
Chapter 1
Without Even Asking

AT BANDON DUNES, ON OREGON'S RUGGED AND REMOTE SOUTHERN coast, men at play pretend they're in the eighteenth-century Scotland of Adam Smith.

By the tens of thousands they come from all over the world to three golf courses in the style of the Royal and Ancient Golf Club of St. Andrews, the official shrine of golf since 1754. Smith lived not far from this shrine when he developed the theory of market capitalism that guides economic policy to this day.

The Chicago entrepreneur who created Bandon Dunes, Mike Keiser, describes it as exceptionally, and unexpectedly, profitable. That he earns outsize profits is surprising. America has 16,000 courses. His lie far from the centers of commerce where his players live. When Keiser wrote a check for his first thousand-plus acres, land that had been on the market for years, his wife thought he might as well have tossed the $2.4 million into the wind. But Keiser paid only half the asking price because no one else had the vision to see what could be done to transform the land. Locals knew it as a place to hunt rabbits and occasionally poach a deer by day, while at night amorous teenagers drove down the dirt roads looking for a secluded spot beside the sea.

Gorse covered the land. Gorse is an Irish shrub that grows in impenetrable stands six feet tall or higher. If ignited during the dry season, its oily leaves burn ferociously. Three times in the past century, gorse fires reduced the neighboring town of Bandon to ashes, the last time in 1936.

By car, Bandon Dunes is a hard five-hour drive from Portland. The path goes through the rich farmlands of the table-flat Willamette Valley. It then winds west over the coastal mountains. Getting caught behind a logging truck, a rare reminder of a once vibrant industry, can slow the pace for miles.

Once the road reaches the coast, it is south for an hour to Coos Bay. It is the only urban area for miles and the only deep-water port right on the coast within a day's sail north or south.

Nature endowed the area with a temperate climate, clear water, and enough timber and salmon to last forever. But the lumber companies, eager to squeeze out ever-bigger profits, cut faster and faster. The firs and cedars matured at their own pace, however. The imbalance continued until there was little left to cut on the private lands. Then the spotted owl became a cause celebre. That added to pressure on government to allow less logging in the area's national forests. New machinery reduced the need for mill workers, and the Japanese began buying raw logs, removing more blue-collar jobs. As the eighties began, the region's timber business collapsed.

Over the decades the government had dammed rivers and creeks for electricity and water storage. To mitigate the damage to nature, government paid for hatcheries to perform tasks that nature had done for free. Still, the runs of chinook and coho dwindled. By 2006, there were not enough salmon to sustain a commercial fishing season.

For a generation now, it has been hard times in what had been a workers' paradise. Families with children moved on. Home-cooked methamphetamine became a scourge. The one hope for a brighter future now lies in all those visitors coming to golf at Bandon Dunes, another 25 minutes down the highway from Coos Bay.
Many of the golfers avoid the long drive, traveling instead in the luxury of private jets. A few arrive in little Learjets with no restrooms. Many more come in private planes the size of junior jetliners. Before the first golf course opened in 1999 perhaps three private jets a year landed at Coos Bay. Now about 5,000 corporate jets arrive annually. Soon that is expected to grow to 7,000 or more private jets, all ferrying players eager to experience what Mike Keiser calls "dream golf."

When players reach Bandon Dunes they discover that, like the Scottish original, the fairways are broad and rough. The links sprawl among the depressions and rises in the coastal dunes. The land seems to undulate, emulating the swells that roll across the Pacific until they crash on the rocks or break on the strip of taupe sand that runs for three miles below the golf course bluffs.

The links at Bandon Dunes appear to be works of nature, so picture-perfect that they suggest Mother Nature retained Kodak as her exterior decorator. In fact, earth graders remolded the sand to create what Keiser calls "nature improved." Then gardeners planted grass and positioned silver beach weed, mock heather, and verbena along the fairway edges.

No trees border the fairways, unlike the strips of forest at country clubs that act like traffic safety barriers separating golfers commuting down narrow green lanes in opposite directions. The only trees at Bandon Dunes are random sentinels, weathered by the salt air and, in the distance, the ridgeline of a once thick forest. The Bandon greens are not the smooth and gently sloping ovals of most courses, but rippled and rolling challenges. The greens cover up to an acre, eight times larger than at a typical country club or municipal course, making it all the more exhilarating to knock the ball into a cup just four and a quarter inches across.

From the courses, two of which Zagat rates as the best in America, not a single house is visible, unlike the mini-mansions and condominiums that wall the edges of so many modern golf courses. No electric power lines mar the views, either.

Bandon Dunes is quiet; peacefully, naturally quiet, an aural oasis in the industrial world. Only rarely does the whine from battery-powered golf carts offend the ear. Except for the rare player who is legally disabled, everyone carries their bag of clubs or hires a caddy. Ocean winds, which unpredictably carry higher-flying balls, silence the burly throat-clearing of diesel rigs hauling raw logs and manufactured goods up and down the grade of Highway 101, an asphalt artery of commerce and pleasure that cuts unseen through a scraggly forest of Douglas fir a mile or so inland.

To walk Bandon Dunes is to gain a sense of how the game was played, and life lived, just before the Industrial Revolution brought us ugly factories, the inescapable noises of machinery, and riches beyond the imagining of those who lived before. Golf began six centuries ago, when life was mostly short, nasty, and boring. Men with time to idle started knocking pebbles around the sand dunes near Edinburgh Castle, aiming to drop them into natural holes. It was addictive. So many military officers missed scheduled drills so they could play gowf that in 1457, King James II banned the game as a threat to national security. In English the original name of the game means "strike."

What Keiser created is a veritable time machine. So thoroughly does the noise and look of the industrial world recede that one could almost expect to encounter Adam Smith, the moral philosopher, strolling along. It is easy to imagine the great Scot working out his economic insights. Perhaps he would be thinking about how pins, which had been a luxury of the rich, became cheaper than cheap once cutting wire, fashioning points, and creating heads were broken into specialized, repetitive tasks.

It was Smith who showed us that pursuit of self-interest, far more than selfless acts of charity, promotes the general welfare. In making the most of one's labors, Smith said, individual enterprise, as if guided by an invisible hand, unintentionally benefits all mankind.

Among the father of capitalism's lesser known but equally significant insights is what he wrote about the eagerness of business owners to make even more profits by thwarting the
invisible hand. He warned that unchecked self-interest, especially when aided by the
government, will spoil the benefits of capitalism.

"People of the same trade seldom meet together, even for merriment and diversion, but the
conversation ends in a conspiracy against the public, or in some contrivance to raise prices,"
Smith wrote in An Inquiry into the Nature and Causes of the Wealth of Nations. "It is impossible
indeed to prevent such meetings, by any law which either could be executed, or would be
consistent with liberty and justice."

Smith followed this with an observation that is crucial to realizing the benefits of the market.
His sage words are usually ignored by those who cite him as their authority for all manner of
government policies:

But though the Law cannot hinder people of the same trade from sometimes
assembling together, it ought to do nothing to facilitate such assemblies, much less to
render them necessary.

Despite two centuries passing, those warnings seem never to have reached all the
presidents, governors, senators, and cabinet secretaries who take the rostrum at the annual
gatherings of the National Association of Manufacturers, the U.S. Chamber of Commerce, and
the conventions of the bankers, farmers, and every other big trade group.

Throughout his writings Smith warned of the damage done when government interferes in
the market by guaranteeing profits or handing out gifts. This damage can exceed that caused
when government taxes unwisely or imposes rules that needlessly obstruct commerce.

It is a universal truth that it is easier to mine gold from the government treasury than the
side of a mountain. Of a subsidy paid to herring fishermen, called in those days a bounty, Smith
observed that it was all too "common for vessels to fit out for the sole purpose of catching, not
the fish, but the bounty."

Today in America, Smith's "bounties" are everywhere. Whole industries outfit themselves to
catch all they can. Most of these subsidies are available only to corporations and those
individuals rich enough to own a substantial business. Everyone, however, is forced to finance
these bounties.

Lobbyists fashion bounties tailor-made for companies they represent. State legislatures and
city councils deliver them by the tens of billions of dollars each year, taking from the many to
benefit the few. Even without spending money, government often confers benefits on the few. It
does so by establishing arcane rules that create an advantage in the competitive market.
Government also grants a lucrative favor for the few when it allows companies to shortchange
workers and, especially, pensioners.

As well-paying jobs like those in the timber and salmon industries fade away, demand for
subsidies grows in the belief that this will keep people working.

Some of these bounties do not even require an ask. They are just there. Mike Keiser knows
that. He had to file applications' for two small subsidies, one of which hardly seems worth the
bother. He hired lawyers and lobbyists to seek a third. Coos Bay business leaders supported
this third subsidy, believing it was a good way to create even more jobs at Bandon Dunes.

Yet Keiser benefits from four subsidies. The last is by far the biggest. He did not even have
to ask for this one. It flows on automatic pilot in such a subtle way that following the trail of
money under government-set rules of accounting would never reveal its true path. Yet this
bounty totals more money each year than the payroll for Reiser's 325 full-time employees,
including their fringe benefits and even the tips they collect from patrons. By some measures
this hidden subsidy, to be examined in the pages ahead, is several times the size of his payroll.

Beneath the exquisite beauty of Bandon Dunes lurks an ugly truth. The economic
development benefits at Bandon Dunes are illusory. From the perspective of one depressed
community, Bandon Dunes is all win. It provides desperately needed jobs. It is making Reiser's
fortune grow rapidly. But from a national perspective, those jobs are a drag on the American economy -because they cost more than they are worth. So even if you never visit Bandon Dunes, never golf there, you are being forced to pay part of the cost for those who do. Many of them are far richer than you will ever be. They hardly need your help.

If subsidies that cost more than the benefits they generate were unique to Bandon Dunes, they would be of little consequence. But subsidies are not confined to one small and needy place. The harsh reality is that for the past quarter century, policies adopted in the name of Adam Smith, policies that supposedly strengthen the invisible hand guiding the market, have weighed down our economy while simultaneously stuffing the pockets of those among the rich and powerful who solicited them or, like Keiser, were just standing in the right place at a lucrative time. This is our story, not of one free lunch, but of the many banquets at which billions and billions of your dollars are being served to the richest among us.

Chapter 2
Mr. Reagan’s Question

IT’S BEEN NEARLY 30 YEARS SINCE RONALD REAGAN ASKED, "ARE you better off now than you were four years ago?" and tens of millions of American voters responded with a resounding no.

With their votes the citizenry fired not just one unpopular and unlucky president but granted the new president, and eventually his party, broad authority to reconstruct the relationship between the government of the United States and its economic system. By overwhelming numbers, middle-class, well-to-do, and wealthy voters agreed that the economic malaise of the seventies—inflation, skyrocketing energy costs, deficits, high unemployment—was the sour fruit of a half-century of government interference with the "invisible hand" of the nation's market-based, capitalist economy.

The promised solution was to get government out of the way—to let business operate largely free of public oversight in the form of government programs, rules and regulations, or at least with a lot fewer of them. The voters agreed to let the "private sector" of companies, corporations, associations, and charitable organizations take over as many of the duties of government as practical. "Government is not the solution," .Reagan famously declared as the battle cry of his revolution. "Government is the problem."

So, it is only reasonable nearly three decades later to ask a new question: Are we better off than we were a generation ago?

On the surface the answer is obvious: Of course we are. Since 1980, the national economy has more than doubled in size in real terms. More than half the wealth built up since the United States began was created in just the past quarter century. Even taking into account population growth, the overall economic success is striking. For each dollar per person in 1980, the economy in 2006 generated $1.68.

At the same time the costs of many goods have fallen and their quality has improved. The real price of color televisions plummeted more than 75 percent—and for the same money you can buy bigger screens with images so fine they reveal every skin pore or errant strand of hair. Even at $3 a gallon, gasoline in 2007 costs about the same in inflation-adjusted dollars as it did in 1980. Tires last far longer, costing less per mile. Airfares are much cheaper. Long distance telephone calls are virtually free. Useful and fun products that did not exist in 1980 can be bought cheaply, from Dell laptops playing feature-length DVD movies to stylish Razr cell phones to iPod music players, smaller and lighter than a pack of cigarettes, that hold 5,000 songs. The stock market has replaced the local bank as the place where people keep their savings. The inflow of buyers has helped drive the total real value of the stock market to five
times its worth in 1980. Seventy percent of Americans own their own homes. A few million own two. All these residences are collectively worth about $20 trillion.

Yet despite all this success in hard dollars and improved product quality, for the vast majority of Americans the answer as to whether they are better off is again, almost three decades later, a resounding no.

The gross numbers and averages about economic growth obscure one overwhelming truth: The benefits of this bonanza flowed overwhelmingly to those at the apex of the economic pyramid. The base of that pyramid has weakened as average incomes have shrunk and more risks were forced upon them by government policies that favor those at the top.

For the bottom 90 percent of Americans, a group we will refer to as the vast majority, annual income has been on a long, mostly downhill slide for more than three decades. The latest tax data, using a conservative inflation adjuster, show that except for 1999 and 2000, the vast majority's average real income peaked at $31,248 way back in 1973. By 2006 it had fallen to $30,659. Even with three decades of economic expansion, the vast majority has to get by on $11 less each week than it did a generation earlier.

Since the economy grew and grew, where did all the money go? Part of it went to corporate profits, which have been growing much faster than wages. And the portion that flowed to individuals as wages, interest, dividends, and other forms of income generated by the market? The growth went straight to the top.

Of each dollar people earned in 2005, the top 10 percent got 48.5 cents. That was the top tenth's greatest share of the income pie since 1929, just before the Roaring Twenties collapsed into the Great Depression.

Within that top 10 percent, basically those who made more than $100,000, the gains were highly concentrated at the very top. Most of the increase went to the top half of 1 percent and most of that to the top tenth of 1 percent, who made at least $1.7 million that year.

How government encourages this concentration of incomes at the very top, resulting in worsening conditions for most Americans, will be examined in a later chapter. For now, keep in mind this one astonishing fact extracted from official government tax data: in 2005, the 300,000 men, women, and children who comprised the top tenth of 1 percent had nearly as much income as all 150 million Americans who make up the economic lower half of our population. Add the income the rich are not required to report and those 300,000 made more than the 150 million.

This growing concentration of income at the top is nothing like the distribution of income America experienced in the first three decades following World War II. Nor is it like that found in Canada, Europe, Japan, Australia, and New Zealand. Instead it resembles the distribution of income found in three other major countries: Brazil, Mexico, and Russia.

In ways that most Americans do not imagine, but that have been thoroughly documented by political scientists, sociologists, and others, these three nations and the United States are alike. They all have a rapidly growing class of billionaires. They have growing, and seemingly intractable, poverty at the bottom. And all four countries have a middle class that is under increasing stress. These four countries are also societies in which adults have the right to vote, but real political power is wielded, by a relatively narrow, and rich, segment of the population.

Many Americans read about soaring incomes at the top and assume that making a lot of money is the just deserts for those who worked hard and created flourishing enterprises. Real economic growth, after all, requires a society of industrious people who labor, save, invest, and take risks in search of economic reward. Those who succeed deserve the fruits of their labors.

But the distribution of income in a society does not take place in a vacuum. It is also the product of government rules. And those rules were written by people, not handed down from some immutable power. Government can, and does, take from some to give to others. Taxing adults so that children can be educated is an obvious example.
Without even touching money, government can cause huge transfers of wealth within the
economy. For example, the Big Four commercial sports leagues are exempted from the laws of
competition, allowing them to charge higher admission prices than they could get in a free
market. Movie theaters and video arcades enjoy no such protection from competition for the
limited amounts people can spend on entertainment.

Government can, and increasingly does, give money to businesses outright. It also funnels it
in subtle ways to places like the Bandon Dunes Golf Resort. Government also gives away public
assets, such as land or minerals, or sells them for far less than their value. Conversely,
government can use its constitutional power of eminent domain to seize private property from
one owner and give the land to someone else, as it once did for President George W. Bush,
making him a wealthy man in the process.

Rewriting the economic rules that define our society in the past few decades has been done
under the banner of "deregulation" and its promise that less government means more economic
growth. The term itself is a misnomer. No society is free of regulation. Everything has rules,
everything. Baseball's rules go right down to how many stitches are on the ball (108).

In the past quarter century or so our government has enacted new rules that have created
not only free markets, but rigged ones. These rules have weakened and even destroyed
consumer protections while increasing the power of the already powerful.

The distribution of incomes also reflects the tools that society provides citizens to support
themselves. Children who go to schools with minimally competent teachers, outdated textbooks,
and asphalt playgrounds are unlikely to have the same economic success as children who
attend schools with master teachers, the latest books supplemented by music, arts, and
laboratories, and expanses of lawn for play.

We do not live in a laissez-faire economy in which there is no interference from government
and people are allowed to do as they please, operating the economy by making contracts with
one another. We have rules. Over the past three decades the rules affecting who wins and who
loses economically have been quietly and subtly rewritten.

The richest Americans and the corporations they control shaped and often wrote these new
rules and regulations under which our economy now functions. The rich and their lobbyists have
taken firm control of the levers of power in Washington and the state capitals while remaking the
rules in their own interests. They have also imbued private organizations with the power to
make rules that few outside of the process understand, but that influence the distribution of
income. These same people also just happen to be the primary source of the campaign
donations that put politicians in office and keep them there. Politicians, as lawmakers, enact the
rules. As presidents and governors they appoint both the administrators who decide when to
enforce the rules and many of the judges who interpret them.

Rules define a civilization. Without rules, there is no civilization. Over the great sweep of
human history, brute force has held sway. But with the Enlightenment, the spread of literacy,
and mass communication, we began to expand the sphere of rule-making beyond warlords and
kings to the nobles; then to the manufacturers and traders, who started the world on its long
march to economic growth; and finally, in America, to the common man. Wherever the world
has civilizing rules based on some moral or practical principle we see prosperity and freedom,
though not always together.

In America, however, the long expansion of who plays a role in deciding the rules has
ended. The base of influence has begun to contract. In part this is because of the campaign
finance system, which transfers power to those who donate and who steer donations. In part it
is because advances in human knowledge have made the economy so much more complex
that fewer people understand, or have the time to learn about, the issues. Less than a century
ago, Congress debated economic policy by reviewing the life cycle of a cow. Today hearings
are filled with talk of complex abstractions such as a. supposedly naturally occurring rate of
unemployment, monetizing debt, and acronyms such as LIBOR (the London Interbank Offered Rate of interest).

The rules on which we founded this nation sought, imperfectly for sure, to create individual freedom with equal justice and opportunity for all. We spent two centuries refining those rules through experience, political struggle, a civil war that cost 620,000 American lives, and a civil rights movement that wrought change peacefully.

To succeed in the long run, rules must have a moral or practical basis and the support of the people. If society says that you may do one thing and not another, there must be some rationale or the rule will be flouted. There is no legitimacy in officials writing rules as they choose simply because they have the power to do so. Such is tyranny.

The Founding Fathers recognized this when they took that great leap to create our republic more than two centuries ago. They provided for checks and balances, recognizing the need to limit power and to control it. To many people, power is of little consequence, just as many people care little about beauty or riches. But to those who lust for power, of what use is acquiring power unless they can abuse it? In this, the philosophy of the power monger is no different from that of the cancer cell, which mindlessly seeks growth for the sake of growth until it overwhelms its host.

To control abuses of power, we write rules. The nature of those rules determines the shape of the society we live in. The rules we put in place during the five decades following the collapse of the Roaring Twenties economy marked a historic change in America.

Beginning with the New Deal in 1933 and, especially, with bipartisan consensus after World War II, our elected leaders worked to build and strengthen the middle class. Government invested in the nation's most valuable assets: the brains of its citizens. Government financed higher education for millions through the GI Bill and made college free or kept tuition so low that anyone with ambition and smarts could get a degree. Government invested in basic sciences, public health, and medical research; built the interstate highways; and allowed unions to negotiate for higher wages. We created consumer protections and environmental protections. We created a set of rules to make America a land with a large, growing, and stable middle class.

An unexpected by-product of this, fueled by the increased value of human minds and the economic demand this knowledge created, was, the rise of a prosperous upper middle class of people who had plenty but still had to work to enjoy the fruits of their labor. These are the two-income professional couples, the working wealthy whose economic substance is far greater than their political influence.

But in the last quarter century or so, we have turned away from these policies, shifting risk onto those least able to bear it by taking away protections for consumers, workers, retirees, and investors.

For more than a quarter century now our government has been adopting rules that tilt the playing field in favor of the rich, the powerful, and the politically connected. These rules accomplish this by taking from the uninformed, handcuffing law enforcement, squelching whistle-blowers, and making it ever harder for those who were wronged to get redress. The new rules have taken special aim at those supposed economic criminals, the regulators.

The reasons for this shift go deep into the human condition.

In his most famous speech, in front of the Lincoln Memorial in 1963, Martin Luther King Jr. said he had a dream that one day his four children would be judged by the content of their character, not by the color of their skin. We have made great, if far from complete, progress in judging people without regard to that superficiality. But on another front we have gone backward. Today we often value people less by the content of their character than by the contents of their wallet.

