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THE U.S. TAX SYSTEM: WHO REALLY PAYS?

Stephen Moore
Senior Economic Writer,
Wall Street Journal
Editorial Board

"It is a paradoxical truth that tax rates are too high today, and tax revenues are too low and the soundest way to raise the revenues in the long run is to cut the tax rates.... [A]n economy constrained by high tax rates will never produce enough revenue to balance the budget, just as it will never create enough jobs or enough profits."—John F. Kennedy, 1963[1]

Even if most policymakers and members of the public instinctively understand the wisdom of President Kennedy's words, tax rates are set to go way up, not down, next year because of the scheduled expiration of the Bush tax cuts at the beginning of 2013. The Obamacare law also raises tax rates on wealthy individuals by an additional 3.8 percentage points next year. President Obama and others in Congress argue that these higher tax rates are justified because of the growing consensus that the rich don't pay their fair share of taxes. Unless we do something to spread the burden more equitably, the argument goes, American society will become more unfair and the economy more unsustainable with each passing year.

At first glance, the tax rate issue seems inseparable from the tax fairness issue, since higher taxes are expected to shift society's wealth from the private sector to the public sector, where, broadly speaking, it is redistributed to lower-wage earners and the needy. In reality, the people at the bottom of

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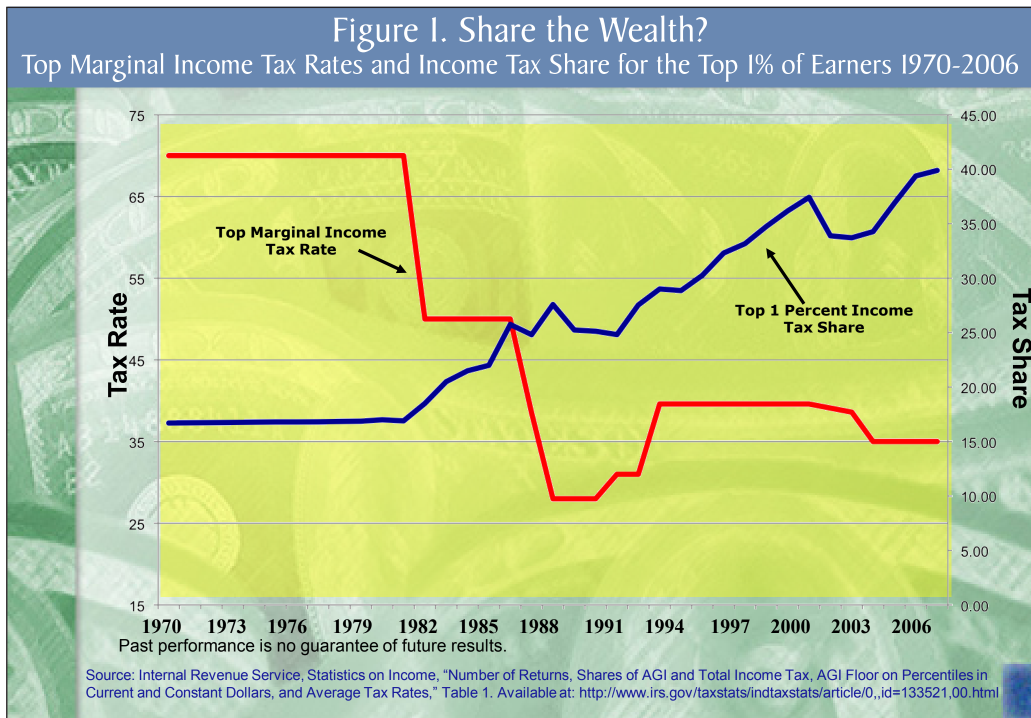
the scale have benefited directly and indirectly from every tax rate reduction dating back to Kennedy's rate reductions in the early 1960s and through the tax cuts adopted early in the administration of George W. Bush. If those lower rates, along with the Alternative Minimum Tax fix, are allowed to expire, the poor will be burdened even more than the wealthy because the whole economic pie will shrink.

