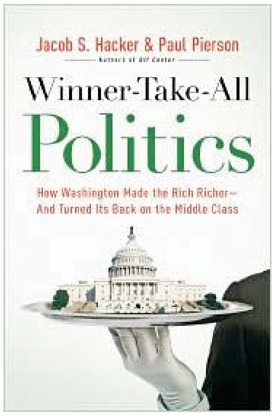

WINNER-TAKE-ALL POLITICS

How Washington Made the Rich Richer – And Turned Its Back on the Middle Class

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About the Author:
Jacob S. Hacker is professor of political science at Yale University. He is a Fellow at the New America Foundation and is the author of several books including *The Great Risk Shift* and *Off Center*.
Paul Pierson is professor of political science at the University of California at Berkeley. He is also the author of several books including *Politics in Time* and *Dismantling the Welfare State*.

General Overview:
The real culprit behind one of the great economic crimes of our time – the growing inequality between the vast majority of Americans and the richest of the rich – isn't any of the usual suspects like foreign trade, globalization, technological changes in the workplace or outsourcing. The guilty party is American politics. The winner-take-all economy is primarily a result of winner-take-all politics.

In the 1970s, a major transformation of American politics occurred which has been carried on by successive administrations. Big business and conservatives have allied to undo the nation's traditional regulations and progressive tax policies which had always helped ensure a fair distribution of economic rewards occurred. Deregulation sparked a thirty-year war which has led to the current winner-take-all economy where the rich get richer and the rewards are not evenly spread out at all.

To again recreate the level playing field which has always characterized the genius of the U.S. political and economic system, American politics will need to undergo a period of renewal similar to that which has happened periodically throughout the nation's history. Ways and means will need to be found which will allow the voice and interests of middle-class Americans to be heard and acted upon in Washington.

The Winner-Take-All Economy

At the end of World War II, prosperity in America was broadly distributed up and down the entire income ladder. Since the 1970s, however, three undeniable facts have emerged:

- The share of income earned by the top 1 percent has gone from 8 percent in 1974 to 18 percent in 2007.
- The shift of income towards the top has been sustained and increasing steadily from 1980 onwards.
- Very few of these gains to the rich have trickled down to middle- and working-class Americans.

When all the economic data is crunched, it is clear the outsized gains of the rich have come at the expense of those lower on the economic ladder. Admittedly, the real household incomes of all groups have risen modestly but by and large these gains are the result of people working longer hours than before more than anything else. Even in the most recent economic downturn – which has been the worst in more than seventy years – the real pretax income of those in the top 1 percent has kept on steadily rising by 10 percent a year while unemployment has risen to the highest level ever recorded.

Some people suggest education is the real culprit and that the economy increasingly rewards those who have the right education. The suggestion that skill-biased technological change is occurring in the economy as evidenced by a shift towards knowledge-based employment is correct, but the undeniable fact is other rich nations have not seen winner-take-all play out in their economies. As they have gone through the same adjustments America has, they have not seen this same phenomena of the rich forging ahead. There is something unique about America's winner-takes-all economy which transcends technological change.

"This is an economic puzzle. It is also a political puzzle. Democracy may not be good at a lot of things. But one thing it is supposed to be good at is responding to problems that affect broad majorities. How could events and trends like these evolve with so little response from democratically elected leaders? Indeed, the puzzle is even deeper. For government was no mere bystander in many of these developments. It actually pushed them along."

How the Winner-Take-All Economy Was Made

The prevailing wisdom is that America's winner-take-all economy is just an economic by-orduct of dynamic marketplaces and the government does not have anything much to do with it at all. The facts speak otherwise. Most of the time, when people talk about government, they focus on the programs which are intended to help those at the bottom of the economic ladder – the minimum wage, the Earned Income Tax Credit and Medicaid for vulnerable children and families. The real story, however, lies in analyzing what political leaders have done for those at the top in terms of taking action or failing to take corrective action when big business have pushed new legislation through Congress.

In practical terms, the federal government has been asleep at the controls when:

- Taxes for the rich have fallen from 75% in 1970 to less than 35% in 2004.
- Trade union membership has gone from one-in-three after World War II to one-in-nine in 2010.
- Executive pay rates have skyrocketed by any standard imaginable – even in down markets.
- Stock options have been freed up to be used to lower the visibility of high payouts for executives.
- Regulatory restrictions on the financial markets were first lowered and then almost eliminated altogether.

