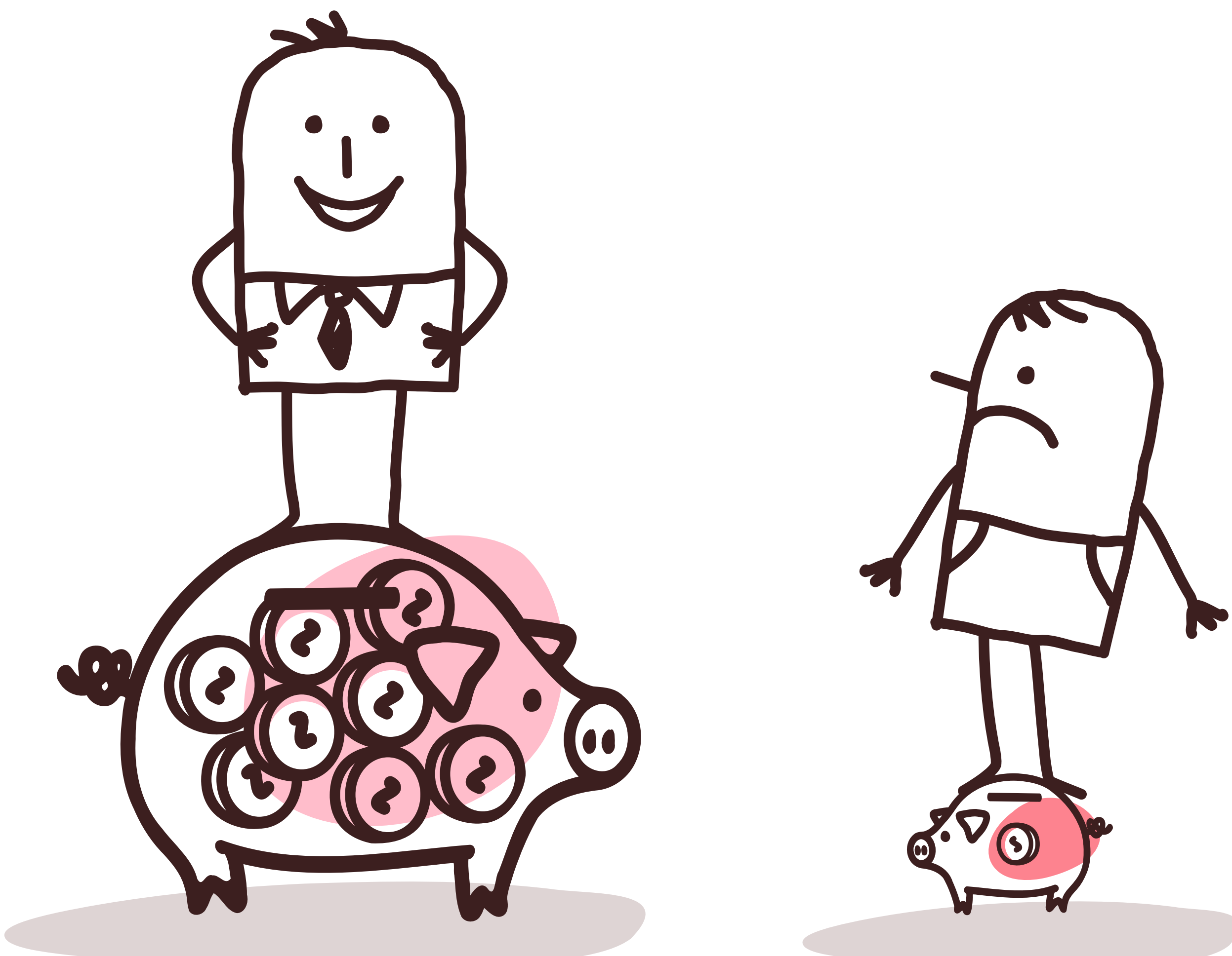
INCOME INEQUALITY IS HURTING ARKANSAS

INVESTMENTS IN OUR PEOPLE WILL MAKE IT BETTER



A REPORT BY ARKANSAS ADVOCATES FOR CHILDREN AND FAMILIES

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INCOME INEQUALITY IS HURTING ARKANSAS
Investments in our people will make it better

