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Economics: Show Me the Money

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Are You the 99% or the 1%?

“We are the 99%” has become a well-known political slogan since the Occupy Wall Street protest in 2011. The remaining 1% represents the wealthiest people in American society. What happened between the “99%” and “1%?” The “occupy” protesters expressed strong grievance of the wealth inequality. Over the past 30 years, the bottom 90 percent has been suffering a serious stagnation until now while the top 10 percent’s wealth has been increasing astonishingly. For instance, according to *Wall Street Journal* 2, May 2016, last year Expedia’s CEO earned $95 million which became the highest among S&P 500 companies (Fitzgerald, Drew and Theo Francis). By contrast, the statistic from *U.S. Census Bureau*, the median household income was $53,657 in 2014, which was lower than the 2007. Before the recent recession, the median household income was $57,357, and the peak median house hold income was $57,843 occurred in 1999 (DeNavas Walt, Carmen and Bernadette D. Proctor 6). Through calculation, the CEO earns more than1770 times to the median household’s income.

Why do people care about this issue? Does the CEO really work 1770 times harder than the median household worker? The majority people realize the wider gap between the top rich people and middle class, the less upward social mobility they have. This means the majority of future generation will face more challenging and narrow developmental space. By contrast, the wealthiest people’s future generation will have the best education, enjoy the best products simultaneously. If we probe this persistently increasing gap, then we can find the series of tax cut policies established thirty years ago which has played a significant role.

Therefore, in order to ease widening income inequality, the top rich people should take their fair tax responsibility, and tax policy to those top wealthy people need to be changed.

There are many economists and organizations illustrate how serious the current wealth inequality is. According to a video “Wealth Inequality in America”, the intensifying gap is shown between the top one percent person and the bottom: the top 1 percent people own 40% of all the nation’s wealth in 2012, by contrast, the bottom 80% only own 7% of nation’s wealth. The top 1 percent people own 50% of stock bonds and mutual funds. By contrast, the bottom 50 percent people only own 0.5% bonds and funds (Politizane). This means rich people, especially the top one percent rich people become much richer, and middle class has been stagnated at the same time.

What is the relationship between tax policy and wealth inequality? Why many economists criticize previous tax reforms play a significant role in exacerbating the income inequality. As Joseph E. Stiglitz, the Nobel Prize winning economist, argues in his new book *The Great Divide: Unequal Societies and What We Can Do about Them,* our progressive income tax system is much lower than last century. During World War II, the peak top income tax rate was 94 percent. Then, it maintains around 70 percent during 1960s and 1970s. Now it becomes 39.6 percent. Even though the top rate has been cut nearly half, the very top rich still use all kinds of ways to lower their tax payment. Stiglitz points out the richest 400 individual taxpayers, who make average income more than $200 million, only pay less than 20 percent of their income in taxes. Even more, 116 of the top 400 earners actually paid less than 15 percent tax rate of their income. For instance, Mitt Romney, the former Republican presidential nominee admitted he paid only 14 percent tax of his income in 2011(Stiglitz 196-99). Obviously, this result should not happen in a fair progressive tax system.

Why does a progressive tax system become less progressive? Many scholars are trying to seek the answer. Olivier Bargain, Herwig Immervoll, Mathias Dolls, Nico Pestel, Dirk Neumann, Andreas Peichl, and Sebastian's research may give people some clues through major tax reforms from 1979 to 2007. They apply a new method for decomposing changes in government redistribution and assessing the effects of U.S. policy reforms on inequality from that period. In light of their research, the major changes in tax system have play an important role in income inequality. For instance, the Economic Recovery Tax Act of 1981 introduced the indexation of individual income tax. As a result, the top marginal tax rate reduced from 70% to 50% in 1982, and other tax rates by 23% from 1982 to 1984. In addition, the top income threshold increased from $85,600 in1982 to $109,400 in 1983, and $162,400 in 1984. Then, the Tax Reform Act 1986 broadened the tax base and reduced marginal tax rates. The top marginal rate was lowered to 38.5% in 1987 and to 28% in 1988. By contrast, the Omnibus Budget Reconciliation Act 1993 increased the income tax rate and the single biggest earned income tax credit. The top rate was risen from 31% to 39.6%. However, the Tax Reform Act 1997 reduced capital gains tax rates (Bargain et al. 1067). Based on isolated analysis, Bargain and his colleagues find taxpayers in the top quintile benefited more from tax policy, while middle and upper middle class benefited least from changes in tax policy. For example, they find the income share of the top 0.01% has risen by 350% with the direct policy effect contributing 18% to the increase from 1979 to 2007. After considering with both direct and indirect effect of tax policy, they conclude "from