If tax cuts work to expand the economy, the income pie gets larger for everyone. For example, tax rate reductions on businesses may mean more money after-tax for hiring more workers, paying them more, or purchasing more plant and equipment and computers that make workers more productive and efficient. Tax rate reductions on investment expand investment and mean more funds available for new businesses to get off the ground and for existing businesses to expand. Lower estate taxes may mean that family-owned businesses don't have to be sold at auction at the time of the owner's death. Everyone benefits.

At stake in the current tax debate in Washington are not only marginal income-tax rates but the tax on capital gains and dividends. Federal taxes are already scheduled to rise by about $700 billion over the next ten years to finance the Patient Protection and Affordable Care Act. In short, Americans face the largest cumulative tax increase since the end of World War II, which could be a mighty blow to an economy already on the verge of double-dip recession.

The truth is that higher taxes starve the very sectors of the economy that create jobs for everyone. They can, for a little while, reduce the incomes of our top-earning citizens—until these people's top-notch accountants are able to redirect their investments away from the most efficient, effective uses of their money and into sleepier investments such as government debt, instead of providing the capital that some high-tech company, for example, needs to develop its next tablet.

Below are a series of statements reflecting popular conceptions and misconceptions about the impact of tax rates on economic productivity and fairness. We'll address these statements (and debunk attendant myths) one at a time.



1. To become fairer, the tax code needs to tax the rich more heavily.

President Obama certainly thinks so. His latest budget proposal raises $1,700 billion in taxes over the next decade by increasing tax rates for the wealthiest Americans as well as for the middle class. He wants a top tax rate of almost 42 percent[2] (up from 35 percent today) on anyone with more than $250,000 in income from salaries, small-business income, and dividends. After paying state and local taxes, some Americans will face tax rates of nearly 50 percent—because for businesspeople and other active participants in the economy, many other types of tax are applied to almost every stage of transactions. As a result, much of those people's wealth, which might otherwise go toward creating jobs, would end up sitting in unproductive tax shelters.

For this and other reasons, high tax rates are the worst way to redistribute income to the poor and the middle class. In 1972, when the highest tax rate on the rich was 70 percent and the top capital-gains tax rate was 35 percent, the richest 1 percent of Americans assumed 18 percent of the income-tax burden. Today, with a top income-tax rate of 35 percent and a capital-gains rate of 15 percent, their share is 39 percent, more than twice as much. This is true because, faced with high tax rates, the rich of 40 years ago put more of their income into tax shelters or foreign countries. They invested less, and they worked less. And the rest of us suffered during the years of stagflation—as we will again, if rates are raised.

Even though taxes are 10 to 20 percent lower in the United States than they are in most other industrialized nations, the U.S. government is more dependent on rich people for taxes than are many of the more socialized economies of Europe. According to the Tax Foundation, the U.S. gets 45 percent of its total federal taxes from the top 10 percent of tax filers, whereas the average for industrialized nations is 32 percent. America's well-off bear a larger share of the tax burden than do the rich in Belgium (25 percent), Germany (31 percent), France (28 percent), and Sweden (27 percent).

Figure 2. Who Taxes the Rich the Most? Share of Taxes Paid by Richest 10%

Country	Share
Australia	37%
Belgium	25%
Canada	36%
France	28%
Germany	31%
Italy	42%
Japan	29%
Sweden	27%
Switzerland	21%
United Kingdom	39%
United States	45%
All OECD Nations	32%

Source: Tax Foundation, "No Country Leans on Upper-Income Households as Much as U.S.," 2011.

2. The rich are paying less in income taxes than they have in the past 50 years.

False. In 2007, the richest 3 percent of Americans contributed a larger share of tax revenues than they have in any year since 1960. For more than half its income, the federal government relies on what it takes from just that 3 percent.

Every year, the Treasury Department examines the distribution of federal taxes by income group. The data for all recent years yield the same conclusion: people at the top not only make a disproportionate contribution to the nation's wealth; they also pay a higher proportion of their collective income than those at the bottom. Let us examine the data for 2007, when

Figure 3. Who Paid How Much in Taxes (2007)

Earners (by percentile)	Share of Income	Share of Federal Income Taxes
Top 1% earned	22% of national income	Paid 40%
Top 5% earned	37% of national income	Paid 61%
Top 10% earned	48% of national income	Paid 71%
Top 25% earned	68% of national income	Paid 85%
Bottom 50% earned	12% of national income	Paid 3%

Source: IRS, 2010.

the richest 1 percent of Americans made 22 percent of all earned national personal income but contributed 40 percent of all personal income-tax revenue. The top 10 percent contributed 71 percent of all personal income-tax revenue. The bottom 50 percent earned 12 percent but contributed just 3 percent of the tax revenues so obtained.

