Broken Faith

Why We Need to Renew the Social Compact

By Robert B. Reich

At this writing, Bill Clinton has a headache that may or may not prove fatal to his presidency. But in his State of the Union address he gave a bravura performance, emphasizing everything that is good about America today and, by implication, everything that's good about him. And he has much to brag about: The budget is balanced. Unemployment is down, as is crime. For the first time in history, this nation has no major rival around the globe—economically, politically, even ideologically. We are, indisputably, Number One.

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What the President failed to mention, understandably, is that almost seven years of economic recovery has done remarkably little for people in the bottom half. Sure, they have jobs, but they had jobs before the last recession, too. The real news is that the median wage—the take-home pay of the worker smack in the middle of the earnings ladder—is still less than it was before the last recession, adjusted for inflation. More people are in poverty. At the same time, the upper reaches of America have never had it so good: Their pay and benefits have continued to rise and their stock and stock options have exploded in value.

The President's pollsters warn him not to mention that America continues to split. It's not what people want to hear. Remember Carter's "malaise"? Republicans, for their part, don't feel comfortable talking about it because they don't have any solutions they find palatable. Corporate America isn't particularly eager to talk about it or even sponsor television programs or advertise in magazines that dwell on it.

America is strangely immobilized. Rather than giving us the confidence we need to move forward, the overall good economic news, combined with a rare period of world peace and global pre-eminence, seems rather to have anesthetized us. But what happens when the good times are over? Future generations looking back on this era will ask why—when today's Americans had no hot or cold war to fight, no depression or recession to cope with, no great drain on our resources or our spirits—we did so little. Little, that is, relative to what the situation demanded. Little, relative to what we could have done. Did we simply assume that the economic expansion would last forever, and that the disparities would automatically shrink? Did we deny the problem to begin with? Or had we simply resigned ourselves to the inevitability of a sharply two-tiered society?

The budget deficit began to vanish last year, even before the White House and Congress reached agreement on how to make it do so officially. Corporations and top earners did so well that more tax revenues poured into the Treasury than had been foreseen. But rather than being dedicated to what has been most neglected and is most needed—universal healthcare, childcare, better schools, jobs for the poor who will lose welfare, public transportation and other means of helping the bottom half of our population move upward—most of this windfall went to the wealthiest members of our society in the form of tax cuts.

The proposals put forward by President Clinton in his State of the Union speech are steps in the right direction but, in truth, their scale is very small relative to the problems they address. Bolder advances were hoped for. One must be careful not to sound overly critical. Few things grate more unpleasantly upon the ear than a liberal whine. Republicans and many commentators will claim that the President has gone back to his original, liberal agenda, and will attack him for failing to indicate exactly how he will pay for what he proposes. He wants to dedicate any budget surplus to shoring up Social Security. But Social Security is not nearly in the dire straits some have made it out to be. And—dare we say it again?—deficits are not bad in and of themselves, certainly not if the money is spent on making more Americans more productive and fuller members of our society.

The most important thing the United States could achieve now is to get back on the track we were on during the first three decades after World War II, toward a more inclusive, more equitable society, in which everyone has a fair chance of making it. We got off that track in the late seventies and have veered even further off it since. In the world's pre-eminent democratic capitalist society, one might have expected just the reverse: As the economy grew through technological progress and global integration, the "winners" in the process would compensate the "losers" and still come out far ahead.

Nations are not passive victims of economic forces. Citizens can, if they so choose, assert that their mutual obligations extend beyond their economic usefulness to one another, and act accordingly. Throughout our history the United States has periodically asserted the public's interest when market outcomes threatened social peace—curbing the power of the great trusts, establishing pure food and drug laws, implementing a progressive federal income tax, imposing a forty-hour workweek, barring child labor, creating a system of social security, expanding public schooling and access to higher education, extending healthcare to the elderly and so forth. We effected part of this explicitly through laws, regulations and court rulings, and partly through social norms and expectations about how we wanted our people to live and work productively together. In short, this nation developed and refined a strong social compact that gave force to the simple proposition that prosperity could include almost everyone. The puzzle is why we seem to have stopped.