In this way we are not unlike the ancients. Just as the Greeks once told tales of those who became intimate with the gods, our society is awash, with television programs, magazines, and
tabloid columns that celebrate the wealthy as gods and demigods of our age. Often we
celebrate wealth for its own sake, without regard to whether it was obtained by means honest or
corrupt, or is used for purposes noble or foul. We not only celebrate the rich for being rich, we
shower gifts and praise on them for nothing more than having money, or sometimes for just the
appearance of having money.

The pursuit of ever more financial zeros and commas on net worth statements has in turn
produced a moral breakdown at the top of our society that has spilled onto the front pages. Most
of the rich have not lost sight of everything but their own net worth. But enough have that they
are twisting our culture and our values in ways that tear at the fabric of society.

In less than three decades presidents of companies have gone from apologizing when they
bad to lay off workers to boasting of the riches they obtained through mass firings. We sing the
praises of investors who owe their wealth not to creating businesses, but to buying companies
in deals that required destroying lives and careers, just so that they could squeeze out more
money for themselves. Too many of us missed the irony when Gordon Gekko, rewriting the
eighth and tenth commandments, looked into the camera and declared "Greed ... is good.
Greed is right. Greed works."

To the addicted, money is like cocaine: Too much is never enough. This mass addiction to
money has grown in the past three decades into widespread theft of shareholder assets by
executives. The well-known cases from the Wall Street bubble—Ken Lay of Enron, Bernie
Ebbers of WorldCom, and Dennis Kozlowski of Tyco—were just the tip of the proverbial iceberg.
Many more got away with cheating their shareholders, their workers, and the taxman than were
ever considered for indictment.

One of the new rules has been to make sure that there are far too few cops on the beat on
Wall Street to even write down all the legitimate complaints, much less pursue more than a
handful of wrongdoers. More important, the actions of Lay and Ebbers and the others were just
part of a massive shift in practices and policies that continues. The Wall Street scandals are
not over; the conduct they revealed is just becoming institutionalized.

Steve Jobs, a founder of Apple computers, was awarded millions in stock options at a board
of directors meeting that never took place. When given too much change by a clerk, the
principled person returns the money. Jobs arranged to have his fraudulently issued options
exchanged for restricted stock worth hundreds of millions of dollars. The government brought
civil charges against Apple’s general counsel and its chief financial officer, the latter of whom
admitted wrongdoing, gave up $3.5 million, and said he had warned Jobs about the improper
pay. Still, by late summer 2007 the government had taken no action against Jobs. The Apple
board, which included Al Gore, portrayed Jobs as an unknowing victim of complicated rules
even though they have been in effect since before Apple went public decades ago.

Jobs was hardly alone in the stock options scandals, "which involved thousands of
executives working for hundreds of companies. Many of these executives took money from
shareholders through deliberate, calculated actions, including fabricating records. They differ
from bandits only in that they wielded pens to steal with stock options instead of pointing pistols
while demanding cash or jewelry. Their techniques were subtle and not overtly violent, but for
society they are worse than street robbery, for their actions undermine the legitimacy of
society’s rules in ways that bandits cannot.

Unlike the common thief or bandit, these executives have the best and brightest lawyers to
explain away misconduct or to obfuscate. In the rare instances when indictments are handed
up, the cheated shareholders sometimes end up paying to defend the thieves who robbed them.
Added to this are the legions of publicists who are paid to report what their bosses want us to
hear, the antithesis of journalism’s call to pursue the facts without fear or favor.

The ranks of these image shifters are growing, while across the country many journalists are
being laid off as people pay less attention to the news, reducing further the chances that
inconvenient facts will become known. Nor have other watchdogs fared better. Later we will examine the fate of the brave bureaucrat who first exposed the stock options frauds.

Best of all for the stock options thieves, they had a friend somewhere in the White House. The federal prosecutors who had dared to go after them were fired. Yet in hearing after hearing before Congress no one would say just who made the firing decisions or why, not even the attorney general of the United States. We were told only that the prosecutors performed poorly, despite sterling written evaluations to the contrary. So not only have the standards of business been corrupted by the love of money, but also one of the most powerful and sensitive centers of power in our government, the Justice Department, has been compromised in the service of greed.

The new rules also enable executive pay schemes that reward those who mismanage companies by handing them vast personal fortunes, even though they destroyed wealth for everyone else. Many of these executives make money in a world in which they face little or no risk but can reap great reward, another area in which Adam Smith, the father of capitalism, warned us about moral failure and its corrosive effects.

All of this can be traced back to how the government sets rules and enforces them. Many wasteful rules are gone. But so are many virtuous rules, replaced by ones that encourage and even reward misconduct.

At the same time that the rules have been rewritten to favor the already rich, new rules have been -written that ensure harsh treatment for the poor, whether they are indolent or the victims of such misfortunes as being born not so bright or healthy as the average person.

In this era of rules for the rich we act as if poverty is a free good, meaning in the argot of economists that it is not scarce but readily available. In that sense poverty is indeed a free good, but it is not a cheap one. Coping with the foul effects of poverty costs us a half trillion dollars a year, a sum greater than what we spend on Social Security benefits. Poverty wastes minds and spirits, robbing all of us of opportunity. When poverty fosters crime it costs us more than the harm done to our wallets and our safety, or even the expense of a system to hunt down, prosecute, and incarcerate offenders. It makes us less trusting, less willing to see ourselves as one people in our great experiment in self-governance. How we deal with poverty as a society is a major factor in why the vast majority are worse off, for unlike the superrich, they cannot live in gated communities, fly in private planes, or hire bodyguards for themselves and private schools for their children.

For a nation whose leaders frequently invoke their belief in the Bible, curious indeed is how the political rhetoric ignores the overriding duty of the New Testament to care for the poor. "Sell all that thou hast, and distribute unto the poor" for "it is easier for a camel to go through the eye of a needle, than for a rich man to enter into the kingdom of God." Jesus said-those who believe must sacrifice for the poor; we sacrifice for the rich at the expense of the poor.

The worst poverty is that of the man who does not know how to fish. Even if he has the means to obtain hook and line, of what good is a tool that one does not know how to use? People with the skills to sustain themselves and improve their lot build our society. Denying the basic skills needed to succeed, starting with a decent education so that one can comprehend more than simple instructions, is itself a form of crime.

Under what theory of morality do we grant those already in a superior economic or legal position ever more power, especially when that power derives from rules in fine print that defy normal human understanding?

Consider one example, the business of lending money. Usury laws that protected consumers against rapacious lenders existed until 1978. Now they are gone because of a Supreme Court decision. In that case the high court warned Congress that it needed to enact new laws to protect borrowers. That warning was ignored in the lucrative trade of selling access, if not votes. In place of rules that protect the vulnerable, the in-numerate, and the foolish, our government has set forth onerous new rules that reward those who prey on the poor. We used
to prosecute loan sharks. Today a television commercial featuring Gary Coleman urges people to borrow money at 99.25 percent interest, paying back almost $10,000 to borrow a quarter that much. These new rules help Goldman Sachs and Lehman Brothers and Citibank exploit the poor, the unsophisticated, and the foolish. These lenders, or their fronts, can now charge rates and impose penalties that were illegal, even criminal, a generation ago. These and other lenders engage in conduct that goes way beyond that of Michael Milken, the junk bond promoter who made a fortune pushing risk onto corporate balance sheets the way addicts inject heroin into their veins. Milken was vilified by many; not so the latest usurers.

The result? In the past 25 years, one American family in seven has sought refuge in federal bankruptcy court. They filed for relief from their creditors, not to immorally scam the system, but because they were forced into it. Exhaustive research by Elizabeth Warren of Harvard Law School and her associates into bankruptcy court filings has proven that the vast majority of people seek refuge from creditors after any two of three events combine: divorce, job loss, or major medical problems.

The response of our leaders to this is instructive, for it shows how much of the wisdom of our founders we have lost. Two centuries ago, a sitting justice on the Supreme Court, James Wilson, was jailed for not repaying money he had borrowed to invest with a fellow signatory to the Declaration of Independence. Back then debtors could avoid imprisonment by securing all doors and windows, conducting business by means of notes tossed in and out of the upper-floor windows. Those sent to gaol usually were held in a place with few locks and keys, where you brought your own furnishings and food. Imagine what would happen today if a brilliant jurist who filed bankruptcy were nominated for the Supreme Court.

Today we do not jail debtors. But under a new bankruptcy law written by credit card lenders, we deny some people the fresh start that the constitutional provisions on bankruptcy were designed to ensure. Senators and representatives, after a decade of gathering up campaign contributions from the lenders and their lobbyists, adopted rules that can leave the sick and the jobless at the mercy of corporate Javerts pursuing Jean Valjeans until they die.

In this same era we have turned what were once denounced as vices into pastimes. Witness the explosive growth of casinos and other gambling. And now we even subsidize some of the gambling halls with money that was promised to help the poor, the elderly, and the sick. In this way does Donald Trump benefit from money intended for the least among us to burnish his image as a supposed billionaire.

The checks and balances provided by oversight, inspection, investigation, and, in extreme cases, prosecution have all been gutted in pursuit of deregulation and supposedly smaller government. It has become difficult and sometimes impossible just to find someone to take a complaint that an employer refused to pay wages or locked people in to make them work or stole the retirement money. When there is no policeman on the beat the greatest beneficiary is not the taxpayer who is relieved of the cost of maintaining that police officer, but the thief. And when bridges, tunnels, and dams are not inspected and repaired we are all in danger.

Despite all the deregulation rhetoric, government grows ever bigger. The number of federal government workers shrinks, but the ranks of people who are hired on contract at much greater cost increases. In 2000 workers hired on contract cost our federal government $207 billion. By 2006 this had swelled to $400 billion—rivaling the expense of either Social Security or interest on the federal government's growing debt.

These contract workers typically cost twice as much as civil servants doing the same work, yet they are even less accountable. In Iraq we court-martial and imprison soldiers who under the stress of relentless urban combat kill innocents in a fit of anger or misjudgment. But the contract soldiers who fight alongside them, at two to ten times the pay, operate in a law-free zone, any killings they commit for foul reason unpunished and, some of our leaders assert, beyond the reach of any law.
At home, government and companies cooperate in withdrawing contracts and other documents from the public record. The profits generated by these companies are used, in part, to lobby for more contracts that drive up costs even further. Executives of these companies are also strategic donors to politicians, helping to ensure the continuing flow of tax dollars to their businesses. This is a benefit unavailable to even the most empire-building bureaucrat.

On another front, government is easing up on rules that ensure clean water to drink and fresh air to breathe. When companies dump toxics instead of cleaning up at their own expense, they force everyone to bear the costs of environmental pollution. The Cuyahoga River in Cleveland was so polluted with flammable chemicals that it caught fire at least nine times starting in 1868. But it was not until the 1969 fire brought national news coverage that national debate ensued about pollution and economic growth. Only then did government adopt rules to give us cleaner air and water—and thus save us some of the anguish and the cost of asthma, cancer, and heart disease. But under the guise of deregulation, many of those rules are being relaxed, repealed, or ignored.

Now we face a similar problem that damages lives and costs us dearly. A growing array of businesses and whole industries profit by dumping their real costs of capital, equipment, and even labor onto the taxpayers. This new problem is economic pollution.

We shall see the economic pollution caused by just one industry in which Tyco International is a major player. This industry owes its entire profits not to unleashing the forces of competitive business, but to silently shifting its largest labor expense onto the taxpayers.

Under deregulation we have created a host of dependent companies that hold out their very large hands to take money from Washington, the state capitals, and towns and cities everywhere. Wal-Mart, Target, and a host of lesser-known retailers all count on government handouts when they open new stores. These subsidies serve not only to enhance their profits, but also to undermine locally owned businesses that are crucial to the social fabric of communities. These retailers are not, by far, the worst offenders, however. Examples abound of companies and industries that foul the national ledgers, degrading the income and wealth of us all through economic pollution.

Sometimes the banner of deregulation can make people rich at the cost of others’ lives. We will follow the career of an economics professor who embraced the idea of getting government out of the way of business, yet made his business career cultivating government, leaving behind a trail of deaths and costs that were shifted onto the taxpayers. His name is John W. Snow and he rose to become our government’s Treasury secretary.

The benefits of the nation’s overall growth in incomes and wealth flow like a mighty river of greenbacks to the powerful, wealthy men and women who have twisted Mr. Reagan’s revolutionary creed. They want more government, just so long as it makes them richer. They have captured for themselves and their class the benefits and rewards of a government that is today as intricately involved with the private sector as it ever has been. They have found the proverbial free lunch, enjoying a sumptuous feast and leaving their bill for the rest of us.

There is, of course, no such thing as a free lunch. Every cost must somehow be accounted for and paid. When bars offered a free lunch in the 1800s, the cost was built into the nickel charge for beer. For our purposes, a “free lunch” refers to an economic benefit received by one party that is paid for by another by government action or inaction.

For example, when a developer receives a plot of land free or at a discount, your taxes may have paid to buy it, the original owner may have been cheated out of its market value, or someone else not at all obvious got stuck with the real cost. When an executive shortchanges the pension plan, making his company appear to be more profitable, he inflates the value of the company stock and therefore his stock options. When the pension later fails and the workers get less than what they were due, or the taxpayers have to make up the part of the shortfall guaranteed by the government’s Pension Benefit Guarantee Corporation (PBGC), the executive
gets a free lunch. Our economy is riddled with these subsidies, many of which are intentionally subtle and hard to detect.

Executives’ free lunch is a major factor in America's growing inequality and why our economy is closest to those of Brazil, Mexico, and Russia in how it distributes resources. The evidence of a growing divide between the superrich and everyone else in America is so overwhelming that all but the few lightweight ideologues among economists acknowledge this harsh truth. When George W. Bush was running for president in 2000 he famously referred to a white-tie audience at a Waldorf-Astoria dinner as the "haves and the have mores." He said that "some people call you the elite. I call you my base." By 2007 even the Bush White House had publicly acknowledged that the divide between the superrich and everyone else was a real concern.

Since that talk about the "have mores," a national debate has arisen over just what is going on. Why are the rich getting so much richer, while the middle class struggles and the poor fall behind? Why are the richest of the rich—billionaires—pulling away even from those whose net worth is in the many millions? The cable and broadcast television networks, national news magazines, and scholarly conferences have all examined the question of why inequality is growing and what it means.

Is education behind increasing inequality, as the White House says? Or could it be globalization, with cheap labor in China and India combining with free trade to create new world-scale fortunes? Or is it technology, from ever-faster silicon chips to drugs that soothe what ails you? Or maybe it is just a proper reward for talent, with corporate executives getting their fair share of the wealth they create for shareholders.

All of those answers are right—and wrong. What they all have in common is that they are just superstructures arising from the same foundation. The real answer, like the focal point of Edgar Allan Poe’s "The Purloined Letter," is right in front of our eyes. We just have to discern it amid the clutter of daily living.

Since 1980 it has become official policy to ensure that the rich receive the benefits of government. This is a shift from government policy in the years after World War II to grow the middle class, remaking America into a land of better-educated and healthier people, a land of suburbs and single-family homes where opportunity was based less on status and wealth than on hard work and merit.

So who is better off today than they were 30 years ago? The middle-aged factory worker whose plant closed even though it earned a healthy profit or the Wall Street investment banker who brokered the deal to ship the machine tools overseas, where pay is three or four dollars per day? The billionaire CEO or the middle manager whose company health insurance has been cut yet again? The war contractor or the brain-injured veteran?

Nearly three decades after Mr. Reagan’s revolution, the single biggest piece of our economy, a third of it, is still government. From raking leaves in city parks to buying stealth bombers that cost $1.2 billion a copy, government takes the same share. But money for the basics that make society work is growing scarce. From those leaves in the park to textbooks to highway bridge maintenance to food safety inspections, money is dwindling because so much has been diverted to the already rich through giveaways, tax breaks, and a host of subsidies that range from the explicit to the deeply hidden.

Evidence that the elites have captured the government and are milking it for their own benefit is so overwhelming that, on one level, you can find it as an unstated assumption in everyday news reports. With this idea in mind, the degree to which it has become part of the background to our national political, economic, and social discussions will leap out at you from the pages of the newspapers and the observations of the pundits. It has become the basis for advertisements about how buying a luxury home or a share of a corporate jet may be within your reach, thanks to an assist from the government.
In the pages ahead we will examine just how thoroughly government has become the servant of the rich, showing how:

• Warren Buffett's company has a two-thirds-billion-dollar, interest-free loan from our government for more than 28 years, just one of many ways that the government has boosted the investment returns for which he is so renowned.

• President George W. Bush owes his fortune not to the oil business, at which he failed, but to a sales tax increase that was funneled into his pocket, a fortune further enhanced by his paying millions less in income taxes than he should have.

• George Steinbrenner not only gets lavish subsidies for his baseball team, he also made a fortune from a scheme that damaged national security.

• Paris Hilton has resources to cavort shamelessly because her grandfather, thanks to government, snatched a fortune away from poor children.

• Donald Trump benefits from a tax that was enacted to help the elderly and the poor, but part of which is now diverted to his casinos.

And beyond these brand-name Americans are legions of the super-rich of whom, few have heard, who owe their fortunes less to their enterprise than to the generosity of our Uncle Sam and his nieces and nephews in state and local government.

There is a reason, that 35,000 people are registered as lobbyists in Washington, double the number of lobbyists employed there in 2000. They are there to seek favors, from outright gifts of your tax dollars to subtle changes in rules that funnel money to their clients, thwart competition, hold you back, and buoy others. Among the ironies is that many of the most damaging policies have been created in the name of Adam Smith, the original modern economist. Indeed, if that eighteenth-century Scotsman could come back today, he might smite the plutocrats setting the government's bill of fare and cast out the rule-changers. No doubt he would remind us of his eighteenth-century insight that subsidy economics are inherently inefficient and wasteful, often costing several dollars to give away one.

Back in 1964 Ronald Reagan started telling a story he repeated many times on the long road to the White House. It was about how the masses ruin democracy by sucking dry the nation. Reagan attributed his tale to an eighteenth-century British historian whose name he consistently mangled, Lord Woodhouselee, Alexander Fraser Tytler. Professor Tytler never wrote the words attributed to him, but they have become central to the argument used by those who came to power with Mr. Reagan, and those who followed, to justify their policies. In one tape-recorded speech, in 1965, Reagan said:

A democracy cannot exist as a permanent form of government. It can only exist until the voters discover they can vote themselves largesse out of the public treasury. From that moment on the majority . . . always vote[s] for the candidate promising the most benefits from the treasury with the result that democracy always collapses over a loose fiscal policy, always to be followed by a dictatorship.

Whoever wrote those words got it partly right. But just as Karl Marx never envisioned commercial sports as the opiate of the masses, neither did most of those who agreed with Mr. Reagan consider the prospect that the elites would be the ones to vote themselves the public's treasure. Of course if Reagan's words were accurate he would never have been elected or re-
elected to the White House, his Democratic Party opponents each offering the public more largesse from the Treasury.

Let’s begin by examining two free lunches. The first case examines the moral hazard in a government policy that rewards reckless corporate behavior. The second explores the reasons so many jobs are headed offshore, and who benefits.

Chapter 3
Trust and Consequences

HALF AN HOUR BEFORE DAYBREAK ABOARD THE AMTRAK SILVER Star heading to New York from Florida, the South Carolina skies were fair. The thermometer hovered comfortably in the low seventies. It was the start of the glorious final day of July 1991. The clickety-clack rhythm of the rails rocked the 407 passengers as they dozed. Among them was Paul Palank, a Miami police sergeant on his way to meet his wife and children for a family reunion near the nation’s capital. Palank loved trains as much as he feared flying.

At a minute past five, the train approached the town of Lugoff, a farming community that the DuPont Company transformed into an industrial center when it built a chemical plant there in 1948. The same tracks that supported Palank and his fellow passengers on their journey north often carried CSX railroad hopper cars filled with chemicals to make Orion, a synthetic "miracle fiber" that came out of World War II research. On a siding parallel to the Silver Star stood a string of empty hopper cars waiting for a CSX train to haul them away to be refilled. Freight traffic was so much more important, and more common, than passenger trains that railroad companies didn’t name the switch Lugoff after the town, or even after the DuPont factory. Railroad engineers called the train switch the Orion Crossing.

The Amtrak train was traveling two miles an hour below the posted speed limit when the twin locomotives and the first twelve cars passed over the Orion Crossing. Then the switch broke.

Six passenger cars hurtled off the tracks. The impact flipped over the first hopper car, whose hardened steel wheels cut like a knife through the metal skin of the passenger cars. By the time everything came to a halt, 77 people were injured and 8 were dead, including Sergeant Palank. He was 35 years old.

More than eight hours later, Angelica Palank arrived at the train station in Alexandria, Virginia, to greet her husband. Eager to see him, Angelica pushed her youngest son Taylor’s stroller just as fast as five-year-old Josef could move his little legs to keep up. As the family waited on the platform, a woman told Angelica that there had been an accident. Angelica did not believe her. A northbound train approached and she felt relieved. When it blew by the station, Angelica turned anxious. She and the children hurried downstairs, hunting for the arrivals-and-departures board. Train 82, the Silver Star, was not listed. She asked a .ticket clerk, who gave her an 800 number to call. The clerk pointed the frantic young mother to a pay telephone. A stranger’s voice at the other end delivered the horrible news.