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Arkansas Advocates for Children and Families
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7 Things You Need to Know About Inequality In Arkansas

- **Flat wages are keeping average Arkansans from getting ahead.** From the late 1970s to the late 2000s, the most well-off Arkansans saw their incomes grow almost twice as fast as the poorest.
- **Inequality is holding Arkansas back.** When all of the wealth is concentrated at the top, low- and middle-income earners cut back on purchases that would contribute to job growth.
- **Low- and middle-income Arkansans are being left behind while the rich get richer.** The typical Arkansan's income has stagnated; in 2012 the median family income was only about five cents an hour above recession levels.[1]
- **Household economic stability is weak in Arkansas, especially for minorities.** If a family is unable to make ends meet for three months without income, they are classified as "Liquid Asset Poor." In Arkansas, this indicator is below the national average and is much more likely to affect minorities.
- **The mobility/wealth gap is widening and decreasing the chances that hard work will move you up the economic ladder.** Of the Arkansans earning below average incomes, less than 27 percent were able to make a significant income improvement over the period of a decade.[2] That means people are stuck, and it's hard to move up. Upward mobility is a staple of the American dream. All Arkansans deserve a fair shot at working their way up the ladder, contributing to our economy, and making this state a better place to live.
- **Capital gains tax exemptions favor the wealthy.** High-income households are more likely to invest in stocks and real estate. The capital gains profits from these investments are taxed at a lower percentage than regular income from a paycheck, meaning the wealthy get a big tax break. In Arkansas, 85 percent of the total taxable capital gains went to people earning at least $100,000.[3]
- **The government can take an active role in addressing income inequality.** Steps Arkansas can take include: (1) enacting a state earned income tax credit; (2) making sure everyone pays taxes based on their ability to pay; (3) investing in programs, such as education, that increase mobility; (4) raising the minimum wage; and (5) strengthening the unemployment insurance system.

Introduction

The gap between the rich and poor in Arkansas is growing, and it is hurting all of us. Increasing inequality in Arkansas holds back economic growth, damages the democratic process, and keeps many low income and minority families stuck in poverty. But it can be fixed. Arkansas will be a stronger state if we correct an unfair tax system that primarily benefits the wealthy, and invest in our workers with programs that increase mobility like unemployment insurance and an increased minimum wage.

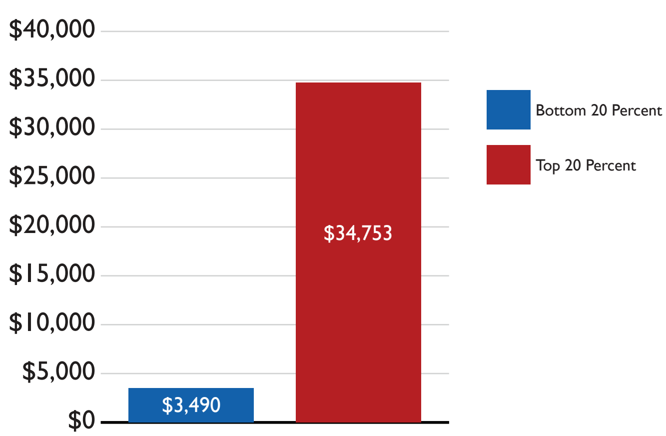
Inequality In Arkansas Is Getting Worse

Inequality is particularly bad for poorer states like Arkansas. The top five percent of Arkansas earners make ten times as much as the bottom 20 percent of households.[4] This ratio still ranks relatively well nationally (44th overall from 2008-2010)[5] but the consequences of these income differences are magnified when average incomes are already much lower than in other states. Arkansas ranks third from the bottom in median household income, which means low- and middle-income earners will feel the pinch of even small increases in inequality.[6]

Over the past several decades, low- and middle-income earners in Arkansas have fallen behind. In the 1970s, top quintile earners made the total annual income of the average bottom quintile earner by March 4, or in about 9 weeks. By the late 2000s, those same top earners make the total annual income of bottom quintile earners by February 24, over a week sooner.[7] From the late 1970s to the late 2000s, wealthy Arkansans saw their incomes grow almost twice as fast as the poor. The top 20 percent of earners in Arkansas saw their average incomes increase by 41.5 percent (or $34,753 in adjusted 2009 dollars) while the bottom quintile saw an increase of only 23.9 percent (or $3,490 in adjusted 2009 dollars).[8] That's over ten times more for the wealthy! This mirrors national trends where the share of income going to the top ten percent is higher than it has been in decades.

