Eight Market-Oriented Proposals That Reduce Income Inequality

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Debates over economic policy are often framed as conservatives supporting market-oriented policies, while progressives support government interventions. However, there are many market-oriented policies that can lead to more equality, an important goal for most progressives. This paper outlines eight policies that are likely to lead to greater equality through an increased reliance on the market.

Progressives have generally looked to government interventions in the market as a way to limit income inequality and reduce poverty. These interventions can be useful, but there is a limit as to how far they can go. A minimum wage can help boost the income of low-end workers, but undoubtedly at some levels a higher minimum wage will increase unemployment among less-skilled workers. Progressive taxation can lessen some of the extremes of inequality produced by the market, but high levels of taxation will have negative behavioral effects and divert substantial resources to tax avoidance and evasion, which are a complete waste economically.

For this reason, it is important to ask about ways in which the market is structured to produce inequality. If a different market structure would lead to less inequality, without reducing efficiency, it would be preferable to addressing inequality through tax and transfer policy.

This paper outlines eight policy areas in which it is arguably possible to structure markets differently, without reducing efficiency. These are not fully worked out policy proposals. Rather, they are intended to provide a basis for discussion.

Reducing Protections for Highly Educated Professionals

There is a large gap in pay between the mostly highly educated professionals in the United States and their counterparts in other wealthy countries. This is the result of both domestic protections, such as licensing standards that limit the number of people in the profession, and restrictions on foreign professionals’ ability to work in their field in the United States. There would be large potential gains from eliminating unnecessary restrictions and getting the pay for US professionals more in line with the rest of the world.

This gap is clearest for physicians. Doctors in the United States earn close to twice as much on average as their counterparts in other wealthy countries. Part of this gap is because primary care physicians and specialists are paid more in the United States, with the gap being far larger for
specialists. However, much of the gap is attributable to the fact that the United States has a much greater ratio of specialists to primary care physicians. In other countries the ratio of primary care physicians to specialists is close to two to one, whereas in the United States the ratio is two to one in the opposite direction.

There is little evidence that the greater use of specialists in the United States leads to better health outcomes in most circumstances. The more plausible explanation is a simple case of rent-seeking, in which medical specialists can determine a standard of care that requires using specialists to make diagnoses and provide treatment in contexts in which primary care physicians would be entirely competent.

If doctors in the United States were paid in line with the average for physicians in other wealthy countries, the savings would be close to $100 billion a year. There are approximately 900,000 doctors, with an average saving of more than $100,000 per doctor.

To a lesser extent, the pay of dentists, lawyers, architects, and other highly educated professionals is also out of line with the pay of their counterparts in other wealthy countries. There are enormous potential gains from making the pay of these professionals more comparable to the pay in other wealthy countries.

The key to bringing the pay of highly educated professionals in the United States in line with their counterparts in other wealthy countries is to reduce unnecessary supply restrictions. For doctors, the most important restriction is the requirement that foreign doctors complete a medical residency program in the United States before they are allowed to practice medicine here. It is difficult to believe that completing a US residency program is the only way a person can become a competent doctor. It should be possible to set clear standards that foreign-trained doctors could meet to practice in the United States under the same terms as a US-trained doctor.

It may also be desirable to expand the number of slots in US medical schools and the number of residency positions, both of which are now strictly limited. Medical school and residency slots involve a substantial expense, but this would likely be an investment with a high return. However, it is far cheaper to train physicians in foreign medical schools and residency-equivalent programs than in the United States. It would be useful to take advantage of this cost difference and expand the inflow of foreign doctors.

There could be similar rules applied for foreigners seeking to meet licensing standards in other highly paid professions. The goal should be to ensure minimal quality standards without unnecessarily excluding people from practicing in high-paying professions.

The obstacles to practicing dentistry are comparable to the obstacles to practicing medicine, with the minor exception that graduates of Canadian dental schools have been allowed to practice dentistry in the United States since 2011. Surely it would be possible to identify other countries where the quality of education in dentistry is comparable to the quality in US programs. Of course, the opportunity for graduates to practice in the United States would give foreign dental schools a powerful incentive to ensure they met US standards.

1 An OECD analysis put the average compensation for general practitioners in the United States in 2004 at $146,000 (Fujisawa and Lafontaine 2008). This is more than 40 percent higher than the average for the other countries in the analysis, even excluding the Czech Republic as an outlier on the low side. This analysis found an even larger gap between the pay of specialists in the United States and specialists in most other OECD countries. It found specialists were paid even more in the Netherlands. The average pay for specialists in the United States was $236,000 in 2003 (in 2003 dollars). By comparison, it was $159,000 in Canada, $153,000 in the United Kingdom, $144,000 in France, and just $93,000 in Denmark. The 2 This would not have much impact on aggregate immigration flows, since even a large increase in flows of professionals—for example, an increase of 150,000 a year—would only add roughly 10 percent to the total number of immigrants arriving each year.
State bar requirements unnecessarily limit the number of people licensed to practice law. Having minimal requirements to determine competency is logical, but there are enormous differences in these requirements across states, as indicated most immediately by the difference in pass rates for the bar exam. There should be an effort to minimize the standards and facilitate unified tests so that lawyers certified in one state can practice in all states. (There is movement in this direction, but it should be accelerated.)

There should be comparable efforts to standardize licensing requirement for other highly paid professionals, such as architects, engineers, and accountants, with the idea being to make these fields as open as possible to immigrants from other countries. This should vastly increase the supply of people working in these professions in the United States and thereby reduce the cost of professional services.

One legitimate concern is that an open-door policy for highly educated professionals could lead to a brain drain from developing countries, with many of their most educated people opting to work in the United States. This could be addressed through a system whereby a portion of these professionals’ earnings is taxed away and repatriated to their home country. For example, repatriating an amount equal to their income tax might be a reasonable target.