Every society possesses a social compact—sometimes implicit, sometimes spelled out in detail, but usually a mix of both. The compact sets out the obligations of members of that society toward one another. Indeed, a society or culture is defined by its social compact. It is found within the pronouns "we," "our" and "us." We hold these truths to be self-evident; our peace and freedom are at stake; the problems affect all of us. A quarter-century ago, when the essential provisions of the American social compact were taken for granted by American society, there was hardly any reason to state them. Today, as these provisions wither, they deserve closer scrutiny.

The first provision pertained to the private sector. As companies do better, their workers should, too. Wages should rise, as should employer-provided health and pension benefits, and jobs should be reasonably secure. This provision of the compact was reinforced by labor unions, to which, by the mid-fifties, about 35 percent of the private-sector work force belonged. But it was enforced in the first instance by public expectations. We were all in it together and as a result grew together. It would be unseemly for a company whose profits were increasing to fail to share its prosperity with its employees and the communities in which they lived. The job of management, proclaimed Frank Abrams, chairman of Standard Oil of New Jersey, in a 1951 address that was typical of the era, is to maintain "an equitable and working balance among the claims of the various directly interested groups . . . stockholders, employees, customers and the public at large. Business managers are gaining in professional status partly because they see in their work the basic responsibilities [to the public] that other professional men have long recognized in theirs."

The second provision of the social compact was social insurance, through which Americans pooled their resources against the risk that any one of us—through illness or bad luck—might become impoverished. Hence, unemployment insurance; Social Security for the elderly and disabled; aid to widows, which became Aid to Families with Dependent Children; and Medicaid and Medicare. "Cradle to grave," Franklin Roosevelt told my predecessor Frances Perkins, "from the cradle to the grave they ought to be in a social insurance system." Roosevelt failed to recognize that handouts might have negative side effects, such as deterring some poor people from trying to fend on their own, or creating some middle-class retirees who regarded the "insurance" as an entitlement, or giving rise to large bureaucracies to administer all of it. Still, for most of the next half-century, most Americans agreed that people who worked hard, or wanted to work hard but nonetheless fell on their faces, should be helped out.

The third provision was the promise of a good education. The national role began in the nineteenth century with the Morrill Act, establishing land-grant colleges. In the early decades of this century a national movement swept across America to create free high school education through the twelfth grade for every young person. After the Second World War, the G.I. Bill made college a reality for millions of returning veterans. Other young people gained access to advanced education through a vast expansion of state-subsidized public universities and community colleges. In the fifties our collective conscience, embodied in the Supreme Court, finally led us to resolve that all children, regardless of race, must have the same—not separate—educational opportunities.

It is important to understand what this social compact was and what it was not. It defined our sense of fair play, but it was not primarily about redistributing wealth. There would still be the rich and the poor in America. The compact merely proclaimed that at some fundamental level we were all in it together, that as a society we depended on one another. The economy could not prosper unless vast numbers of employees had more money in their pockets. None of us could be economically secure unless we shared the risks of economic life. A better-educated work force was in all our interests.

The unraveling began in the late seventies and early eighties, and continues today. Consider first what has happened to the notion that as companies do better, their workers should too. Profitable companies now routinely downsize their work forces, or they resort to what might be called "down-waging" and "down-benefiting." Layoffs in the current expansion are occurring at an even higher rate than in the expansion of the eighties. Companies are replacing full-time workers with independent contractors, temporary workers and part-timers; they are bringing in new full-time workers at lower wage scales than current workers, or are subcontracting the work to smaller firms offering lower wages and benefits. Employer-provided health benefits are declining across the board, and health costs are being shifted to employees in the form of higher co-payments, deductibles and premiums. Defined-benefit pension plans are giving way to 401(k) plans without employer contributions, or to no pensions at all. Meanwhile, beginning in the early eighties, U.S. companies began battling against unionization with more ferocity than at any time in the past half-century. The adjusted incidence of companies illegally firing their employees for trying to organize unions increased from 8 percent in the early seventies to around 30 percent in the early eighties, where it has more or less remained.