In the weeks ahead the families of the injured and dead settled their claims, discovering in the process how remarkably modest payments are to the survivors of transportation crashes and to the heirs of those less fortunate. Only Angelica Palank refused to go along. She did not believe the crash was an accident. She did not believe her Paul died because of some random bit of misfortune that no one could have seen coming. Determined to learn all she could about how Paul was killed, Angelica sued.

To get the truth Angelica Palank would have to put herself through law school. She could never flinch as she took on one of the richest corporations in America, a personal trial that extracted a heavy, toll on her and her children. Ten relatives died in one year, but still she stuck to her cause. Friends and neighbors cut the grass and brought meals. At one point, she nearly lost her home to unpaid property taxes. It was scary and nasty, as is all litigation about real
wrongs. When she found lawyers willing to take her case—Christian D. Searcy and F. Gregory Barnhart in West Palm Beach—their work began to peel back layer upon layer upon layer of corporate denials and superficial government inquiries. In time they uncovered a trail pointing not to bad luck, but to policies with a blatant disregard for safety.

The compulsion to increase profits can blind men to risk, especially when those at risk are strangers. Society imposes rules on corporate behavior to protect public safety in the face of baser impulses. These rules require enforcement, though. They also require a corporate culture that appreciates the importance of safety. As Adam Smith wrote, "The object of justice is the security from injury, and it is the foundation of civil government."

For more than two decades, the ideology of blind faith in markets, combined with the view that government is inherently inferior to self-regulation, has caused politicians to trim enforcement funds. Trim long enough and the little cuts sever muscle. Ultimately they slash to the bone. Such was the case in the derailment of the Silver Star. But it took one diligent woman and her lawyers more than a decade to demonstrate how harmful these ideas about trusting all companies to do right can be.

Before Angelica Palank’s lawsuit got going in earnest, the National Transportation Safety Board examined the crash. The investigators quickly deduced that the accident was not a chance happening. Rather, it resulted from improperly done repairs. Railroads—like airlines, meat-packing plants, and other businesses where hidden dangers lurk—employ inspectors to double-check what safety workers do. This saves lives and avoids lawsuits. Yet the safety board found that the CSX inspectors somehow failed to notice the Orion Crossing was in a dangerous state of disrepair.

CSX maintenance crews had used shims to level the crossing, even though the switch "is not designed for adjustment." Granite rock, known as ballast, covered the wobbly switch mechanism. Once the investigators cleared the ballast away, they found this vital switch was without a proper pin to hold the pieces in place. The switch was held together with nothing but a rusty nail. The safety board concluded that CSX inspectors "could have and should have seen the switch deficiencies during a normal inspection and, with appropriate action, could have prevented the accident."

Although businesses complain frequently about excessive government paperwork, neither the railroad nor the Federal Railroad Administration, the agency that is supposed to set and enforce safety standards, required much recordkeeping. CSX’s inspection process, the safety board concluded, "lacked an adequate documentation procedure."

The roadmaster and some of the work crew used the jury-rigged shims because their employer never allowed them enough time or money to do their jobs properly. CSX cut corners to inflate its profits, which in turn meant riches for its executives, whose pay packages were tied to reported profits and the price of CSX shares.

John W. Snow, a lawyer and college economics professor who rose to become the CSX chief executive, was an early champion of markets as the most efficient regulator of transportation industries. It was an idea he promoted as an assistant secretary in President Ford’s Transportation Department before he joined the railroad. Under his leadership, the railroad aggressively cut costs.

CSX publicists encouraged articles about Snow's drive for efficient capital investment. Typical of the stories was one praising the company's change from four engines to three on some hauls. These trains arrived later, but still on time, while saving the cost and fuel of an entire locomotive. His handlers did not make him available for stories about the bridges that became eyesores after years, and then decades, without painting. And in polishing Snow's image as a champion of efficiency, they certainly did not encourage anyone to look at the systematic shortcuts in safety.
Palank and her lawyers dug deep into the cutbacks in safety, deeper than the National Transportation Safety Board. They looked for systemic changes, for a pattern. Eventually they found CSX workers who would talk: Alien Clamp and Robert Griffith.

For three years, Clamp was an apprentice foreman under Buster Bowers, the roadmaster on the section of track in South Carolina where Paul Palank died. Clamp testified that it should have been obvious to CSX that there were too few men to perform the required safety inspections and maintenance. In the crew's race to cover track as quickly as possible, Clamp testified that Bowers never "performed a disassembly inspection, never walked a switch, and conducted no inspection, or inadequate inspections." Clamp said under oath that Bowers even directed him to fill out false inspection reports.

CSX tried to get this testimony thrown out. Five years had passed between the time Clamp last worked under Bowers and the Lugoff crash. CSX said that made the testimony ancient and unreliable. A Florida state appeals court let the testimony stand, noting that the other rail worker, Robert-Griffith, confirmed that Bowers also had instructed him to falsify inspection reports.

At trial, CSX urged jurors to not believe the former employees. One Palank lawyer, Greg Barnhart had a counterargument: "CSX said, 'Why would we do that?' We said it was to save $2.4 billion," the money CSX had saved on maintenance.

In his own way, Barnhart was showing the jury the deadly effects of economic pollution. He explained how CSX benefited because it shifted the cost of maintaining safe tracks off its owners and onto the unsuspecting public, which unknowingly assumed a risk of injury or death.

The first jury that heard the Palank case awarded the family $6.1 million as compensation for their loss. Then came the second trial before a new jury, its purpose to determine whether CSX should be punished on the theory that the Lugoff crash was the result of greed encouraging a corporation to turn a blind eye to danger.

The second jury heard all about the $2.4 billion not spent between 1981 and 1993, most of those the years when Snow was fully in charge of CSX. The jury heard how in 1987 the Federal Railroad Administration had told CSX that its practices were unsafe. They heard how the company stuck to its cost-cutting policies anyway.

Testimony showed that the National Transportation Safety Board findings, alarming as they were, had missed much more damning facts. A panel of three Florida judges later wrote that the Orion switch was defective and the cross pin had been broken for at least seven months prior to the derailment. The Orion switch had been installed backwards ten years earlier, and part of the broken cross pin was buried under several inches of [granite] ballast placed between the ties more than seven months prior to the derailment. The evidence further shows that a proper inspection would have revealed the broken cross pin. In, addition, there is evidence that CSX had actual knowledge that the cross pin was defective because the record shows that CSX periodically greased a plate installed on the switch with graphite to make the switch operate.

What that meant was that for a full decade CSX had escaped paying the cost of repairing the Orion switch. Every day CSX trains loaded with freight, including toxic chemicals, crossed the Orion switch. So did Amtrak passengers, unaware they were riding over the equivalent of a bomb waiting to go off.

The jurors were incensed. They awarded the widow and her children $50 million in damages, taking 1 percent of CSX's net worth. The jurors also wrote a note on the verdict form: "It is hoped that CSX trainers will emphasize [the] need to inspect both ends of cross pins."

Judge Arthur J. Franza upheld the punitive damages award. He delivered a stinging rebuke of CSX. "The clear and convincing evidence shows that Silver Star No. 82’s tragic derailment
was caused by willful, wanton negligence," Judge Franza wrote, adding that he considered the railroad's conduct to be "borderline criminal."

"Clearly," the judge wrote, CSX "knew of the peril created by its reductions and the company chose to proceed on its own course."

Then the appeals began. Three Florida judges who took up CSX's pleas for relief ruled against the railroad. The judges said that testimony by former employees showed that "CSX knowingly endangered public safety."

The judges called CSX's conduct a "flagrant violation of the public trust . . . Keeping with the policy that punitive damages should punish and deter, a jury of six reasonable persons concluded that $50 million would adequately communicate to this defendant that this type of reprehensible conduct should not and would not be tolerated."

The appeals court approvingly quoted Judge Franza, who ruled that while CSX saved more than $2 billion, "society paid with eight human lives. . . . The clear and convincing evidence showed that the price of cost-cutting safety to turn over larger profits is too great of a price."

CSX then appealed to the Florida Supreme Court, saying that its conduct was reasonable. Further, any damage should be based only on the value of the section of track near the crash site, not the company's entire net worth. The Florida Supreme Court rejected CSX's claims.

Finally the litigation came to an end in early 2002, more than a decade after Paul Palank's death, when the United States Supreme Court said that it would not hear CSX's appeal.

Angelica Palank said she felt that she had accomplished her goals. She had proven that the crash on July 31, 1991, was not bad luck but the predictable result of deliberate misconduct that flowed from the top of the company. After paying her lawyers and income taxes on the punitive damages, she donated the rest of the money to a foundation in her husband's memory. Today a few million dollars remain to finance grants for a cause her husband cared about deeply, abused and neglected children in and around Miami.

CSX said it was disappointed that the Supreme Court would not give it a chance to show that the jury and the Florida judges were wrong. CSX even suggested the proper punitive damage was zero. Kathy Burns, one of the CSX publicists, called the punitive damage award "unwarranted and excessive."

Lobbyists from CSX and other companies had, in the meantime, descended on Tallahassee to persuade the state legislature that big punitive damage awards were bad for business. Today Angelica Palank could not get $50 million in punitive damages because of a law signed by Governor Jeb Bush. It severely limited any future damage awards no matter how awful the misconduct.

Even with the award that the courts left standing, the cold calculus that cutting safety is immensely profitable remains in place. The total damages to the Palank family, both to compensate them and to punish the company, came to a bit more than $56 million. The money paid to all of the others, who settled without litigation, was a fraction of this. Viewed in the context of what CSX saved, however, even the total damages were not punishment at all, just a minor cost of doing business. For every dollar CSX saved by cutting corners on safety it only had to give back four cents.

We teach children that crime does not pay, but the grown-up truth is that "borderline criminal" behavior can pay handsomely.

From the perspective of CSX, or any railroad, the economics of shortchanging safety continue to make sense. Two years after the Palank case ended, James E. Hall, a former chairman of the National Transportation Safety Board, told The New York Times that the loss of lives in rail accidents reveals "a systemic failure . . . It's been something that has just not grabbed the attention, unfortunately, of the public." He was speaking of deaths at rail crossings, but his point is equally valid across the board.

Although many travelers worry more, as Sergeant Palank did, about dying in a plane crash or being hit by an 18-wheel rig on the highway, since the year 2000 Americans have been dying
at the rate of about one per day at railroad crossings. A few of these deaths are suicides by train or the bloody product of fools driving around signal arms. Some are also the result of crossing arms that fail to activate. Others occur because signal arms sometimes bob back up after coming down, endangering even careful drivers and their passengers. At crossings with no signals, foliage that the railroads have not trimmed in accordance with the rules add to the death toll as people drive unaware onto tracks just as millions of pounds of steel bear down on them.

In Britain only about 18 people per year die at rail crossings. Major crossings have fencelike barriers that cars cannot flit around. Even after taking into account that America has five times as many people as the United Kingdom, the death rate at crossings in America is four times that of Britain.

Between 1995 and 2000 derailments increased 28 percent, nearly triple the 10 percent increase in freight hauled. Yet even with more accidents and more deaths, the economics of cutting spending on safety are compelling from the railroad's perspective. The fines imposed for safety violations in the United States are minor, more like parking tickets than deterrents. The maximum fine is $20,000. The average fine is about $1,600. So the railroads play the percentages, weighing risk versus cost. Risk wins easily.

Most switches are safe. And not every unsafe switch will fail. Keeping every one of the thousands of switches around the country in proper repair is very costly, especially as a competitive market drives transportation prices down. After all, the jury-rigged repair of the backward Orion switch held for years. Those switches that do fail will probably damage cargo, not kill people. Even killing people doesn't cost the railroads very much. As the CSX case demonstrated, all the injured and the families of the dead except Angelica Palank accepted their modest settlements quickly. So long as insurance costs less than repairs, this dangerous trade-off will continue 110 matter what the railroad industry says about its commitment to safety.

Since the imperfect rules of the marketplace actually reward dangerous risk taking, the only thing that could prevent this lethal gamble is effective government regulation. In this century just 4 of the first 3,000 rail-crossing accidents were fully investigated because of ever-tighter budgets for government safety offices. One railroad, Union Pacific, even said that federal regulators were so overworked they told the railroad to "stop calling" after every crash, which explained a big drop in minor accidents it reported.

The industry, since 2001, has steadily tried to assure the public that all is fine with the railroads because accident rates are falling. Then came eight CSX derailments in seven weeks as 2006 turned into 2007. That prompted the Federal Railroad Administration to send inspectors out across 23 states. Their inspections of CSX found more than 3,500 violations, 199 of them rated serious cases of failure to comply with the law.

What no one reported at the time is that railroads are by far the most deadly form of commercial transportation in the country, the exact opposite of the industry's carefully orchestrated campaign to deceive with statistics. "Freight rail is by far the safest way to move goods and products across the country," the Association of American Railroads tells the public.

Few people realize how deadly trains are because crashes usually involve one or two deaths and thus get little attention in the news. They also lack the emotional appeal of plane crashes, which fill us with a sense of dread because flying through the air at nearly the speed of sound seems to defy common sense.

Still, airliners are America's safest form of transportation by far. Some 600 million passengers board planes each year, yet often a year and sometimes several years pass between fatal crashes. Big trucks kill about 5,100 people per year, trains about 930, and airliners about 140.

Measure deaths by the distance traveled, however, and trains are 52 times more deadly than trucks. Trains kill 130 people per 100 million miles traveled, compared with 2.5 deaths in big-rig truck accidents and 1.9 deaths in plane crashes, Transportation Department statistics
show. It is easy to miss that because the official government statistics use a measure of only a million miles per accident for trains, but 100 million miles for trucks and airliners.

Bad as those official figures are, they severely understate how dangerous trains are. Truckers drive on highways surrounded by cars. Trains run long stretches through rural areas where there are no crossings. In such places a crash would hurt only the engineers on board and perhaps some jackrabbits. If we had a measure of people killed per 100 million miles of travel in populated areas, where roads cross-tracks and homes are almost as close by as freight cars parked on sidings, the death rate would be many times greater than the official figures.

Just as the CSX workers found ways to deal with demands that they inspect more track in a shorter amount of time, government agencies also adjust to unrealistic budgets. Some workers in private businesses fake reports and make slipshod repairs. The more noble of them work off the clock if necessary in an attempt to set things right. Some CSX workers testified that they worked extra hours for no pay, but that even these efforts were not enough to overcome the callousness of the railroad’s management and its dogmatic belief in market ideology.

The government agencies, without anywhere near enough money to oversee safety, play similar games. They tell Union Pacific to not call, they write superficial reports, and when it comes to accidents at rail crossings, they thoroughly investigate only 4 out of 3,000 cases.

These responses are human nature at work, as predictable as eating when hungry. Give managers more than they can possibly do and they will find a way to redefine their workload to what can be done. When cuts in budget and personnel increase gradually, the public unwittingly accepts unsafe conditions, just as the clickety-clack of the rails lulled passengers into sleep until the Orion Crossing’s deadly repairs gave way.

Even a reliable system of safety rules, means nothing, however, if there are no consequences for misconduct. At the end of the day, after litigation that went all the way to the United States Supreme Court, for CSX there were no consequences. CSX paid nothing for its recklessness.

CSX simply sent a bill to Amtrak seeking reimbursement. It sought, and got, the full amount it had paid to the injured and the families of the dead. Amtrak even paid the $50 million that the jury ordered to punish CSX. Since the government owns Amtrak, what CSX did, in effect, was to stick the taxpayers with its bill.

The jurors, though, had no idea. Reporter Walt Bogdanich, who won a Pulitzer Prize for exposing unsafe rail conditions, grows animated when he describes “this sham trial, an absolute sham in which everyone on the jury thought CSX was being punished and CSX knew that no matter what happened it would not cost them one cent.”

When Amtrak was formed in 1971, the freight railroads persuaded Congress to let them stop carrying passengers. But they wanted more than to shed that obligation. The freight railroads wanted to be insulated from any claims arising from Amtrak using their rails. The railroads reasonably sought not to be responsible for claims arising out of misconduct by Amtrak. A crash caused by a drunken Amtrak engineer or a badly repaired axle on a passenger train should be paid for by Amtrak.

Congress looked out for the freight railroads, which unlike Amtrak were a vibrant source of campaign support. A federal law shields the freight railroads from claims by Amtrak passengers and anyone hurt by an Amtrak train. Under federal law all claims arising from Amtrak passengers, even in cases where Amtrak was not at fault, must be paid by Amtrak.

Under these rules it does not matter that Amtrak did nothing “wrong, its trains traveling below the speed limit, its crew alert and sober, its rolling stock in sound condition. It does not matter that the courts found the cause of Paul Palank’s death was CSX’s reckless disregard for human life. Under the contract, all that matters is, at the moment the rails or a switch or a shoddy repair job gives way, does the train passing overhead belong to Amtrak? Only if a freight train is overhead when the failure occurs is the freight railroad on the hook for the damages.

What this means is that CSX and John Snow got a free lunch. You got stuck with their bill.
Economists have a term for situations in which someone gets rewards but has little or no incentive to avoid risk: a *moral hazard*. The term is usually applied in insurance cases. A policy that covers every cent with no deductible may cause people to be less vigilant about husbanding their lives or property. A policy may even encourage the unscrupulous to burn down a failing store to collect the insurance money and avoid bankruptcy. We are reminded of this most often by those exposes on local television in which a hidden camera captures a firefighter or construction worker building a brick wall in his backyard at a time when he was collecting workers’ compensation. What we seldom see exposed are the roofing contractors whose disability insurance forms list 35 low-risk secretaries and 1 high-risk roofer, allowing them to cheat on their premiums.

Those who occupy the executive suite and gamble millions of dollars on the lives of others are rarely seen as engaged in morally hazardous conduct. Yet reward without risk is a form of moral hazard that blinks us to the consequences of our acts. The trade-off between safety and stock price is an important part of the story of how the ideology of blind faith in markets is remaking America. But the moral hazards of this blind faith are not limited to cutting corners on safety. We also have rules that encourage a new way to make the rich richer at the expense of working people. It is a strategy called *labor arbitrage*.

Chapter 7
Your Land is My Land

MANY COMMERCIAL SPORTS FRANCHISES IN AMERICA HAVE NEVER earned a profit from the market. The only increases in value that the teams reported came from the taxpayers. Among them was the Texas Rangers baseball team during the nine years, it was owned by a partnership put together by George W. Bush, a tax-shelter salesman who went on to become governor of Texas and president of the United States.

When the Rangers opportunity came along, Bush was a man of modest wealth, though he had a valuable asset in his father, then serving as president of the United States, as well as a gold-plated Rolodex. Young Bush got on the telephone and raised money from truly wealthy investors to buy the team. He bought a 2-percent stake for $600,000 using borrowed money.

On the surface the Rangers were not an attractive investment. Their owner had pulled them out of Washington in 1972 and moved them into an aging minor league stadium that guaranteed they would lose money. A subsequent owner, oilman Eddie Chiles, tired of his expensive hobby. Chiles was looking to sell the team before his time on Earth ran out. Bush told potential investors that buying the Rangers was a sweet deal because all the team needed to become valuable was a new stadium. He brimmed with confidence about solving that problem even though he had no experience in baseball, construction, or stadiums, and a track record of not paying close attention to the details that make or break oil-and-gas tax-shelter investments.

What followed was an early indicator of Bush's extraordinary success at marketing. Bush is arguably the greatest salesman of our time, having sold not just friends but political opponents on a war costing more than a trillion dollars and thousands of lives with the kind of pay-no-attention-to-that-pool-of-oil-under-the-engine polish that used car salesmen only dream about.

The Rangers investors had pockets plenty deep enough to build a new stadium, but that was not what Bush had in mind. Bush planned to have taxpayers pick up the tab. That would seem to be a hard sell in Texas, where root canals are more popular than taxes. But he succeeded.

One of his first moves was to threaten to move the Rangers out of Arlington, a prosperous suburb midway between Dallas and Ft. Worth. It was the same tactic Modell has used, the one that the Ohio attorney general described as a kind of blackmail.
The tactic worked. Bush and his allies arranged for a special referendum, held in January. Arlington voters were asked to approve a half-cent increase in the sales tax. The proposal emphasized how much of the money spent at Arlington's amusements parks, car dealerships, and shopping malls came from people who lived outside the city. That also meant that many of those who would be taxed would not have a vote. The Bush investor group hired professional campaign consultants—Democrats—to manage the election. The opposition, predictably, objected to higher taxes. More than that, they protested that it was just not right for people rich enough to finance their own stadium to force others to buy it for them. The campaign pros, with $130,000 to spend, easily rolled over the barely organized local opposition in the special referendum, in which few people voted.

The new stadium required about 17 acres of land. The Bush partners wanted more than 200 acres to develop a whole entertainment zone including hotels and restaurants. Not everyone wanted to sell their land. In a free-enterprise economy, the Bush partners would have had to bid up the price of land until willing owners decided to sell or, if that failed, move on to another location.