Given the much higher pay in the United States and the relatively low training costs in developing countries, this could make it possible to train two or three professionals for every one that emigrates to the United States. This should ensure that the home countries share in the benefits from the increase in trade in professional services.°

In addition to opening up these professions to more international competition, it would be desirable to increase domestic competition as well. First, setting up a licensing procedure that allowed professionals to practice across state lines should help address local shortages. While there may be formidable political obstacles, there is little economic argument for not having a single national standard for professionals. National standards really are a necessity for fuller international coordination as well.

Setting up a licensing procedure that allowed professionals to practice across state lines should help address local shortages.

Even if establishing national standards proves to be a high bar, much can be done at the state level to increase competition. Currently, licensing boards for these professions are dominated by the members of the profession. They determine not only the requirements for practicing the profession but also the boundaries for the work done by the profession. This means doctors draw the lines for what work must be done by a doctor, as opposed to a nurse practitioner or other health professional. Dentists determine the boundaries for the work that can be performed by a dental hygienist and work that requires a licensed dentist. Medical specialists set the standards for exams and treatments that a primary care physician can deal with and the situations requiring a specialist’s attention.

This situation would be expected to lead to rules that exaggerate the need for the more highly paid workers. The standards being set likely require doctors and dentists for procedures that could be done perfectly well by less highly skilled and less highly paid professionals. The same would be the case with medical specialists setting standards that underutilize the skills of primary care physicians.

°There would be some loss of tax revenue associated with a system of repatriation, but this would almost certainly be dwarfed by savings to the government, especially in health care, for which the government funds more than 60 percent of spending, either directly or through tax deductions. It would require some time and political negotiations to determine the exact size and structure of these payments, but presumably they would be scaled to the wealth of the professional’s home country. It does not make sense to make payments to rich countries, but the poorest countries should get generous compensation. The compensation for middle-income countries need not be as generous.
The obvious remedy would be to construct licensing boards that are dominated by persons with expertise in the relevant area but who are not actually in the profession for which standards are being set. This could mean that researchers in public health who are not doctors dominate the licensing boards setting standards for treatment by doctors and determine the boundary for diagnoses and treatments requiring specialists, as opposed to primary care physicians. Boards should include nurses and other health professionals to ensure that the standards recognize their expertise. Boards dominated by engineers could set the standards for architects and vice versa.

An increase in the supply of professionals, primarily from foreign countries, coupled with a reduced demand, could lead to sharp reductions in pay. This could translate into substantial cost savings for consumers and substantially boost economic growth.

**Facilitate Medical Travel**

The cost of major medical procedures in the United States is far out of line with the costs in most other countries. This is true even if the comparison group is other wealthy countries, but the difference in costs is considerably larger with many developing countries.

Several developing countries, most notably India and Thailand, have established modern facilities designed to serve a Western population. In these cases the price of major procedures can be significantly lower, making it possible for patients to travel to these countries with family members, stay for a period of recovery, and still have substantial savings. It would be beneficial to have policies that facilitated medical travel to take advantage of these potential savings.

This would affect income inequality by lowering the pay of doctors and administrators in the health care industry, most of whom rank in the top 1-2 percent of the pay structure in the United States. The savings from lower-cost health care would translate into a real pay increase for the rest of the country, either directly through lower payments for health care or indirectly through a lower tax burden as a result of reduced government spending on health care.

Table 1 shows some examples of the gap in the prices for procedures in the United States compared with other countries. The average price of hip-replacement surgery in the United States is $40,400, compared to less than $12,000 in the United Kingdom. (There is enormous variation around this $40,400 figure in the United States, which raises another set of issues.) The cost in Argentina is just $3,600, less than one-tenth of the cost in the United States, for a gap of more than $36,000. Heart bypass surgery costs an average of $73,400 in the United States, compared to $14,100 in the United Kingdom and $8,900 in Argentina. These gaps indicate enormous potential savings if a substantial portion of major surgeries needed by people in the United States were performed in lower-cost countries.

Table 2 shows the total number of each of these four procedures performed in the United States in 2010. The second column shows an estimate of potential savings, assuming that total costs, including travel expenses, are $10,000 above the costs in the low-cost country, which is Argentina in each of these cases. Argentina is an outlier among this group since it is a middle-income country, not a wealthy country. A full list, including modern facilities meant to accommodate medical travel in countries such as India and Thailand, would likely show several countries with prices comparable to those in Argentina.

<table>
<thead>
<tr>
<th>Procedure</th>
<th>United States</th>
<th>Argentina</th>
<th>Spain</th>
<th>United Kingdom</th>
</tr>
</thead>
<tbody>
<tr>
<td>Hip Replacement</td>
<td>$40,364</td>
<td>$3,565</td>
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<td>$11,889</td>
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<td>Knee Replacement</td>
<td>$25,637</td>
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<td>$7,833</td>
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<tr>
<td>Heart Bypass Surgery</td>
<td>$73,420</td>
<td>$8,882</td>
<td>$17,437</td>
<td>$14,117</td>
</tr>
<tr>
<td>Angioplasty</td>
<td>$28,182</td>
<td>$2,851</td>
<td>$9,446</td>
<td>$14,366</td>
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Table 2. Potential Savings from Using Foreign Medical Procedures (in 2010 Dollars)

<table>
<thead>
<tr>
<th>Procedure</th>
<th>Number (2010)</th>
<th>Total Spending (Millions)</th>
<th>Savings Per Procedure</th>
<th>Total Savings (Millions)</th>
</tr>
</thead>
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<tr>
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<td>$13,401</td>
<td>$21,799</td>
<td>$7,237</td>
</tr>
<tr>
<td>Knee Replacement</td>
<td>719,000</td>
<td>$18,433</td>
<td>$7,445</td>
<td>$5,353</td>
</tr>
<tr>
<td>Heart Bypass Surgery</td>
<td>395,000</td>
<td>$29,001</td>
<td>$49,538</td>
<td>$19,568</td>
</tr>
<tr>
<td>Angioplasty</td>
<td>500,000</td>
<td>$14,091</td>
<td>$10,331</td>
<td>$5,166</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>5,166,000</strong></td>
<td><strong>$74,926</strong></td>
<td><strong>$37,323</strong></td>
<td></td>
</tr>
</tbody>
</table>

Source: CDC (2010).