The relentless drive among American companies to reduce their labor costs is understandable. Competition is more treacherous in the new economy, where large size and low unit costs no longer guarantee competitive advantage, and where institutional investors demand instant performance. Yet it is also the case that the compensation of senior management and professional and highly skilled technical workers has escalated in recent years. In large companies, top executive compensation has been increasing for more than a decade at the rate of more than 10 percent per year, after inflation. And although these executives have no greater job security than others, when they lose their jobs it is not uncommon for them to receive "golden parachutes" studded with diamonds.

The second provision of the social compact—that of social insurance—is also breaking down. We see evidence of this in those who have been asked to bear the largest burden in balancing the budget—disproportionately the poor and near poor, whose programs have borne the largest cuts. Unemployment insurance now covers a smaller proportion of workers than it did twenty years ago—now, only 35 percent of the unemployed. Even before welfare "reform," welfare payments were shrinking in many states. In fact, the entire idea of a common risk pool is now under assault. Proposals are being floated for the wealthier and healthier to opt out. Whether in the form of private "medical savings accounts" to replace Medicare, or "personal security accounts" to replace Social Security, the effect would be much the same: The wealthier and healthier would no longer share the risk with those who have a much higher probability of being sicker and poorer.

The third part of the social compact, access to a good education, is also under severe strain. The Clinton Administration has expanded opportunities at the federal level—more Pell grants and low-interest direct loans for college, school-to-work apprenticeships, tax breaks for education and training. But the federal government still accounts for only 8 cents of every public dollar spent on primary and secondary school education in the United States; states and localities divide the rest. As Americans increasingly segregate by level of income into different townships, local tax bases in poorer areas cannot support the quality of schooling available to the wealthier. Public expenditures per pupil are significantly lower in school districts in which the median household income is less than $20,000 than in districts in which the median is $35,000 or more—even though the challenge of educating poorer children, many of whom are immigrants with poor English language skills or who have other social or behavioral problems, is surely greater than the challenge of educating children from more affluent households. De facto racial segregation has become the norm in many large metropolitan areas.

Across the United States, state-subsidized higher education is waning under severe budget constraints, and its cost has risen three times faster than median family income. Elite colleges and universities are abandoning need-blind admissions policies, by which they guaranteed that any qualified student could afford to attend. Young people from families with incomes in the top 25 percent are three times more likely to go to college than are young people from the bottom quarter, and the disparity is increasing.

Why is the social compact coming undone—especially at a time when it's most needed? I do not have a clear answer, but I do have several hypotheses. The first is that Americans no longer face the common perils of depression, hot war or cold war that were defining experiences for the generations that reached adulthood between the thirties and the sixties. Each of these events posed a threat to American society and culture. Each was experienced directly or indirectly by virtually all Americans. Under such circumstances, it was not difficult to sense mutual dependence and to conceive of a set of responsibilities shared by all members, which exacted certain sacrifices for the common good. Today, fewer Americans remember these events or the social bonding that accompanied them. Peace and prosperity are wonderful, but they do not necessarily pull citizens together in common cause.

Second, in the new global economy, those who are more skilled, more talented or simply wealthier are not as economically dependent on the local or regional economy surrounding them as they once were, and thus have less selfish interest in insuring that their fellow inhabitants are as productive as possible. Alexis de Tocqueville noted that the better-off Americans he met in his travels of the 1830s invested in their communities because they knew they would reap some of the gains from the resulting economic growth—in contrast to Europe's traditions of honor, duty and noblesse oblige. "The Americans . . . are fond of explaining almost all the actions of their lives by the principle of self-interest rightly understood," he said. "They show with complacency how an enlightened regard for themselves constantly prompts them to assist one another and inclines them willingly to sacrifice a portion of their time and property to the welfare of the state." Today, increasingly, the geographic community where a person lives is of less consequence to his or her economic well-being. It's now possible to be linked directly by modem and fax to the great financial or commercial centers of the world.