All of these factors suggest business has enjoyed the upper hand in both Washington and the broader workplace for quite some time now. There have been deliberate failures on the part of elected officials to work energetically towards offsetting increasing inequality. In fact, U.S. public policies of recent decades have actively nurtured rising inequality rather than address it. Contemporary American politics seems to have fallen victim to a system where the most powerful and the most well resourced entities reign supreme.

"During my seven and a half years in Washington, nothing astonished me more than witnessing the powerful special interest groups in full swing when they thought a proposed rule or piece of legislation might hurt them, giving nary a thought to how the proposal might help the investing public. With laser like precision, groups representing Wall Street firms, mutual fund companies, accounting firms, or corporate managers would quickly set about to defeat even minor threats. Individual investors, with no organized labor or trade associations to represent their views in Washington, never knew what hit them."

– Arthur Levitt, former chairman of the Securities and Exchange Commission

A Brief History of Democratic Capitalism

It has long been recognized the imbalance between rich and poor is the Achilles's heal of any republic. In fact, the history of the United States with its own distinctive form of democratic capitalism has been marked by periods of gridlock and deference to economic power. These have always to date been followed by dramatic moments of political renewal where the concerted efforts of political reformers have restored the balance.

While political and economic freedom do go hand-in-hand, they are always in tension with each other. Political equality lies at the heart of democracy in that "all men are created equal" but in the marketplace, money matters a lot. While the rich and the poor may have one vote each, economically the "golden rule" reigns supreme – he who has the gold makes the rules. Whenever markets operate in damaging ways, it is expected politics will correct the imbalance.

The Founders when constructing the new American republic were well aware deep class divisions would undermine democracy. They therefore specified voters did not need to be property owners so the median voter would have political influence. It is this median voter which ultimately drives what politicians do. The median voter's income is below the average income and therefore politicians seeking the median voter's vote will be motivated to redistribute income through government mandate. The government and the law have always acted as a counterbalance to the influence of property and the markets.

The challenges facing America today are certainly not new. The Roaring Twenties were an era of unbridled capitalism dominated by free market sentiment and industry-dominated politics. It wasn't until they gave way to the Great Depression that substantial reforms of governance in order to address new economic realities came about. In the most concentrated burst of economic reform in American political history, the New Deal was ushered in under the guidance of President Franklin D. Roosevelt. Banks were regulated and consumer deposits were insured. The securities industry was placed under tight new restrictions. Taxes were levied on the rich and public spending increased to boost the economy, ultimately creating jobs for the destitute and poor. The end result was a new economic order premised on the concept the federal government had a mandate and responsibility to stabilize the economy, provide widespread economic security and where necessary redistribute wealth from rich to poor.

The ongoing health of American democracy has always depended on these periodic renewals. They ensure that new economic changes which arise don't cripple the government and allow the powerful to steamroll the rest of us. Since the late 1970s, America has been primed for another of these renewals but it seems to have been placed on long-term hold. The winner-take-all economy of recent years seems to be the manifestation of one of the fears expressed by the Founders that the balance of government would tip towards those who had the greatest resources and therefore the most economic clout. How American politics has managed to close the long era of shared prosperity and usher in the winner-take-all economy – regardless of which party is in power – is a phenomena worth examining in much greater detail.

The Unseen Revolution of the 1970s

Conventional political history suggests the 1960s were an era of rising discontent where the fabric of America unraveled in the blowtorch of civil rights, Vietnam and rising crime. Conservatives, led by Richard Nixon, seized the White House and pioneered the politics of resentment based on an "us-versus-them" mentality. The simple fact is, however, Nixon's election in 1968 wasn't really a switch point in American politics. Rather, it was the election of Carter in 1974 which heralded in a major shift in economic policy. In the mid- to late-1970s, the call for deregulation became overwhelming as there was a general perception marketplace regulation was a serious curb on economic growth.

Most people view elections as gladiatorial contests between nominees but the reality is much of what elected politicians do is mundane and mind-numbingly detailed. The critical factors are public policy – what the government actually does – and organized interest groups. The ability to dictate policy is the grand prize of election and the main competitors are not the voters who are usually blissfully ignorant about many matters but organized groups who are professionally organized and well resourced to push their political agendas forward. Elections are made for TV because they involve head-to-head competitions between high profile candidates but it is those organizations operating in the background who push whichever politicians ultimately get elected which are the real long-term winners. Over the last thirty years, organized business groups have become much better at what they do and subsequently have become the crucial actors in the political fights which are taking place.

"Of the billions of dollars now spent every year on politics, only a fairly small amount is directly connected to electoral contests. The bulk of it goes to lobbying – sustained, intense efforts to shape what happens in Washington. Officially, over $3 billion is now spent every year by lobbyists. This figure has nearly doubled in just a decade and almost certainly dramatically understates true expenditures to influence policy. For powerful groups the center of action is in Washington, not the swing states. And more and more over the past thirty years, Washington has become their playground."