The last column shows the potential savings if all the surgeries in each category in 2010 had been performed in the low-cost country, with the $10,000 travel cost assumption. The savings would have been $7.2 billion for hip-replacement surgery, $5.4 billion for knee-replacement surgery, and $19.6 billion for heart bypass surgery. The total potential savings for these four surgeries would have been $37.3 billion.

While it is unrealistic to imagine that most of these medical procedures would be performed in other countries, it is plausible that a substantial fraction would be, if patients could be given a portion of the savings as an incentive. If insurance companies and government health care programs split the savings, then many people would likely take advantage of this opportunity. Most of these procedures are not performed on an emergency basis, so patients could make plans with their families, their regular physicians, and the facilities in the host countries to schedule an operation.

If 30 percent of these procedures were performed in other countries, the savings would be more than $11 billion annually. A fuller list of procedures is likely to take the potential savings to more than $15 billion.

In addition, exposing the US medical system to direct competition with lower-cost foreign providers should help put downward pressure on prices in the United States. To some extent, domestic providers may choose to lower prices to protect their market. However, they may also alter their techniques, for example using fewer specialists, to bring their costs in line with their foreign competitors.

The awareness that patients can secure large savings from traveling abroad for procedures may also lead to more comparison pricing domestically. Providers that charge excessive prices without obvious benefits in outcomes may then be forced to lower prices or risk losing much of their market.

A major factor obstructing medical travel is the lack of an appropriate institutional structure. First, few people would likely travel to another country for a major medical procedure if they could not be assured of the quality of the care. There are currently private accreditation groups, but there have been issues raised about their integrity.

An intergovernmental organization that could certify that facilities meet high-quality standards would be useful. Such an organization could largely rely on existing national systems where countries have a track record of maintaining high standards. In other countries, a system of inspections would likely be necessary. This could be financed by a tax on medical travel.

Because people in the United States generally know little about the quality of health care in other countries, a solid system of accreditation is essential for the growth of medical travel. Patients in the United States must be assured of the quality of care they would receive in another country, otherwise very few will risk going to another country for a major medical procedure. Relative to the enormous potential gains, the costs of establishing a trustworthy accreditation system would be small.

A second important issue would be to establish a clear system of legal liability that could ensure patients they would be compensated if a procedure were not carried through properly. Along with establishing an accreditation system, this would provide assurance of the quality of the care patients would receive in another country. The system need not replicate the US malpractice system, but it should provide patients with the confidence that they will be compensated for lost earnings and
any additional medical care that proves necessary because of failed procedures.

The third issue is that third parties, either government programs or private medical insurance, pay for the vast majority of these procedures. As a result, the savings would not directly accrue to patients, giving them no incentive to consider medical travel. This could be remedied by a system in which the patient is rebated a portion of the savings.

For government programs, this could be done directly. For example, Medicare could rebate half of the savings from having a procedure carried through outside of the United States. Private insurers could also adopt similar policies. This would likely involve some regulatory issues since regulatory boards would have to authorize the practice. That could happen on a state-by-state basis, or alternatively the federal government could impose rules that require state regulatory boards to allow rebates for medical travel.

If patients could directly pocket a substantial fraction of the savings, they would have a powerful incentive to consider having major medical procedures performed in a country with lower costs. For example, if a patient needing heart bypass surgery got to keep half the savings minus travel costs, they could possibly pocket as much as $25,000 by having the procedure performed in the United Kingdom, or even more in some facilities in developing countries. If an accreditation system assured patients that they would get high-quality care in these countries and a well-working malpractice system provided compensation in the event of mistakes, many patients would likely take advantage of the option.

When procedures are performed in developing countries doctors and other health care professionals may be pulled away from treating the host country’s population, reducing their access to health care. In principle, the host countries could tax medical travel and use the revenue to train additional health care professionals, thereby ensuring that the host country’s population benefits as well.

In this situation, as in the case of professionals from developing countries coming to the United States, it is possible to establish mechanisms that ensure that training more professionals more than offsets the loss of highly trained professionals serving the domestic population. This is important not only as an ethical matter but also from the standpoint of maintaining political support in the host countries. If an influx of foreign patients is seen as subtracting from the supply of medical professionals to serve the domestic population, the industry will be a source of resentment, which could lead to pressure to limit its size or shut it down altogether. On the other hand, if a tax on the medical travel industry supports training doctors and health care professionals and providing medical services to the domestic population, it is more likely to enjoy public support.

**Allow for the Internationalization of Medicare**

There are huge gaps between the per-person cost of health care in the United States and other wealthy countries (Table 3). This suggests the possibility of large gains.

If seniors in the United States could use what the federal government pays for their Medicare to buy into the health care system of other countries, there would be large savings that could be split between the patient and the government. Since Medicare beneficiaries are overwhelmingly retired, they need not worry about being in close proximity to a workplace.

Furthermore, many people have family ties to other countries. Many beneficiaries would likely shift over to another country’s health care system if it were allowed. As with medical travel, this policy would reduce the pay of doctors and administrators in the health care industry and effectively raise real wages for everyone else.

