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[Aller au sommaire du numéro](#)

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Résumé de l'article

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Anatomy of Income and Wealth Inequality in the United States

by

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1. Introduction

Much has been written about income and wealth inequality in the United States toward the end of the 20th and the beginning of the 21st century in books (Stiglitz, 2015; Stiglitz, 2012; Sachs, 2011) in journals (Muczyk, 2007; Muczyk & Coccari, 2009) and in Op/Ed columns (Krugman, 2015; Kristof, 2014; and Rugaber, 2014). While there is agreement that wealth discrepancy has never been greater since the great depression, there is controversy over whether this is good or bad, what are the causes, what the consequences are, and what to do about it.

The commonly listed causes of income and wealth discrepancy are as follows: The manner in which U.S. elections are financed, the offshoring of well-paid manufacturing jobs as a result of Globalization, excessive executive salaries, the decrease in private sector unionization and the resulting diminution of union power, inadequate education so far as preparing the American workforce for high-tech jobs is concerned, and the ownership of capital with its outsize rate of return. While the authors do not take issue with the proposed causes, they submit that they are just the visible manifestations of a larger underlying cause – The Iron Law of Oligarchy.

1.1 Definition of Iron Law of Oligarchy

In 1911 the German sociologist, Robert Michels, published his book “Political Parties.” In this book he proposes a controversial hypothesis “that true democracy might very well be impossible.” This is the case whether we have in mind a political system or a business enterprise. Michels presents the argument that rule by an elite, or oligarchy, is inevitable as an “iron law” within any democratic organization as part of the tactical and technical necessities of organization. In his book, Michels

goes on to say: “It is organization which gives birth to the dominion of the elected over the electors, of the mandataries over the mandators, of the delegates over the delegators.” Michels migrated to Italy and joined Benito Mussolini's Fascist Party, as he believed this was the next logical step of modern societies.

His ideas influenced another brilliant German sociologist, Max Weber (1947), who also considered democracy an illusion and conceived of bureaucracy as the ideal organizational form to accomplish society's business; and the Canadian born American economist, John Kenneth Galbraith (2001), who argued that large corporations manipulated consumer preferences to their advantage through advertising, which also encouraged the “keeping up with the Jones' ” mentality, which, in turn, stimulates economic activity. After all, about 70% of U.S. GDP is due to consumer spending.

It should be made clear at the outset that the ruling class employs a variety of expertise to assist them with the task of controlling an immensely complex society, but their wealth makes that quite practical. Among the most indispensable of the handmaidens of the oligarchs are the lobbyists. For example, according to Public Citizen, a watchdog group, eighteen families have already spent more than \$200 million to repeal the estate tax (Muczyk and Coccari, 2009) to this date and still spending. Nor are they finished. The 2015 Republican controlled House budget includes the elimination of the estate tax.

It is interesting to note that contemporary Russia is ruled by oligarchs as a replacement for Marxism as modified by Lenin. That is why the U.S., in response to the Russian annexation of Crimea, levied sanctions first against the Russian oligarchs close to Putin, himself a wealthy man. It also appears that China is on the verge of being ruled by oligarchs, purges notwithstanding.

1.2 Contemporary Oligarchs

Every society since the dawn of civilization has been ruled by an elite class (oligarchs). This effort attempts to identify the contemporary ruling class in the U.S., describe how it rules, the consequences of its rule, and proposes the actions that are needed to alter the consequences.

It is evident from the income and wealth distributions that the ruling class (oligarchy) in the U.S. own more wealth than the bottom 90 percent (Kristof, 2014). Stated another way, the top 10% receive almost half of all income and own 75% of the national wealth (Krugman, 2014). The average income of the 1% of earners in 2012 was \$1.3 million (Boak, 2014), and the top 1% receive 75% of the capital gains. Over the last three decades 100% of all income growth went to the wealthiest 10%. Piketty (2014) demonstrates that the outsize return on capital is one reason that the top 1% has accumulated part of its wealth. If the return on capital (r) is greater than the growth rate of the economy (g), then inequality will tend to increase. This is due to the fact that wealth grows faster than wages when r is greater than g . This is how the rich get richer, since they have much more wealth to begin with. However, as Orszag (2015) observes, if you exclude land and housing, capital has not risen as a share of the U.S. economy. Of course, the low capital gains tax rate (15%) helps as well. This is why Warren Buffet pays a lower tax rate than his secretary.