3. When all the other taxes are counted, the rich get off easy.

It's true that the Social Security tax is somewhat "regressive," in comparison with the income tax. But the payroll tax makes much less difference than people might think. Payroll taxes of just under 15 percent (combined total of employee's and employer's share) are charged on the first dollar of income earned by a worker, and the tax is capped at an income of about $110,100 in 2012. The Tax Policy Center, which is run by the Urban Institute and the Brookings Institution, recently studied payroll and income taxes paid by every income group. It found that the highest-income 1 percent of Americans still pay a combined (income plus payroll) average rate of 26.1 percent, while the poorest fifth of Americans receive a refund of 0.9 percent, largely through the Earned Income Tax Credit. As Figure 3 illustrates, even when the regressive effects of the payroll tax are counted, the rich contribute a greater fraction of their income, and make a greater contribution to federal tax revenues, than other income groups.

Figure 4. Impact of All Federal Taxes (2009)

Cash Income Percentile	Percent of All U.S. Federal Tax	Average Effective Tax Rate
Poor	-0.2	-0.9
Working Class	3.1	6.6
Middle Class	10.5	13.4
Upper Middle Class	19.2	17.2
Wealthy	67.2	22.9
Top 10 Percent	52.0	23.9
Top 5 Percent	40.3	24.8
Top 1 Percent	22.9	26.1
Top 0.1 Percent	10.8	27.9

Source: Tax Policy Center, Table T09-0358 and T09-0357

4. Tax cuts are just Robin Hood in reverse, taking from the poor to give to the rich.

Since we have just shown that the rich pay more in taxes than the poor, it might appear that tax cuts disproportionately benefit the rich. But the economy is not a static, limited resource in which winners gain at the expense of everyone else. Tax rates can change the size of the pie, since they affect how people act in the economy.

Imagine that a 90 percent or even 100 percent tax on income over $100,000 were imposed. What would that mean for the economy? A lot of people would stop going to work, or seeking promotions, or working second jobs, or running their businesses. And who would want to start or expand a business under such a punitive tax regime? The higher the tax rate, the lower the incentive to lift a finger, propose new ideas, or create a single new job.

Low rates might be beneficial for the private sector, but we cannot pretend that we don't have a government or that it doesn't need funding. So in balancing the interests of the private sector and the claims of government, we need to focus on yield—how to raise the necessary revenue to fund government without shrinking the private economy. We must discover the optimal tax rate, which is the lowest possible rate that will produce sufficient revenues to pay for government's services.

How can we tell when taxes are too high? The most common side effect of excessive tax rates is an economic downturn or, in the worst case, a recession, such as we suffered repeatedly through the 1970s. The near-doubling of tax rates on the rich in the 1930s under Herbert Hoover and Franklin Roosevelt played an important role in extending the length of, and the suffering from, the Great Depression. In recessions, the rich do a little less well, but the poor suffer terribly.

Figure 5. Share of Individual Income Taxes Paid

	Top 1%	Top 5%	Top 10%	Top 20%
1980 top tax rate: 70%	17.4%	34.9%	47.6%	56.3%
2004 top tax rate: 35%	36.7%	58.5%	70.8%	84.0%

Source: Tax Policy Center Historical Shares of Federal Tax Liabilities for All Households by Comprehensive Household Income Quintile, 1979-2007

Recoveries, like the 25-year boom launched by Ronald Reagan's tax cuts, lift all boats—especially those of the people most vulnerable to economic ups and downs.

5. Lower tax rates can make the tax burden fairer.

True. In the early 1960s, the highest income-tax rate was 91 percent. That rate was slashed to 70 percent during the Kennedy administration and remained there until 1981. President Reagan slashed the top tax rate to 50 percent, then to 28 percent in 1986. Even though the tax rate fell by more than half, total tax receipts in the 1980s increased, from $517 billion in 1981 to $1,030 billion in 1990, reflecting strong growth of the economy. In view of the results, taxes also appear to have become fairer: since the late 1970s, even as tax rates fell by half, the amount of taxes paid by the wealthy, and their percentage of total income taxes paid, increased vastly.