The basic logic of this proposal is straightforward. The federal government pays an average of $12,900 each year for seniors’ Medicare (CMS 2016). Roughly 20 percent of beneficiaries also receive Medicaid. These payments average $10,400 per senior beneficiary. By comparison, the per-person cost of health care for the over 65 population in other

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4 This figure is derived by taking total Medicaid spending for beneficiaries over age 65 in 2012 ($85.8 billion) (CMS 2012), dividing by the number of dual eligibles (9.6 million), and assuming 4.0 percent annual spending growth to get 2016 spending.
<table>
<thead>
<tr>
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<td>$13,946</td>
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<td>$6,425</td>
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<tr>
<td>Germany</td>
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<td>$1,018</td>
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</tr>
<tr>
<td>Greece</td>
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<td>Portugal</td>
<td>$2,514</td>
<td>$6,538</td>
<td>$9,072</td>
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<tr>
<td>Spain</td>
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<td>$7,536</td>
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<td>OECD Average</td>
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<td>$12,456</td>
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<td>$8,847</td>
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Several issues would have to be addressed in implementing the policy. First, other countries would have to be prepared to allow an influx of US citizens under some sort of permanent resident status arrangement, if not actual citizenship. If such a program were put in place, the receiving countries would undoubtedly want to strictly limit the number of people allowed to enter initially to ensure that the flow was manageable and that newcomers were not disrupting their health care system.

The program’s design would have to be structured to protect against adverse selection in either direction. If any receiving countries were to get a disproportionate number of high-cost beneficiaries, it would quickly make the program uneconomical the same as in the United States. This almost certainly overstates the cost in other countries.

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5 This figure takes average per capita health care spending in other countries and assumes that the ratio for per capita spending on the over 65 population to the overall average is
for them. Similarly, if those leaving the United States proved to be more healthy than the beneficiary population as a whole, it could increase Medicare costs.

There will be no perfect way to protect against adverse selection, but rules that make the buy-in a one-time choice, with severe penalties for reversals, would probably be necessary. For example, if a person elects at age 65 to buy into another country’s health care system, they could be precluded from later opting back into the US system or could only be allowed to do so with a large penalty.6

The prospect of a substantial number of people traveling to other countries for their Medicare is attractive for reasons beyond just the potential savings to the government. First, since it is voluntary, presumably people who opt to take advantage of health care systems in other countries would actually prefer living there. Providing people the opportunity to spend their retirement in another country, if that is what they choose, should be considered a positive outcome. In this case, by construction this decision should impose no cost on either the receiving country or the United States. In fact, both should gain by splitting the savings from the difference in health care costs.

The second reason this internationalization of Medicare would be desirable is that it can alleviate demand pressures on the US health care system. Reducing the overall demand for health care should affect health care prices, meaning the actual benefits would exceed the per-person savings, assuming prices in the United States are unchanged. With the grossly disproportionate use of health care by the elderly, if any substantial share of beneficiaries took advantage of the option to buy into other countries health care systems, it would noticeably affect demand and prices in the United States. For example, if 10 percent of beneficiaries took advantage of this option, it would reduce total health care spending by roughly 5 percent, assuming that the beneficiaries taking advantage of this option had average expenses for the Medicare and Medicaid populations.

The third reason an internationalized Medicare program would be valuable is that it could expose large numbers of Americans to alternative approaches to health care. As is well-known, the United States is a huge outlier in per-person health care costs. To some extent this may be associated with better patient care and outcomes, but there is good reason to believe that much of it is waste attributable to rent-seeking behavior by providers. If a substantial number of Medicare beneficiaries had positive experiences with lower-cost health care systems in other countries, then it may make changes in the United States more acceptable politically.

**Develop Alternatives to Patent Financing for Prescription Drugs**

The pharmaceutical industry can both be a source of extraordinary incomes for those at the top and a major expense for households. The top executives in the pharmaceutical industry earn salaries that can run into eight figures. Successful researchers can make tens or even hundreds of millions of dollars off their patents.

On the expense side, the country spends more than $430 billion annually on prescription drugs, more than 3.3 percent of total consumption expenditures. If drugs were instead sold at generic prices, spending would fall by 80–90 percent. While some of the savings would need to be used to pay for research through an alternative mechanism, this could still leave room for substantial gains in real wages.

Patent monopolies can provide an effective incentive for developing new drugs, but they have all the predicted effects of a government-enforced monopoly. Since drug companies are often able to sell protected drugs at several thousand percent above the marginal cost, they have an enormous incentive to promote their drug even in contexts

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6 Such a rule could be structured around preexisting conditions. For example, a beneficiary may be able to return to their Medicare coverage in the United States with a modest penalty but would not be covered for any major preexisting conditions. There will inevitably be specific instances in which this could make for political problems (i.e., a dying cancer patient who wants to come back to the United States to spend his remaining time with his children), but these are not necessarily insoluble.
in which it may not be the most effective treatment for a condition. They also have incentives to conceal evidence that questions the safety and effectiveness of their drugs. Patents also lead to unnecessary duplicative research as drug companies will often attempt to innovate around a patent to share in the patent rents of an existing drug rather than develop a drug for a condition for which no treatment is currently available.

There are alternatives to patent-supported research. The government already spends more than $30 billion a year on directly funded research through the National Institutes of Health. The amount of direct funding could be doubled or tripled to replace patent-supported funding.

There have been various proposals to use public funding for a prize system under which the government buys up a patent and puts it in the public domain (e.g., Stiglitz and Jayadev 2010). While this system would allow new drugs to be sold in a free market, it would still leave in place the incentives for secrecy in the research process itself. The prize payments would also likely be a source of considerable controversy.

By contrast, additional funding could be paid to directly support research. The additional funding could be paid out to private corporations through long-term (e.g., 8–12 years) contracts that are subject to competitive bidding. This would avoid most of the concerns about the government micromanaging research and political interference. It also has the political advantage that research-oriented pharmaceutical companies would be able to bid for this funding and therefore could benefit from this system. This payment system would be comparable to how the United States pays military contractors, except all this work would be fully public, whereas there is a real rationale for keeping military research secret.