Huge executive salaries is another. A chief executive officer now makes about 257 times the average worker's salary, up sharply from 181 times in 2009 (Sweet, 2014). This is why some persons familiar with this trend refer to the present as the age of the "Imperial Corporate Presidency." Chairmen of boards of directors argue that these large salaries are necessary to attract the best candidates, but this is a bogus argument. Talented individuals are attracted to medicine, law, science, academia, and the military by much more reasonable salaries, and they are every bit as gifted as corporate executives. Some of these executives run companies that lose money. How much would these people be worth if their companies actually made a profit?

Meyerson (2015) illustrates how the return of corporate profits to shareholders through dividends and share repurchases has further enriched the large investors. High level employees of the Blackstone Group and Kohlberg Kravis Roberts, private equity firms, have their income from managing other people's money taxed at the capital gains rate of 15% instead the ordinary income rate of 35% because of something called "carried interest." The 2015 Wall Street bonus pool was roughly twice the total annual earnings of all Americans working full time at federal minimum wage (Kristof, 2015). Lastly, large inheritances have exacerbated the wealth gap. While the media focuses on the top 1%, to be more specific, the greatest beneficiaries of the income and wealth gaps is the top 0.1% (Krugman, 2014). Furthermore, as the wealth of whites leveled off as the economy began to recover between 2010 and 2013, blacks and Hispanics experienced continued decline (Fletcher, 2014).

Further evidence of income and wealth inequality is provided by a statistical measure called the Gini coefficient. A value of zero means perfect equality. A coefficient of one implies maximum inequality (Gini, 1936). For OECD countries in the late 2000's, the income Gini coefficient ranged between .24 and .49. African countries had the highest pre-tax Gini coefficient with values between .63 to .70. For the same period, the U.S. had the fourth highest measure of income inequality (.48) out of the 34 OECD countries (Weinberg, 1996). A coefficient above .50 is considered high. Countries like Chile, Bolivia, Mexico, and Central America countries fall into this category. The U.S. is not far behind.

The wealth index is even higher for the U.S. Economist Edward Wolff recently estimated the Gini coefficient for household wealth to be .87. Thus, America has become a society of haves and have-nots. The U.S. is approximately halfway between full equality and a situation in which the country's income is in the hands of a few. We are halfway between a socialist utopia and an oligarchy (Babones, 2012). Upward mobility, once America's strength, is now little more than a myth (Kristof, 2014).

Certainly some oligarchs do considerable good. Bill Gates, Warren Buffet, and George Soros immediately come to mind, and the Koch brothers sponsor science programs on television. But that is beside the point. Plutocrats can do everything they want on considerably less money than they possess, but the middle-class needs additional wealth to improve its condition and realize its potential.

2. How the Ruling Class Games the System?

He who says oligarchy also says control. Oligarchs have controlled societies since time immemorial in a variety of ways. The question then is: How do contemporary oligarchs control American society?

2.1 Control of Elections

Through financing campaigns. Elections, especially national ones, have gotten quite expensive. As the result, those individuals who pay for the campaigns acquire considerable influence. It stands to reason that in a two-party system, if you own both parties, you can sleep well the night of the election. In other words, if you wish to make sense out of American politics, follow the money. While the Democrats are considered the party of Big Labor, or what is left of it, and Trial Lawyers, and the Republicans of Big Energy and Agribusiness (Krugman, 2015), Wall Street has contributed equally to both parties (Elliot, 2014) until President Obama blamed investment bankers for the “big recession of 2008” (Krugman, 2014). Now Wall Street clearly favors Republicans.

In this presidential election many of the Republican candidates already made their pilgrimage to Las Vegas to obtain the blessing and money of Sheldon Adelson, the casino mogul and patron of Republican and Israeli causes. One wealthy man has kept Rick Santorum, former Republican senator from Pennsylvania, in the hunt for the presidency of the U.S. for several presidential cycles. Marco Rubio, on the other hand, is the beneficiary of the largesse of another billionaire, Norman Braman. To counter the Republican advantage, Democrats are seeking their own mega donors.