CHANGE IN REAL DOLLAR INCOME SINCE 1977

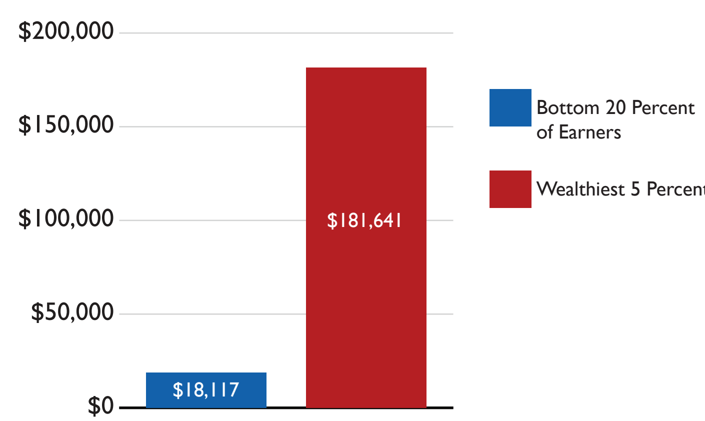
Income growth for wealthy far outpaces that of the poorest Arkansans



SOUCE: From CBPP's 2012 "Pulling Apart" data report found at http://www.cbpp.org/files/11-15-12sfp.pdf

WEALTHY ARKANSANS MAKE 10 TIMES MORE THAN THE BOTTOM 20 PERCENT OF EARNERS

Average yearly income from 2008-2010



SOUCE: From CBPP's 2012 "Pulling Apart" data report found at http://www.cbpp.org/files/11-15-12sfp.pdf

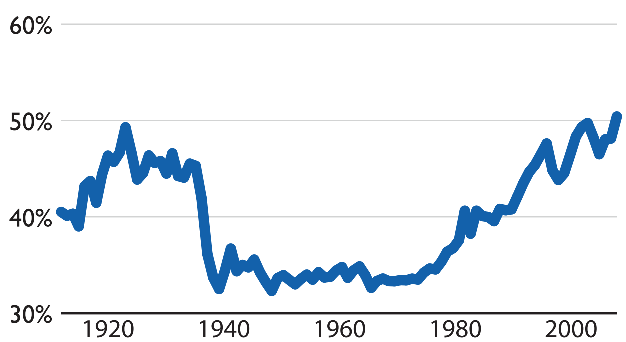
In more recent years, the wealthy have seen vast increases in income while low- and middle-income families are still struggling with conditions very similar to those during the depths of the recession. Recent Gross Domestic Product (GDP) growth in Arkansas has particularly benefited high-income earners. In the late 2000s, the average income of a top five percent earner in Arkansas was $181,641. The average income of someone in the bottom 20 percent was only $18,117. If the total increase in personal income in Arkansas from 2009 to 2012 was shared equally, all Arkansans would have seen their earnings go up by $1,588.13 a year.[9] Instead, the median annual income for an entire household in Arkansas went up by only $94.85 during that time (a raise of about five cents an hour).[10,11] Gains since the beginning of the recovery in 2009 are leaving out low- and middle-income families in favor of the very wealthy.

Inequality is bad for economic growth

We know that there are differences in income (otherwise everyone would earn the same amount), but it is important to note how big these differences are, and how they change over time because these differences effect the total health of our economy. The real problem is that income inequality affects all of us, not just small subsets of the population. William Gross, founder of the investment firm Pacific Investment Management Company, recently said, "Developed economies work best when inequality of incomes are at a minimum" and a recent survey from the Associated press shows that a majority of economists agree that inequality is bad for the economy as a whole.