In contrast to the secrecy in the current system, in which companies have incentive to disclose as little information as possible to avoid helping competitors, a condition of funding should be that all research findings are posted on the web as soon as practical. (This rule would apply to both prime contractors and any subcontractors.) In addition, all patents would be placed in the public domain on a copyleft basis. This means that anyone could freely use the patent as long as any subsequent innovation was also kept in the public domain. If a party wanted to use a patent for private purposes, they would have to negotiate for the rights with the government.

This pattern of research is likely to be far more efficient than research done in secret since researchers would be able to quickly build on others’ successes and learn from their failures. Recent research found that even short-term patent protection of genes discovered as part of the human genome project hurt future innovation (Williams 2010). The patents examined in this study lasted for an average of just two years. Patents with a 20-year patent life are likely to be far more harmful to innovation.

Recent research found that even short-term patent protection of genes discovered as part of the human genome project hurt future innovation.

There is also the advantage that there would be little incentive to spend large amounts of money researching duplicative drugs. While the current system gives drug companies a large incentive to innovate to get a portion of the rents received by a breakthrough drug, there would be little incentive in a system of direct financing to devote resources to developing a drug for a condition for which an effective treatment already exists.8

In addition to the likelihood that directly funded research would be more efficient on per-dollar basis than research supported by patent monopolies, there is also the advantage that it removes any

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8 While having a choice of drugs for a condition can be beneficial, since not everyone reacts the same way to a drug, in general resources would be better spent seeking treatments for conditions for which no effective treatment is available than on developing the third, fourth, and fifth drugs to treat a condition for which the first drug is already quite effective.
direct link between profits and the use of the drug. This eliminates the incentive for drug companies to promote their drug even when it may not be appropriate. These sales efforts are an economic waste and can lead to bad health outcomes when pharmaceutical companies mislead the public on the safety or effectiveness of their drugs (Katari and Baker 2015).

Wholly transforming the system of financing drug research would obviously be a radical move. However, developing a piecemeal path to a new system is possible. Most research spending goes to clinical trials. The government could finance this portion of the research process while still leaving the preclinical portion subject to patent financing.

Companies engaged in publicly financed testing (again operating on long-term contracts) could buy up the rights to promising compounds. In this case also, the results would be available on the web, and the patents and other rights to exclusivity would be accessible to others on a copyleft basis. When drug tests proved successful and went through the Food and Drug Administration approval process, the drug would be immediately available as a generic. These drugs could compete with drugs for which the research was entirely supported through the patent system.

An advantage of publicly funding clinical trials is that by having all research results publicly available, independent researchers would be able to analyze the data. This would allow doctors to make more effective treatment decisions since they would know if a particular drug is better for some types of patients than others. For example, they would know if clinical trials showed a drug to be more effective for men than women or younger people than older people and if it leads to complications when combined with other drugs. Since the clinical trial data are currently under the control of the company that paid for the tests, this information is currently only available if the company had both done the analysis and decided to disclose the results.

There is an enormous amount of money potentially at stake here. The country is on pace to spend more than $430 billion in 2016 on prescription drugs. If these drugs were sold without patents or related protections, they would likely cost less than 20 percent of this amount.

**Replace Corporate Income Tax with Pseudo-Equity Stake**

The corporate income tax distorts investment decisions and leads to a substantial waste of resources in compliance and avoidance costs. Nonetheless, it remains a substantial source of revenue at the federal and state levels.

Also, insofar as the tax is born by capital, it provides a way of taxing capital income. Given the enormous inequality in stock ownership, any tax on capital income is inevitably progressive. For these reasons, there is little support for simply abandoning the corporate income tax even if there may be efficiency benefits.

A way to eliminate most of the compliance costs and distortionary impact of the corporate income tax, while still getting an equivalent amount of revenue for the government, would be to allow companies to grant an amount of nonvoting shares of stock (e.g., between 15 and 30 percent) to the government. These shares would track common stock.

If a dividend is paid for common shares, then the same dividend would be paid to the government for each share it holds. If the company buys back a fixed percentage of its common shares, then it would also purchase back the same percentage of these preferred shares at the same price. If the company issues new shares, then it grants enough new nonvoting shares to the government to leave its stake constant. In the event of bankruptcy, the government’s preferred shares would have the same standing as common shares. If there is a takeover of a company that has issued shares to the government, whether by another company or in a leveraged

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9 The published data would include patients’ individual characteristics, such as gender, age, weight, and other health conditions. These would be general enough to ensure patients’ anonymity.

10 There is dispute on the extent to which the corporate income tax is a tax on capital (see Hassett and Mathur 2006; Burman, Gravelle, and Rohaly 2005).
buyout, the purchaser would be obligated to buy back the government shares at the same price as they paid for common shares.

If a large portion of the corporations currently subject to the income tax opted for the share issuance system, it would substantially reduce the oversight costs for the tax.

The shares would be nonvoting because this is not an effort to have the government take control over private corporations. The nonvoting shares would give the government no authority in running the company. They would simply give it a stake in the company’s profits in the same way that it now has a stake through the corporate income tax.

This approach would make the before and after tax incentives for corporations identical. In most respects, the government-owned shares would not alter the incentives for paying out dividends, share buybacks, or retained earnings. Each decision would lead to pretty much the same outcome for shareholders, as is the case with the current system.

For example, if a company chooses to pay out $1 billion in dividends to its shareholders, then it would have to pay out $250 million in dividends to the government for the shares it holds, if it has a 25 percent stake. If it instead opted to use this $1 billion to buy back shares of stock, it would still have to pay the government $250 million to buy back the percentage of shares it holds. If it decides to retain the money to finance future investments, the government will get its 25 percent share of the returns on these investments as well.