The Politics of Organized Combat

"Business must learn the lesson that political power is necessary; that such power must be assiduously cultivated; and that when necessary, it must be used aggressively and with determination – without embarrassment and without the reluctance which has been so characteristic of American business."

– Future Supreme Court justice Lewis Powell, 1971.

It is widely recognized that from 1969 to 1972, the American business community suffered a series of political setbacks with the creation of the Environmental Protection Agency, the Occupational Safety and Health Administration, the Consumer Product Safety Commission and others. In response, big business organized itself. The number of corporations which had public affairs offices in Washington grew from 100 firms in 1968 to more than 500 firms in 1978. Registered lobbyists surged from 175 firms in 1971 to more than 2,500 by 1982. And even more impressively, companies started learning how to work together. Corporate Political Action Committees increased from less than 300 in 1976 to more than 1,200 in 1980.

These business interests were initially spurred by what was perceived to be the federal government's overreach but they soon learned how to apply the tools of marketing and communications to generate mass grassroots political campaigns. Business also massively increased its political giving just as the costs of running campaigns began to skyrocket because of television. Not only that but a number of wealthy families also started pouring resources into efforts not just to fund candidates for reelection but also to shape the broader political climate. They became much more willing to openly put their money where their true ideology was. Idea factories were built rapidly and on a massive scale which politicians could not ignore.

As all of these companies got better at coordinating their efforts towards shared goals, they became much more proactive in flexing their newfound political power. When President Jimmy Carter attempted to establish a new Office of Consumer Representation, the Business Roundtable and a coalition of hundreds of firms orchestrated a massive grassroots attack which ultimately saw the bill voted down even though the Democrats controlled both Congress and the White House. Carter had campaigned on tax reform and when he introduced a bill which called for a hike in the capital gains tax and some simplification of the tax code, an amendment in the House bill was made which in fact cut the capital gains tax rate in half instead. Three years later after Ronald Reagan was elected, the 1981 Economic Recovery and Tax Act was passed. This reduced top income rates and put in place generous new depreciation rules and enough tax loopholes to ensure corporations paid sharply reduced taxes overall. In essence, this was a rewrite of the nation's tax laws in favor of winner-take-all outcomes.

The Middle Goes Missing

As the corporations have become better organized at lobbying for their interests, those organizations which have traditionally amplified the thoughts and interests of middle- and working-class Americans have gone AWOL. A good illustration of this is the American Legion. Unions were on the front lines of all the major economic battles of the mid-century but in the 1980s union membership declined rapidly. That diluted the influence of the unions and weakened the American Legion's funding base. It also meant when the key pieces of winner-take-all legislation were being considered, an important group who had always argued passionately for the rights of the working class were absent from the debate. To some extent, unions have been replaced by advocacy groups but these are fragmented and relatively ineffective.

There is, however, one striking exception to the trend away from grassroots organizations which represent the middle class. Christian conservatism has helped bring large numbers of moderate-income voters into politics as an organized force. And due to the fact most of these groups are strongly focused on nonmaterial issues like abortion and gay marriage, they are more likely to align with the Republican Party than they are with the Democrats. That means not only is the Republican Party favored by more affluent voters but it also often the party of choice of moderate-income Christian conservatives as well. Bottom line this means Republicans attract more support from lower- and middle-class voters because of the Christian conservative connection than they normally would as a result of any of their economic policies.

One of the distinguishing features of contemporary American politics is the fact both parties have largely deserted the center in favor of the wings. There has been a high degree of polarization – Republicans have moved to the right while Democrats have moved to the left. American politicians and political leaders are now much less responsive to the electoral middle than they have traditionally been. This trend does reflect the fact voters themselves are now more polarized and firm about their views than they were in the past but it also suggests the landscape of American politics has tilted dramatically. Business groups are now much more influential because they're better organized and tend to be more savvy about how they approach things. A broad range of organizations which once brought traditional voters into politics (like the unions) have lost ground although as previously noted the evangelical movement is now much more mobilized than it was in the past bringing low- or moderate-income into an unexpected alliance with powerful financial interests through the GOP. The news media, which has traditionally acted as a watchdog informing voters, has faced increased pressure to provide entertainment packaged as news rather than rigorous analysis of political policies. The cumulative effect of all these factors means the playing field has tilted and politicians are struggling for supremacy and to retain relevancy. In practical terms, today nobody is genuinely representing the interests and preferences of middle class voters.