This trend continued into George W. Bush's presidency: by 2007, the top 5 percent paid a larger share of individual federal taxes than the bottom 95 percent—for the first time since the Great Depression.

Along with fairness came opportunity, growth, and jobs because the money freed up for consumption and investment had a multiplier effect. Lower tax rates affect every economic decision. Just as consumers might forgo a vacation if they do not expect a tax refund, investors will take fewer risks if they expect their profits to be taxed away. Indeed, lower tax rates encourage investing in America (rather than China), where investors and entrepreneurs will start or expand businesses and create jobs. High taxes, by contrast, nudge people toward safe, sleepy investments or offshore tax shelters.

When President Kennedy was promoting tax rate reductions in 1963, he stated that the best way to promote economic growth "is to reduce the burden on private income and the deterrents to private initiative which are imposed by our present tax system—and this administration is pledged to an across-the-board reduction in personal and corporate income tax rates."[3]

Even though the truth of Kennedy's words has been confirmed, this country now faces the absurd prospect of a huge, automatic rise in tax rates in January 2013, when the Bush tax cuts expire. Many Democrats want to raise taxes for those earning more than $250,000—the bulk of America's investors and entrepreneurs—while most Republicans want to keep all the lower tax rates in place. The Bush tax cuts passed Congress in May 2003. The major changes were as follows:

- The tax on dividends was cut from 39.6 percent to 15 percent.
- The tax on long-term capital gains was cut from 20 percent to 15 percent.
- The highest marginal personal-income tax bracket fell from 39.6 percent to 35 percent. The lowest tax bracket fell from 15 percent to 10 percent.

Figure 6

Tax Revenues After Bush Tax Cuts Billions of 2009 Dollars		Tax Revenues After Clinton Tax Increase Billions of 2009 Dollars	
2003	$1,900.50	1993	$1,510.90
2007	$2,413.10	1997	$1,889.30
Real Revenue Growth	27%	Real Revenue Growth	25%
Average four year real revenue growth, 1970-2009 was 7%			

Source: White House Office of Management and Budget, Historical Table 1.3

- The tax on business investment in plant, machinery, and equipment was lowered.

Of course, wealthier Americans saved more in taxes than poorer Americans, since they had more money at stake. But the non-wealthy benefited significantly—and not just in their take-home pay. They saw more hiring by businesses, a stronger stock market, and other favorable reactions to the lower tax rates in 2003–07. At the same time, tax revenues rose more after the Bush tax cuts than they did after the Clinton tax increases. And the economy grew faster.

Moreover, after the 2003 tax cuts, payments by the rich increased faster than anyone else's. Total taxes paid by households earning $1 million or more in a given year more than doubled in 2003–07, even as the tax rate was lowered.

Figure 7 shows what happened to the number of Americans who declared more than $1 million in income on their tax returns through 2007. In just three years, the number earning at least $1 million more than doubled. The best way to get more money from taxpayers is to create more rich people.

Not only did the dollar payments of the rich rise, but the percentage of the total tax burden that the rich paid also increased. The rich are now paying more than they would have paid had the Bush tax cuts not gone through.

Figure 7. Taxes Paid By The Rich
Billions of Dollars, Adjusted Gross Income Tax

	2003	2005	2007
$1 million to $5 million	$78	$123	$155
$5 million to $10 million	$19	$35	$44
$10 million or more	$35	$78	$111
Total $1 million more	$132	$236	$310

Source: Internal Revenue Service, Number of Individual Income Tax Returns, by Size of Adjusted Gross Income, Tax Years 2001-2009

Figure 8. Tax Returns Reporting Over $1 Million

Year	Returns
2003	181,284
2005	303,817
2007	392,221

Source: Internal Revenue Service, Number of Individual Income Tax Returns, by Size of Adjusted Gross Income, Tax Years 2001-2009

Figure 9. Rich Pay More Under Bush Tax Cut
Income Tax Shares (2004)