Third, any social compact is premised on "it could happen to me" thinking. Social insurance assumes that certain risks are commonly shared. Today's wealthy and poor, however, are likely to have markedly different life experiences. Disparities have grown so large that even though some of the rich (or their children) may become poor and some of the poor (or their children) will get rich, the chances of either occurring are less than they were several decades ago. The wealthy are no longer under a "veil of ignorance" about their futures, to borrow philosopher John Rawls's felicitous phrase, and they know that any social compact is likely to be one-sided: They will be required to subsidize those who are poorer.

A final point: People at or near the top, or even in the upper tiers, simply don't see that much of the bottom half anymore. Separated geographically, economically and culturally, the poorer members of society have all but disappeared. The people who produce or talk on the TV shows, who write the editorials and columns and who raise the money for political candidates have no reason to suppose that so many people in this country are still having a hard time of it. Marketeers and advertisers don't pay much attention to them because they have little buying power relative to the people in the top half. Pollsters don't pay much attention because they vote far less than the people in the top half. The people they do see or pay attention to are doing just fine, some of them extraordinarily well. So it's easy to conclude that everything is going fine for everyone.

Perhaps all these hypotheses are at work, to some degree. But there should be no doubt that, unchecked, the disintegration of the social compact threatens the stability and moral authority of this nation. It even threatens continued economic growth. Those who bear a disproportionate share of the burdens and risks of growth but enjoy few if any of the benefits will not passively accept their fates. Unless they feel some stake in economic growth, they are likely to withdraw their tacit support for free trade, capital mobility, relatively open immigration, deregulation and similar aspects of open economies that generate growth but that simultaneously impose losses and insecurities on them.

Now, when the economy is performing well, is the time to re-knit the social compact. Start with a more progressive income tax—at all levels of government. Then put more resources into schools serving the bottom half (sure, give parents a choice of public or charter schools, and even try vouchers, but give kids from poor and working-class families especially big vouchers with a lot of money backing them up). Give working parents refundable tax credits for what they spend on daycare. Require companies to pay a minimum healthcare wage of at least one dollar per hour for health insurance, and to pay proportionally the same tax-free fringe benefits they give their top executives to their front-line workers and their part-timers and contract workers. Make it harder for them to fire workers for forming unions. Require them to devote a tiny (one and a half) percent of their payrolls to upgrading the skills of their employees, or contribute the difference to a common fund to upgrade the skills of everyone who needs it. I offer these as a sampling; the nation is not wanting in good ideas.

But the real job of re-knitting the social fabric has to begin where the threads start. That means getting more people involved in the gritty, grimy job of politics starting at the local level, where every year there are close to 90,000 races—the overwhelming majority of them nonpartisan—for offices like school board and city council. It means convincing good people to run for office, maybe running yourself, getting on the phone, getting out the vote, mobilizing your friends and acquaintances; creating strong local alliances among the poor, the near poor, unionized and nonunionized hourly workers, religious groups, community-based groups, universities and others. And it means committing time and effort to initiatives that stress values—that have a message, not just a program. Leadership does not depend for its efficacy upon holding a formal position of authority. True leadership is a matter of keeping people's attention focused on the problems they would rather avoid, and it can be exercised by anyone. We seem to have too many people in formal positions of authority who are not leading, and too many at the grassroots resigned to the way things are.

The current trends—the bottom half going nowhere while the top soars, a waning social compact—is not sustainable. When the current expansion slows, those who are barely staying afloat or who are sinking will not remain silent. Yet by that time, I fear, their voices may resound not to progressive ideals but to the virulent politics of resentment. History yields ample warnings. The social compact is a promise we made to one another, and we are not keeping it when we can most afford to.

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