Those who control elections not only control Congress, which writes the tax code with its rates and loopholes, but the Presidency as well, which among other important matters, determines the nature of the Supreme Court; and the Court's decisions have a significant impact on elections. Citizens United, which equated money with speech, and affirmed that in the eyes of the law corporations were persons entitled to the protection of their free speech, buttressed the power of American oligarchs; as did *McCutcheon v. Federal Elections Commission*, which eliminated the limit on total political contributions by a single individual.

2.2 Control of costs as a way of increasing profits:

Offshoring manufacturing jobs. Initially, employers decreased costs by outsourcing work to non-union contractors whose workers were paid less and received fewer benefits. Yet even low paid workers were protected by minimum-wage laws and some hour, health, and safety regulations.

However, minimum wage in America is still much higher than the going rates in low-wage nations like Mexico, China, India, Russia, Indonesia, Philippines, Malaysia, and so on. It soon occurred to numerous companies that offshoring to “sweat-shop” nations manufacturing production that had been performed in the U.S. would decrease costs and increase profits even more (Muczyk, 2007). The official line was that offshoring was necessary to be competitive and would result in less expensive goods. But mostly it resulted in bigger profits and higher executive pay.

It appears as though the State Department, whose goal is to maintain cordial relations with the world rather than looking after the interests of Americans, is determining economic policy and business practices. Wealthy nations should provide aid to poorer ones, but through foreign aid not through trade policies.

As Muczyk and Coccari (2009) point out, digitization coupled with the fiber optic highway, exposes many service jobs to offshoring as well. A study by the University of California, Berkeley estimates that 14 million U.S. jobs (11% of the total workforce) are vulnerable to offshoring. Princeton economist and former vice president of the Federal Reserve Board, Alan Binder, estimates that between 42 and 56 million U.S. jobs are susceptible to offshoring. Tax incentives for offshoring create additional incentives to engage in this practice (Muczyk and Coccari, 2009). Clearly, technology plays a role in destroying jobs everywhere, as it always has. Hopefully it continues to create more jobs than destroys, but that is not inevitable.

3. The Truth about Free Trade

While all consumers benefit from lower prices resulting from offshoring, corporations run by oligarchs also benefit from higher profits; and since they are also shareholders from higher share values and dividends. But all this comes at a high cost. It makes economic sense for labor-intensive work to be performed in lower-wage countries, providing there are proper safeguards for workers and the environment. However, the better paying jobs that are lost will not be replaced by jobs that pay as much or more than the offshored ones, but by lower paying service jobs (Muczyk and Coccari, 2009; Lowry, 2014). Motorola, Texas Instruments, GE, HP, IBM, Microsoft, Dell, and every Silicon Valley venture firm are spending billions of dollars in Asia to take advantage of cheap, educated, and motivated labor (Muczyk, 2007). Tax incentives need to be devised to keep these jobs in the U.S.

The theoretical justification of free trade is David Ricardo's 1817 "Theory of Comparative Advantage." However, the economists who subscribe to this theory (and they are in the majority) seem to be oblivious to the chronic trade deficits with no end in sight, and to de-industrialization due to the loss of well-paying manufacturing and high-tech jobs (Muczyk, 2007; Muczyk and Coccari, 2009). Such blind faith independent of data brings the discipline of economics much closer to religion than science (Naim, 2009). Admittedly, U.S. consumers benefit from lower prices until they lose their jobs and their communities lose their tax base. Then what?

Most of the benefits of free-trade have already been realized. A series of past trade agreements, going back almost 70 years, has brought tariffs and other barriers to trade to a very low level so that changes in currency values play a more significant role (Krugman, 2015). It appears more and more that free trade is not a mechanism to enrich all trading partners but an effective vehicle for transferring wealth from the industrialized countries to third world ones (Tupy, 2015; Zakaria, 2011) and to U.S. oligarchs. The elected officials who are sensitive to this data and the disappointing results from the NAFTA and CAFTA treaties have been reluctant to give President Obama fast-track authority for additional trade agreements with the Trans-Pacific nations. Organized labor also opposed giving the president fast-track authority for the same reasons (Meyerson, 2014; Muczyk and Coccari, 2009).