1979 to 2007, tax policy aggravated the trend of growing inequality in pretax incomes: tax policy had a positive (negative) effect on the income share of taxpayers above (below) the 80th percentile. Hence, without any tax policy changes, observed inequality today is predicted to be lower" (1080). Many middle class were satisfied with these tax cut policies because they could decrease tax payment. However, the top rich people saved more tax payments. Considering the whole tax responsibility, the top wealthy people transfer more tax burden to middle class through these tax cut policies.

In addition to income tax policy, the wealth transfer tax, which includes estate tax, gift tax, and generation-skipping tax, also declined significantly. Originally, the main function of these transfer taxes is to minimize the wealth concentration. However, after a series tax reforms, the influence of these transfer taxes has been weakened. Based on Goldburn Maynard's research that in 1981, Congress lowered the estate tax rate and increased the exemption from $175,000 to $600,000. Then in 2001, President George W. Bush signed into law to lower the estate tax to 45% and raised the exemption to $3.5 million. At the end of 2010, President Obama lowered the estate tax rate to 35% and increased the exemption to $5 million. In 2013, the estate tax rate increased to 40% (Maynard 161). Can you believe the exemption become $5 million? How many middle class can own a $5 million estate? Obviously, these tax reforms did not adhere to the original purpose which should have focused on minimizing the wealth concentration. However, these tax reforms materially aggravate wealth concentration and exasperate inequality. This exacerbation of inequality is not only harmful to large majorities' lives, but also harmful to the whole society. Hence, taking tax reforms is imperative to offset income disparity.

There are many approaches can be taken to help contract the income inequality. Economist Robert Reich, who was Secretary of Labor under President Bill Clinton from 1993 to 1997, put forward some constructive proposals. He suggests raising the federal minimum wage, expanding the earned income tax credit to boost poor families' income, and unionizing low-wage workers. Even though some economists believe that the minimum wages will lead to more unemployment. However, Reich responses that those workers can strengthen their bargaining power through a union, and gain a fair share from economic growth (162). Some people also question about whether the expanding earned income tax credit will encourage idle people. However, if the expansion is particularly aimed at education, no matter children's education or skilled development, this will help ease the wealth inequality in the long run. As previous statistic find, the highest marginal federal income tax rate dropped more than half since 1981. Therefore, a higher tax on the wealthy people should also be considered, such as increase the exemption amount, raise the luxurious estate tax, eliminate tax loopholes. Some people think the top rich earners may transfer their wealth through global economic business. However, America is still an attractive and ideal place which has the largest purchasing power and the most safety investment environment. Similarly, Stiglitz proposes increasing taxes to those corporations which do not invest in America (212). Consequently, this suggestion will not only bring more tax revenue, but also encourage more domestic investment and employment.

Since the tax cut policy was established thirty years ago, the wealth gap between the top rich people and middle class has been widening persistently. The exacerbation of income inequality is detrimental to a healthy economy. Therefore, tax policy must be changed to address this serious disparity. If we do not take any action to reverse the situation, our future generations will face more struggling and exploitation. Furthermore, the loss of upward mobility and stagnation in middle class would increase the social conflict between the rich and poor. The fairer the tax system is, the more upward social mobility and the more energetic society people have. As result, a healthy, fair economic society also will improve gross productivity and average living standards. All in all, closing the wealth inequality gap, easing the stagnation of the middle class, and building a dynamic economy will benefit the "99%."

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