In these ways, this route should be equivalent to a corporate income tax in appropriating for the government a share of corporate profits to support government spending. And it would sharply reduce the amount of resources devoted to dealing with the corporate income tax.

In principle this alternative to the corporate income tax could be either mandatory or voluntary. If it were mandatory, the process would involve setting a date by which corporations subject to the income tax would have to issue the required number of nonvoting shares to the government. After that point, the corporate income tax would no longer be applied to corporate profits. The transition period need not be a single date. It would be possible to set a time period over which companies must issue shares with the corporate income tax continuing until all shares are issued.

Companies could also be allowed to voluntarily switch from a corporate income tax to issuing nonvoting shares. A voluntary system would suffer from a problem of adverse selection, with the corporations that are subject to a higher effective tax rate than the required share allocation choosing to issue shares, while the corporations that have a lower effective tax rate remaining with the current system. However, this could still lead to a desirable outcome from the standpoint of imposing a more uniform and efficient system of corporate taxation.

If a large portion of the corporations currently subject to the income tax opted for the share issuance system, it would substantially reduce the oversight costs for the tax. This would make it easier for the IRS to combat tax evasion and identify the tax-avoidance schemes used by the corporations that were still subject to the corporate income tax. Also there would be a positive side to the self-selection process since the companies that opted to remain subject to the income tax must believe that they can pay a substantially lower tax rate than the implicit rate from the share issuance option. These are exactly the companies that present substantial enforcement or avoidance issues under the existing system.

**Individual Tax Credits as a Replacement for Copyrights**

Copyrights are increasingly difficult to enforce in the internet age. Governments have been pressed to adopt more repressive laws to assist copyright holders in enforcement and restrict the development of technologies to limit the ability to reproduce copyrighted material. Third parties have also been drafted into copyright enforcement, with web intermediaries now required to remove material alleged to be infringing at a copyright holder’s request. These problems could be avoided if
creative workers were paid in advance for their work, without relying on copyright protection.

Copyright protection also supports many of the highest incomes in the economy both directly and indirectly. The direct support is in the form of the royalty payments received by top earners in the music industry, movies, and even professional sports. While live performances account for much of these individuals’ earnings, they also get large incomes from copyrighted material. In addition, the entertainment industry offers high salaries for its top executives, with much of its revenue dependent on copyright protection. And intellectual property law is one of the highest-paying areas in the legal profession.

For these reasons, moving away from a copyright system to support creative work would likely reduce inequality. Also, if recorded music, movies, books, and other creative work were all freely available on the internet, it would increase real wages for the rest of the population.

A way to finance creative work without having a government agency of culture or its equivalent would be to have a modest individual tax credit (e.g., $75 per adult per year) that could be devoted to support whatever creative workers or intermediaries they chose. The model for this system would be the tax deduction for nonprofit organizations.

To be eligible to receive funding through this system, a person would have to register in the same way that a nonprofit does. This means simply telling the IRS what creative work a person does. The IRS makes no judgment of quality, just as it does not assess the quality of a think tank or the veracity of the beliefs of a particular religion. The condition of getting money is that a person would not be eligible for copyright protection for a certain period of time after receiving funding through the tax credit system (e.g., three to five years).

The taxpayer would have a credit dedicated for their creative work. They could either use it or not. This would lead to the creation of a vast amount of books, music, movies, and other creative material available at no cost on the web. This system would compete with copyrights as an alternative funding source for creative workers who want to remain in the existing system.

The desirability of an alternative to copyright monopolies should be apparent from the efforts that governments and corporations have been forced to make to limit unauthorized copying. People have faced substantial prison sentences or large fines simply for making unauthorized reproductions of copyrighted material available from their computers.

Policing copyright has also required blocking internet sites in other countries that post copyright material without authorization. Just as some countries have become tax havens to escape taxes imposed by the United States or Europe, countries can set themselves up as islands that do not enforce copyrights from other countries. This can become a basis for continually escalating efforts at avoidance and detection, all of which is a waste of resources, from the standpoint of an alternative system that does not depend on copyright monopolies.

In the United States, new technologies, such as digital audio recorders, have sometimes been delayed or blocked because they could make it more difficult to protect copyrighted material. When new technologies are introduced, there are frequent lawsuits over whether these technologies infringe on copyrights and therefore their manufacturers should be forced to pay compensation.

Similarly, the entertainment industry has sought to make colleges and universities partners in copyright enforcement, lecturing incoming students on the importance of respecting copyrights. In fact, the entertainment industry has managed to arrange for the Boy Scouts and Girl Scouts to offer merit badges in respecting intellectual property (Techdirt 2014).

Perhaps the greatest cause for concern in the abuse of copyright enforcement is the increasing effort to hold third parties responsible for inadvertent copyright infringement. Current law requires copyright holders to notify intermediaries of infringing material and request that it be removed. The Stop Online Piracy Act and the Protect Intellectual Property Act, the Senate counterpart, would have required internet intermediaries such as Facebook and Google to police their sites for infringing material. While these bills did not get approved, the entertainment industry continues to push for comparable measures, with their inclusion in trade pacts being one possible route for getting such strong rules into law.
By contrast, it should be relatively easy to protect against major abuses of the tax credit system. For example, if a creative worker became hugely popular while being supported by the tax credit system and then sought to have work copyrighted during the period in which they were not entitled to protection, their copyright would simply be unenforceable. Since there would be a public record of the period in which they were receiving money through the system, it would be possible to determine that they were not entitled to copyright protection, and therefore they would be unable to take any legal action against infringers.

It also should be possible to have measures that would protect against more trivial types of fraud, such as two individuals agreeing to trade their tax credits so both can pocket $75. Imposing a modest minimum sum as a condition of getting money through the system (e.g., $2,500–$3,000) would make this sort of fraud difficult. Even this low floor would require a substantial amount of coordination, which would put a person at serious risk of detection for relatively small gain.11

Perhaps the greatest cause for concern in the abuse of copyright enforcement is the increasing effort to hold third parties responsible for inadvertent copyright infringement.