A free market, the kind Adam Smith wrote about and that Milton Friedman canonized, gives great power to reluctant sellers, especially the last owner, provided the project cannot succeed without his parcel. By holding on while others sell, the last person can command a premium price, sometimes an extraordinary price. That high price is also a reward for taking the risk that the proposed project will collapse, leaving the landowner waiting until another opportunity to cash in comes along.

Bush and his partners decided to ignore market principles. They were practical businessmen. They simply had the city of Arlington seize all the land they needed and more, using government's power of eminent domain to get the land they coveted, but were unwilling to buy in the market.

The Bill of Rights sets the standard for payment of seized property as "just compensation." Invoking eminent domain inherently lowers market values. It does this by putting a cloud over continued ownership, making *just* a synonym for discounted. Eminent domain also creates an incentive for governments to offer the lowest price they can get away with. Landowners who do not like the price offered by government can go to court. Such a challenge requires deep pockets to finance litigation, itself a risky enterprise. Most people, faced with a government determined to seize their property, just take what they can and get out.

When government uses its power of eminent domain for a public purpose—a new military base or a highway or to preserve, a swamp that is nature's nursery for fish and fowl—the compelling question is whether an alternative piece of real estate could be used, perhaps land whose owners want to sell.

When government uses this power to take one man's land to enrich another man, a moral hazard arises. The hazard was well known to America's founders. Alexander Hamilton, at the Constitutional Convention in 1787, said that protecting "the security of property" was one of the two "great objects of government."

The moral hazard is that the powerful and connected will manipulate the levers of government to redistribute wealth, forcibly taking from someone else so they can grow richer still. The Texas Republican Party repeatedly recognized this moral hazard in its platform. One year it said, "Public money (including taxes or bond guarantees) or public powers (such as eminent domain) should not be used to fund or implement so-called private enterprise projects." The platform did not mention sports stadiums back, then, but they were specifically cited in later years.

The Mathes family, rich but not so well connected as Bush, fought to save their Arlington horse ranch from condemnation for the new stadium. They were certain that the value of their 13 acres would continue to rise as Dallas and Ft. Worth grew into a megalopolis. And they liked their horse ranch. The city's best offer of $800,000 was, in their view, beneath contempt.
Because of a fortune made in manufacturing early television sets under the Curtis Mathes brand, the family had the resources to hire one of the best eminent domain lawyers in the state, a Corsicana attorney fittingly named Glenn Sodd.

Sodd said the case was about "welfare for billionaires," the abuse of the system by the politically connected and the morally suspect taking of land, not for a vital public project, but to add to the fortunes of a few rich men. The trial in Ft. Worth lasted two weeks. It took the jury just 90 minutes to award the Mathes family $5 million. Interest increased that figure by half. A free market would have resulted in an even higher price, had the Mathes family held out until late in the game and then sold without government interference. But they did not want to sell at any price. They were forced out.

The sports authority that the city created had already leveled the land. It sold stadium bonds to build a beautiful old-style brick and granite stadium. It planted cooling trees throughout the extensive parking areas that occupied what had been the Mathes family horse ranch. The Rangers negotiated a rent-to-own deal. It was nothing like what happens when the poor rent-to-own appliances. The poor pay exorbitant interest rates, so only a little of their money goes to paying for the purchase. The Rangers, however, got their deal interest free. Every dollar they paid in rent was counted toward the purchase price. So was the money they spent maintaining the stadium. On top of this, they had the right to buy the stadium for $60 million, even though the cost of building it was more than three times that much. What Bush told the investors was right. This was one sweet deal.

The lawyer who represented the city's sports authority in the financing was Ray Hutchison, a Republican insider, husband of Senator Kay Bailey Hutchison and, by all accounts, the leading authority on Texas municipal bond finance. Hutchison said the total value of the subsidy was $202.5 million.

That figure illustrates how subsidy economics concentrates money in the hands of a few while destroying broader wealth, which is at the core of the economic malaise felt for so long by a majority of Americans.

The investors Bush assembled paid $86 million for the Rangers. They sold nine years later for $250 million. The $164 million profit was $38.5 million less than the subsidy.

This shortfall goes to the core issue in subsidy economics: whether the subsidy produces a greater overall gain than it costs.

Martin Feldstein, a Harvard University economics professor and former adviser to President Bush, pointed out that some government subsidies benefit society. "A subsidy for flu vaccines is good because if you are vaccinated I am less likely to get flu by contagion." But job subsidies are a drag on the economy, he noted, "unless the local gain exceeds the loss in the rest of the nation."

Respected economists have intensively studied subsidies for commercial sports teams. Three decades of published research all points to one conclusion: subsidies for commercial, sports teams never produce a net gain for society. They are just a government-sponsored transfer of wealth from the many to the few.

In Texas, the numbers reveal that the Bush partnership failed to add any economic value to the Rangers, either. Every dollar that Bush and the other investors pocketed when they sold the team came from the taxpayers, from that subsidy. And even their $164 million profit is illusory because it does not take into account inflation. Adjust the purchase price upward for inflation and the profit drops to $134 million. This means that the Bush investors captured less than two-thirds of the money they took from the pockets of taxpayers.

An alternative way to look at this is that the Bush group captured the whole subsidy when they sold the team for $250 million. That would mean that the value of the team itself plummeted to less than half what the investors paid Eddie Chiles. By trading away top players for minor talents and other mismanagement, this argument goes, the team itself was worth less money.
Either way the result is the same. Bush and his investors made no economic profit from the market when they sold the team. The only money they received came from the increased sales taxes that flowed into the stadium deal.

Hutchison told me that the fact that the investors captured only a portion of the subsidy should surprise no one. Subsidies, he said, are inherently inefficient. Hutchison said that in his experience no one ever captures the full value of the subsidy, much less adds value to it.

Bush has always portrayed the Rangers deal as a successful investment. "It has been a win-win for everyone involved," Bush said in 1998. That is a curious argument since those taxpayers who never attended a baseball game lost some of their money to higher taxes and received nothing in return.

When Bush spoke about the Rangers deal he never called it a subsidy. He last talked about it when he was starting his run for the presidency. His advisers wanted to get the question of hypocrisy out of the way as early as possible. They did not want nagging questions comparing the candidate's public statements about limited government and his personal conduct in enriching himself at the public trough. Bush stuck to a few practiced lines. He said simply that the whole Rangers affair "was a successful business venture for me and my partners."

From the point of view of those at the receiving end, subsidies are a successful investment. Just as the lenses and mirrors of telescopes concentrate light from distant galaxies and funnel it to a single point, so did the Rangers subsidies gather pennies and dollars from children buying crayons and adults buying new cars. These taxes were then funneled into the pockets of Bush and his partners. Bush has always maintained that, since voters approved the tax hike, there is no issue worth discussing.

On his 1998 income tax return, which he made public, Bush reported a long-term capital gain of almost $17 million from the Rangers sale. Based on the stake he bought he would have earned a bit more than $2 million. Bush got far more because his partners gave him a 10 percent stake as compensation for putting the deal together and being one of two general partners. That is a common arrangement, with the general partner often getting 20 percent. The other general partner, who actually ran the organization, got only five percent.

That Bush and the other general partner together received only 15 percent shows, in economic terms, how risky the venture was. The Rangers investors got a better deal than the usual 80/20 split; they got 85/15. One risk was that the taxpayers would not pay for a new stadium or allow the use of government's power to condemn land for it. Another risk was whether Bush could pull off the tax subsidy deal, even with his father in the White House and many people eager to curry favor with the son. Up until this time, in 1989, he had never held public office, had a history of collapsing business ventures that had been rescued by friends of his father, and was known as a hard-drinking party animal, though he said he had given up booze cold turkey in 1986 and has admitted in a backhanded way that he had given up cocaine by 1974.

Bush did pull off the Rangers, deal, though. He went on to be elected governor of Texas in 1994. He used part of the profits to buy a 1,583-acre nonworking ranch near Waco.

His financial disclosures show that proceeds from the sale of the team accounted for most of his net worth and possibly all of it. A precise number is not possible for two reasons. Disclosure reports allow officials to list a range of values for investments, and 1998 was the first time Bush had to file a detailed report, not like the minimal disclosure required of state politicians in Texas. However, analysis of his income from the investments suggests at least three-fourths of his net worth came from the Rangers deal.

Having grown rich off a sales tax, Bush was not done profiting off the tax system. His 1998 tax return shows.

The IRS issued a directive in 1993 that is relevant to Bush's tax return. "A partnership capital interest for services provided to, or for the benefit of, the partnership is taxable as compensation." The 10 percent share the partners gave Bush is just what the IRS procedural
guide described. It should have been taxed as compensation, not as a long-term capital gain on an investment. The top tax rate for compensation in 1998 was 39.6 percent, plus another 2.9 percentage points for the Medicare tax.

In spite of this clear directive, Bush treated the entire $16.9 million from the Rangers deal as a long-term capital gain. He paid only the 20 percent rate on such gains. The result was that after paying taxes Bush pocketed $3.7 million more than the law, and the IRS directive, seem to allow. Treating such compensation as capital gains is, however, widespread and not often challenged by the IRS.

Under government rules, tax returns are accepted as filed unless the IRS audits and then challenges a return. The two years that Bush's return would have been most likely to be selected for audit, 2000 and 2001, were the record low years for audits of high-income Americans. The richest taxpayers benefited mightily those years because, at the insistence of the most right-wing Republicans in Congress, the IRS focused on tax returns filed by the working poor. In 1999, for the first time, those who made less than $25,000 were more likely to be audited than those who made more than $100,000. The next year the overall audit rate, already a record low, fell almost 50 percent. In the following year the audit rate for high-income Americans fell even more. Bush's chances of getting audited: about one in 370. So, like the vast majority of people who fudged on their taxes, or flat-out cheated, Bush got away with it.

Chapter 14
Indentured Scholars

ONE OF THE MOST SALIENT FEATURES OF THE NEW ECONOMIC ORDER is exploding levels of debt. Young people and home buyers, even the government itself, face spiraling debt that is converting the ownership society into a debtor society with ever fewer reserves, either individual or joint. In turn this new debt load, combined, with the sale of public assets like roads and water systems, means huge incomes for those positioned to take advantage of these burdens, all part of the new approach to using government to enrich the few.

For three decades, government has been cutting back on investing in the nation's most valuable asset, young minds. Adjusted for inflation, tuition at four-year public colleges more than doubled between 1980 and 2005, a period when incomes for the vast majority were essentially unchanged. Tuition rose from an average of $2,175 to $5,100. Add to this the costs of books, lab fees, meals, and either a dorm room or commuting to campus.

Seven out of ten taxpayers make less than $50,000 a year. For these families, even state college has become an onerous and often impossible burden, especially for families with more than one child. For those in the bottom half, whose average reported income is less than $15,000 per year according to the Tax Foundation, college is a goal too far, even for many smart and motivated students.

As recently as the mid-eighties, federal Pell grants to poor students covered 60 percent of the cost of attending a public college. That share has been nearly halved as Congress has cut the so-called discretionary -budget. An estimated 200,000 young people do not attend college each year simply because they lack the resources. Many do not finish because they cannot sustain the cost for four or more years.

About two-thirds of college students who graduate are in debt, a prospect unimaginable in the fifties, sixties, and most of the seventies. Many owe more than their parents make in one or even several years. And this debt limits their options to develop themselves and to benefit society through important work, such as teaching, policing, and research.

Jason Clark learned to cook on the job. He wanted to do more than short-order work, so he sought formal training. Because his father is disabled, Clark had to finance his schooling on his
own. He applied to the Pennsylvania Culinary Institute, a private, for-profit college, filling out applications for two loans totaling almost $30,000.

Six months after Clark graduated his first bill came, showing an interest rate of 13 percent. Clark did not recall agreeing to such a high rate or even signing a promissory note. Clark asked the lender, Sallie Mae, for a copy of the promissory note. He also asked for an extra six months before starting payments because he could not find work. Sallie Mae has never produced a copy of any note signed by Clark, but it did raise his interest rate to 18 percent.

Clark is just one of hundreds of thousands of students who borrow money each year to improve themselves through education. In all, students borrow about $85 billion each year, most of it at single-digit interest rates with repayment guaranteed by the taxpayers.

Nearly a fourth of these loans come from lenders, like Sallie Mae, EduCap, and Nelnet, that are free to charge any interest rate they want. Normally, the riskier the loan, the higher the interest rate. That is how lenders make up for loans that sour. But the interest rates that these lenders charge bear no relationship to risk that the loans will not be paid back. Thanks to Congress, these lenders operate almost risk free. Yet they are allowed to charge high-risk rates and to collect about $18 billion a year in government subsidies.

The reason their risk is small is that, under rules set by Congress, there are only three ways to retire these debts: pay them back in full, become totally and permanently disabled (and convince the lender that is so), or die broke.

Even if a student goes bankrupt, federal law prohibits the discharge of student loans, both those guaranteed by the government and those made on onerous commercial terms. Our Congress, in adopting these policies, has made the unstated assumption that everyone who gets a college education will succeed. That some people will become sick or injured, that others will fail to find work in the field they prepared for or will go into occupations that pay poorly, or will have a child requiring round-the-clock care, or any of a hundred other things that make life itself a risky venture, are not contemplated under this government policy.

To buy the lucrative business of students, many college lenders made under-the-table payments and other disguised forms of compensation to college admissions officers and others at Johns Hopkins, Columbia, and many other colleges and universities. Some colleges even solicited money from the lenders, promising in return to steer business to them.

Many students who were told they would pay interest rates of perhaps 6 percent or so found their loans were at two or three times that rate. At the Web site StudentLoanJustice.org hundreds of former students tell the same stories over and over again: how they were lied to, hit with thousands of dollars in collection fees for supposedly disappearing when finding them was as easy as dialing 411, and told they have to pay whatever interest rate the company picks, with no rights except to pay until they die. Under these one-sided rules, loans of $20,000 become $50,000 and loans of $30,000 balloon to more than $112,000. Is this any way to perpetuate a society?

While the government imposes harsh rules on students, it treats lenders with extraordinary leniency. The Education Department inspector general found in 2007 that one lender, Nelnet, had received $278 million in improper subsidies. The government let Nelnet keep the money. Sara Martinez Tucker, the undersecretary of education, told my colleague Jonathan Glater that seeking repayment would set a precedent that might require asking other lenders to return improper subsidies they had received. That, in turn, might drive out of business some smaller firms that make student loans, thus reducing competition. Translation: mercy for bankers, but not for borrowers.

That consideration goes to lenders and virtually none to borrowers is central to the creed of government as a source of greater wealth for those already rich enough to have money to lend.

For lenders, this government guarantee that they will be repaid produces phenomenal profits. Albert Lord, who ran Sallie Mae for years, built a fortune so large that he tried to buy the Washington Nationals baseball team. He built his own private golf course in Maryland, not far
from Washington, using the riches he made off students to separate himself from them and the rest of society, just as the Sun King commissioned a palace in which his mistress could dine without having to even look at the servants.

Sallie Mae started out in 1972 as a government-sponsored entity to help students. That was under the old government policy of nurturing the middle class. Under the new rules of government as the helpmate of the rich, President Clinton signed legislation in 1997 making Sallie Mae an independent, investor-owned business known as the SLM Corporation.

What Clinton, and Congress, did not do was remove the stern loan repayment rules that show no mercy to student debtors. The result? Sallie Mae earned an astonishing 51 percent return on equity in the five years through 2006. This is more than triple the rate of return on equity earned by the banking industry.

Lord engineered the transformation to a private concern and arranged to obtain about 2 percent of the company, mostly through stock options. In 2007, when the kickback scandals and complaints from students and their parents about exorbitant interest rates finally began to get a hearing in Congress, Lord arranged to sell the firm for $25 billion. The buyers included Bank of America and JPMorgan Chase, banks that instead of competing in the market agreed to cooperate in this venture.

Jason Turner, a financial analyst, is typical of those who are embittered by what they see as a corrupt system that enriched Sallie Mae owners and others. He borrowed $16,000 in the eighties to attend college, but today with fees and deferred high-rate interest, Sallie Mae says he owes more than $50,000. Turner believes improper fees totaling more than $10,000 inflate that figure.

"It is impossible to get any documentation of the original debt or an honest accounting of how the current balance on the loan is calculated," Turner said, echoing a common complaint. Documents he was sent create the impression that the federal government is after him to pay off this debt, but a close reading shows that, in fact, the letters come from collection arms of Sallie Mae.

"My spouse and I have a solid middle-class income," Turner said, "yet we can't even pretend to think about buying a home because of these student loans. Al Lord gets to have his own golf course, but my child can't have a backyard to play in."

Another big beneficiary of the government's policy of requiring most students to borrow money to get an education and then shielding the lenders from risk is Catherine B. Reynolds, the head of a nonprofit foundation in McLean, Virginia, bearing her name. Despite its legal status as a charity, the Reynolds Foundation does business as EduCap and refers to itself as a company. It pays like one, too. Reynolds makes a million dollars a year from the foundation even though it has assets of only about $200 million. Her salary is many times what the executives of charitable foundations of that size typically make.

Her job comes with an unusual perk. This perk must be disclosed, but the foundation-cum-company did its best to obscure the perk, which it described this way: "Based on the recommendation of an independent security review, the corporation has implemented certain security measures including security-related services for officers and directors. The value, of any services provided for any incidental personal use is treated as a fringe benefit to the recipient."

Could anyone reading that tell that the charity had bought a $30 million Gulfstream jet that Reynolds uses as her personal taxi?

EduCap can afford that perk and the big pay because of its skill at steering student applicants away from the lowest-cost aid and toward its expensive loans. EduCap hands out brochures that imply that it is hard to get government-backed low-interest loans, that they have inflexible payment terms and are too small to be of much help, none of which is true. The brochure instead touts what it claims are the benefits of its loans, including the false claim that
they are more flexible, while ignoring the higher interest rates, the fact that these rates can be raised without warning, and the prospect of huge fees and costs.

The idea that young minds should be a source of immediate profit is among the most coldly calculated changes in government which, over the past three decades, have taken from the many to enrich the few. The idea that a borrower cannot escape a debt because of a government rule is unlike that of any other modern country. Indeed, in Western Europe, students who borrow money do so on terms related to their ability to pay, with investment bankers bearing more of the cost than nurses and forest rangers.

In America, the trend is toward more financial aid to the affluent and less to the poor, another example of widespread sacrifice for the rich. The nonprofit Education Trust compared financial aid to students at the top public university in each state during 1995 and again for 2003. It found that aid to students from families with incomes of more than $100,000 increased more than fivefold, while help for students from families making less than $20,000 dropped 13 percent. "Many of these flagship institutions have become, more and more, enclaves for the most privileged of their state's young people," the Education Trust concluded.

President Bush, who likes to refer to himself as the education president, vowed as a candidate in 2000 to increase Pell grants significantly. Instead, as president, his budgets cut Pell grants for poor college students in two ways. The maximum grant was reduced. In addition, funding was cut so much that each year as many as 375,000 students who qualified did not get Pell grants because the fund ran dry.

On another front, in at least a dozen states, government seeks to make the foolish, the addicted, and the poor pay the costs of making sure Johnny and Jane can read, write, and do their numbers. Some of the proposals seem fit for comedy routines rather than serious policy.

Governor Rick Perry asked the Texas legislature in 2004 to give billions of dollars of tax relief to homeowners, especially mansion owners. Under his plan the amount of money the state would have to spend on education would depend in part on the skills of women like Vanity, Destiny, and Rio, who sell lap dances at the Yellow Rose, a topless bar in Austin. In addition to a tax of five dollars on each admission at the nude dancing clubs, Perry wanted to raise taxes on beer and cigarettes and install video lottery terminals at gasoline pumps.

Governor Perry's proposal suggested that his own education came up short on arithmetic. His combination of onetime gimmicks and what he called "taxes on unhealthy behavior" would have raised $10 billion less than the property tax relief he proposed, forcing massive cuts in education spending after a few years. But then that was consistent with his budget. He was proposing over two years to cut state spending on education by nearly a billion dollars, despite a finding by a state commission that most Texas children did not have an education that prepared them for college. Making them fit for college would cost an additional $3 billion per year.

While Texas lawmakers rejected the Perry plan, California, Kentucky, Maryland, Missouri, Tennessee, Utah, and West Virginia are among the states that have shifted part of the cost of schooling to taxes on gambling and topless bars. In New York, George Pataki tried when he was governor to raise money for education by making video lottery terminals more widely available.

There is one final way that government policy discourages the poor and those of modest means from attending college, which in the short run saves the costs of educating them, but imposes a long-term drag on the economy. The application form for federal aid is so complicated that 1.5 million students who are eligible for aid do not even apply.

In contrast to these trends, across most of the modern world a college education remains so inexpensive that anyone with the necessary brains and discipline can earn initial and advanced degrees.