A Tale of Two Parties

As the influence of organized labor waned and the influence of organized business came to the forefront, both the Republican and the Democratic parties scrambled to adjust to these new realities in the 1970s. Republicans had a first-mover advantage because of their natural affinity for big business and they started to construct direct linkages between various interest groups and candidates through the powerful bonds of campaign money and favorable economic policy. The Republicans also invested in cutting-edge fund-raising techniques built around direct-mail operations and soon the GOP was raising unprecedented sums. Republican fund raising went from $12.7 million in 1976 to $26 million in 1980 from small donations and from $29 million in 1976 to $78 million in 1980 in hard money donations (the regulated dollars used to explicitly support specific candidates). In simple terms, the Republicans were first out of the blocks in capitalizing on the new opportunities and could therefore allocate more money than the Democrats to the critical electoral races where the candidates seemed reasonably even matched.

The Democratic Party didn't really get organized with regards to better fund raising mechanisms and stronger links to Political Action Committees until the mid-1980s, and this reorganizational effort took a number of years. Even then, there were still some stark differences. Business gave money to the GOP for party building efforts and to contest close electoral battles whereas money given to the Democrats went largely to individuals who were viewed as moderates to finance their reelections. The Democratic Party made strenuous efforts to be more business-friendly in the 1990s with varying degrees of success. To further strengthen this perception, many Democrats began to accede to and in some cases even cosponsor Republican initiatives which supported the emerging winner-take-all economy.

From there, the deregulation bandwagon started to gain some serious momentum. In industry after industry, those who were still regulated called for more freedom from any oversight. The prevailing economic logic of the late-1980s within both the Republican and the Democratic parties was economic regulation was now outmoded and market regulation should be the new long-term norm. More and more, Washington started weighing in on the side of the have-it-alls.

Building a Bridge to the Nineteenth Century

During the 1990s, winner-take-all politics got into high gear. During the economic expansion of that decade, the average pre-tax income of the top 0.01 percent increased at more than 16 percent a year – meaning their real incomes nearly tripled. In the ongoing expansion of 2002 - 2007, their incomes would more than double again as both Republican and Democrat administrations of that era would practically outbid each other to show friendliness to business and especially to Wall Street. Support for freewheeling, turbo charged capital markets from Washington was almost universal as winner-take-all came to full fruition.

The Republican Party that emerged during the 1990s under the leadership of Newt Gingrich were exuberant cheerleaders of the winner-take-all economy calling for deregulation and for the retreat of government from the provision of public goods. This new incarnation of the GOP had none of the party's traditional go-slow fiscal conservatism. The GOP's radicalization of its economic policy was brought about by two new pools of Republican supporters – the South and conservative evangelicals. They were supplemented by small business owners who organized and then established a presence in the GOP along with a cadre of activists who were devoted to making ongoing tax cuts a pillar of Republican doctrine. In fundamental ways, all this new blood contributed to the train of thought government spending should be progressively limited so as not only to reduce the deficit but also to allow additional tax cuts as well. Overall, the GOP clearly turned to the right on economic issues and exuberantly embraced the winner-take-all economy.

Democrats Climb Aboard

As the Republicans embraced winner-take-all politics during the 1990s, logic would suggest this would be a perfect opportunity for the Democrats to go in the opposite direction. In this case, logic would be wrong. Over the course of the decade, the Democrats started by accommodating winner-take-all policies and eventually embraced the winner-take-all philosophy lock, stock and barrel. Many of the party's officials moved to the moderate right on economic matters with the result the Democrats over time lost the ability to articulate effectively their case for policies which would provide meaningful checks on concentrated economic power. Powerful Democrats chose to fully support the new economic order rather than put forward their traditional point of view.

Admittedly, this threw up a few conundrums for the Democratic Party. One was how could a party which had historically positioned itself as being for the little guy and organized labor suddenly project itself as being a reliable partner of business? The solution, as applied during the Clinton presidency, was to put forth initiatives which appealed to the general populist sentiment at a superficial level but when you got into the details it became clear what was being proposed would appeal to business. As with most political policy matters, the devil was in the detail, not the headline. Clinton would go on to recast his electioneering social investment strategy as an interest rate strategy once in power. His administration accepted tight budget constraints rather than offer direct support to the middle class. Republicans might have been out-in-the-open zealots for the winner-take-all economy but the Democrat's response during their periods in control was pretty much to sit back and do nothing to unwind the general direction legislation was heading. Put another way, the Democrats became masters of the drift.

