Fixing capitalism: stopping inequality at its source

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The basic facts on the growth in inequality in the United States and elsewhere over the last four decades are well-known. There has been a rise in inequality throughout the OECD, but it has been most pronounced in the United States where the share of income going to the top ten percent has risen by 20 percentage points, with the top one percent alone gaining 10 percentage points of national income. If these gains were reversed, it would allow for an increase in the before-tax income of the bottom ninety percent of the population of almost 40 percent.[1]

The usual response from those on the left to these facts are proposals for strengthening labor unions, higher minimum wages, and other labor market protections, as well as more progressive tax and transfer policies to make after-tax income less unequal. While these are sound policy proposals, it is important to recognize that the upward redistribution that we have seen did not just happen as a natural outcome of the market.

The upward redistribution was the result of deliberate policies that were put in place for the purpose of redistributing income upward. These policies could be altered in ways that don't lead to the same degree of inequality, and which are also likely to increase the efficiency of the economy.

The most obvious, and probably most important, of these policies are patents and copyrights. These government-granted monopolies have been strengthened and lengthened over the course of the last four decades. Patents and copyright monopolies do serve a public purpose; they provide incentives for innovation and creative work. However, they are not the only ways to provide incentive. Furthermore, they can always be made stronger or weaker, depending on policy goals and the relative efficiency of these mechanisms compared with alternative incentive mechanisms.

It speaks to the bankruptcy of economics that it is standard for economists to assert that technology is a major or *the* major factor driving inequality, when it should be completely evident that it is our policies on technology, not technology itself, that leads to inequality. In a world without patents and copyrights, Bill Gates would likely still be working for a living instead of being one of the world's wealthiest people.

This paper analyzes some of the ways in which our policies have led to the immense wealth held by those at the top of the income distribution. In addition to patent and copyright monopolies, it also discusses the treatment of the financial sector, rules of corporate governance, and the laws governing Internet intermediaries like Facebook and Google.

The point of this exercise is to show ways in which we can structure the market differently so that it does not lead to extreme inequality. It is fine to try to address inequality with tax and

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[1] These numbers are drawn from Saez, 2018.

transfer policy, but it is much better to structure the economy in ways that do not generate so much inequality in the first place.

The rich and very rich have long recognized that capitalism in an incredibly malleable system. They have taken advantage of this malleability to structure it in ways that make them the main beneficiaries of economic growth. If progressives fail to recognize this malleability, and instead treat market outcomes as largely given, we will be at an enormous disadvantage in the debate over reducing inequality.

Patent and copyright monopolies

It is truly astounding that the role of patent and copyright monopolies in redistributing income upward is not more widely recognized. These government-granted monopolies are quite explicitly policy interventions, yet they are routinely treated as though they are an inherent feature of the market, with their specific form (e.g. length and scope) rarely figuring in a discussion of income distribution.

At the most basic level, we could envision capitalism without these monopolies existing at all. An economy with all the same property relations we have today, except for patents and copyrights, would have a very different distribution of income. It is standard wisdom among economists and other policy professionals that technology has increased the demand for education, especially for skills in the science, technology, engineering and math (STEM) areas. This is in turn has been a major factor in the growth in wage inequality of the last four decades.

But suppose we were in a world without patents and copyrights, and we had no alternative policies in place to replace the incentives provided by these monopolies. In that case the amount of money going for research into the development of new drugs, medical equipment, chemicals, software and computers would plummet. The demand for workers with skills in these areas would also plunge. In that case, we would not be seeing any technology-induced increase in wage inequality, as there would be no reason to believe that people with college and advanced degrees in the STEM fields would be doing especially well in the labor market.
The price of all these items would be far cheaper, since they would sell in a free market where anyone could produce the latest prescription drug, MRI machine, or computer without regard to who might take credit for their invention. That would mean that real wages for workers with less education would be considerably higher, since the price of much of what they consume would be much lower.

This simplistic thought experiment is important since it should drive home at a very basic level the fact that inequality in market outcomes is entirely the result of how we choose to structure markets, not the exogenous development of technology. This doesn't mean that we have not benefitted enormously from the innovations that have come about as a result of the incentives that were provided by patent and copyright monopolies. But we have to understand that these are policy tools that can be altered and, in some cases replaced by alternative mechanisms that might be equally or more effective in providing incentives, while not producing the same amount of inequality.