There was a time when college in America was free, or nearly so. But now the GI Bill and government policies that placed the costs of education on taxpayers, a benefit extended to the next generation, have withered in the face of demands by the wealthiest to reduce the burdens
of government. As the costs of college have grown faster than inflation, and predatory lending practices have become common, the growth in advanced education has predictably slowed. More men earned doctoral degrees in 1975 than in 2005. The total number of PhDs grew only because the number of women receiving doctorates tripled to 23,000 over the same period. The number of bachelor's degrees earned by men grew just 18 percent during those years. The total number of four-year degrees grew by a bit more than half because so many more women earned degrees.

In a world of growing complexity and technological demands, shortchanging higher education through rising tuition and high-cost loans is tantamount to a policy of reducing future economic growth so that the few today can have more. It is a kind of hidden tax on the future.

Chapter 19
Paying Twice

AT THE CORE OF THE ARGUMENT THAT MARKETS ARE BEST LIES ADAM Smith's observation that, in a free market, prices will fall to the lowest level at which proprietors can 'stay in business. Professor Sarosh Talukdar of Carnegie Mellon University decided to look into how this applies to the auction markets for electricity.

Talukdar created an ideal market. His simulated market had ten electricity generating companies, each of equal size, selling power; and ten utilities, also of equal size, buying power. The sellers seek the highest prices, while the buyers want to pay the lowest prices possible. There was more than enough capacity to supply the market.

In this idealized market, prices would be expected to fall as buyers took only the lowest bids. Instead, prices rose. And as time passed and more trades were made, the prices the buyers had to pay rose higher and higher. The results astonished Talukdar, so he ran four variations of the market experiment to test the findings. The results were always the same. Prices rose.

This pattern of rising prices suggests strongly that the sellers were colluding. The classic way to raise prices is for sellers to meet in secret and agree to fix prices at higher levels than the market would set.

But in Talukdar's experiment, collusion was impossible. The sellers could not have met in secret to fix prices because they were not people, but simple computer programs called learning algorithms. The programs were so simple that high school students with a knack for software could have written them.

What the experiments showed was that sellers could jack up prices in this market because the buyers are forced to buy. If the price of a share of stock or a piece of land is too high, buyers can walk away. Not so electricity, where the utilities that distribute the power are required to supply it. In this auction, the sellers all paid attention to the prices offered by other electricity sellers, then raised their own prices to higher and higher levels. So long as no one broke ranks and undercut the market, the sellers overall got higher prices and fatter profits, than they would in a competitive market.

This unstated coordination gave the producers of electricity what economists call market power, which means the ability to set prices higher than a competitive market would allow. Within less than a hundred rounds of bidding, Talukdar's experimental auctions resembled not so much a competitive market as a cartel, in which many sellers obtain monopoly power by coordinating their actions to artificially inflate prices. 'That is what OPEC, the Organization of Petroleum Exporting Countries, does openly when members collude on setting the price of oil by limiting production.

"Collusion is a crime," Talukdar noted, "but learning is not. My studies show it is easy to learn from the signals given by others how to get the benefits of colluding without breaking the law."
Professor Talukdar is a computer scientist, not an economist. He thinks as an engineer thinks. "In building complex systems, whether it is a manufacturing process or a jetliner," he said, "you have to have rigorous verification to see if what you designed actually works the way you intended. But that is not the practice with economists, who do not verify the design of trading markets. Economists have this faith in markets, that markets are always a good thing."

Defenders of the electricity auction system, especially the owners of power plants, insist that the system has produced lower prices than the old regulated system, whose rates covered costs and provided a virtually guaranteed profit to the utilities. But the figures they point to show that prices fell, not because of market forces, but due to the rate caps and freezes that government imposed. Numerous studies found no benefit to consumers. One Cornell University study concluded, "There is no evidence to support the general expectation that deregulation would result in lower electricity prices." Instead, the evidence points to competition resulting in the higher prices that Talukdar's experiment found.

Talukdar said that his experiments show that "the design of markets matters a great deal and the design must be verified to see if it really works as a free market." Frank Wolak, a Stanford University economist who favors competitive markets for electricity, said Talukdar is right. The design of markets matters a great deal, Wolak said, because "even small flaws in the design of markets can cause enormous harm to consumers in very little time."

The damage was, and is, huge. Marilyn Showalter, an advocate for publicly owned power systems, analyzed Department of Energy data. The data showed that in the 12 months ending in May 2007, electricity in states that adopted Enron-style laws cost $48 billion more than the average cost in states that retained traditional regulation, which ties prices to the costs of production. That is $132, million per day in excess costs that act like a tax on the customers paying the bill.

In adopting Enron's recommendations to create electricity markets, state legislators did not take into account many unique aspects of electricity that affect its suitability for market auctions.

In markets for stocks, pork bellies, airline tickets, and houses, potential buyers have the option to walk away if the prices are too high. A stock can be bought on another day. Bacon is not required for breakfast. A trip can be deferred, and so can plans for a new house. But utilities in California, Connecticut, Illinois, Maryland, Texas, and a dozen other states must buy power every day. Many corporate-owned utilities, under laws Enron drafted, were required to sell their own generating plants. They are forced to buy power in the electricity markets since they no longer produce electricity themselves, but are still required to supply all that customers want.

Unlike the stock market, where vast numbers of strangers buy and sell, the electricity markets involve a relative handful of buyers and sellers. In New Jersey, for example, just 10 generators won bids in 2006 to supply a third of the state's base load of power for the next three years.

In many markets, the buyers and sellers are related companies under a single corporate umbrella. When regulated utilities sold their power plants, the buyers were often unregulated sister companies owned by the same corporate parent. In such arrangements, if the unregulated company that owns an electric power plant gouges the utility, the result is big profits for the parent company, creating a perverse incentive to raise prices.

Finally, electricity trades repeat each day. Power is sold for specific time periods, often an hour or quarter hour, a day or two before it is needed. The short periods allow prices to be affected by changing demand from customers as they turn on air conditioners on hot afternoons or flip off lights at bedtime. Because auctions occur so often, those who generate power for sale can get an idea of what the market will bear by studying the weather report and historic patterns of demand. This is where the analysis of trading patterns that drove up prices in Talukdar's experiment conies into play.

Moreover, electricity markets operate in government-imposed secrecy. Individual stock investors can make sure they got a fair price by checking the prices paid just before and after
their trade. But the Federal Energy Regulatory Commission and the electricity exchanges it authorizes stamp many trading records confidential, though some records are made public months or years later. Many times even this knowledge is misleading, however, as the markets include not just the owners of power plants, but brokers who act as fronts.

Finally, the very nature of electricity means that it must be produced, transmitted, and consumed in an instant. Automakers can cut production when vehicles do not sell. Investors who hold too much of a particular stock can sell it in blocks over time to get the best price. But electricity cannot be held in inventory.

There is one other crucial difference between electricity and stock markets. In electricity markets, every seller gets the highest price—even when it is higher than the price at which they were willing to sell. That is the rule in the electricity auction market: the highest winning bid sets the price for all.

Contrast this to the stock market. Someone who wants shares of a company buys them at different prices, perhaps $10 a share to start, and then, as word gets around that someone is accumulating shares, paying $20. The average of these prices may be $15. Not so with electricity. In electricity markets, everyone gets the highest price that is accepted. It is as if the stock market buyer had to pay $20 for every share, even the ones offered for sale at half that price.

Giving every seller the high price for the day, hour, or other time period creates a huge incentive to hold generating stations offline to restrict supply and thus drive up prices. This was exactly what was shown in the fax that Vice President Cheney refused to examine when he told Representative Jay Inslee, “You just don’t understand economics.” This system also creates incentives to apply what is learned, as Professor Talukdar showed, to rig prices.

Consider what happened on March 2, 2003, in the Texas electricity market. Power was being auctioned off in quarter-hour segments for the next day. Some power was offered for free, presumably by nuclear power plants, which must run at the same rate around the clock. Several dozen bidders then offered power at various prices.

The average of the bids required to supply all the power that was needed came to $83 per megawatt hour. But the bid that cleared the market, the bid that provided the last megawatt of power needed to meet demand, was more than $200. Under the rules for electricity markets, every generating company was paid the high bid of more than $200 per megawatt hour. The difference between the individual prices that the sellers offered and the price actually paid was $150,000. That money was extra profit for all but the top bidder.

In the auction for the next quarter-hour period, the bidding pattern changed. There were still generators offering power for free. But the high bid for the last few megawatts, of power needed by customers was $990. Every owner of a generating plant got that price, even those offering power for free. The extra profit? More than $800,000 in just fifteen minutes.

The industry calls these inflated prices "hockey stick" bids because, when plotted on a chart, the prices show a long handle that rises slowly with a spike at the end like the blade on a hockey stick.

Official state reports identified only as "Company C" the bidder who set the price at nearly $1,000. Years later it was identified as TXU, which owns both the regulated Dallas electric utility and, through a sister company, a host of power plants. Although historically stocks of utilities were reliable but slow to appreciate, TXU has been one of the best-performing large company stocks between 2002 and 2007, showing just how valuable the pricing manipulations of "Company C" were to its bottom line.

The system was a perfect arrangement to get, not the lowest possible prices, but a free lunch through inflated prices, served up by government, rules. Any one of the many TXU generating plants could make a high bid that produced windfall profits for the others. Because the power was sold to regulated utilities, which by law must provide whatever power customers demand, the price was just passed on. But customers had no idea that in some quarter-hour
segments they were paying exorbitant prices. Why? Because all customers get is a monthly statement that adds up the prices paid for every fifteen-minute period into a single total.

Technology allowing residential and small-business customers to know what price they pay each moment for electricity has been available for decades. In the seventies, utility regulators in California and some other states said they would make it widely available to encourage people to reduce their use of power during periods of peak demand. Somehow, though, it just never happened. And without that knowledge of prices at each instant, customers cannot know when their pockets are being gouged.

The supposed markets for power enable price gouging in still other ways. California has 1,400 power plants, which ought to be more than enough for a vibrant market and, as Adam Smith observed, should drive prices down to the lowest level at which the businesses can afford to continue operating. But ownership of those California plants is so concentrated that just six generating companies can set an artificially high price for electricity virtually all the time, research by Carnegie Mellon University shows.

New Jersey and Illinois are among the states that conduct annual electricity auctions. In New Jersey, just 10 generators won contracts to supply a third of the state’s base load of power through 2009. The price? It was 55 percent higher than the previous year’s three-year bid.

In Illinois, prices also soared. Among the winning bidders to supply power? An unregulated sister company of Commonwealth Edison, the Chicago utility, both of which are owned by Exelon. In essence, this is a system in which an unregulated company earns outsized profits from a regulated company, which in turn earns virtually guaranteed profits and, by law, can pass on the prices it pays for electricity to its customers. Think of this as the anti—Adam Smith policy.

That electricity is sold in what are called markets, but are really mechanisms to rig prices and cheat customers, has become obvious even to the large industrial and commercial customers who initially bought into Enron’s campaign to make generating electricity a competitive business. They have seen their own prices rise, not fall. Robert A. Weishaar Jr., a lawyer for many big industrial customers, told the Federal Energy Regulatory Commission that his clients were being taken for a ride and damaged by commission policies that allow price gouging. "The 'markets' that are rolling off the commission's production line are not fit for their public purpose," he wrote.

The Federal Energy Regulatory Commission, however, rejected all such complaints out of hand. Under its circular logic, once it declares that a market for electricity has been created, whatever prices markets produce must by definition be fair and just, because markets produce fair and just prices.

Faux markets are not the only way that customers are having their pockets picked under current policies originally promoted by Enron. When competition began, most states that adopted the Enron proposals required utilities to sell their power plants. They not only allowed them to be sold to sister companies that were unregulated, they allowed them to be sold at bargain-basement prices.

Most plants were sold for the cost of construction minus the amount that had been depreciated, that is, the amount written off on the company’s books. This was allowed even when the plant had actually risen in value. Said Lynn Hargis, who was a longtime federal government energy lawyer before joining Ralph Nader’s Public Citizen: "Selling a power plant for its depreciated value is the equivalent of selling my grandmother’s house for what she paid for it decades ago, less depreciation, while ignoring its real value. Nobody would do that."

For electricity customers it was even worse than that. The utilities demanded that they be paid in full for the value of the plants that they had not yet written off. These were the "stranded costs" in the Trojan Horse bill that the Texas legislature, and the legislatures of many other states, passed to mollify the utilities.

Across the nation, state utility regulators let the utilities sell bonds so they could immediately pocket ill cash the value of the plants that they transferred to their unregulated sister companies.
Then the cost of these bonds, plus interest, was added to electric bills. For residential customers of Centerpoint, the old Houston Lighting & Power, this will add an average of almost five dollars to their bills every month for 14 years.

Some of these plants were then resold at huge profits. Centerpoint sold 60 power plants that generate most of the power for the Houston area to a joint venture of four investment firms—the Blackstone Group, Hellman & Friedman, Kohlberg Kravis Roberts, and Texas Pacific Group. The price was less than $1 billion. Just eighteen months later, the four investment firms resold the plants for a profit of almost $5 billion. It was a deal that even by the standards of Texans produced awe, though no shock.

Sempra Energy, parent of the utility in San Diego, and two investment partners bought nine Texas power plants in 2004 for $430 million. Less than two years later, it sold just two of the nine plants for $1.6 billion. A group led by Goldman Sachs, the investment bank, bought power plants in upstate New York, Pennsylvania, and Ohio starting in 1998. It sold them in 2001 for a profit of more than $1 billion.

The prices of these and many other plants rose because of the easily rigged markets for electricity that make it possible for owners to inflate prices. Robert McCullough, the utility economist whose fax on price manipulations Vice President Cheney dismissed without reading it, said that from Maryland to Texas to California, the sale of power plants by utilities to sister companies had no benefit for customers. "The same energy is generated by the same plants, owned by the same owners, and sold to the same customers, simply at a vastly higher price," he said.

Ralph Nader said regulators should have required price protection to shield consumers from a "double-header corporate gouge, where the defenseless customer is paying twice for the same power plants." But wait. There’s more.

Paying twice for the power plants is not the only way that electricity customers are forced to double up their costs. Across the country, electricity customers pay taxes that are embedded in the rates they pay. Because utilities are legal monopolies, they must recover all of their costs from customers, ranging from the price of fuel and the chief executive’s expense-account lunches to income taxes on profits.

These taxes do not always make it to government, however. When state utility boards set electric rates, they assume that the utility will file its own tax return. But often when the utility has a corporate parent, the parent files the tax return and the parent may not pay any taxes. When that happens, the utility and its parent company eat a free lunch at the expense of their customers.

The system that allows the corporate parents of utilities to pocket taxes has many defenders. Paul Joskow, a Massachusetts Institute of Technology utility economist, said, "For the customer, the result is the same." He meant that if utilities filed their own tax returns and paid the taxes, their rates would be the same as when they pass the taxes on to their corporate parents.

Mike Hatch, when he was Minnesota attorney general, said Joskow's argument is hollow. "Essentially, utility ratepayers pay the tax twice," Hatch said, "once through the utility bill and again through the lost revenue to government that means either higher taxes for them or fewer government services."

Hatch provided help to Myer Shark, a Minnesota lawyer who spent the last years of his life trying to recover $300 million in taxes, embedded in the rates paid by that state’s electric customers, that never reached government. The taxes benefited Xcel Energy, which operates in ten states, though Shark sought recovery just in Minnesota. To Shark, who was in his nineties when he took on Xcel, pocketing taxes violated laws prohibiting "unjust enrichment" by legal monopolies like utilities.

"The law says that utilities are entitled to a just and reasonable return, but when they keep the taxes, they are earning an unjust and unreasonable rate of return because those taxes add
to their profits," he said. Just days before he died in 2007 at the age of 94, Shark filed the last legal papers intended to make sure a court would decide his case and reject any efforts to dismiss it because he would not be around to argue further.

The champion at pocketing taxes was Portland General Electric, during the years 1997 to 2004 when it was the only operating business owned by Enron. Each year Oregon residents and businesses paid about $92 million to cover Portland GE’s income taxes. But Portland GE, like virtually all electric utilities with a corporate parent, did not file its own tax returns. Instead, Enron filed the tax returns. Enron did not pay taxes, thanks to its use of hundreds of shell companies in the Cayman Islands and other tax havens. That meant that Enron pocketed an extra $92 million a year from Portland GE customers, a total of nearly $1 billion dollars during the years it owned the utility.

News that Portland GE did not pay taxes caused an uproar in Oregon. The state was so hard-pressed for money that some counties could not afford sheriffs patrols. The Oregon legislature passed a law in 2005 to require that any taxes embedded in utility rates be turned over to government. Not only did Portland GE fight the law, so did Warren Buffett, who had just acquired Oregon’s other big corporate-owned utility, PacificCorp. Both wanted to profit off taxes.

Buffett is a master at delaying the payment of taxes not for a little while, but for a generation. His MidAmerican Energy Company owns electric and natural gas utilities, with operations from Oregon and Utah through Iowa and east to Britain. It paid just 4 percent of its American profits in federal corporate income taxes in 2006, far less than most Americans paid on their incomes. On its overseas profits, MidAmerican paid a 21 percent tax.

MidAmerican will have to pay the rest of his American taxes, but not for a long time. It deferred $666 million in taxes in 2007. In 2035 it will have paid just half of those taxes. A tax not paid today but in the distant future is like getting an interest-free loan from the government, which is to say from the rest of the taxpayers. Imagine how rich you would be if you had bought a house 28 years ago, got an interest-free mortgage, and only now had to pay the price you agreed to so many years ago. Like Buffett you would be rich. When the government finally gets those taxes -from Buffett's company it will get about 40. cents on the dollar. You will have to make up for those missing 60 or so cents through higher taxes, fewer services, or interest payments on more government debt.

This interest-free loan has not meant cheap electric rates. When it comes to charging high prices, Buffett plays hardball, extracting every dollar the regulators will allow his utilities to charge, as people in six Iowa cities discovered. For years Iowa had nine corporate-owned electric utilities plus a sprinkling of city-owned systems that sold power at lower prices. Then MidAmerican and another firm, Alliant Energy, consolidated the corporate-owned utilities into just two entities. Because consolidation lowers costs, people in Johnson County and five small towns tried, without success, to get lower rates, hoping this would both save them money and help local manufacturers create more jobs. Rebuffed, they organized to buy out MidAmerican and run municipal systems so they could get their power for less.

Buffett’s agents immediately went to work to make sure electricity prices would not fall. His firm spent more than half a million dollars in Johnson County. It also filed a petition to lower rates, though more than four years later rates remain unchanged.

But Buffett’s key move was getting legislation to thwart not just six towns but to punish the people in the nine cities with municipal power for giving advice on how to convert from corporate power to municipal power. MidAmerican drafted bills that would have made the existing city-owned systems pay taxes, prevented them from making changes as technology and the times always require, and blocked them from offering any new services, such as municipal Internet or cable television service. Buffett's lobbyists bluntly told the Iowa Association of Municipal Utilities that it would make the legislation go away on one condition: that the association stop giving advice to the six towns on how to switch to municipal power. Bob Haug, the association’s executive director, told his members that the influence of Buffett's lobbyists showed how the
state of Iowa had been transformed into "Iowa Inc." He said that given MidAmerican's grip on the legislature the association had no choice but to bow to MidAmerican's demand that it adopt a resolution promising to never help any Iowa citizens seek a municipal power system.

Carol Spaziani was a librarian in Iowa City before she retired. She became a leader of the municipal power campaigns. Spaziani said that she watched in amazement and horror both at how Buffett used government to enrich himself at the expense of others and at how eager state legislators and others were to bow to the will of his lobbyists. She said she was also struck by the inability of the news media to articulate the issues of a matter crucial to the local economy, and, when they were covered, how it was written up as a political dispute worthy of only a few words on the inside pages.

"On television I keep seeing this beneficent billionaire who is portrayed as someone we should all respect because he is so rich, and he has given so many billions to charity," Spaziani said. "What I don't see is coverage about how Warren Buffett is forcing people in Johnson County to pay more than we should for electricity, and how that means fewer jobs and hardship for people just so he can make more billions."

But wait. There's still more.

State regulators generally allow utilities to earn a profit of 10 percent or so. Yet despite this limit on profits, investors famed for earning much bigger returns, like Warren Buffett, are buying electric utilities. Kohlberg Kravis Roberts & Co. and the Texas Pacific Group, which teamed up to make those enormous profits buying Texas power plants, are in the game. The two firms worked jointly in 2007 to buy TXU, the big Dallas utility involved in the hockey stick bids. This joint venture came after KKR failed in its attempt to buy Tucson Electric Power in Arizona and Texas Pacific tried to buy Enron's Portland General Electric.

Why would investors famed for much bigger returns want electric utilities earning a solid, but modest, profit? The answer reveals how much government has become an ally of the rich in exploiting those with less.

After Enron bought Portland GE it raised rates, ending decades of cheap power. The revelation that it pocketed almost a billion dollars of taxes customers were forced to pay in their monthly electric bills turned many in Portland against both Enron and the local electric utility.