Simple arithmetic indicates that a vast amount of creative work could be supported through this system. A tax credit of $75 per adult would make more than $15 billion a year available to support creative workers, if 80 percent of the eligible population took advantage of the credit. By comparison, in 2014 consumers in the United States spent $16.6 billion on recorded music in all forms and $12.1 billion on movies available on DVDs (BEA). A substantial portion of this spending went to intermediaries and the physical costs of producing and distributing the material, as opposed to the creative workers themselves. If $15 billion could be made available with even this modest tax credit, it would likely produce a sum that is comparable or larger than the money the copyright system actually provides creative workers.12

In addition to making a substantial amount of material available at zero cost, this tax credit system would also facilitate the creation of derivative works. While creative workers would still be entitled to full credit for their work (lack of copyright does not authorize plagiarism), creative workers could build on material that has attracted substantial public interest.

For example, in recent years various books have been written and movies have been made about the fictional detective Sherlock Holmes. This is possible without getting the copyright holder’s consent because the copyright has long expired. If the Sherlock Holmes books were not protected by copyright, other authors many decades ago could have written their own accounts of the adventures of Sherlock Holmes. This would not have precluded Arthur Conan Doyle from writing his own sequels, and his work would still be clearly distinguished from that of other writers. Readers would simply have had the additional option to read accounts of Sherlock Holmes that were not written by Doyle.

The issue of derivative works has come up in a variety of contexts. For example, numerous lawsuits have claimed copyright infringement because a new song was arguably too similar to an earlier copyrighted song. In another instance, the publisher of *Harry Potter* pressed a copyright suit against a club that wrote *Harry Potter* stories to share with each other.

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11 The current system of tax deductions for charitable contributions is much more susceptible to this sort of gaming. A person can establish a bogus charity to which a wealthy friend could make large contributions. Since the tax deduction would be worth 40 percent of the contribution for a person in the top income bracket, this arrangement would allow the two to split 40 percent of whatever amount was contributed. While the tax credit system proposed here would have a relatively modest limit of around $75 per person, in principle millions of dollars of taxable income could be sheltered through a scam that need involve only two people.

12 The credit’s reach would go beyond just recorded music and movies since it could also apply to writers and other types of creative workers, but these numbers should give an idea of the order of magnitude involved.
Under the current copyright system, only a relatively small number of creative workers are able to earn substantial income. The deadweight losses and the enforcement costs are enormous relative to the amount of income generated for creative workers. A tax credit system is a nonbureaucratic alternative that allows individuals to allocate funds to the creative work they find most valuable. On grounds of both economic efficiency and respect for individual freedom, this system is likely preferable to the copyright system. Of course, this could be determined by allowing the two systems to operate in parallel with both individuals and creative workers having the option to use the system of their choice.

**Work-Sharing Alternatives to Unemployment Insurance**

The current system of unemployment insurance gives an incentive for employers to lay people off rather than reduce their hours. This is because workers can get half of their pay (up to an earnings threshold) if they are unemployed, but they get no compensation for having their hours cut. Instead of encouraging layoffs, we should want a system that encourages firms to meet a reduction in demand with reducing work hours.

Keeping people on the job, but with fewer hours, keeps them in contact with the labor force. They will continue to upgrade their skills with new technology, and they will not have to deal with the trauma of unemployment. Twenty-six states now have work-sharing options in place, but more could be done to promote their use. As it stands, the take-up rates are low even in the states that have a work-sharing option available, largely because employers are not even aware that it exists.

There are successful models of work-sharing programs in other countries. While most OECD countries have some type of work-sharing system in place, Germany is really the model system. Its downturn in 2008–09 was every bit as severe as the downturn in the United States, but it experienced no comparable increase in unemployment. Its GDP fell by 6.9 percentage points from the first quarter of 2008 to the second quarter of 2009. In the United States, the drop was only 3.6 percentage points. In the United States, unemployment rose from 4.7 percent in November 2007 to a peak of 10.0 percent in October 2009. Over the same period, Germany’s unemployment rate fell from 8.2 percent to 7.7 percent.

The idea that it is better, other things equal, to keep workers employed working shorter hours than having them be unemployed should be noncontroversial. A large body of literature shows the negative effects associated with unemployment, especially long-term unemployment (e.g., Davis and Wachter 2011). Being laid off from a job is itself often traumatic. Long-lasting unemployment can lead to depression, alcoholism, and even suicide. Many of the older long-term unemployed will lose their attachment to the labor force and may never be employed again. The impact on families is also painful. Unemployment is associated with higher divorce rates and worse educational outcomes for children.

For these reasons, it would be desirable to incentivize employers to respond to reductions in demand by cutting work hours rather than laying off workers. Unfortunately, the current system of unemployment benefits in the United States and its institutional structure push employers in the opposite direction.

Historically, most benefits, such as health care insurance and defined benefit pensions, have been provided on a per-worker basis. This means that these benefits became largely overhead costs associated with hiring a worker. As a result, employers often prefer to have workers put in overtime hours, even if it means paying an overtime premium, rather than hire additional workers. The overhead costs of hiring a new employee could easily exceed any savings on overtime premiums.

This cost structure is changing. Defined benefit pensions are increasingly rare in the private sector, although even defined contribution pensions have some overhead costs associated with adding new workers. Fewer employers offer health care insurance, although the vast majority of workers continue to get health care insurance through their employer. This may change because of the Affordable Care Act, if it survives in something like its current form, since workers can now access insurance through the health care exchanges. Also, it is becoming more common for employers to
prorate their portion of the payment for insurance, depending on the hours an employee works.