Democrats have played major supporting roles in all critical policies which have enabled the winner-take-all economy to gain momentum. By failing to hold their ranks as a voting block especially in the Senate, they have allowed tax cuts highly skewed to the top to be enacted. Democratic senators voted against the introduction of sensible accounting rules which would have seen stock options expensed at the time they were issued which was another issue near and dear to big business. These regulations would have moderated the explosion of CEO pay through the insistence of honest and transparent accounting but Democrats in the Senate blocked these efforts. Leading Democrats supported almost all of the deregulatory initiatives of the 1990s which would have been stopped in their tracks if there was not majority support at a time when the Democrats controlled the Senate.

Battle Royale

In the fall of 2008, just as the presidential election campaign was reaching peak intensity, the United States faced a full-fledged financial calamity firmly rooted in the winner-take-all economy. As credit dried up, the stock market collapsed, home foreclosures skyrocketed, unemployment spiked and consumers closed their wallets. As policymakers responded with desperate measures to try and forestall a total collapse of the financial system, a new president arrived who articulated the case for major change. In a campaign speech, then candidate Barack Obama had stated: *"We've lost some of that sense of shared prosperity. Now, this loss has not happened by accident. It's because of decisions made in boardrooms, on trading floors, and in Washington. Under Republican and Democratic administrations, we've failed to guard against practices that all too often reward financial manipulation instead of productivity and sound business practice. The American economy does not stand still and neither should the rules that govern it. Unfortunately, instead of establishing a twenty-first century regulatory framework, we simply dismantled the old one, aided by a legal but corrupt bargain in which campaign money all too often shaped policy and watered down oversight. In doing so, we encouraged a winner-take-all, anything goes environment that helped foster devastating dislocations in our economy."*

When President Obama took office ten months after making that speech, he announced an ambitious legislative agenda for his new administration. It included a huge economic stimulus plan, a major revision of federal spending priorities, near-universal health care, a massive overhaul of financial regulation and highly ambitious climate change legislation. If enacted, these proposed laws would effectively mend some of the most serious distortions created by the winner-take-all economy. And yet despite the fact all the planets seemed to be in alignment, by the end of his administration's first year, President Obama would describe his legislative agenda as having been hit by a "buzz saw" and torn to shreds. In almost every case, these ambitious reforms died in the Senate – in spite of the fact President Obama was the first man in almost half a century to have moved directly from the Senate to the Oval Office. President Obama's agenda posed too substantial a threat to the biggest beneficiaries of the winner-take-all economy and they were too well organized and too well funded to be defeated. (In 2009, the Chamber of Commerce alone spent $144.5 million lobbying against President Obama's reform agenda, $79.2 million of that expenditure being in the fall quarter alone. Should it therefore come as any surprise the Chamber of Commerce's voice was more prominent during the various debates than were those of the middle-class citizens of this nation?)

So what can be done about winner-take-all politics? The beauty of the American political system is every so often eras of drift are punctuated by intense periods of renewal where stalemates get addressed. America is poised for a period of political renewal which will flush out entrenched interests and realign the nation's dynamic market economy with the demands of an increasingly complex and fast-moving society. There is no silver bullet cure for winner-take-all but to genuinely reverse the trend towards economic hyperconcentration at the top, three pillars will need to be put in place:

1. The capacity of entrenched elites and those who control sizable financial resources to block needed reforms will need to be reduced.
2. Ways will need to be provided so more of those voters whose voices are currently drowned out by the moneyed interests can be heard by the politicians who represent them.
3. The development of groups which can provide an ongoing, organized capacity to mobilize middle-class voters and monitor government policies and politics on their behalf will need to come together.

Of these three pillars, the last is the most important and at the same time the most difficult to construct. Unless and until pressure can be brought to bear and then sustained to make politicians more responsive and open to citizen engagement, nothing else matters. It's unlikely this role will be played by the reinvigoration of unions as this appears to be a concept which has passed its use-by date. Perhaps advances in information technology will rise to the call and provide the middle-class with better organizational tools. Regardless, until mass engagement of the middle-class becomes feasible and sustainable, it will be an impossible task to relevel the playing field of American politics.

Overall, there are good grounds for optimism this renewal will happen. America has done this before and it will do so again in the future. This is one of the key distinctive features of the American Constitution. The founders deliberately sought to steer a course between the twin dangers of tyranny and incapacity. They rejected the concept of an absolute monarch but astutely realized squabbling, veto-ridden factions were little better. Therefore, they provided a robust mechanism of collective governance which is capable of periodic renewal from the inside out. They knew that political equality is not just an ideal but a necessity in a free and vibrant nation. They decreed definitively that democracy was the rule of the many, not just the fortunate few. It will have to be so again.

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