Then, in October 2003, the city's long Enron nightmare appeared to be coming to an end, thanks to Neil Goldschmidt, the most influential politician in the state. Goldschmidt was elected mayor in 1972 when he was just 32, the youngest mayor of a major American city. He went on to become transportation secretary under President Carter and governor of Oregon. He was instrumental in making Portland a vibrant, livable city, with mass transit, bicycle lanes, and ways for minorities and others to have a voice in city affairs.

Goldschmidt announced that Texas Pacific proposed to buy Portland GE, and that he would shepherd the deal through Oregon's Public Utility Commission. At his side stood two business leaders, Gerald Grinstein, the chairman of Delta Airlines, and Tom Walsh, a prosperous developer. The promise was of local leadership of the utility, although the investment money was coming from far away. Things soon took many unexpected, even salacious, turns.

Texas Pacific instantly persuaded state officials to seal most of the documents about how it would finance the purchase. It claimed that the information would be of value to competitors, a curious argument, since Portland GE is a legal monopoly that has no competitors. But Oregon's Public Utility Commission, whose members were so lackadaisical that the chairman was known to nod off during official proceedings, went along. Lawyers representing big industrial customers, consumer groups, and others could see the financial records, but only if they promised not to reveal what was in them.

Ann Fisher, a veteran utility lawyer who represented downtown building owners, was vexed by what she saw. So Fisher wrote an essay for The Oregonian. She wrote that the sealed files told a very different story than the public announcements about the purchase. Fisher took care not to disclose any specifics that might be of value to Portland GE's mythical competitors, but
she wrote that from the viewpoint of Texas Pacific, a 50 percent profit was not out of the question. Her words suddenly turned an issue that bores most people into the hottest topic in town.

Soon after that, someone slipped the sealed documents to an exceptionally savvy reporter named Nigel Jaquiss. He had made a fortune as a Wall Street oil trader and then decided his children would have a better life if their father had a job he really enjoyed. Jaquiss reported for the local alternative newspaper, *Willamette Week*.

Using skills he had learned at Goldman Sachs, Morgan Stanley, and Cargill, Jaquiss plowed through the documents and determined that Texas Pacific had found a way to earn more than three times the rate of return that was authorized for Portland General Electric. The key was a complicated ownership structure with a lot of debt and very little cash, which meant that the real risk if anything went wrong would be borne not by the owners of the utility, but by its customers. The public knew none of this, thanks to the official secrecy.

Such official secrecy in regulatory proceedings is becoming commonplace across the country. It fits the ideology that government is the problem, which it certainly is for some corporations when government acts as a guardian of the people against profiteers. It also has its attractive benefits for politicians, allowing them to do their work and even make subtle side deals to benefit friends without a spotlight on their actions. Keeping people in the dark also reduces the risk that the public will realize how much of its government has been twisted into a tool of the rich seeking to expand their riches at the expense of those with less.

The disclosures about the financial aspects of the deal followed an earlier story by Jaquiss that discredited Goldschmidt. It was the story of a secret that many of Oregon's business and political elite had known about, and many others had suspected or heard about, but that everyone had kept to themselves for more than three decades. Jaquiss showed how a few prominent Oregonians had even traded on the secret, getting official favors from Goldschmidt when he was in office.

The secret was that Goldschmidt, when he was mayor, repeatedly had sex with a 14-year-old girl, a neighbor whose mother was a close political ally. None of those who knew had stepped forward to protect the girl or to have Goldschmidt arrested for statutory rape. For years Goldschmidt paid the victim hush money. There was no indication that anyone among Oregon's elites ever shunned the child rapist, but plenty of evidence that some of those who knew turned to him when they needed to work the city, the county, or the state for official favors. Goldschmidt was, by all accounts, the man to see about getting government to help the rich and powerful, both fixer and kingmaker.

When Goldschmidt realized that the intrepid reporter Jaquiss had all the facts to break a story in the weekly newspaper, he went to *The Oregonian*, the largest daily paper in the state. He hoped that by giving the big daily newspaper a scoop he would get as friendly a story as possible, one that would not carry the sting that was certain to come from Jaquiss. It was a smart move. The next morning *The Oregonian* reported that when Goldschmidt was mayor he had "an affair" with a girl of 14.

The financial disclosures and the sex scandal eventually brought an end to the Texas Pacific bid. Jaquiss won an extraordinary honor for a reporter at a weekly newspaper, a Pulitzer Prize. The city of Portland tried to buy the utility, promising to pay more than anyone else, and then to lower rates, because as a municipal utility it would not have to pay big executive salaries or dividends. The corporate lawyers and executives who by then controlled Enron declined to take this high bid. Instead they had Portland GE issue stock, and it became a freestanding company. One that immediately asked for a hefty rate hike and a change in rules that shifted the risk of rising fuel prices entirely onto customers. As with Warren Buffett's hardball moves in Iowa, corporate power worked to make sure customers paid the highest possible prices for electricity.
What is significant about the Portland deal is how it exposes the willingness, even eagerness, of government officials who are supposed to be acting on behalf of the public to use official secrecy to benefit private interests. And even when Texas Pacific's fixer was revealed to be a sexual predator whose victim was a 14-year-old girl, the local elite did not turn on him, did not demand an inquiry, and did not question their own complicity. Instead, the state conducted a long, costly, and ultimately failed investigation to try to determine how Jaquiss got hold of the financial documents. The state tried to pin the blame on Ann Fisher, who had acted honorably, and who had not been the source of the documents.

Fisher paid a terrible price for being honest. She lost her business clients. She has had a tough time finding new ones, as the tightly knit Portland business elite closed ranks.

And Goldschmidt? After laying low for months he resumed working for clients seeking subtle favors from government. But unlike his public announcement in the utility deal, Goldschmidt adopted a lower profile, working the telephones and backrooms.

Advocating competition, and then using government as a way to make deals shrouded in secrecy that promise enormous profits and few risks for those getting richer, is a core strategy for those who have discovered how easily government can be turned into a source of personal enrichment. Next, let's examine the career of one of the biggest beneficiaries of this self-serve approach to government.

Chapter 21
Unhealthy Economics

WHEN LINDA PEENO BECAME A PHYSICIAN, SHE TOOK THE HIPPOCRATIC OATH, including a promise to, patients to "keep them from Iarm and injustice." In time that vow began to weigh on Dr. Peeno's conscience. Her job was not to make patients well, but to make a company well at their expense.

"In the spring of 1987, as a physician, I caused the death of a man," Dr. Peeno told Congress in 1996. "Although this 'was known to many people, I have not been taken before any court of law or called to account for this in any professional or public forum. In fact, just the opposite occurred. I was 'rewarded' for this. It brought me an improved reputation in my job, and contributed to my advancement afterwards. Not only did I demonstrate I could indeed do what was expected of me, I exemplified the 'good' company doctor: I saved a half million dollars." Dr. Peeno never saw her patient, a man who needed a heart transplant. Dr. Peeno examined "a piece of computer paper, less than half full. The 'clinical goal' was to figure out a way to avoid payment. The 'diagnosis' was to 'deny.' Once I stamped 'deny' across his authorization form, his life's end was as certain as if I had pulled the plug on a ventilator."

She stamped that death sentence at her desk in a 23-story marble office building in Kentucky; the patient was in California, a state where Dr. Peeno was not licensed to practice medicine.

What Dr. Peeno described is not an anomaly. It is only an extreme example of the predictable results of what government policy is doing to health care, a system that enriches the few at the expense of the many.

Nearly all decisions by health care corporations about providing care are routine. The companies would argue that all of their decisions are made in accord with the law. But that is mere cover, ignoring the bigger issue: whether the system is moral or even economically sound. The government rules shaping health care have created a whole industry of makework that drives up costs, denies care to some, makes it next to impossible for the already sick to get health insurance, and condemns others to needless pain and early death, while simultaneously making a few men and women fabulously rich.
From the perspective of the health care companies, these rules allow them to do business with only the more profitable patients, avoiding those most in need of care. In turn, that allows them to increase profits or lower premiums. Unless there is serious competition to expand by taking patients away from competitors, the preferred choice is bigger profits.

At its core, government policy makes health care a business. The purpose of business is to maximize profit. That is the appropriate standard for taking care of capital, but not people's health. Yet a strong push is underway to make health care even more of a business, backed with huge new federal subsidies to for-profit health care corporations. These subsidies are being lavished on for-profit health insurance companies despite studies showing that nonprofit health systems tend to provide superior care.

If health care as a business worked, it would be a success story to embrace. If it resulted in lower costs, more and better care, and longer lives, it would be just what the doctor ordered. The American system provides superb acute care, trauma care, and access to the highest technology. But by every other objective measure—cost per capita, health status, longevity, costs of paperwork, and economic pollution—the uniquely American approach to health care is a complete failure. We pay more, enjoy shorter lives, and are drowning in infuriating makework, filing claims and making appeals, while distorting the whole economy because one giant component is a commercial activity.

No other modern country regards health care as an insurance business. While some nations refer to their plans as health insurance, they mean that in the political sense, just as we call our basic old-age pension system of Social Security a "social insurance" program. No other country uses the word insurance in the business sense, which means to spread risks. The business sense of insurance includes the concept of examining claims to see if they fall within the contractual boundaries for payment, which was Dr. Peeno's job. This is how we ration health care in America, through contracts that limit care and exclude coverage—and by having tens of millions of people go without any insurance at all.

Because we tie most health care insurance to employment, this system is making us less competitive in the global economy. That is because no other country makes employers record the cost of health care for their workers on their books. Everywhere else this cost is part of the national ledgers just like the costs of police, education, and lifeguards.

In Europe, Japan, Canada, Australia, and New Zealand, people benefit from a system of health service, not health insurance. In many of these countries doctors still make house calls. The overwhelming majority of people who seek immediate care are treated that day or the next, which is also true in America. But the other countries do not spend vast sums on reviewing claims for payment and billing, a deadweight drain on the American economy that costs every man, woman, and child more than a dollar per day.

Individual purchases can make things worse, not better, as shown by our history with fire insurance. There was a time in this country when people paid commercial fire companies to protect their property. But instead of replacing lost property, as we do today, these policies insured that firefighters would fight any fire at your home or business. A problem arose when the house abutting yours caught fire. If that owner had paid a different fire company, or none at all, your fire company would not put out the blaze even though it was a threat to your property. Only when your building was ablaze was your fire insurance company obligated to act—and that could be too late. That system died when we recognized that fires are a public problem, not a private one. Our solution was to have government provide fire-protection as a public service. People relinquished having their choice of fire-fighting companies, but saw that government monopoly on fire-fighting service saved far more lives and protected property much more efficiently than the market did. Accident and illness are, like fires, public and social problems, not individual ones, that are mostly efficiently treated as public service.

In America we do not speak of police insurance, or education insurance, or, when vacationing at the seashore, lifeguard insurance. Rather, we pay taxes for police, education,
and lifeguard services because these are essential services for a civil society. When we need a cop, we dial 911. How quickly the police respond depends on their judgment as to the urgency of the call compared to other demands for service at that moment. When a child is five years old, the government does not require proof of ability to pay before a child may start kindergarten. And when someone caught in a riptide cries out for help the lifeguard does not check a list to see if the person has paid in advance to be saved and also whether the coverage included Tuesdays before noon when the sky is overcast. But that is exactly what we do in health care, because we use a business model instead of a service model. In the process we also take from the many to enrich the few.

Complex bureaucratic systems to deny care based on subparagraph k at page 454 of a contract are also uniquely American. That does not mean other countries do not ration care. They do. But they do it as a matter of policy—as opposed to profit. These other countries place limits on care, such as not giving heart transplants to octogenarians. If you are in your eighties and need a transplant you may prefer our system, which will extend your long life a bit more. But the cost of that is paid in less care or no care for those much younger, who as a result are less likely to live to see their ninth decade. Rationing would be eliminated if voters were willing to spend enough on health care to cover every demand for service.

Adam Smith tells us "what improves the circumstances of the greater part can never be regarded as an inconveniency to the whole. No society can surely be flourishing and happy, of which the far greater part of the members are poor and miserable." His remark was not aimed at health care, yet it deals with the issue of how we allocate scarce goods in an imperfect world in which choices are inevitable.

No other country spends as large a share of its economy on health care as the United States. And that share is growing rapidly, crowding out other economic activity, especially investment in the next generation. Roughly every sixth dollar in the American economy was spent on health care in 2007. Our government has projected that by 2015 we will be devoting every fifth dollar to health care. In most modern countries health care accounts for less than one-tenth of their economies.

The inefficiencies of the American health care system also create jobs. However, that is hardly an argument for maintaining our existing health care system. If all we wanted was to create jobs we could ban giant earthmovers at construction sites and hire teams of workers with teaspoons to move dirt. Even if we wanted to treat health care as a jobs program, it would be better to put more nurses to work on hospital floors than to have so many clerks in the billing department.

The uniquely American system of health-care-as-a-business results in some poor countries having better health outcomes than the United States. America ranked thirty-sixth among nations in its rate of infant mortality in 2006. The Central Intelligence Agency estimated American infant mortality at 643 deaths per 100,000 live births, slightly worse than Cuba at 622. That American infant mortality rate was actually an improvement. In 1960, we experienced 2,600 deaths per 100,000 live births. But the falling infant death rate slowed after 1980, even though medical advances continued. The rate virtually stopped falling in 1996, the year when Congress and President Clinton ended all basic welfare programs for the poorest children and mothers in America.

There is another awful cost to a policy of health care as a business: No one in the modern world ever goes bankrupt because of medical bills, except in the United States of America.

It is true that sometimes, for some conditions that are not life threatening, people in other modern countries have to wait weeks or months for treatment. But even people in America with health insurance have learned that scheduling appointments, getting referrals to specialists, getting insurance company approvals for those referrals, making appointments with the specialists, getting evaluated, and then finally getting treatment can also take months.
After the care is provided, an insurer can come back and say it made a mistake, demanding that the patient personally pay all their bills retroactively. That is far different from nations delaying some nonemergency medical services.

But no delay is comparable to the medical, economic, and moral harm done by a system in which at least 45 million Americans go without health insurance coverage. The American system is completely at odds with the biblical morality publicly embraced by nearly every elected politician, which imposes a duty to sacrifice for the poor. Yet someone without insurance who gets cancer becomes eligible for government-provided care only at the point where they become permanently and totally disabled. That is to say, when treatment seldom will help and death is virtually inevitable, care begins.

And who goes without health coverage? By and large, families who work but earn a modest income. Among those making $65,000 or more, roughly those Americans in the top 25 percent income group, health insurance is nearly universal. But among Americans with less than average income, 57 percent are without health care.

Health care as a business also imposes another drag on our economy, one that gets very little attention. It is the inefficient deployment of human capital caused by America's unique lack, among modern nations, of universal health care service. In the debates over the tax treatment of hedge and private equity funds, those huge unregulated investment pools, Congress has devoted plenty of attention to getting the most efficient deployment of capital so that we get maximum economic bang for the buck. Yet the inefficient deployment of human capital caused by treating health care as a business gets almost no attention from policy makers and, in turn, from the news media.

Many people who have a medical condition such as cancer, or who have a dependent with a condition, stick with their current employer because they have insurance whose payment policies they know. Under, the Health Insurance Portability and Accountability Act of 1996, a new employer cannot exclude a preexisting condition from coverage. But every plan is different; every plan has its unique internal rules and policies. Changing jobs itself also involves a risk because one lacks seniority and the new job may not work out, which could result in unemployment. Under the 1996 law anyone who goes 63 days without a job loses some of their limited rights on health care coverage for preexisting conditions. All of this acts as a curb on efficient deployment of human capital. Government policy that discourages people from moving to new jobs that would make the most efficient and effective use of their skills is a drag on the economy, not to mention individual human happiness. Europeans, Canadians, Japanese, Australians, and New Zealanders never give a moment's thought to these matters because their health care is not connected to holding a job.

On the other hand, the lucky few who have positioned themselves to take advantage of the government rules are becoming fabulously wealthy under government policies that result in taking from the many to benefit the few. Government policy has replaced legal limits on pay with sky's-the-limit pay plans that have produced billion-dollar fortunes for the lucky few. It has made plundering public assets immensely profitable.

The idea of health care as a tax-free fringe benefit began with Roosevelt and the economic controls of World War II. But the drive to make health care into a part of corporate America through government giveaways began with the Nixon era. Those subsidies have grown from little weeds into a mighty forest of government giveaways to the few. Next, how health care started down the road to high costs, frustration, and riches for the few by taking from the many.
Chapter 26
Not Since Hoover

The fact is that income inequality is real; it’s been rising for more than 25 years.
President George W. Bush, January 31, 2007

FOR THE RICHEST AMERICANS, THE YEARS SINCE 1980 HAVE BEEN very good. There were the seven fat Reagan years, we see that this gross figure is misleading, because the slice is not distributed at all evenly among the top 30 million Americans.

For the bottom half of the top 10 percent, the pie was sliced a bit thinner (11.5 percent in 1980 and 11.2 percent in 2006). For the next group, those standing between the ninety-fifth and ninety-ninth rungs on the income ladder, the slice of pie grew somewhat. It increased from 13.2 percent to 15.3 percent.

It is when we start looking closely at the top 1 percent that things get really interesting. Their share of the income pie more than doubled, from 10 percent to 22.8 percent. Numerically this group is three million Americans, but in terms of how much money they make it is hardly a cohesive group. To get into the top 1 percent required an income in 2006 of $376,378. At the very top, several people made several billion dollars. It would take someone at the threshold of the top 1 percent nearly 3,000 years to make a billion dollars. So, we will cut this slice of income pie even more finely.

First, there is the top tenth of 1 percent, or 300,000 Americans. People in this group lived alone or in families with an income of at least $1.9 million for 2006. Their slice of pie more than tripled in size. They earned 3.4 percent of the 1980 pie and 11.6 percent of the 2006 income pie.

Then, let’s consider the very best off, the 30,000 Americans, or 14,836 tax units, who made at least $10 million in 2006. Their slice of income pie in 2006 was four times larger than in 1980. They went from almost 1.3 percent of the pie in 1980 to 5.5 percent in 2006.

So the vast majority had less pie in 2006 than in 1980. And even among the top 10 percent - with their larger slice, nearly all of the growth

The Rich Get a Bigger Slice

Share of Income Reported on Tax Returns

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<tr>
<th>The Vast Majority</th>
<th>The Rich</th>
<th>The Superrich</th>
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<tbody>
<tr>
<td>People in 2006</td>
<td>270 million</td>
<td>30 million</td>
</tr>
<tr>
<td>1980</td>
<td>65.4%</td>
<td>34.6%</td>
</tr>
<tr>
<td>2006</td>
<td>50.7%</td>
<td>49.3%</td>
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Source: Piketty and Saez

went to the top 1 percent—especially those at the very top who were already very rich, yet whose slice of pie grew even fatter.

Put another way, the rich, enjoyed a bigger slice of the national income pie since Herbert Hoover was president. Indeed, their income share was virtually the same as in 1929, the last of the Roaring Twenties and just ahead of the Terrible Thirties.
President Kennedy famously said that a rising tide lifts all boats. If a rising tide of income makes everyone better off, then changes in the shares people get do not matter so much. But that is not what is happening. Instead, as the numbers for average incomes show, the yachts are becoming personal ocean liners while the runabouts and dinghies, tied to the dock, are being swamped.

The national economy, adjusted for inflation, more than doubled in size from 1980 to 2006. However, because the population grew by a third during those years, growth per person was only about two-thirds. That is, for each dollar per person that the economy produced in 1980, by 2006 output had grown to about $1.70. So what happens when we look at the income ladder using a conservative inflation adjuster.

The average real income of the vast majority rose slightly, from $28,975 in 1980 to $30,659 in 2006. That equals an average annual wage increase of 3 cents an hour or $1.20 a week. So while the overall economy did quite well, the vast majority did not share in that prosperity. Moreover, if we reach back a bit further we find a decline in income for the vast majority. The average income for the bottom 90 percent of Americans in 1973 was $31,248. That is $590 more per year than this group’s average income in 2006. So after a generation of economic growth, over 33 years, the vast majority has to get by on about $75 less per week.

The declines are even greater if we examine the bottom half of the income ladder, which in 2006 was about 150 million Americans. Piketty and Saez did not prepare such a breakdown. But the Tax Foundation, a group that favors less taxation, did. Adjusted for inflation, the bottom half had an average income of $16,689 in 1980. That fell to $14,526 in 2006. That meant making ends meet with $42 less per week than in 1980.

There have been some offsetting changes. The portion of income paid in federal income taxes by the bottom 150 million Americans has been cut in half, the Tax Foundation calculated. Back in 1980 their average tax rate was a bit more than 6 percent, while in 2005 it was just under 3 percent. That means the after-tax decline was $31 a week, not $42; or in 2006 earning on 89 cents for every 1980 dollar.

Things were a little different at the top of the ladder. For starters, to reach the ninetieth rung required $104,366 in 2006, up from $82,598 in 1980, Piketty and Saez calculated. That meant someone who was at the ninetieth rung in 1980 had to get an annual raise, after adjusting for inflation, of only $837 each year just to stay in place.

The higher one stood on the ladder above that, the more it took to stay in place. The threshold to be in the top 1 percent rose in tandem with the economy. Gross National Product per capita grew 6.7 percent, compared with an 88 percent increase in the threshold for the ninety-ninth rung on the income ladder.