The area where the strongest case can be made that patent monopolies have not been a good mechanism for supporting research is prescription drugs. Patent monopolies both create

the absurd problem of making life-saving drugs unaffordable and lead to perverse incentives for drug manufacturers.

The first point is straightforward. Drugs are almost invariably cheap to manufacture and distribute. Without patent monopolies, most drugs would be selling for little more than the price of generic aspirin. There would no issue of affordability, except for the very poor.

However, when we give companies patent monopolies, we get into a situation where drug companies can charge enormous prices for drugs that are often essential for people’s health and/or their life. Then we have the absurd situation where progressives push for government intervention to impose price controls or negotiate prices, as though the world with a government-granted patent monopoly is somehow a free market.

In addition to the problem that the government has created an artificial monopoly, we can’t even tell the standard story of consumer sovereignty, where the consumer knows how much a product is worth to them. In the case of prescription drugs, we almost always have third party payers, in the form of either the government or insurers. The price that is paid is therefore almost entirely the result of political decisions, either directly as a result of a government determined price, or indirectly through government regulation of insurers.

But coping with exorbitant prices is perhaps the less important part of the problem. Patent monopolies not only provide incentives for drug companies to develop new drugs, they also provide incentive for them to market them as widely as possible. This means that they have incentive to promote their drugs in contexts where they may not be the best treatment for a specific condition. They also have incentive to conceal evidence that their drugs may not be as effective as claimed or that they could be harmful.

The most obvious example of companies responding in this way to patent incentives is the pushing of opioids by Purdue Pharma and other manufacturers. These companies have paid billions in settlements based on the allegation that they deliberately misled doctors on the addictiveness of their new generation of opioid drugs in order to maximize sales. Needless to say, these drug companies would have had much less incentive to lie to doctors if their opioids were selling as cheap generics.

The patent system also encourages secrecy in research. Science advances most quickly when it is fully open and findings are widely shared. However, a company hoping to gain a key patent on an important drug is not going to make its latest research available for potential competitors. We see this sort of situation with the coronavirus, where research teams around the world raced to develop an effective vaccine. Progress would almost certainly be far quicker if all their results were shared so researchers could benefit from the successes and failures of their fellow scientists.[2]

It is of course possible to have alternative mechanisms to finance research. The United States spends more than $40 billion a year financing biomedical research through the National Institutes of Health. This funding could be expanded to replace the roughly $75 billion a year in private research supported through patent monopolies.[3]

[2] To some extent this sort of sharing is happening with research on vaccines and treatments of the coronavirus, but it would be even more pervasive if no one had an interest in gaining a patent monopoly.
[3] The figure for 2018 was $75.1 billion, Bureau of Economic Analysis, National Income and Product Accounts, Table 5.6.5, Line 9.

The additional money could be routed through private drug companies in a manner similar to the way the Defense Department awards long-term contracts to develop weapon systems. The big difference is that, while there are good reasons for keeping military research secret (we don't want ISIS to be able to get information on our latest weapons systems off the web), there is no reason to want to keep biomedical research secret. A condition of the funding can be both, that any patents are in the public domain, so new drugs are sold as cheap generics, and that all findings must be posted on the web as soon as practical.

It is not necessary to go into great detail here on the mechanics of a system of publicly funded drug research, the point is that there are plausible alternatives to the system of patent monopoly financing that are arguably far more efficient.[4] And, it is important to realize that there is an enormous amount of money at stake. In the case of prescription drugs alone, the difference between the monopoly protected prices we pay now, and the free market price, would almost certainly come to more than $400 billion annually. This is approximately 1.8 percent of GDP, far more than the current amount raised through the corporate income tax.

