life outcomes ultimately proved either favorable or unfavorable. Rawls’ philosophical expression was that the public should judge policy as if they saw their futures through a “veil of ignorance”; a more common expression would be that citizens should be objective in choosing policies that will apply to them however their lives evolve as well as to others in different circumstances. This would suggest a tax law that would provide the relief that people would want if their incomes turned out to be low, and higher but not excessive tax rates that they would be willing to pay if their incomes turned out to be high. This consensus of the American people offers sound guidance. Tax policy requires balance that is fair to everyone — that follows Rawls’ dictum such that people would accept it not knowing what their life outcomes will be, such that they would consider it fair whether their incomes were high or low. This will necessarily be a compromise between
the political extremes, but that is what democratic policy making for all of the people is about. An ironic ray of hope is that our nation’s tax system today is grossly inefficient. This is to say that it achieves less of all of our objectives — fairness, economic growth, simplicity, and revenue sufficiency — than we could expect. The shinier side of this coin is that an improved income tax can deliver far better outcomes in every respect. A reformed income tax would avoid preferential tax law provisions that can directly cause inequality by favoring politically influential groups. And it could much better encourage new and innovative investments by allowing profitability in the marketplace, rather than favors in the tax law, to allocate resources. It also could have a broader tax base, such that overall tax rates could be lower — not higher — than today, but with a fair distribution of the burden. The Tax Reform Act of 1986 is a good model of what could be accomplished, and how.

- **The Earned Income Tax Credit** (EITC) is in effect a federal government wage supplement for low-wage workers, increasing at a fixed percentage of wages from the first dollars earned and then later phasing out as earnings increase further. It explicitly supports working families (and at a lesser rate, single workers). It supplements modest wages, which makes work more attractive for those whose hourly reward is the least. It does not add to employer costs, as does the minimum wage, and thus does not deter hiring or fuel inflation. On the other hand, it is administratively challenging, and it can discourage work for some by increasing implicit tax rates over the income ranges where it is phased out. The EITC could be restructured to make it easier to administer effectively, especially if undertaken at the same time as fundamental tax reform.

- The **corporate income tax** is highly controversial and often misunderstood. Some believe that the amount of tax paid by corporations is an important and independent contributor to tax fairness. We would emphasize that the true determinant of fairness is the total amount of tax paid either directly by (in the individual income tax) or indirectly on behalf of (through the corporate income tax) **people**. One could imagine tax systems in which the total tax for particular taxpayers would be the same, but relatively more might be paid directly through the individual income tax, and relatively less might be paid indirectly through the corporate income tax — or vice versa. It is not clear that one alternative combination is inherently more or less “fair” than the other. However, one combination might prove to be far preferable in terms of its implications for economic growth and opportunity. We need a constructive public dialogue to reform our tax system to achieve all of our objectives, including fairness and economic growth and opportunity.
Many corporations argue that the convoluted US tax system (including the preferential provisions referenced above) and its relatively high statutory rates inhibit R&D and capital investment here. On the other hand, many critics argue that traditional US corporations should be “patriotic,” remain and invest in the United States, and pay higher taxes if that should result. We ask those critics to look at the bigger picture. The world economy is constantly changing. Many flagship US corporations of 50 years ago no longer exist, including some because they succumbed to international competition. And every day, new firms enter onto the world stage, often with no particular national identity — or at least much less so than was the case in the more insular economy of the years just after World War II. The United States is the largest market in the world, and as such, there is good reason for many firms all around the world to consider investing here to serve our consumers — even if their traditional identity is not American. However, just as traditionally US firms might lose competitive ground or even fail if faced with an uncompetitive US corporate tax system, so firms from other nations might pass up the opportunity to invest here for the same reason. American workers would lose jobs and opportunity under either contingency. We need a competitive corporate tax system to give American workers jobs and rising incomes.

Clearly, tax reform is a massive undertaking, and will be highly contentious, but along with systemic health care reform, it is one of the most valuable possible steps toward greater equality of opportunity and reduced economic inequality. Our nation will not provide opportunity and rising incomes unless we pursue a competitive tax system.

In sum, we see our goal of equality of opportunity not as an absolution, or even mere aspiration. It is rather an obligation and a commitment. Without true opportunity, all of our societal objectives — prosperity, productivity, and innovation — are out of reach. The ills of irremediable inequality and economic stagnation — cynicism and despair — remain. The society that is left is unsatisfying even to those who succeed. And success itself is in jeopardy, as the creative workforce atrophies and the markets for products and services slowly migrate elsewhere.

The debate over inequality should bring the nation together, not tear it apart. Our goal should be greater and equal opportunity, which we believe would raise every member of our society; we should not rest until we achieve that goal.
Notes


5 Anthony P. Carnevale and Jeff Strohl, “How Increasing College Access Is Increasing Inequality, and What to Do about It,” Rewarding Strivers: Helping Low-income Students Succeed in College, Richard D. Kahlenberg (ed.) (New York: Century Foundation Press, 2010), p. 158. For example, one study found that students from the highest quartile of SAT-equivalent scorers, but the lowest socioeconomic quartile, were less likely to graduate from college than students from the highest socioeconomic quartile but the second lowest SAT-equivalent quartile.