To reach the top tenth of a percent, however, required increasing income since 1980 by nearly $1.3 million, to more than $1.9 million in 2006. Arid for the very top, the best-off 1/100 of 1 percent, the threshold rose from $2.4 million to $10.5 million. Looking at the average income of that top group provides an even more startling figure. Their average income was $5.1 million in 1980, but more than $29.7 million in 2006, a record. Remember that increase in annual income, $19.2 million, is after adjusting for inflation.

The pattern here is clear. The rich are getting fabulously richer, the vast majority are somewhat worse off, and the bottom half—for all practical purposes, the poor—are being savaged by our current economic policies.

That those at the top have been pulling away from everyone else in the past three decades is now so long established, so visible across many different measures of income, and so well analyzed that it is accepted by everyone who has examined the data, save for a few ideological crack pots at some of the ideology-marketing organizations that pose as think tanks. Even President Bush, a man who has joked about how closely he is identified with what he called “the haves and have mores,” sees this growing divide as a problem. “I know some of our citizens
"worry about the fact that our dynamic economy is leaving working people behind," he said early in 2007. "We have an obligation to help ensure that every citizen shares in this country's future."

To appreciate fully how much the fruits of economic growth are, under current government policies, being concentrated in the hands of the few, it is useful to perform another kind of analysis. We will examine the ratio of income growth between different groups over several long periods of time, starting with a comparison between the lower 90 percent, our "vast majority," and the top 1 percent.

Let's consider three eras. The first would be from 1950 to 1975, a quarter century when a rising tide did lift all boats and the nation was transformed into a land of broad prosperity. Setting the second era from 1960 to 1985 allows us to incorporate an early part of the era in which government began changing its policies in ways favored by many of the rich. Finally, it would be good to compare 1980 with 2005, but that will not work mathematically because the ratio would include negative numbers, since the income of the vast majority declined slightly. So instead we will use 1981, a recession year, to compare to 2005. The vast majority's average annual income was $114 higher at the end of those 24 years.

The measure is a ratio. For each additional dollar going to each person in the vast majority, how many went to each of those in the top 1 percent?

For 1950 to 1975, the ratio is four dollars more at the top for each dollar going to the vast majority. For 1960 through 1985, the ratio is $17. And for 1981 through 20.05, it is almost $5,000.

Dramatic as those numbers are, they understate the concentration of income. Let's now compare income growth for the vast majority with the top 1/100 of 1 percent, those 30,000 Americans at the very top of the income ladder.

For 1950 to 1975, the ratio was $36 to one. For 1960 through 1985, it was $459. And for 1981 through 2005, it was $141,000 to the dollar.

*Incomes Rose Only at the Top*

**Average Annual Income**

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<tr>
<td>People in 2006</td>
<td>270 million</td>
<td>3 million</td>
<td>30,000</td>
</tr>
<tr>
<td>Avg. Income 1973</td>
<td>$31,248</td>
<td>$386,519</td>
<td>$3,971,279</td>
</tr>
<tr>
<td>1980</td>
<td>$28,975</td>
<td>$399,779</td>
<td>$5,092,388</td>
</tr>
<tr>
<td>2006</td>
<td>$30,659</td>
<td>$1,242,595</td>
<td>$29,726,889</td>
</tr>
<tr>
<td>Change After 33 Years</td>
<td>(589)</td>
<td>$856,076</td>
<td>$25,755,620</td>
</tr>
<tr>
<td>Percent Change</td>
<td>(2%)</td>
<td>(221%)</td>
<td>(649%)</td>
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Examining different periods produces the same basic result: since the market-based solutions came to dominate government policy, the winners have been the rich, the very rich and, most of all, the superrich "have mores."

A major component of the markets-are-the-solution policies has been the drive to lower tax rates on those with high incomes and on investors. When President Reagan, was elected, the top income tax rate was 70 percent, meaning on the last dollar of income those at the top paid 70 cents in taxes. Those high rates fueled the sale of tax shelters, which, advocates of lower
rates said would be a much smaller problem if rates were cut. (Instead, tax shelters continue to proliferate among the rich.)

Today the top tax rate is 35 percent. President Bush said during the third election debate in 2004 that most of the tax cuts he sponsored went to low- and middle-income Americans. That was not even close to true.

In fact, most of the savings—53 percent—will go to people with incomes in the top 10 percent over the first 15 years of the cuts, which began in 2001 and would have to be reauthorized to keep them in effect through 2015. More than 15 percent of the tax cuts will go to the top tenth of 1 percent, a group that is now 300,000 people.

In addition, because of the Bush tax cuts, those earning more than $10 million a year pay a smaller share of their money in income, Social Security, and Medicare taxes than those making between $100,000 and $200,000.

The Tax Policy Center calculated these numbers at my request in 2005. Their help was sought because the computer models used by the government do not parse the top 1 percent, despite the enormous span of incomes it represents, and a model at the Heritage Foundation was not yet operating.

The center is a joint project of the Urban Institute and the Brookings Institution, two middle-of-the-road-to-liberal research organizations in Washington. The economists leading the Center—Len Burman, Bill Gale and, Gene Steuerle—served as tax policy advisers to President Reagan, the first President Bush, and President Clinton: Again and again over the years, officials at the Bush Treasury Department have gone out of their way to express respect for both the reliability of the Tax Policy Center model and the integrity with which the economists who created it have approached their work.

So when shown the center's analysis and asked for comment, it was not surprising that the Bush administration said it had no quarrel with any of the findings. A spokesman deemed the model used to generate the estimates "reliable."

The administration did press one point that it said was important. The tax cuts sponsored by President Bush have made the income tax system more progressive, shifting the burden slightly more to those with higher incomes. The administration emphasized that the president supports a progressive tax code in which the more you have, the greater the share of your gain is paid in taxes.

The idea of progressive taxation is central to democracy. Indeed, the idea that taxes should be based on ability to pay was intertwined with the birth of the first democracy, 2,500 years ago. Ancient Athens had been a tyranny in which each person paid the same tax—a hard burden for most, a trifle for the rich. Then a moral principle was developed: The more one gained economically from living in civilized society, the greater one's duty to maintain that society by paying taxes. Every classic worldly philosopher—Aristotle, Plato, Adam Smith, Karl Marx, David Ricardo, John Locke, and all the rest—endorsed this moral principle, arguably making it the most conservative principle in Western civilization.

However, the Bush administration claim that the recent tax cuts had made the income tax system more progressive seems to fly in the face of a recent Internal Revenue Service study. It found that the taxpayers in the top tenth of 1 percent also saw their share of taxes decline in 2001 and 2002. The Tax Policy Center computer model results also did not seem to support the Bush administration's claim. Then a Treasury spokesman, Taylor Griffin, explained. Griffin said that the income tax system is more progressive if the measurement is based on the share borne by the top 40 percent of Americans, rather than the top tenth of 1 percent.

The Bush administration is right that the share paid by the top 40 percent is higher now than it was in 2000. Those in the 39.9 percent immediately below the very top may find small comfort in that detail, however.

There was another point the Bush administration could have made, but did not. It concerns the 400 very-highest-income taxpayers, a truly thin slice of Americans. To get into that group in
2000 required an income of at least $88 million. They averaged almost $174 million each. Those 400 taxpayers, about 1,200 people, were so well off that they had more than 1 percent of all the reported income in America in 2000. The Bush administration continues to analyze the incomes and taxes of the top 400 taxpayers, but will not disclose the numbers for years after 2000, which would have shown the impact of the Bush tax cuts.

Here is what I found by analyzing the 2000 data as if the Bush tax cuts had applied. A separate analysis by Robert S. McIntyre of Citizens for Tax Justice, using more sophisticated techniques, produced almost identical figures.

Out of their average incomes of nearly $174 million, under the Bush tax cuts the top 400 taxpayers would have paid the government 17.5 percent in income, Social Security, and Medicare taxes. For people who make $100,000 to $200,000, the tax burden is much higher at 20.6 percent.

Even more interesting results arise from comparing the effects of the Bush tax cuts with the changes for investors that President Clinton signed into law in 1997. During Clinton's two terms, the effective income tax rate of the top 400 fell from almost 3.0 percent to 22.2 percent. Applying the Bush tax cuts yields a rate of 17.2 percent for income taxes only. That means Clinton gave the richest of the superrich a much bigger tax cut than Bush. Under Clinton, their effective tax rate fell by almost eight cents on the dollar; under Bush, it fell only five.

Societies in which the few deepen their pockets while the many see theirs grow lighter are not stable. America is so fabulously prosperous that we have seen only at the extreme edges the kind of political upheaval that can grow from a loss of hope and a lifetime of work for a shrinking paycheck. And when the growing income gap of America is compared to other countries, we look most like three nations whose societies most Americans would not find appealing—Brazil, Mexico, and Russia.

A young life is a terrible thing to waste. Most modern nations try to limit childhood poverty for reasons both moral and practical. Better than one in six American children live in poverty, about 12.3 million children in 2005, the Census Bureau calculated. Compared to other modern nations, many of them far less rich, the United States does poorly by its children. In terms of material well-being, the United Nations ranked the United States seventeenth on a list of 20 modern countries, right below Portugal.

Allowing so many children to grow up in poverty imposes huge costs, but is of little or no value in terms of soliciting campaign contributions. So just how much does it cost our society to have so many children grew up in poverty? What are the costs of reduced productivity, smaller incomes when they grow into adulthood, a greater propensity to commit crimes, and the costs of being less healthy? About $500 billion a year, according to a study commissioned by a liberal advocacy group, the Center for American Progress. But once Congress heard that report in early 2007, and the inevitable criticisms that the number was just an estimate, it quickly turned its attention back to matters more pressing to the party of money.

Even Alan Greenspan, the once-obscure economist whom President Reagan elevated onto the national stage and who then served as Federal Reserve chairman, warned Congress in 2004 about the widening gap between the rich and the poor. "For the democratic society, that is not a very desirable thing," Greenspan said.

We now have almost three decades of experience with the idea that markets will solve our problems. The promised results are not there and there is no reason to believe that they are over the next horizon, just a few more subsidies away. Electricity costs more and its delivery is less reliable. Many hundreds of billions of tax dollars have been diverted to the rich, leaving our schools, parks, and local government services starved for funds. Jobs and assets are going offshore, sometimes to the detriment of not just the economy, but national security.

We have layered subsidy upon giveaway upon legal absolution for reckless conduct in a chaotic attempt to protect jobs, and it has riot worked. We pour billions into subsidies for sports teams and golf courses, a folly Adam Smith railed against in his day. Our health care system
costs us far more than that of any other industrial country and yet we live shorter lives than the Canadians, Europeans, and the Japanese. We stand alone among modern societies in making tens of millions of our citizens go without health care, many of whom die or become disabled because of this nutty idea that medicine is a business, not a service. We have erected obstacles to the earnest but poor who seek to better themselves through library study and higher education.

And our politicians in both parties are hypocrites of the first water, nearly every one of them. They vote to make the poor sacrifice again and again so that the rich can have more, yet they run for office handing out photos showing that they regularly attend religious services. To those who do not get this last point, take a moment to ponder the inner thoughts of the Pharisees. Do you think they thought themselves evil? Of course not. In their own minds, they had justifications for what they did, assuring themselves that they were the most moral of men.

Except for our technology, our electricity and powerful motors, we are the same as the ancients. And like great societies that we can look back upon, which reached a high point and then headed down the road to oblivion, we too are taking from the many to give to the few. "He that oppresseth the poor to increase his riches, and he that giveth to the rich, shall surely come to want," it says in Proverbs 22. Wise words to memorize.

We have become a society in which this injunction, and many others like it, are ignored. Even when we seek to help people, as with the drug benefit for older Americans, the mechanism often is designed first and foremost to take care of the corporate rich. The net effect of our policies, the evidence for which is overwhelming, is that we are redistributing income up. Through subsidies and tax cuts and rules that depress the incomes of most workers, the immediate future looks very bright for the already rich. Indeed, to borrow from the song, their future's so bright they gotta wear shades. :

So what, if anything, can we do? Here's the good part. After reading all of these blood-boiling stories, we actually can do something. The whole idea of America is that we can solve any problem we want to solve. We can form a more perfect union, establish justice, ensure domestic tranquillity, provide for the common defense, promote the general welfare, and secure the blessings of liberty to ourselves and our posterity. For some thoughts on what we can do, please read on.
Conclusion
What To Do?

This disposition to admire, and almost to worship, the rich and the powerful is the great and most universal cause of corruption of our moral sentiments.
Adam Smith

Woe unto him that buildeth his house by unrighteousness, and his chambers by wrong; that useth his neighbour's service without wages, and giveth him not for his work.
Jeremiah 22:13

RONALD REAGAN SET THE NATION ON A NEW COURSE IN 1980 with his simple question, “Are you better off now than you were four years ago?” We now have a quarter century of experience and data that allows us to judge whether to stay the course or change direction.

In real terms, America today is more than twice as wealthy as in 1980 and the economy is putting out two-thirds more per person. Those are tremendous accomplishments. So where are the benefits of all this increased wealth and economic output?

Incomes for the vast majority have stagnated, not grown. The share of workers earning poverty-level or lower wages declined only slightly, from a little more than 27 percent of all workers in 1979 to a little under 25 percent in 2005. For private production and nonsupervisory workers, which covers four out of five wage-paying jobs, pay increased in real terms, but just barely. The increase was the equivalent of getting a raise each January of about a penny an hour. This average wage increased from $15.78 to $16.11, or just 33 more cents per hour after 26 years.

Family incomes are up slightly, but that is because more people hold two jobs and a growing share of women with children earn wages. Having less time for child rearing imposes its own social costs.

The percentage of American children living in poverty in 2004 had barely changed since 1980, with growing poverty among whites and Hispanics more than offsetting a one-third decline in the poverty rate among young African Americans.

Year after year, we are told there is less money for the basics that sustain society. Hospitals close. Libraries reduce hours, buy far fewer books, and in some places are shuttered. Schools eliminate classes in music and art and, in some places, reduce the teaching of arithmetic because of federal mandates to test in only one subject, reading. Maintenance of the infrastructure is deferred for lack of funds, a malign neglect of public assets that results in the collapse of bridges and dams, in sinkholes that appear out of nowhere, and explosions of steam pipes and other unseen urban support systems.

This is not for lack of government spending. Despite all the rhetoric about cutting taxes, combined federal, state, and local spending as a share of the economy is basically the same now as in 1980.

The official figures understate reality, however. Government keeps borrowing as well as taxing. Borrowing is a kind of tax on the future that crowds out other spending. Interest on the federal debt in 2006 totaled more than $405 billion, an amount equal to all the individual income taxes paid from January through mid-May. The government did not have the cash to make all of these interest payments, however, since so much of it was paid by taking on more debt.

Our state and local governments also cut spending on basics, while taking on ever more debt. Under Governor Jeb Bush, for example, Florida cut state taxes by $19 billion while borrowing $22 billion on which its citizens now must pay interest.

This has happened when the overwhelming focus of policy in Washington, and to a lesser extent the state capitals, has been on the economy. Both parties have bought into the Reagan
policy of speaking about government in economic terms, mostly in how it takes from you in
taxes and costs business through regulation. Ask not what you can do for your country; listen
instead to what government should do for your bottom line.

At the same time, those at the top have done fabulously well. Chief executive officers, who
in 1980 made about 40 times what workers did, now make hundreds of times more than their
workers. The hedge-fund managers make astonishing sums, the top 25 each averaging $11
million per week in 2006, while paying taxes at lower rates than middle-class workers.

In 2007 just three hedge-fund managers made nearly $10 billion—John Paulson at $3.7
billion, George Soros at $2.9 billion, and James Simons at $2.8 billion. That was their one-
year income, not their accumulated wealth. On most of it they paid a 15 percent federal income
tax or, through deferrals, no tax. The share of national income going to the top 1 percent, the
top tenth of 1 percent, and the top 1/100 of 1 percent are at levels not seen since Herbert
Hoover was president. The share of stocks, bonds, and other corporate wealth owned by those
at the top keeps rising despite all the individual retirement plans government has promoted to
replace the traditional defined-benefit pension. The number of people with savings accounts at
the bank or credit union dwindles, while the supply of tax-free bonds sold to the highest-income
Americans proliferates.

These results should not surprise. For a generation the policy of the federal government has
been to make the rich richer, even when those riches come at the expense of everyone else.
There are many elements to this policy. Giveaways of money and seizures of property to avoid
market forces, for example, impoverish everyone but the recipients of this largesse. Rules that
make it easy to rig markets, break unions, and shortchange workers all benefit the rapacious
among the rich. Then there are trade policies that allow capital to move freely across borders,
combined with a determined effort to make less government information available on the
grounds that it will interfere with the privacy of businesses. For the already rich the least risky,
most profitable way to grow even richer is through government favors, be it cash, property,
favorable rules, or law enforcement that either lacks the resources to act or looks the other way.
We have gone astray.

The founders did not create America to make us rich. Washington, Jefferson, Franklin, and
the others were among the wealthiest men in the colonies. They were not seeking to enhance
their own wealth when they stuck their necks out. They risked their lives and property for the
principle of self-determination, for the idea that whatever our problems, we can solve them
ourselves better than King George, a parliament we did not elect, or any power not accountable
to the people.

The founders risked their lives so that the human spirit might flourish, and make the world a
better place. They created America so that we could be free to live our lives as we choose
without regard to religion or creed, to which we have since added race and gender.

At first, they failed. The original American government collapsed because the Articles of
Confederation bore little relationship to the self-evident truths articulated by Jefferson and the
common sense of Thomas Paine. That failure should remind us that the government we have,
and the freedoms it protects, are perishable.

The second American republic has endured for more than two centuries because, under the
Constitution, we devised elegant and principled solutions to problems that have vexed man
since the first organized society. One was the need for a government with the revenue and
authority to act, but that derived its powers from the consent of the governed, working for their
benefit, not as a power unto itself. Another was creating a structure of three separate and equal
branches to make, administer, and interpret laws. This structure limits the use of power, the
great corrupter.

Under the Constitution, we enumerated the rights of the people, including the right to speak
our minds, worship or not as we choose, and be free from predation by the state, which
historically dealt with the inconvenient individual by having him killed or thrown in the dungeon.
All of our other rights ultimately stand on that one, habeas corpus, the right to have our case for freedom heard by an independent judiciary. Since then, we have expanded the franchise beyond white men with property to everyone who reaches adulthood.

In this way we created a nation of laws, not of men. We set forth the principles for this bold experiment in 52 words whose eloquent wisdom we too often forget:

>>We the People of the United States, in Order to form a more perfect Union, establish Justice, insure domestic Tranquility, provide for the common defence, promote the general Welfare, and secure the Blessings of Liberty to ourselves and our Posterity, do ordain and establish this Constitution for the United States of America.


Yet for more than a quarter century, we have acted as if economic gain is the great purpose of government. Our Supreme Court has equated with free speech the dollars given to politicians in the form of campaign contributions, concentrating the corrosive effect of money on sound policy by giving greater voice to those with both the means and the reason to influence who wins elections. Our policies have resulted in concentrations of wealth and income at the very top that make us more like Brazil, Mexico, and Russia than Canada, Europe, Japan, and Australia. And we have seen that the fear Reagan spoke of—that the rabble would drain the government's treasury—has come true, but with a twist. It is the rich who are gorging themselves on the government with giveaways, favors, contracts, rules that rig the economy, tax breaks, and secret deals.

No society can endure if it ignores the problems of a growing share of its people. Adam Smith told us this when he wrote, "What improves the circumstances of the greater part can never be regarded as an inconvenience to the whole. No society can surely be flourishing and happy, of which the far greater part of the members are poor and miserable."

We are not merely 300 million individuals who share the same geography, but a society—and a great one provided we remain true to the precepts of liberty and justice for all.

Three principles can help guide us to make wise decisions about our economic policies. They epitomize the fact that rules define a civilization:

A society that does not embrace a common purpose for its existence has no standard against which to judge itself, making it vulnerable to the corruptions of men who chafe at the limits of law.

A society that does not address the needs of its members, especially the vulnerable, weakens itself from within while wasting its most valuable resource, the minds and talents of all its citizens.

A society that takes from the many to give to the few undermines its moral basis and must in the end collapse.

How many of your family, friends, and neighbors are you willing to see bankrupted by medical bills or condemned to awful disabilities or early death because they cannot afford proper health care? How much should you, your family, and people like you sacrifice so that corporations, including insurance companies, can maximize their profits by providing only the minimum care necessary?

What does it profit us if we remove from our land the jobs of the many who work with their hands? How do we benefit as a society when government rules tell the owners of factories, patents, and copyrights to go offshore?
Why do we allow less and less competition—there are only four major accounting firms, for example—when there is clear evidence that this results in higher prices and worse service? Do we want to become a society mostly of service workers, when for many that means being a servant? Will it all fall apart, as Scott Cook, the one-armed Oregon entrepreneur, warns, because we pursue short-term profit, focus on service jobs, and subsidize the rich while diminishing the bounty nature provides us?