SHARE OF INCOME GOING TO TOP 10 PERCENT AT HISTORIC HIGHS

Percentage of all US income going to the top 10 percent of earners by year, since 1917.

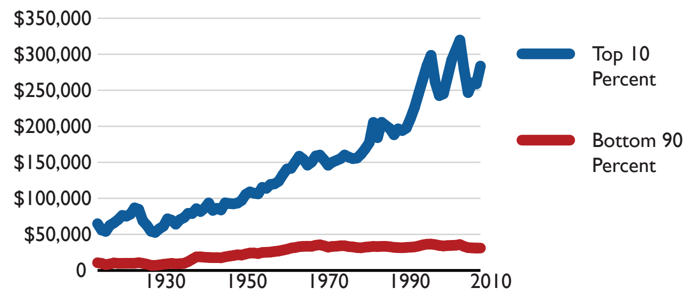


SOURCE: "The Evolution of Top Incomes in the United States," Emmanuel Saez, UC Berkeley, September 3, 2013

Unfortunately, huge gains are being dumped on the already super wealthy while low- and middle-income families are seeing their incomes slowly inch up or even stagnate. This growing inequality means that even as the economy expands, many Arkansans will still be facing near recession levels of income. The low- and middle-income earners in Arkansas whose pay has leveled off are also the consumers that drive job growth through making purchases. If their incomes are going nowhere, the heart of the economy will suffer. There will always be some degree of inequality, but it becomes an issue when we reach a level so extreme that it imperils the overall economy and the ability of low- and middle-income families to earn enough to put food on

INCOME GAP WIDENS, RICH GET RICHER

Incomes for those at the top have increased drastically since 1919. For the bottom 90 percent, it's a different story.



SOURCE: "The Evolution of Top Incomes in the United States," Emmanuel Saez, UC Berkeley, September 3, 2013

the table. If these families aren't making enough money to spend on goods and services, the economy slows down as a result.

Inequality Damages The Democratic Process

The impact of income inequality isn't just felt in citizens' wallets; it has an impact on our political systems too. The ability to make major campaign contributions is becoming increasingly important in influencing public policy. Growing income inequality is therefore limiting the ability of low- and middle-income citizens to exercise their voice and have an impact. Evidence has shown that "growing income inequality also has exacerbated discrepancies in political influence in federal, state, and local government."[12] An equal voice should be given to all voters, not just to the super wealthy. James Lardner, author of "Inequality Matters," says "as the gap in political participation between social classes rises and financial resources become more relevant in the American political system, the voice of the poor will increasingly fall on deaf ears in government."[13]

Low-Income Families And Minorities Are Stuck

Low- and middle-income Arkansans (and their children) who are seeing stagnating wages have a harder time accumulating wealth and are more likely to get stuck making a certain amount of money with little hope for a raise. In a 2012 PEW study, Arkansas fell short of the national average in terms of relative upward mobility.[14] Low- to middle income Arkansans are particularly unlikely to move up the ladder. Seventy three percent of Arkansans with below average incomes were still stuck there after 10 years, hardly able to move up at all.[15] These problems are even worse for lower income minorities in our state.

Inequality is also a symptom of a lack of opportunity to succeed. It is becoming more and more difficult to break into the middle and upper classes. The number of Americans who believe that their kids will be better off than they are "has plummeted from 62 percent in 2009 to 47 percent [in 2011]."[16] Fewer people are moving up (or down). Americans want to know that if they work hard, they can achieve financial success, provide for their families, and have the chance to move up the economic ladder.