	Top 1%	Top 5%	Top 10%
Treasury Estimate Without Tax Cuts	30.5%	50.2%	62.6%
Actual Tax Payments With Tax Cuts	36.7%	58.5%	70.8%

Sources: Tax Policy Center Historical Shares of Federal Tax Liabilities for All Households by Comprehensive Household Income Quintile, 1979-2007: http://www.taxpolicycenter.org/taxfacts/displayafact.cfm?DocID=558&Topic2id=20&Topic3id=22
US Department of the Treasury Fact Sheet: Who Pays The Most Individual Income Taxes: http://www.treasury.gov/press-center/press-releases/Pages/js1287.aspx

The rich also paid a larger share of total personal income taxes paid following the 2003 tax cuts, partly because those tax cuts provided a big cut in middle-class taxes and took a big percentage of Americans off the tax rolls completely.

All these wealth-creating policies would be reversed if the 2003 cuts are allowed to expire in January 2013. Not only would those with high incomes be affected: the Alternative Minimum Tax would return, and because it has not been indexed to account for income inflation, it would affect 30.1 million Americans, swelling the tax bills of people making less than $100,000 a year by $2,000–$3,000.

Here is what will happen if nothing is done about extending the Bush era tax cuts and abolishing Obamacare taxes:

If those tax rates go up, many economists believe that it will push the stock market lower, contract the real economy, and possibly contribute to a double-dip

Figure 10. The Tax Time Bomb

	Tax Rate Now	Tax Rate in 2013
Income Tax Top Rate	35%	41%
Long-Term Capital Gains	15%	23.8%
Dividends	15%	43.4%[4]
Estate Tax Top Rate	35%	45%

Sources: Tax Policy Center 2013 Budget Tax Proposals Analysis and Author's Analysis

recession like the one that Americans suffered under President Jimmy Carter. Our current recovery is too fragile—we are still 4 million jobs short of where we were in 2007—to withstand such a blow. Except in the face of a conflict like World War II, it's almost never a good idea to raise taxes, but it's especially foolish when the economy is still struggling.

6. All those tax cuts created deficits that have mortgaged our children's future.

False. The lower tax rates brought in more money because they helped the economy to grow and created more jobs and more wealth. Reagan's tax cuts caused federal tax receipts almost to double, from $517 billion to $1,032 billion. As *The New York Times* stated on December 8, 1992: "One popular misconception is that the Republican tax cuts caused the crippling federal budget deficit now approaching $300 billion a year. The fact is, the large deficit resulted because the government vastly expanded what it spent each year."[5]

A growth spurt similar to the one following Reagan's tax cuts came in response to Bush's. The Congressional Budget Office (CBO) reports that in the first four years of the Bush tax cuts, federal revenues increased by $786 billion—the largest real increase in history. From 1981 to 2007, every time tax rates were reduced, tax payments by the rich climbed:

- At a top rate of 70 percent in 1980, the top 1 percent paid $47 billion in federal taxes. Today, at a 35 percent rate, they paid more than $400 billion. Even adjusting for inflation, that is a nearly 300 percent increase in tax payments by the rich.
- After the Reagan income-tax cuts in 1981, the highest-earning 1 percent more than doubled their collective income-tax payments, from $50 billion in 1981 to $114 billion in 1988.
- After the 1986 tax reform act, income-tax payments by the rich rose from $70 billion to $146 billion in 1993.
- After the 2003 tax cuts, payments by the rich increased from $256 billion in 2003 to $451 billion in 2007. Some of those revenue gains were inflated by the housing bubble, but there was certainly no revenue loss.

What matters most in collecting the taxes needed to run the government is how fast the economy grows and how many jobs are created. Raising tax rates on the prosperous—especially small-business owners, who would be exposed to higher taxes if the 2003 tax cuts expire—can be counted on to shrink the economy and stifle job creation.

All this talk about tax increases is really a political diversion from the real problem in Washington: overspending. The federal budget is now $3.8 trillion, compared with roughly $2 trillion in 2000. Reagan used to cast aside calls for higher taxes with a simple retort: "Never give a big spender a bigger allowance." The spending disease is what really threatens to paralyze our economic future.