4. The Role of Corporate Interests in Drafting the Trans-Pacific Partnership Trade Bill is Instructive

500 non-government advisers participated, and 85% of them were industry executives or lobbyists (Milbank, 2015); the real beneficiaries of the trade bill. Yet! Congress managed to pass the fast track bill after all the lobbying was completed.

Third world countries are anxious to welcome U.S. plants not only because of the employment opportunities, but also because through joint ventures they acquire the latest U.S. technology. After a while, armed with state of the art technology, they strike out on their own. But without a vibrant U.S. market, to whom will they export? After all, the U.S. consumer is the engine that drives international trade.

All theories rely on assumptions. The Theory of Comparative Advantage is no exception. It assumes immobility of factors of production, but as has been demonstrated, the fiber optic highway coupled with the computer is the equivalent of extreme labor mobility. Moreover, those nations that rely on commodities for their comparative advantage are vulnerable to market price fluctuations due to unforeseen circumstances. In years bygone, countries such as Columbia with a comparative advantage in coffee, suffered greatly whenever the price of coffee plummeted. Ditto for Chile when the price of copper, Chile's comparative advantage, dropped significantly. Brazil felt the pain when the British in the 1880s took stolen rubber plants to Malaya (Muczyk, 2007). The current example is the countries relying on oil exports. The steep drop in crude oil prices has wreaked havoc with their budgets. Also, in the absence of controls, capital will flow to wherever it receives the highest rate of return.

5. Eliminating Countervailing Power

Diminishing the clout of private sector unions. Sixty years ago, 35% of America's workforce was unionized, almost entirely in the private sector. Today, 11.3 percent is. About half (49.6%) of this minority are government workers whose union dues do much to elect their employers. Governor Scott Walker of Wisconsin, however, is leading the charge to break the power of public sector unions by limiting the issues that public sector unions can negotiate. UAW membership has plummeted as far and as fast as the city of Detroit has – from 1.5 million in 1979 to about 380,000 in 2012. Union president, Bob King, has said: “If we don't organize these transnationals, I don't think there's a long-term future for the UAW.” By transnational he meant a factory making foreign-brand vehicles in the South (Will, 2014). It is estimated that the decrease in private sector union membership accounts for between 25 and 33 percent of the increase in income inequality among men in the U.S. (Kristof, 2015). Union membership in Germany, Japan, and South Korea is greater than in the U.S., but these are different unions, and more will be said about the differences in a subsequent section of the article.

6. Consequences of the Wealth Gap

While economists have documented the economic costs of the income and wealth gaps, principally putting the brakes on economic growth and promoting

economic instability (Stiglitz, 2015; Stiglitz, 2012; Sachs, 2011), other social scientists have cataloged a host of other maladies fostered by income and wealth inequalities. As Princeton economist Alan Kruger observed, in countries with wide income gaps, children of poor parents were more likely to grow up to be poor adults. This explains why more equal societies almost always do better than their less equal counterparts. However, social scientists, starting with Daniel Patrick Moynihan in 1965, are now putting the role of the family in proper perspective. As sociologist Lawrence Mead enunciated nearly 25 years ago: “The inequalities that stem from the workplace are now trivial in comparison to those stemming from family structure. What matters for success is less whether your father was rich or poor than whether you knew your father at all.” That is the result of the crucial role of family structure which provides the habits, mores, and dispositions that equip individuals to take advantage of opportunities (Will, 2015; Porter, 2014).

7. Can Anything be Done?

A certain amount of income and wealth disparity is desirable in a free-market economy as both a reward and inducement for hard work and creative enterprise. But huge discrepancies create significant problems. If the U.S. Government is serious about decreasing the income and wealth gaps, it should pursue the following agenda:

7.1 Need to Revise the Tax Code

President Clinton during his first presidential campaign observed: “America is evolving a new social order, more unequal, more divided, more impenetrable to those who seek to get ahead. Although America's rich got richer...the country did not...the stock market tripled but wages went down.” Consequently, the tax rates on the rich need to go up, including the capital gains rate, and the tax loopholes need to be eliminated. Some commentators argue that the corporate tax rate is already too high compared to our trading partners. But how may corporations pay that rate? As Lawrence Summers points out: “The ratio of corporate tax collections to market value of U.S. corporations is near a record low, thanks to various loopholes. And the estate tax can be substantially avoided by those prepared to plan and seek sophisticated advice.” Of the ten richest Americans, four are scions of Sam Walton, founder of Walmart. The Koch brothers, darlings of conservative causes, are beneficiaries of the estate tax law as well, and there are many others. It is high time to tax the beneficiaries of this inequality. We can start by increasing the estate tax. With up to 15% of national income, inheritance is making a comeback from a postwar low of 4%. Furthermore, the earned-income tax credit should be increased to incentivize working and saving (Summers, 2014). Currently, our trade deficits are of such magnitude that the U.S. has become the largest debtor nation. Yes! Our trading partners purchase much of our debt, but experience dictates that major creditors by virtue of being bankers can gain considerable leverage over the policies of the borrowers (Muczyk, 2007). Certainly, the saving rate of Americans should go up considerably to ameliorate this condition.

The apologists for the oligarchs highlight the fact that the one percent of taxpayers with the highest income paid 34.3% of federal individual income tax. However, they conveniently overlook the fact that the top 20% received almost as

much income as the bottom 80% combined. Moreover, they ignore the tax burden of the more regressive taxes such as, payroll, excise, sales, etc. (Muczyk and Coccari, 2009).

7.2 Dealing with Offshoring

Companies that establish subsidiaries in low tax countries pay the lower tax if they certify that their profits are invested abroad. So why stay in the U.S.? Consequently, eliminate tax incentives for offshoring. We can become a producing nation again by insisting that products sold in the U.S. A. are made in the U.S. and/or that the exporting countries import from the U.S. about as much as they export to the U.S. Warren Buffet's plan of "Import Certificates" with which Lee Iacocca agrees, presents the viable mechanics for managing such a scheme. Ronald Reagan while U.S. President showed the way with respect to Japanese automobiles, and South Korea and the Europeans have gotten the message as well, but not China, India, Indonesia, Malaysia, and the Philippines (Muczyk, 2007).

Germany should serve as an example for the manufacturing sector. While it has large manufacturing corporations to be sure, it has many more small and medium size manufacturing establishments that are operated as family enterprises. While they lack the advantage of economies of scale, they overcome them with greater flexibility and better motivated employees. Also, German law requires union representation on corporate boards, which creates a more harmonious union/management relationship than exists in the U.S.

7.3 The Truth about Education

The education story-line goes like this. We live in a period of unprecedented technological change, and too many American workers lack the skills to cope with that change. The truth of the matter is that American education for the masses has fallen behind industrialized nations (Kristof, 2014), but that has little to do with the income and wealth gaps. Education provided to the scions of elites is still nonpareil. Actually, the inflation-adjusted earnings of highly educated Americans have gone nowhere since the late 1990s. Paul Krugman observes: "As for wages and salaries, never mind college degrees—all the big gains are going to a tiny group of individuals holding strategic positions in corporate suites or astride the crossroads of finance. Rising inequality isn't about who has the knowledge; it's about who has the power (Krugman, 2015)."

President Obama's plan to provide free Community College education to American students is at best a modest beginning to narrow the income gap (Porter, 2015). The increasing focus on science, technology, engineering, and mathematics (STEM) will in all likelihood produce better results, as will making four year college/university education more affordable for all. But this will not be easy. While the U.S. yearly graduates 90,000 engineers, China alone graduates 350,000 (Muczyk, 2007). But since youth unemployment is such a huge crisis, one solution may be to follow the German model. Germany's eight percent youth unemployment rate is about half that of the U.S. The biggest difference is that Germany takes vocational education seriously. Young Germans are getting classroom education along with on-the-job training that gives them practical skills they can sell in the labor market.

Also, German employers form groups that work with government officials to define training programs that will provide the skills that they need. Thus, employers work with schools to develop a workforce for major employers in the area.

7.4 Increase Economic Growth

One way to increase growth is to let more people live and work in the U.S. More workers mean a larger GDP, and immigration reform could increase the size of the U.S. workforce by about 16 million in 2033, or an increase in the labor force of about 9 million (Merrell et al., 2013).