Do we really want to tax ourselves so that rich men can spend less flying in luxury to play golf? Must we be forced by the coercive power of government to give part of our sustenance to the mass opiate of our age, commercial sports? How much are you willing to give up from your paycheck so that Dick Cabela and Johnny Morris can sell fishing tackle and guns from stores that you bought for them with your taxes? How many hours are you willing to work each year so that Tyco can get free labor to check out burglar alarms?

How much more are you willing to pay each month for electricity on the theory that competitive markets are superior to regulation, when the evidence shows that regulated utilities and municipally owned systems provide reliable power at lower cost? Do you want more markets that are easily manipulated?

Do you want a government that allows trillions of dollars of borrowed money, wrapped in veils of secrecy by unregulated hedge funds, to influence the markets in which government says you must keep your 401(k) nest egg? Are you willing to give the government a much larger share of your income than do the hedge fund managers who every few days make more than you will in a lifetime?

The gifts, favors, and tax breaks we bestow on the rich would shock the conscience of Andrew Mellon, the oil man and banker whose words are often invoked in support of current policies favoring the rich. As with Adam Smith, Mellon's words are often quoted selectively by those who shill for the rich. Consider what Mellon wrote in his 1924 book *Taxation: The People's Business*:

> The fairness of taxing more lightly income from wages, salaries or from investments is beyond question. In the first case, the income is uncertain and limited in duration; sickness or death destroys it and old age diminishes it; in the other, the source of income continues; the income may be disposed of during a man's life and it descends to his heirs.

> Surely we can afford to make a distinction between the people whose only capital is their mental and physical energy and the people whose income is derived from investments. Such a distinction would mean much to millions of American workers and would be an added inspiration to the man who must provide a competence during his few productive years to care for himself and his family when his earnings capacity is at an end.

"People." "A man's life." Mellon shows empathy when he employs those words—a moral sensitivity missing from the acts of our elected officials who embrace the policies of taking from the many to benefit the few. As our government has focused increasingly on riches, its leaders have lost sight of our people.

The problem of taking from the many to further enrich the few will change only when we begin to address it. We must start by acknowledging our failures, just as the founders did when the Articles of Confederation proved unworkable.

For starters, look at what we have done to health care. America spends more and gets back less from its system than any other industrial country. We rank by various measures down with Cuba, of all places. That alone should scream at us that our policy of corporate health insurance does not work. That one in seven of us has no health coverage at all should shame us. Even apart from shame, on a practical level having so many people without health care coverage is a drag on our economy through lost productivity—from injuries and illnesses not properly
treated, lives shortened, and financial devastation caused to families who played by the rules, but were not winners in a system that makes caring for people a profit-driven business.

Just as counterproductive is our policy of driving up the cost of housing through government policies. The result is making us poorer, not richer, by adding enormously to debt burdens. The official data show that for every additional dollar of home equity people added since 1980 they took on two more dollars of debt. We have replaced the ideal of home ownership with a hamster wheel, with most citizens working harder and harder to pay mortgage interest and saving ever less for retirement. This is folly.

And all of the welfare we shower on the rich, from Warren Buffett to George Steinbrenner to Dick Cabela? The market cannot work its magic when Buffett gets a freebie. Competition cannot set the price when an industry is exempted from the laws of competition. Honest businesses like Gander Mountain cannot succeed when the government slips money to the competition. Bad money drives out good.

Regulation by detailed rules has not worked. A century ago the reformers of the Gilded Age believed that if we just got the rules right, a just society would follow. Instead, the rules became ever more finely diced, creating unintended opportunities for mischief and often creating loopholes and favors for those whose conduct the rules were supposed to constrain.

Those rules work best which are self-enforcing, rules that by their nature reward proper conduct and punish misconduct. A good example can be found in the rules that for many decades governed lawyers and accountants. Under the old partnership rules, each partner was fully responsible for the deeds of every other partner. This created an incentive for lawyers and accountants to police their partners, to stick in their noses ' at any hint of misconduct, out of pure self-interest. The rule created a simple reality: look the other way, lose your house.

But at the start of the current era of government for the rich, those rules were changed. Now we have "limited liability partnerships." The LLP structure rewards those who look the other way. Under these new rules, you may lose your investment in the firm itself, but that is all your liability. Given the brazen misbehavior by the major accounting firms, and by more than a few law firms, it is time to go back to the old rules.

The fundamental policy for those on whom we confer power as lawyers, accountants, executives, and stewards of other people's money should be rules that make the costs of misconduct so high that no rational person would violate them. As New York Times columnist Gretchen Morgenson says, if you add up all the fines imposed on Wall Street and compare them to the profits these firms earn, the penalties get lost in the rounding. Fines, whether imposed on railroads for safety violations or on Wall Street for cheating investors, are meaningless unless they are so large that they take back all of the ill-gotten gains and then take even more to make the price of misconduct too dear to risk.

We should not allow the fact that many issues today challenge normal human understanding and as a result create opportunities for cheats. We need to strengthen law enforcement to thwart thievery by contract or computerized calculation. We need to vote out officials, even ones we like for some emotional reason, when they work against our interests. When it comes to handouts to the rich, we need to just say no.

So what to do?

The solution lies not in changing this rule or that, but in altering our attitude about our power to shape our democracy. We are not powerless to address any of these problems or the many others that confront us. It may seem that the problems are so large, and individually we are so insignificant, that we must just accept things as they are. We are encouraged in this belief—that we lack the power to change the course of history—by those who profit from our meekness. But the notion that we cannot shape our own destiny is nonsense. It is also profoundly un-American.

It is also morally reprehensible for the rich to take from those with less. If our hearts do not tell us this is so, the Bible does again and again and again. So do all of the other great religious and moral texts that have come down to us through the ages. In this the ministers, rabbis,
imams, and other moral leaders can exert great influence by preaching from the religious texts, citing the myriad references to how it is wrong to give to the rich, wrong to take from the poor, wrong to build up great wealth by taking even from the merely prosperous to add to the fortunes of the rich.

To fail to do this is to push us back to the time when property was theft, when the rich were so only because of what they took from others by force or threat. The creation of wealth through the concepts of ownership, trade, insurance, the time value of money, and the rise of mass manufacturing and now digital design has been an enormous benefit to mankind. So have the advances from our knowledge of how to manipulate the physical and conceptual worlds, from vaccines and clean water to algorithms. No good can come from undermining the legitimacy of property, but much damage can be done by abusing the coercive power of government to take from those who have less to benefit those who have more.

As part of this, we need to restore the ethos that cheating is wrong. Period. If we honor athletes who take steroids to pump up their performance, how can we complain when business owners pocket subsidies? Cheating, like pregnancy, is not a halfway condition.

Taking a stand will no doubt be difficult for those organizations that purport to favor free markets, because so many of their donors are on the dole. They should ask themselves how much they are willing to sully their reputations, where they will draw the line. Would they take money from a drug lord? An embezzler? From those who solicit subsidies? Better to fold with integrity than press on with dishonest money.

What of those who assert, as many business owners interviewed for this book did, that if the rules allow them to take subsidies then there is nothing "wrong with doing so? Indeed, one billionaire argued that failing to take a subsidy could be seen as a wrong in itself, a failure to maximize profit for shareholders. Must one take money left on the counter by a merchant? Just because you can do something does not mean you must, or even should. Their attitude serves to reinforce the importance of rules in shaping behavior.

For years now I have traversed America speaking about the issues in this book and my previous work, Perfectly Legal. I expect to continue doing so as future books are published about the real problems of the American economy, our nation, and the world. Everywhere people ask variations of the same question and express a similar concern. In churches and unions halls, in private clubs and community college lecture rooms, over delicate wines with the privileged and macaroni salad with the poor, the question is pretty much the same: What can we do?

The companion concern to this question is the widely held view nothing can be done, that "they" are too powerful to allow any change. The abuses you have just read about can be stopped. The problems can be solved. My part was digging out the facts, stripping away the complexity, and making it meaningful for readers. Now comes your turn. It will not be easy, but it can be done.

We can solve any problem we choose to address. No one, and no "they," is too powerful, too unaccountable, too entrenched to prevent society from improving itself.

The only thing that is un-American is the belief that we cannot solve a problem.

We can exercise our power as a people to make the world, as Susan B. Anthony reportedly said in her last moments, "a better place" and that when a cause is just, victory is inevitable if only we are diligent and persevere.

Solving our problems will not be easy. It will not happen overnight or even in a few years. It requires resolve. It took us a long time to dig ourselves into all of our debt, into our policies of taking from those with less to give to those with more, into creating a society of corporate socialism at the top and raw market forces down below. But we can change our country for the
better. And we must if we are to endure as a nation and for the promise of our founding that people can be free and the promise of liberty fulfilled.

Our nation began with the enslavement of human beings enshrined in our Constitution, yet we got rid of slavery. It cost more than 600,000 lives in the Civil War and the mess it left behind still lingers, but those who wrapped slavery in moral language and claimed it was right were vanquished. Women wrought from men the right to vote. We enacted over time a multitude of laws that created a better America. Claims that it was morally just that small children work in factories have been swept into the. dustbin of history, along with a number of other self-serving nonsense perpetrated by the rapacious among the rich and their shills. And keep in mind that many of the reformers were themselves among the wealthiest of Americans; they understood that the problem is not money, but its proper place. As it says in the modern versions of Timothy 6:10, “the love of money is the root of all sorts of evil.”

Change in a democracy begins with people acquiring knowledge. That is the purpose of the stories in Free Lunch and its predecessor, Perfectly Legal—to empower people to understand the subtle, obscured, and complicated ways that their pockets are being picked, responsibilities are being shed, and unnecessary obligations imposed on you. These policies were designed to be deceptive, but now their real purpose and effect are out in the open. So here are some steps you can take:

SPREAD THE WORD. At the local coffee shop; the barbershop or hair salon; on the steps at the church, mosque, or synagogue; with friends and family and everywhere else, tell people what you have learned. Think about how to reduce to brief, cogent points what issues trouble you the most. And then encourage others both to learn more and to engage others. Consider giving friends and family gifts of Free Lunch with a note about the reasons you want them to read it, and perhaps a caution about how angry it may make them.

Write letters to the editor—brief letters, just two to six sentences—when a giveaway of your tax dollars makes the news. E-mail reporters, columnists, and the chattering classes on television with pointed and brief comments. Write to those who receive subsidies, and in the case of companies to their boards of directors and even stock analysts. Again, be brief and pointed. One letter may not have much impact, but a steady stream of them from many people will.

Call the hosts on talk radio (and challenge those "who describe themselves as conservative but speak in favor of gifts of taxpayer money to the already rich, as with the subsidies to retail stores and sports; stadiums described in these pages). On those rare occasions when elected officials and candidates for office make themselves available in public, show up and ask questions. For maximum effect write your questions in advance and hone your words. Better, get several friends to come so you can all ask questions that are related. Taking time to focus questions to elicit answers is crucial to getting your points across. And tell politicians that if they vote to take money from you to funnel it to those better off than you are that you will fight them.

Get in touch with the editorial page editor of your local newspaper and editorial directors of local TV stations and educate them.

DEMAND DISCLOSURE. When a news account reports that a "tax increment" financing deal is in the works, write to the agency and demand the contracts and details. The agency may well refuse your request, which you can then use as the basis for a (brief) letter to the editor, for calls to talk shows, and for spreading the word in other venues to raise both issues of income transfers-up and the secrecy surrounding them.

In particular, call in to C-SPAN and other shows and ask those who say they are there to urge lower taxes what they have done, and will be doing, to stop giveaways to private
businesses and wealthy individuals. And, really, write down your remarks in advance so you can be focused and have the greatest impact.

Here is a line I urge you to memorize:

If it is a sound investment the market will make it. If the investment is un-sound, why should taxpayers be forced to subsidize it?

When a giveaway project does go through, write, go to public forums, and find other ways to demand accountability, to demand that promised jobs and investments actually come through or that the money be paid back, with interest.

These informal actions may seem meaningless, but they can change our national debate. Politicians are the same whether they lived in ancient Rome or today in Rome, New York. They hold a wet finger up to detect shifts in the political winds and they alter their behavior or, in time, find themselves voted out.

There are formal actions you can take, too.

ORGANIZE AND DONATE. Join existing groups that fight giveaways. They exist across the political spectrum. If your area lacks an organization that is critical of these policies, organize your community—religious leaders, social services providers, owners of local businesses, union leaders—to start your own. Find a hall for a meeting, get some knowledgeable people in, and hold a community forum with flyers that make compelling points about how your tax dollars are being diverted and the effect on your pocket and on government services. Public employees from teachers and nurses to police officers and biologists can be valuable allies in this cause of making sure that tax dollars are used only for public purposes, not for private enrichment.

Urge transit, taxpayer watchdog, and other groups to demand that Congress end the subsidy to railroads that absolves them of all responsibility for the people maimed and loll by their actions. When a train crashes and people are injured or killed use it as an opportunity to raise issues of railroad safety practices and the shifting of private responsibility into taxpayers.

In some states there are consumer organizations dedicated to looking out for customers in utility rate cases with names like the Citizens Utility Board or Consumer Advocate or Public Interest Research Group. Ask them to raise issues like the diversion of tax dollars—built into the rates you pay for power, gas, water, and telephone services—for private gain. In these matters the best allies you may find will be big businesses because they pay a lot for power, water and other utility services.

Donate money to organizations that fight these policies. If you are in a position to make significant gifts, in the thousands of dollars or more, make gifts conditioned on their being used for specific purposes, such as holding a Saturday community conference on giveaways.

Do more than give money. Give your time. You will find that when you donate time you will be more effective and, if the organization makes a difference, more generous.

The more aggressive may want to go further, working to shame those who take from those with less to add to their fortunes as with Donald Trump and the poor of New Jersey and the Hiltons and poor children. Consider contacting charities that give awards (which are, at their core, fund-raising devices) and telling them they should be ashamed to honor the person they choose. In some cases organizing a demonstration at the charity gala may have an impact, making the charity wary and creating an opportunity to get news coverage, of the issues.

SHOP. For those buying a home or investment property, do not just accept the land title insurer proposed to you. Tell your real estate agent, lawyer, or other professional that you expect them to find the lowest-cost provider. Ask your bank or other mortgage lender the reasons they do not buy this insurance wholesale. That is an especially good question to ask credit unions, which are nonprofit lenders, and their national association. Also, write to your state insurance commissioner and ask what steps have been taken to stop price gouging. Ask your state legislators to hold formal public hearings on the reasons this industry is allowed to
charge twenty times or more the reasonable costs of land title insurance and ask that the lawmakers to put serious teeth into the laws barring "referral fees" and other disguised bribes. Press existing organizations, like Consumers Union and the AARP (which originally stood for American Association of Retired Persons and now goes solely by the abbreviation), to take up the cause and note that even Forbes magazine investigated land title insurance price gouging.

One reform that deserves intense scrutiny is public financing of elections. The obvious concern is that such a system would benefit incumbents. However, the limited evidence available so far from Maine and Arizona is that voters appear more likely to toss out incumbents when the public finances campaigns.

We should also return to, and expand, the promises Newt Gingrich made in the 1994 elections about making Congress act openly and not as a power unto itself. Indeed, we should expand on those now forgotten promises. Requiring members of Congress to keep a log of every meeting and contact, and making it available for inspection on request as well as posting it on the Internet in a standard format each week in a permanent archive, would do much to create transparency. Except for matters of national security, all government policy making officials—presidents, governors, cabinet secretaries, agency heads, and judges—should be required to keep logs of whom they met with, the subject, and to make them available on request. Internet posting in standard, searchable format would be better. And such Internet posting would not be difficult in this digital age.

There is another major reform that could speed the return of a government that cares more about its people than the bottom lines of a few. It goes to the corrupting influence of money in selecting who rises to elective office, gaining the power to make the laws, administer and interpret them. Our Supreme Court has sanctioned this legalized bribery, saying we can do little to reduce the influence of money on elections. In that case, let's forget about campaign finance reform and focus instead on politician finance reform.

Americans seek a free lunch when they do not pay the real costs of government, but instead expect elected officials generally, and members of Congress in particular, to rely on the kindness of strangers. Free rides in the company jet, golf outings, dinners, and a host of other emoluments naturally exert a tug on the system, pulling it toward those who do the giving. In recent years, we have seen politicians hire their spouses as fund-raisers and pay them a portion of the donations they raised. Others see their family members hired by the very groups who lobby them.

We cannot stop all of these abuses. But we can stop many of them by taking a principle in our Constitution and expanding on it. We allow every representative and senator to send out all the mail they want for free. It's called the franking privilege. Let's extend that concept to their expenses.

Let each member of Congress spend however much he or she deems necessary to do his or her job. If we can imbue representatives and senators with the power to make laws, surely we can give them the authority to manage their own expense accounts.

This would come at a price: No more free trips, no more free meals, and no more gifts. Senator, if you need to inspect the cleanliness of the sink behind the bar at a resort in Tahiti, go right ahead, just give us the receipts with an explanation of the costs. We will collect the receipts from every elected representative monthly and post it all on the Internet in a format that makes for easy analysis.

Every dollar, and every meeting, must be disclosed. And we will pay for it all, subject only to the usual penalties for embezzling, the punishments accorded by the full House or Senate because of their exclusive right to judge the fitness of members, or the decision by voters to oust a spendthrift.
In this we can move politics back toward the people and away from monied interests. The penalties for taking anything—even a free shot of whiskey—should be swift, certain, and severe. Take a gift, go to jail. Call it zero tolerance for lawmakers.

Let us also pay the real costs of maintaining two households, one back home and one in Washington, as well as going back and forth as often as the lawmaker chooses. Sure, the Congresswoman from Hawaii will spend more on travel than the one from Northern Virginia, but people are smart enough to figure that out.

This approach will cost us more in terms of the budget for Congress. But it would save us far more by reducing the giveaways, the rigged rules, and the favors for the rich. Think about all the lawmakers who for a few thousand dollars cost the taxpayers millions, even billions. Surely paying the real costs of Congress has to be cheaper than the dishonest system we have now. A free lunch always costs more than an honest one.

Just debating the idea that we should pay the full costs of Congress would have value, opening our eyes to the subtle ways that we systematically corrupt our political system. A debate on making members of Congress into public servants, instead of beggars for favors, would get us thinking as a nation about how every single free lunch cheats us all.

In the end, we must be the ones who make our government work, fulfilling the promise of the preamble to our Constitution. No one else is going to do it for us. Reform begins with you.

Notes

This book is based largely on my reporting for The New York Times, that of other reporters, and extensive reporting for Free Lunch by me and those retained as reporters for this book. The primary sources for official data are the statistical reports posted on the Internet by the Bureau of Labor Statistics, the Census Bureau, the Commerce Department, the Congressional Budget Office, the Federal Reserve, the Internal Revenue Service, and the White House Office of Management and Budget.

I have taken one liberty for clarity. In the few places where people's thoughts are recounted in italics, their recollections are presented with more formal structure than had they been quoted directly as they recalled their thoughts and feelings.


Chapter 2. MR. REAGAN'S QUESTION

9 On the surface: Computed from Bureau of Labor Statistics and Census Bureau data.


11 In ways that most Americans: Organization for Economic Co-operation and Development Factbook 2007- at sourceoecd.org/factbook.

18 **Consider one example:** 99.25 percent interest at www.cashcall.com/General/Rates.aspx.


24 **There is a reason that 35,000 people:** From Hamilton, Lee. "We Pay a High Price for Special-interest Lobbying," The Center on Congress at Indiana University, www.centeroncongress.org/racUo_cormentaries/we_pay_a_high_price_for_special-interest_lobbying.php, and reports at opensecrets.org.

25 "**A democracy cannot exist**": "Roar Approval for Barry," *Manchester Union Leader*, March 6, 1964, front page.

### Chapter 3. TRUST AND CONSEQUENCES

26 **Half an hour before daybreak:** "Railroad Accident Report: Derailment and Subsequent Collision of Amtrak Train 82 with Rail Cars on DuPont Siding of CSX Transportation Inc. at Lugoff, South Carolina, on, July 31.


34 **Measure deaths by the distance traveled:** author e-mail interview with Tom White, Association of American Railroads, April 18, 2007; hazmat.dot.gov/riskmgmt/riskcompare.htm (adjusted for different measures, one million miles for trains and 100 million for trucks and airliners).

### Chapter 7. YOUR LAND IS MY LAND

79 **The Mathes family:** Records of Sports Facilities Development Authority, Inc. and *City of Arlington v. Clairwood, N.V., Ramshire, N.V.*, Cause # 91-47154-1 Tarrant County, Texas, numerous news accounts, and interviews with attorneys Glenn Sodd and Ray Hutchinson.

### Chapter 19. PAYING TWICE


193 **Some of these plants were then resold:** Johnston, David Cay, "In Deregulation, Plants Turn into Blue Chips," *The New York Times*, October 23, 2006.

### Chapter 21. UNHEALTHY ECONOMICS


Chapter 26. NOT SINCE HOOVER

For the richest Americans: From the Piketty and Saez tables cited in the chapter; computations by the author using conservative deflator CPI-U-RS.