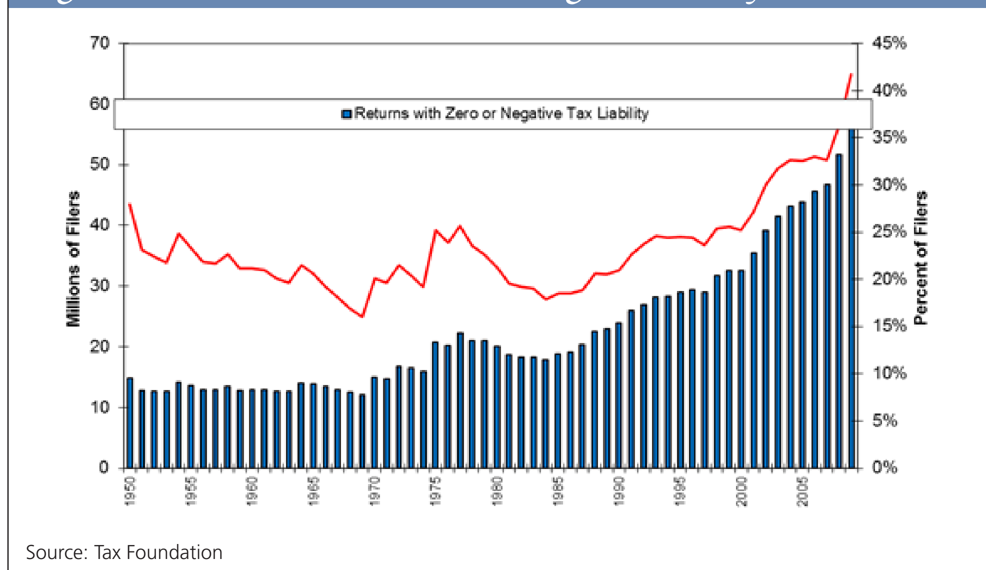
7. Ordinary Americans pay more than their fair share of taxes.

Every year, fewer Americans pay any income tax at all. The nonpartisan Tax Foundation found that in 2009, nearly 42 percent of Americans who file tax returns end up paying no tax. In 2008, that percentage was around 36 percent.[6] Many of these Americans actually received a check from the IRS because of the tax credits that they claimed.

8. The 15 percent tax on investment income, which is well below the income-tax rate that most salaried workers pay, is a gift to the wealthy.

If it is, it's one that a majority of Americans benefit from. The latest polls show that 54 percent of Americans own stock and benefit directly from lower capital-gains and dividend taxes. But that is probably the smaller part of how ordinary taxpayers benefit. Capital gains are what is left over when an investment—in a

Figure 11. Tax Returns with Zero or Negative Liability, 1950 to 2009



stock whose price could have tanked, or a new business that could have gone bankrupt—succeeds. Investing is therefore different from drawing a paycheck, which is almost certain to clear. It makes sense to reward productive risk-taking with a lower tax rate.

Lower capital-gains rates also increase the amount of taxes paid. The 1997 capital-gains tax cut reduced the long-term rate from 28 percent to 20 percent. In the subsequent three years, the amount of taxable capital gains almost doubled. When President George W. Bush cut the rate again, to 15 percent, a 107 percent increase in revenues from 2002 (the year before the rate was reduced) to 2005 resulted.

One explanation is the effect of taxes on decision making. When tax rates are high, people postpone selling stock that they own and thus claiming a profit, even if it would be more rational, from a strictly economic standpoint, to do so right away. In short, the tax code, and not good business sense, is making economic decisions for them. By keeping investors from reallocating their capital to its highest, best use, high taxes promote economic inefficiency and damage productivity. They also shrink the volume of gains that can be taxed.