And prescription drugs are just part of the story of the impact of patent and copyright monopolies. Medical equipment is expensive almost entirely because there are patents on MRIs and other scanning devices, kidney dialysis machines, and other forms of therapeutic equipment. The difference between current prices and free market prices would almost certainly be more than $100 billion a year. Software could be transferred at zero cost in the absence of patent protection. If we add in video games, books, recorded music, movies, and other video material, we could easily be looking at savings of more than $1 trillion a year in a patent/copyright free world, roughly half of annual corporate profits.[5]

In short, there is an enormous amount of money at stake with the current patent and copyright system. And, the beneficiaries are of course primarily those at the top end of the income distribution. In addition to Bill Gates, the list of the country's richest people is chock full of those who have made their fortunes from patent and copyright monopolies. An analysis of the 100 richest people on the Forbes 400 found that more than 27 percent of the estimated wealth came from sources that were heavily dependent on patent and/or copyright monopolies. Adding in the marginal cases brought the figure to more than 43 percent of their wealth (Baker, 2020; Dolan and Kroll, 2018).

It is an enormous analytic and political mistake for progressives to treat these vast fortunes as simply market outcomes. The beneficiaries of patent and copyright monopolies have been quite active in structuring them in ways that ensure they get as much money as possible. Progressives should be every bit as active in pushing in the opposite direction.

The financial industry: making vast fortunes and only incidentally serving the real economy

A vibrant economy clearly needs a strong financial sector capable of both quickly and cheaply processing transactions and also providing capital to businesses and households. Unfortunately, this is not a good description of the U.S. financial industry. While it provides the basis for a larger share of top one percent incomes than any other sector of the economy

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[4] For more discussion of alternative funding systems see Baker, Jayadev, and Stiglitz 2017, Baker 2016a, and Baker 2020.
[5] These calculations are explained in more detail in Baker, 2020.

(Bakija et al., 2012), it is certainly not efficient in processing transactions and channeling capital to its best uses.

At the most basic level, the narrow financial sector (securities and commodity trading and investment banking) has exploded as a share of GDP. This sector increased from 0.44 percent of private sector output in 1970 to 2.35 percent of private sector output in 2018.[6] Given the Internet bubble in the 1990s and the housing bubble in the last decade, it would be difficult to maintain that the sector has been directing capital to its best uses.

Other parts of the financial industry also do not seem to be serving the real economy well. Private equity and hedge fund partners disproportionately sit among the list of the very highest paid people in the country, often drawing annual pay checks in the tens of millions and sometimes hundreds of millions. It is difficult to see what these people do to justify such extraordinary incomes. This is not a moral judgement on the behavior of private equity and hedge funds (which is often bad for both the economy and society), it is simply a comment on their failure to produce outsized returns to their investors.

In the 1980s and ’90s, private equity funds did consistently outperform the S&P 500 index by substantial margins. Since 2006, however, the median private equity firm’s performance just matched the S&P 500 and underperformed broader indexes, like the Russell 3000, that include the smaller companies that PE firms typically buy (Appelbaum and Batt, 2017).

Many hedge funds have done even worse by their investors. A recent study of the ten-year returns of the endowments of the Ivy League schools found that the endowments of all eight schools lagged a simple indexed portfolio that was 60 percent stock and 40 percent bonds (Markov Processes International, 2018). In some cases, the gap was substantial. Harvard set the mark with its annual returns lagging a simple 60/40 portfolio by more than 3 percentage points. This is actually a very low bar, since hedge funds are inherently risky, which means that a more appropriate comparison might be a 70/30 portfolio or even 80/20. Comparisons with these higher-risk portfolios over this period would make the performance of the endowments look even worse. Needless to say, the hedge fund managers, who control the bulk of the money in these endowments were very well compensated for losing these schools large amounts of money.

Another way that the financial industry makes large amounts of money at the expense of society is by writing deceptive contracts that effectively allow it to exploit its customers. For example, many banks charge large fees for late mortgage checks or for even short-term overdrafts of a bank account that many of their customers are not aware of until they have to pay them.

There is no social purpose served by providing incentives for deceptive contracts that allow for abusive practices. We should not want to give companies incentives to find creative ways to cheat their customers. Nor should we want to force people to carefully scrutinize contracts to ensure that they are not being ripped off. This is a case where regulations requiring simple standardized contracts can provide clear efficiency gains to the economy and likely much less revenue to the financial industry.

