

Here's What 'Income Equality' Would Look Like

By Scott Hodge

(*Wall Street Journal*) President Obama has talked a lot recently about reducing income inequality. Yet he neither acknowledges how much money the government is redistributing, nor how much more would be needed to close the income gap. Perhaps that's because the project would require redistribution on a staggering scale.

That's the upshot of two separate studies published in November 2013 by the Congressional Budget Office and the Tax Foundation. While they used slightly different methodologies, each study measured the amount of existing redistribution by the federal government—by comparing how much Americans get back in total federal spending (everything from transfer programs to national defense) to how much they pay in all federal taxes (everything from income taxes to excise taxes). Both studies show that the federal tax-and-spending system already is extremely progressive and redistributive.

Looking at prerecession data for non-elderly households in 2006 in "The Distribution of Federal Spending and Taxes in 2006," the CBO found that those in the bottom fifth, or quintile, of the income scale received \$9.62 in federal spending for every \$1 they paid in federal taxes of all kinds. This isn't surprising, since people with low incomes pay little in taxes but receive a lot of transfers.

Nor is it surprising that households in the top fifth received 17 cents in federal spending for every \$1 they paid in all federal taxes. High-income households hand over a disproportionate amount in taxes relative to what they get back in spending. What is surprising is that the middle quintile—the middle class—also got more back from government than they paid in taxes. These households received \$1.19 in government spending for every \$1 they paid in federal taxes.

When we add up who paid what and who got what for the 91 million non-elderly households in 2006, the CBO's data indicate that federal tax-and-spending redistributed \$1.2 trillion from the top 40% of households to their fellow Americans. Half of this amount benefited the bottom 60% of non-elderly households while the rest benefited seniors.

The Tax Foundation study, "The Distribution of Tax and Spending Policies in the United States," used postrecession 2012 data for all 150 million U.S. families (as opposed to households). It put the amount of federal redistribution from top earners at \$1.5 trillion, with state and local governments redistributing another \$500 billion. These results don't include the latest hike in top marginal tax rates to 39.6% from 35% or [Affordable Care Act](#) subsidies.

The overwhelming conclusion from both studies is that, as a group, the vast majority of Americans receive more back from government in spending than they pay in taxes. Even this large amount of redistribution falls far short of closing the inequality gap. So how much more redistribution would be needed to make every family equal? Quite a lot, it turns out.

According to the Tax Foundation study's estimate, the average market income for American families in 2012 was \$81,600. (Market income includes wages, business and capital-gains income, and health and retirement benefits, but excludes transfers.) A typical American family in the lower income quintile, on the other hand, has an average market income of \$9,560 and gets \$21,158 more in spending than they pay in taxes. Thus we would need to give them roughly \$50,882 more in federal transfers to raise their overall income to the average market income of U.S. families.

A family in the middle quintile has on average a market income of \$56,885 and gets \$7,376 more in spending than they pay in taxes. (Although these families are in the middle fifth of the population, their average incomes are actually below the national average.) So to raise their overall income to the U.S. market-income average, the government would need to give them \$17,339 in transfer payments above what they are currently getting.

Naturally, for families in the first three quintiles to gain, those in the top two quintiles have to lose. Families in the fourth quintile have an average market income of \$100,240 and pay \$4,089 more in taxes than they receive in spending. Thus, we would need to take an additional \$14,551 from these families to bring their market incomes down to the national average.

Families in the top fifth have an average market income of \$311,400 and pay \$65,573 more in taxes than they receive in spending. Thus we would need to take an additional \$164,227 from them in higher taxes to lower their market incomes to the national average.

Since there are millions of families in each quintile, these numbers begin to add up. To guarantee everyone in America an average income, the federal government would have to take an additional \$2.4 trillion in income from the top 40% of families—in one year. This would bring the total amount of income redistributed from the top to nearly \$4 trillion.

Many people believe the "rich" can afford to pay higher taxes since they command a disproportionate share of the nation's income. However, the current amount of redistribution already takes 21% of the top quintile's income. That would have to soar to 74% to make every family in America "average."

These are the missing pieces of the current inequality debate. To recap: Current federal tax-and-spending policies combine to redistribute \$1.5 trillion each year from the top 40% of Americans to the bottom 60%. To close the income gap to zero would require \$4 trillion.

The questions to those who say we should do more to narrow the income gap are: Where on that continuum should we aim, and what policies would achieve these goals without bringing the economy to its knees?

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