As John F. Kennedy said in 1962: "The tax on capital gains directly affects investment decisions, the mobility and flow of risk capital …[,] the ease or difficulty experienced by new ventures in obtaining capital, and thereby the strength and potential for growth in the economy."[7]

9. A higher capital-gains rate would just level the playing field.

It's true that many very rich people get their income from capital gains and dividends, which are taxed at a lower rate, but that lower rate is deceptive because it is a tax on top of the tax that corporations pay before they pay any of their profits to shareholders. In the U.S., the rate that corporations pay on their profits can be as high as 39.2 percent when including state taxes. (The compensation that they pay their employees is a tax-deductible business expense.) The real tax rate on corporate income paid to individuals through capital gains and dividends is not 15 percent but closer to 40 percent. A higher capital-gains rate would just compound the injustice. In 2007, middle-class families earning between $34,000 and $50,000 paid an effective 14.3 percent of their income to the federal government, according to the CBO. In 2007

(the most recent year for which data are available), those earning more than $2 million paid an average of 24.9 percent. That 15 percent rate cannot be said to tilt the tax system in rich people's favor.

10. The "wealthy" are likely to be the people next door.

In a country of more than 300 million people, the number of fabulously rich people—the top entertainers, athletes, hedge-fund managers—is tiny. Most of the people in the top income-tax category are small-business owners and investors. Most small businesses are S corporations, meaning that they are taxed at their owner's individual-income rates, according to the Senate Finance Committee. Thus, when tax rates go up on the rich, they go up on small businesses.

How the wealthy are doing, as well as how numerous they are, has a big effect on the revenues that the government can collect. Because the economy has done so poorly in recent years, tax payments by a dwindling number of the rich have plummeted. According to IRS data, 390,000 tax filers reported adjusted gross income of $1 million or more for 2007. These people paid $309 billion in taxes. In 2009, there were only 237,000 such filers, a decline of 39 percent, and the total taxes they paid declined to $178 billion, a drop of 42 percent.

Those with $10 million or more in reported income fell to 8,274, from 18,394 in 2007, a 55 percent drop. As a result, their tax payments plummeted by 51 percent.

Figure 12. Recession and the Rich

	2007	2009	%change
Tax Returns			
$200,000 and above	4,536,000	3,924,000	-13
$1 million and above	390,000	237,000	-39
$10 million and above	18,394	8,274	-55
Taxes Paid			
$200,000 and above	610 bill.	434 bill.	-29
$1 million and above	309	178	-42
$10 million and above	111	54	-51

Source: IRS Statistics of Income, 2011

These disappearing millionaires go a long way toward explaining why federal tax revenues have sunk to 15 percent of GDP in recent years. The loss of millionaires accounts for at least $130 billion of the increased federal budget deficit in 2009.

Today's "tax fairness" activists are concerned mainly about income inequality. But raising taxes contributes to downturns and recessions, which may, unfortunately, be the only way to increase equality. And recessions fall inordinately on the less well-off. Are financial losses for all levels of income an acceptable price to pay for greater equality of income? The recession and weak recovery of the past four years have been income levelers. In 2007, those who made more than $200,000 earned about 35.2 percent of our nation's total income; in 2009, that figure went down to 33 percent. In 2007, those with incomes above $1 million earned 17.3 percent of the nation's income; by 2009, that figure was down to 12.9 percent. So we have created a more equal society—by making America poorer.

11. It is increasingly harder to climb the economic ladder, and changing the tax code will help.

Barack Obama seems to think so. Since the early 1980s, he says, the rungs of the economic ladder have been sawed off, making the upward climb increasingly futile. He also alleges that a child born into poverty in the years immediately after World War II had a better than 50–50 chance of moving into the middle class; and a child born into poverty in 1980 had a 40 percent chance of moving up; but a child born today will have only a 33 percent chance of "making it to the middle class." *The New York Times* reports that other nations have much more income mobility from one generation to the next than does the United States. It cites research that finds that most Western European and English-speaking nations have higher rates of mobility. The *Times* reports that in the U.S.,

42 percent of those born into the bottom fifth of income stay there as adults. In many other industrial nations, only about 33 percent or 25 percent born into the bottom quintile are found there as adults.[8] Are these gloomy portrayals true? Not exactly.

The story on income mobility across generations in the U.S. is admittedly mixed. The questions are whether a person born poor is likely to be poor when reaching adulthood and whether children who grow up in rich households are much more likely to be rich as adults. In other words, how much does it matter who your parents are, in terms of your own success? We would like to think that what matters most is individual initiative and hard work, not one's genes or one's head start in life.