[6] The size of the sector was calculated from Bureau of Economic Analysis data by taking the lines for compensation in the securities and commodities trading industry and also investment funds and trusts (Bureau of Economic Analysis, National Income and Product Accounts Tables, Table 6.2D, lines 59 and 61 for 2014 and Table 6.2B, lines 55 and 59 for 1970).

Another area where the financial industry makes large profits at the expense of the economy and society is by designing tax avoidance schemes. There is insufficient appreciation of tax avoidance as a source of inequality. If a company can save $1 billion on its taxes, in principle it would be willing to pay lawyers or accountants up to $999 million to do it. The tax avoidance industry can be quite lucrative for effective practitioners. (This can blur into outright tax evasion, but we can be generous and focus on legal activity.)

There are simple policies that can radically reduce the amount of resources drained off by the financial sector and the extraordinary incomes going to its top earners. At the top of the list would be a modest financial transactions tax. This would drastically reduce the volume of trading in the sector, while raising a substantial amount of revenue. For example, a tax set at 0.2 percent on stock trades, and scaled for other assets, could raise in the neighborhood of $120 billion annually, more than 0.5 percent of GDP (Baker, 2016b).

Most estimates put the elasticity of trading volume with respect to price near -1.0, which means that the reduction in expenditures on trading would be roughly equal to the amount of revenue raised from the tax. This would mean that ordinary investors would effectively see the burden of the tax fully offset by a reduction in other trading costs, leaving them unharmed by the tax. The burden of the tax is then borne fully by the financial industry in the form of less trading revenue. (This assumes that the cost of the tax is passed on fully in higher costs per trade.)

This sort of tax can be seen as equivalent to a sales tax on the financial industry. There is no reason that the financial sector should be exempted from the sort of sales taxes, or value-added taxes, that are imposed on other industries, a point that has even been noted by the International Money Fund (2010).

Also, it is important to remember that the financial markets depend in very fundamental ways on the backstop of the Federal Reserve Board and other central banks. We saw this in the financial crisis in 2008 and 2009, where the major banks were directly bailed out by central banks and governments. There were also numerous interventions to keep markets operating smoothly.

This happened again with the coronavirus, where the Federal Reserve Board engaged in trillions of dollars of asset purchases to sustain an orderly market. These interventions are arguably desirable from the standpoint of the economy as a whole, but they undeniable help to prop up the financial industry. The sector would face enormously higher risks if it did not have central banks and treasuries explicitly providing insurance against extreme events.

The private equity industry also relies very directly on the government since it makes much of its money through the public sector. More than a quarter of its funding comes from public sector pension funds. Public sector funds have an incentive to place money with private equity funds because they can impute higher returns to these investments than their investments in equities or other assets. As a result, the pensions appear better funded, even though returns on private equity have not been exceeding returns on market indexes.

Private equity funds are also benefited by the secrecy around their fees. It is a standard practice for private equity funds to prohibit their investors from disclosing their fees. It is likely that fees would be considerably lower, along with the paychecks to private equity partners, if public pension funds were required to clearly disclose all terms of their contract.

There is a similar story with hedge funds. They routinely require their clients not to disclose the terms of their contracts. This means that students, professors, and other employees at major universities will never know how much money they paid hedge fund partners to lose their schools money. In the case of hedge funds, their income is probably also helped by the fact that many hedge fund partners are friendly with the university administrations that employ them. While it may not be appropriate for the government to require private universities to disclose hedge fund fees, that is the sort of demand that progressive students, faculty, and workers can reasonably demand of a university administration.

Getting rich through deceptive contracts is exactly the sort of abuse that the Consumer Financial Protection Bureau was intended to stop. Obviously, the Trump administration supports deceptive contracts as a way to get rich, but that is not intrinsic to capitalism.

In the case of the tax shelter industry, the best way to limit its size is to limit opportunities and incentives for avoidance. This means thinking carefully about the structure and the size of a tax. A more progressive tax is not always better, if it proves not to be enforceable. As a simple and obvious point, if we impose a 90 percent marginal tax rate, we are paying the rich 90 cents to hide $1.00 of income. When we are talking about incomes in the millions and tens of millions of dollars, many rich people will find ways to take advantage of this implicit payoff.