Despite these changes, there are still tax and institutional incentives for employers to reduce the number of workers rather than the average number of hours per worker. Inertia is also an important factor in this decision. Layoffs have been the standard mechanism for dealing with a reduced demand for labor, so it requires some initiative on management’s part to pursue a route of reducing hours instead. For these reasons, it is appropriate for the government to institute a well-running work-sharing system and provide modest incentives to encourage its adoption.

On the former point, the federal government should act to ensure that all states offer a work-sharing option in their unemployment insurance system. Support from the federal government in covering startup costs has led several states to add work-sharing programs to their unemployment insurance systems since the 2008–09 recession. The federal government should continue to make funds available so states do not have to bear the cost of establishing work-sharing programs.

It is equally important to update many of the programs now in place. Many of these programs have antiquated systems that date from the late 1970s or early 1980s when they were initially established. In some cases, they still rely on paper records since the systems were never computerized. At a minimum, from the employer’s standpoint, it should be no more difficult administratively to use a work-sharing system than to use the traditional unemployment insurance system.

**A Vacant Property Tax**

Vacant properties often impose large negative externalities on their communities. This is especially true if they are not well maintained since the property can harbor rats and other pests, in addition to being an eyesore. It may also be used by squatters or be a haven for crime. For these reasons, communities have a clear interest in ensuring that vacant properties are properly maintained.

But even if the property is properly maintained, a vacant property is a waste of resources. Land or structures that could provide benefits are instead sitting idle.

The land market, like the labor market, can be slow to adjust. Owners of residential and commercial properties are often reluctant to lower sale or rental prices. This leads to a situation in which potentially valuable property can sit idle for long periods of time. If property were taxed for being vacant for substantial periods of time (e.g., four months), it would provide a strong incentive to lower prices and rents so that the property is used.

A vacant property tax can have a similar effect on the real estate market to that of reducing unemployment benefits and other supports on wages. It is generally accepted that a generous system of unemployment benefits keeps wages higher. If the benefits are higher, workers can stay unemployed for longer periods of time and reducing the labor supply keeps wages higher than would otherwise be the case.

Similarly, a tax on vacant property increases the cost of leaving it vacant. This means that property owners have more incentive to lower rents enough to find a tenant or lower the sale price enough to find a buyer. This would effectively increase the supply of real estate since fewer properties would be sitting vacant. The result should be downward pressure on the property and rental prices.\(^3\)

The slow adjustment of real estate prices was a problem following the collapse of the real estate bubble. There was a glut of residential and nonresidential property in much of the country. Many property owners had difficulty coming to grips with the new market environment. They saw the run-up in prices of the bubble years and expected that the bubble prices would soon return. Rather than accept a lower price to sell or rent their vacant

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\(^{3}\) A possible countervailing factor is that a vacancy tax could reduce the incentive to build. Assuming developers have perfect foresight, they would project some vacancy rate for the productive life of their building. If we impose a vacancy tax, the cost incurred for the projected periods of vacancy would be higher, although they percentage of time the property would be vacant would be less. The net effect would undoubtedly reduce the expected returns from the project, but it seems unlikely that this could reduce supply by enough to offset the benefits of a lower vacancy rate.
properties, they waited for prices to return to their bubble peak.

This tax has two especially nice features. First, since most property is already subject to a property tax, it would be relatively simple to tack on an additional tax based on the assessed value. The second attractive feature is that even efforts at evasion increase the cost of keeping property vacant. For this reason, it is giving property owners more incentive to use the property, which is the point of the tax.

The value of the nationwide residential housing stock is more than $16 trillion. At the trough of the market following the bubble’s collapse, almost 11 percent of this property, or $1.8 trillion, was reported vacant year-round. If this property were taxed at just 1 percent its assessed value, it could raise $18 billion a year. If a comparable amount were raised from taxing vacant commercial properties, the sum would be $36 billion a year.

Of course, there would be large variations by state. The states that have been hardest hit by the downturn would stand to raise the most from such a tax.

At the trough of the market following the bubble’s collapse, almost 11 percent of this property, or $1.8 trillion, was reported vacant year-round.

Unlike most taxes, all the side effects from this tax are positive. If property owners do not want to pay the tax, then they can just rent out their property. Or they may sell the property to someone else who actually plans to use it. Either outcome would push down residential and commercial rents.

In some cases, property owners may not be able to pay the tax and would simply give up the property. That is unfortunate, but it is better that the property be in the hands of someone who can use it productively than have it just sit idle.

Lower rents could really boost living standards. For middle-income families, rents are often more than 40 percent of income. If rent fell by 10 percent, this would be equivalent to a 4 percent increase in wages. Lower commercial rents would mean more stores and other businesses—think of it like a tax cut.

This route would be especially desirable in eurozone countries such as Spain and Greece where it is necessary to reduce large trade deficits. Since they are on the euro, these countries lack the most obvious mechanism for fixing a trade deficit: devaluing the currency.

The route being pushed by the European Central Bank and the International Monetary Fund is to have these countries experience an internal devaluation in which wages and prices fall to the point at which competitiveness is restored. This is proving to be a long and painful process. However, this process could be made much less painful if rents fell sharply. This would substantially reduce the cost of living for workers in these countries, possibly allowing them to see rising real wages even if their nominal wages remained stagnant or fell slightly.

**Conclusion**

This paper has outlined eight policies that are likely to reduce income inequality through greater reliance on market mechanisms. In each case, greater equality should be associated with more efficient outcomes. While more research would be needed on these policies, there are almost certainly situations in which an increased reliance on the market will lead to less inequality. Any agenda for reducing inequality should see market-oriented policies as an important potential tool.

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14 These countries also have institutional obstacles to lower rental and real estate prices, which a vacancy tax would not address.
About the Author

Dean Baker is the codirector of the Center for Economic and Policy Research.

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