One thing we do know for certain is that today's workers are generally a lot wealthier than their parents were at the same age. A study by Ron Haskins, based on Pew Foundation data, found that about 66 percent Americans have higher incomes than their parents did at the same age. Even more impressive: when adjusting for family size, 81 percent have a higher income than their parents did. So it is not true that our parents were better off than we are.

But there does seem to be considerable controversy and some distressing news about the ability of low-income Americans to climb up from the bottom rungs of the economic ladder. Most studies now find that about 40 percent of low-income children in America have a low income as adults. If one's probability of being poor were not related to one's parents' income, that figure would be close to 20 percent. Even more distressing is that less than 20 percent of Americans who grow up in a poor household move into the high-middle-income or high-income category. It is getting harder for a poor person to rise to the top income level, according to the analysis by *The New York Times*.

A new analysis by Scott Winship, an economic studies fellow at the Brookings Institution, a left-of-center Washington think tank, has looked at the mobility data and is not so negative about the trends. Winship, an expert on economic mobility, points to at least six prominent studies on "intergenerational income mobility." That is, research that compares the income status of parents with that of their children when they become adults finds "either no change or rising mobility" in recent decades. Winship also examined data from a national longitudinal survey of children born between 1962 and 1964 and children born between 1980 and 1982 and compared these cohorts' income when they reached the age of 26 to 28 with their parents' incomes, and found that upward mobility from poverty to the middle class rose from 51 percent to 57 percent over these two periods. He is reluctant to conclude definitively that mobility increased but is emphatic that "the data provides absolutely no evidence that economic mobility declined, whereas the president said it has fallen by 10 percentage points."[9]

Even more confounding is President Obama's assertion that only one in three kids born today will move out of poverty. That is not based on any data or any factual measurement but is pure conjecture by researchers. How does anyone know what the income 25 years from now will be of a child born today? More to the point, what is the value of such negative speculation? As Winship puts it, "all the president is doing is reinforcing any doubt among the poor that they can make it if they try."[10] It is like trying to teach a six-year-old to ride a bike but telling her in advance all the reasons she will probably fall.

But Winship agrees that a more permanent underclass in America is emerging. "In particular, it's American men who fare worse than their counterparts in other countries."[11] Men in poor households have a hard time finding their way into higher income classes—but not primarily because of economic factors limiting mobility. Social factors—divorce, out-of-wedlock births, bad neighborhoods, and extremely dysfunctional schools that don't train children to be highly functioning adults—are responsible. Most experts on the left and right agree that one of the most important steps

to reduce income inequality and give every American a fair opportunity to succeed is school choice, so that parents can opt out of failing schools. Welfare reform that continues to promote work over the dole is also critical, as well as policies that promote intact families.

There is little doubt that government can redistribute wealth: taxing high-income individuals can and has increased equality. But there is little evidence to suggest that this results in increased economic mobility for the poor. A 2006 study by Chul-In Lee and Gary Solon finds that intergenerational income mobility has not changed significantly despite various changes in tax rates: "[O]ur results … suggest that intergenerational income mobility in the United States has not changed dramatically over the last two decades."[12] That study makes it difficult to see how raising taxes on the wealthy will generate increased income mobility for the poor, and it underscores the point that equality is not synonymous with economic mobility.

Stephen Moore is the author of the forthcoming book Who's the fairest of them all? *from Encounter Books.*

ENDNOTES

[1] Quoted in Arthur B. Laffer, Stephen Moore, and Peter J. Tanous, *The End of Prosperity: How Higher Taxes Will Doom the Economy—If We Let It Happen* (New York: Simon & Schuster, 2008), p. 56.

[2] This figure includes the phase-out of deductions under the Affordable Care Act (ACA).

[3] Quoted in Laffer et al., p. 48.

[4] This figure and the capital gains figure includes the 3.8 percent surtax imposed under the ACA.

[5] David Rosenbaum, "The Push and Pull Over Taxes," *New York Times*, December 8, 1992, p. D1.

[6] Tax Foundation, "Federal Income Tax Returns With Zero or Negative Liability," October 18, 2011. http://taxfoundation.org/article/federal-individual-income-tax-returns-zero-or-negative-tax-liability-1950-2009 .

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[8] Jason DeParle, "Harder for Americans to Rise From Lower Rungs," *New York Times*, January 4, 2012, p. A1.

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