Much tax avoidance is in the corporate sector. We can design a simple and virtually unavoidable corporate income tax. We can simply require companies to give the government non-voting shares in an amount equal to the legislated tax rate (e.g. a 25 percent tax rate means the government's shares are equal to 25 percent of the total shares outstanding). These shares get the same dividend or buyback treatment as any other shares. This means that the only way that companies can cheat the government out of its tax take is by cheating its shareholders as well (Klein, 2017).[7]

While the policies outlined here just scratch the surface, they show that there are effective ways to limit the vast fortunes that are being made in the financial sector. None of these or other proposals in any way imply the end of capitalism as a system. A capitalist economy with a financial transactions tax and a requirement that corporate income taxes be made through government-owned non-voting stock shares, is still very much a capitalist economy. However, it would be a capitalist economy with far fewer vast fortunes being made in the financial sector

Out of control CEO pay

In the last four decades, CEO pay at large corporations has increased from 20 to 30 times the pay of the typical worker, to more than 200 times the pay of a typical worker. It is not uncommon to see CEOs of major corporations earn more than $20 million in a single year, and paychecks of $30 or $40 million are no longer rare.

[7] There have been efforts in recent years to limit one aspect of corporate income tax gaming by making the share of a multinational corporation's income that is taxable in a country, proportional to its sales in that country (Morgan 2016, Morgan 2017). This limits a common form of tax avoidance where companies claim the bulk of their income accrued in countries with low tax rates. The system of basing taxes on returns to shareholders described above would require this sort of mechanism, but it has the advantage of getting around other forms of gaming that result in the understatement of profits.

No one can question the explosion of CEO pay over the last four decades, but there is a dispute over whether it can be justified. The argument in support of soaring CEO paychecks is that their pay reflects returns to shareholders. In this story, if shareholders skimped on CEO pay, say by giving them $2-$3 million instead of $15 to $20 million, they would get less talented people as CEOs, or alternatively they would get CEOs who did not work as hard. The result would be lower stock returns. So, in a world where stockholders are assumed to be the ultimate controllers of the corporation, the extraordinary CEO pay that we have seen is justified by the returns they produce for shareholders.

The big problem with this argument is that returns to shareholders do not appear to be closely related to CEO pay. In their book, *Pay Without Performance*, Lucien Bebchuck and Jesse Fried (2006), reviewed a large body of evidence suggesting that CEO pay had little relationship to the returns they produced for shareholders. There is much evidence in this book to support that view, but just to give the most egregious failing in the structure of CEO pay, the incentive component of CEO pay rarely compares returns to a reference group. This means that if the stock price of the company rises due to a general rise in the stock market, the CEO will be richly rewarded. Or when events outside the CEO's control leads to industry specific gains, such as the impact of a rise in world oil prices on the shares of an oil company's stock price, the CEO is again richly rewarded. It is possible to write contracts that base CEO pay on stock returns relative to a set of comparable companies, but pay packages are rarely designed this way.

Since Bebchek and Fried wrote their book there have been several other noteworthy studies on this topic. For example, Shue and Townsend (2016) did an analysis of awards of stock options in the 1990s as the stock market soared. The huge run up in the market meant that the value of an option increased enormously over the course of the decade, yet almost no boards reduced the number of options granted to their CEOs. They suggest a form of "money illusion" in the awarding of stock options. Boards did not want to be seen as cutting CEO pay. Schieder and Baker (2017) looked at patterns in CEO pay in the health insurance industry following the implementation of the Affordable Care Act (ACA) in 2013. One of the provisions in the ACA ended the tax deduction for CEO pay in excess of $1 million. With the 35 percent corporate tax rate in effect at the time, this implied an increase of more than 50 percent in the after-tax cost of CEO pay to employers. If insurers were equating the returns provided by the CEO with their pay, this change in the tax treatment should have unambiguously led to a reduction of CEO pay in health insurance relative to other industries.

The paper reviewed a wide variety of specifications, controlling for revenue growth, profit growth, stock price appreciation and other factors. In none of them did it find any evidence of a fall in CEO pay in the health insurance industry relative to other sectors.