7.5 Increase Equity Investment

If Piketty (2014) is correct, and (r) is really greater than (g) , then the rest of us (99%) need to own more stocks and bonds. This could be achieved by some sort of Social Security privatization scheme. Piketty himself proposed this in France several years ago (Gupta, 2014). This idea was floated in the U.S. as well but was dismissed because of the risks involved. But there is a way to improve the reliability of investment income. The Center for American Progress has proposed a “Safe Retirement Plan” that would combine the best of both defined contribution and defined benefit plans and protect against the erosion of retirement benefits. In general, such a plan would better manage the risk and cost of the typical 401(K) plan (Davis and Madland, 2013).

Another alternative is for private sector employers to emulate the Federal Employee Retirement System (FERS). That plan is a three-legged stool. One leg is Social Security. Another is an annuity (1% of the average of the highest three years; 1.1% after 20 years of service). The third component is the Thrift Savings Plan. (TSP), which is voluntary. An employee contributes a certain amount up to a maximum every paycheck, and the employer matches that amount. The combined sum can then be invested in any of five approved funds—three stock funds and two bond funds. The employee can change the allocation frequently. Upon retirement the employee can take the TSP funds out in installments, one lump sum, or annuitize the funds. One of the authors is the beneficiary of that plan, and considers it one of the best conceived plans from an employer/employee standpoint.

7.6 Decrease Incentives for Rent Seeking

Competition drives down profits. Rent seeking, on the other hand, consists of the many ways by which our current political process assists the oligarchs to keep profits high at the expense of everyone else. It includes laws that make the marketplace less competitive; that permit CEOs to receive outlandish salaries; that provide preferential treatment for special interests in the tax code, *inter alia*. For example, a law prohibits the Federal Government, the largest purchaser of medicines, from bargaining with the pharmaceutical industry over quantity discounts (Stiglitz, 2015). While patents are a form of rent seeking, the justification for them is more credible. A repeal of these laws and a more rigorous enforcement of anti-trust laws would reduce rent seeking behavior to the benefit of the public good.

8. Conclusion

Let us not delude ourselves. The plutocrats are not going to be knocked off their lofty perch without a fight. They have their supporters in the press, on television, and on the radio, as well as in Congress, and they know how to fight. The first blows will take the form of name calling. Those in favor of narrowing the income and wealth gaps will be called socialists or worse. Piketty has already drawn fire (Douthat, 2014). Another convenient allegation is that proponents of narrowing the income and wealth gaps are fostering “class warfare.” As Warren Buffet has noted succinctly: “There’s been class warfare going on for the last 20 years and my class has won” (Stiglitz, 2015). Also, assertions of envy by the have-nots of successful individuals will be advanced as well for good measure.

The Wall Street protest received a modicum of attention for a while, but petered out soon enough, when the protesters were discredited by being characterized as a bunch of unwashed hippies trying to gain attention. The oligarchs know about the French Revolution, the Bolshevik Revolution, the Chinese Revolution, the Cuban Revolution, and most recently the Arab Spring, and will try to ameliorate the middle class only as much as is necessary to prevent radical action. The lower class will be mollified by a modest safety net. Scare tactics simply will not work.

What is needed to narrow the gap in income and wealth disparity is a movement much like the right to vote movement by women (Suffragettes) and their fellow travelers, by organized labor in the 1930s, by the Civil Rights activists of the 1960s, the current climate change movement, and so on. The leaders of this movement must make the case that a vibrant middle-class is the greatest job-creation engine that this economy possesses, something Henry Ford understood, and dispel the myth that all or most of the plutocrats are job creators. A prosperous middle-class has been the best argument against Marxism that the West was able to devise, and still is. Persons who would like to narrow the income and wealth gaps already have their heroes. The bibliography of this article includes the prominent ones.

The great depression brought about the legislation that resulted in dramatic social change and a more equal society. However, another great depression is out of the question because of the horrific costs to everyone. Since many of the remedies to the current income and wealth gaps require legislation, getting elections financed by tax revenues is a precondition. Politicians running for elected offices must be convinced that they are jeopardizing their election chances unless they are prepared to vote for legislation that is instrumental in diminishing the income and wealth gaps. Individuals should get active in party politics at the grass roots level and demand of their candidates support of the middle-class agenda. This must be a bi-partisan effort. Given the record number of millionaires in Congress, and in light of how well Republicans have done in recent elections at the federal, state, and local levels, this constitutes a daunting challenge to say the least, but one that merits a heroic effort. After all, we have the numbers on our side and the opportunity to prove Michels, Weber, and Marx wrong.

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