Another study (Marshall and Lee, 2016) examined patterns in CEO pay for 429 large firms over the years 2006-2015. It found that CEO pay was actually negatively correlated with returns to shareholders. Again, this is hard to reconcile with a story where high CEO pay is explained by the returns they provide to shareholders.

Perhaps the most damning piece of evidence in this respect is the simplest. If we take returns to shareholders over the last two decades, they have actually have been relatively low by historical standards. From 2000 to 2020, real annual returns have averaged less than 4.0 percent. That compares to a longer-term average real return in prior decades of 7.0 percent. This story is changed little if we move our reference point back a couple of years to 1998 to

avoid the peak of the bubble or move back to January of 2020, to skip the recent fall related to coronavirus pandemic. Returns have still been low by historic standards.

It is hard to tell a story of companies being run to maximize shareholder returns, in contrast to a prior period where companies were ostensibly pursuing a broader range of goals, if shareholders have not actually been getting especially good returns. What corporate management has most obviously succeeded in doing is maximizing the pay of corporate management. Since CEOs have been more successful at getting high pay for CEOs than getting high returns for shareholders, it reasonable to assume that this is what in fact they have been trying to do.

It is easy to tell a story whereby CEOs and top management are effectively able to rip off the companies for which they work. Corporate boards typically owe their allegiance to top management, who usually play a large role in their selection. Once a person gets on a board, it is almost impossible for them to be removed by shareholders. Well over 99 percent of the board members nominated for re-election by the board win re-election.

Since being a board member of a large corporation is extraordinarily lucrative –the pay is typically well over $100,000 a year for roughly 150 hours of work -- most board members will want to remain on the boards where they serve (Clifford, 2017). The route to keeping a seat is by not offending other board members. This presumably means not asking questions like “could we get a CEO who is just as good for half the pay?” In this world, board members are sitting on huge piles of corporate money and have no reason not to want to keep their CEO and other top management happy. This means that CEO pay essentially can rise without check.

It is also important to understand that this is not just an issue with the CEO; after all, there are not that many CEOs. If the CEO is getting paid $15 to $20 million, it is likely that the chief financial officer and other top executives are getting paid close to $10 million. And the third tier in the corporate hierarchy can be getting pay in the range of $2 to $3 million. It would be a very different world if the CEO was getting a paycheck in the range of $2 to $3 million, as would be the case if we still saw the pay ratios of the 1960s and 1970s. And of course, more pay going to the top means less pay for everyone else.

The excessive pay for CEOs also affects pay in other sectors of the economy. It is common for top executives for charities and major universities to earn more than $1 million a year. This is justified by the valid claim that they would be earning far more money if they were running a corporation of comparable size.

There is nothing intrinsic to capitalism that requires a corporate governance structure that effectively gives control to top management. There are many ways that governance can be reformed to give more effective control to shareholders and/or workers.[8]

One very simple reform would be to take advantage of the “Say on Pay” provision that was put in place in 2010 Dodd-Frank financial reform bill. This provision requires that the CEO’s pay package be put up for a non-binding vote of shareholders every three years. As it stands, the vote is non-binding and less than 3.0 percent are voted down.

[8] Under Germany’s “co-determination” policy, workers hold 50 percent of the board seats of major corporations. CEO pay is considerably lower on average in Germany.

However, it would be possible to have some real consequence for a negative vote. Suppose corporate boards would forfeit their pay if a pay package was voted down. It probably would not take too many negative votes to get boards to start asking whether they could get away with paying their CEOs less money.

There are undoubtedly other changes to corporate governance that could be effective in putting downward pressure on CEO pay, but the point is that there is nothing intrinsic to capitalism that requires CEOs get paid $15 to $20 million a year. We have in place a structure that promotes these sorts of pay packages. We could have a different structure, that is every bit as capitalistic (perhaps even more so if it gives more control to shareholders), but has much lower pay at the top.

The United States would still be capitalist if Facebook was subject to the same libel law as CNN

Two of the great sources of personal fortunes in the last decade are Facebook and Google. Both companies have near monopolies in their respective areas, which raises serious anti-trust concerns. Their near monopoly status is undoubtedly due in part to network effects which give a dominant actor a large advantage over smaller competitors, but both companies have acted aggressively to buy up potential competitors. If we are concerned about equality, and efficiency, then we need an effective anti-trust regime, which does not appear to have been the case in recent decades.

However, beyond the issues of anti-trust, there is also a question of how these huge companies are regulated. Most immediately, it is difficult to understand the rationale for Section 230 of the 1996 Communications Decency Act. This is a provision that exempts Internet intermediaries from being subject to the same rules on libel as traditional media.

This provision, which was passed into law in the early days of the Internet, arguably makes sense insofar as intermediaries can be seen as common carriers, like a phone company, which has no involvement with content. But a company like Facebook, that sells ads, sells promoted material on people's pages, and sells personal information about its users, does not fit the conventional definition of a common carrier.

Since Facebook is heavily involved with the content on its system, there is no reason it should not be subject to the same liability laws as media outlets like CNN or the New York Times. This means not only that it would be responsible for any items that it sponsored, but also for circulating libelous material through its system.

This point is important and often missed in the discussion. If the *New York Times* were to run an op-ed column or an ad with material that was false and damaging to an individual or corporation, it could face substantial legal liability, even though it was not the originator of the content. By contrast, Section 230 exempts Facebook from the same responsibility for spreading false and damaging claims through its system.

It would be impossible for Facebook to effectively screen the hundreds of millions of items posted daily by its billions of users. However, it could review items that are called to its attention and remove them if it determines them to be libelous. Since Facebook also has a

record of all the people who viewed a specific item, it could also be required to send a correction to all of these people.

If Facebook faced such requirements, it would require a large amount of additional staffing, which would substantially reduce its profits. However, this is a requirement that Facebook's competitors in the traditional media have long been subject to since their inception. There is no obvious rationale for holding Facebook, or other Internet intermediaries to a more lenient standard, simply because it is on the Internet.

Setting up such a system would be very expensive for Facebook. And, Mark Zuckerberg has said that he doesn't want to be responsible for determining what is true and what isn't. But this is a call that his competitors in traditional media outlets have to make all the time. If Zuckerberg decides that he and his corporation lack the same capabilities as a traditional media company, then he can turn to operating Facebook like a common carrier, which means no charging for ads or tracking users' behavior. Facebook, can just be a bulletin board where people pay a fee for the service.

This would likely be a huge hit to Facebook's profits. The company would likely have to hire tens of thousands of people to review complaints. It would undoubtedly also occasionally lose libel suits as a result of failing to promptly remove libelous material. A less profitable Facebook would make Mark Zuckerberg and other Facebook millionaires and billionaires considerably less rich.

Ending the Section 230 exemption would have an impact on other Internet companies as well. The impact would almost certainly not be as large as with Facebook, but this would amount to a leveling of the playing field between Internet media outlets and traditional ones. This is a reform that would in no way jeopardize the status of the U.S. as a capitalist system, but it would limit one of the main routes to great fortunes in recent years and also make a far more level playing field in the media industry.

Conclusion: capitalism does not have to be structured to give all the money to the rich

Capitalism is an incredibly malleable system. This is a fundamental point that anyone with an interest in politics or economic policy should recognize. It is important for two reasons.

First, we don't have a spare system in the trunk. For better or worse, we are going to have a capitalist economy long into the future. This is in part because of the inherent difficulties in constructing a fundamentally new system. We can't just get out our blueprints and then put them into practice. But part of the difficulty also stems from the malleability of the capitalist system. If the system were ever threatened in some fundamental way, there is enormous room to make changes to head off the challenge: in effect buying off the opposition.

The other reason it is essential to recognize the malleability of capitalism is because we must realize that the massive increase in inequality over the last four decades was by design. There was nothing intrinsic to the dynamics of capitalism that led to this inequality. The rich used their power in ways to redesign the structure of the economy so that a much larger share of income flowed upward. To a large extent they were able to get away with this restructuring because they altered important rules, like those on patent and copyright monopolies, when no one else was paying attention.

The time has come for progressives to start paying attention. We have to look at how the rules are structured. And, we have to be every bit as aggressive in restructuring them in ways that lead to more equality as the rich have been in rigging them to make themselves richer.

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