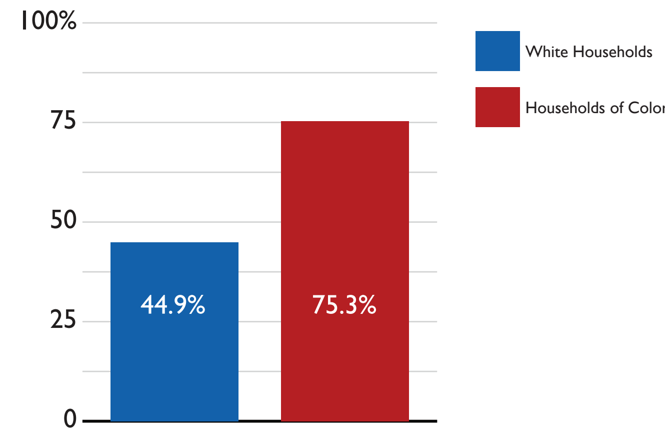
Inadequate savings makes it harder to afford things, like higher education, that can lead to a rise in income down the road. A lack of savings also makes it harder to weather an unexpected financial crisis, like an injury, that can devastate a family's economic situation. Ideally, talented, hardworking citizens would frequently succeed far beyond where they started. The economic mobility project found that, nationally, "Those born at the top and bottom of the income ladder are likely to stay there as adults. More than 40 percent of Americans raised in the bottom [20 percent] of the family income ladder remain stuck there as adults, and 70 percent remain below the middle."[17]

Minority households in Arkansas face additional barriers because they don't have the same rates of educational attainment that help high-income, white families obtain degrees and profitable careers.[18] A recent report funded by the Mary Reynolds Babcock Foundation and the Annie E. Casey Foundation finds that in Arkansas "The overall mathematic gap between white and black students is the 15th largest in the nation, and scores for African Americans in Arkansas are the worst in the country." Furthermore, African Americans in Arkansas are less prepared for college, scoring 15-20 percent below average on college entrance exams like the ACT test.[19] Without a strong educational foundation, minority and low-income families are more likely to see financial hardships as adults.

Inequality in Arkansas is even more likely to affect minority citizens. Many low-income families find it hard to increase their earnings, but non-white households are even more susceptible to a financial crisis because of higher rates of financial insecurity measures like liquid asset poverty, meaning an inability to make ends meet for three months without income. From 2006 to 2010 overall liquid asset poverty in Arkansas showed a modest decrease (from 52.5

PERCENTAGE OF ARKANSAS HOUSEHOLDS THAT EXPERIENCE LIQUID ASSET POVERTY

Minority households find it harder to make ends meet for three months without income



SOURCE: http://scorecard.assetsandopportunity.org/2013/measure/liquid-asset-poverty-by-race

percent to 51.6 percent), but at the end of 2010 minority households were still far more likely to experience this type of poverty than white households (44.9 percent compared to 75 percent).[20] These differences are due in part to the massive and ongoing educational achievement gap between white and minority students.[21] That's why it's so important for Arkansas to create a fair tax structure and an education system that helps everyone achieve.

Unfair Tax Policies Are Making It Worse

How are the top earners able to grow their wealth so much faster than the average Arkansan? Part of the answer is that high-income households are more able and more likely to invest in stocks and real estate. The "capital gains" profits from these investments are taxed at a lower percentage than regular income from a paycheck, giving high-income earners a break that poorer people don't get. In Arkansas, 85 percent of the total taxable capital gains went to people earning at least $100,000, and half of the total taxable capital gains income went to people earning at least a million dollars annually.[22] The Arkansas General Assembly made this gap worse by passing major capital gains tax cuts in the 2013 legislative session. A full explanation of the tax changes passed in the 2013 legislative session that primarily benefit upper-income taxpayers is available from the "Better Foundation" report at www.aradvocates.org.

The same is true nationally. A recent UC Berkeley report found that "the top one percent captured 95 percent of the income gains in the first three years of the recovery."[23] Additionally, the top five percent of the income distribution in the United States collected 87 percent of the total earnings from capital gains in 2012 alone.[24] A 2012 report from the Center on Budget and Policy Priorities confirms that "the gains of economic growth show up increasingly as capital income such as interest and dividends rather than increased wages, salaries, or benefits. Thus, wage earners benefit less from economic growth than wealthier owners of assets like stocks and investment properties."[25] So even with a growing economy, many working Americans are still falling behind.

We Can Fix It

A 2011 PEW poll found that a vast majority of Americans want their government to take action to promote economic mobility. "An overwhelming 83 percent want the government to either provide opportunities for the poor and middle class to improve their economic situations or prevent them from falling behind or both. We want to see hard work pay off equally no matter where someone starts out on the socioeconomic ladder, and Americans across party lines are calling for government action to level the playing field.[26] This feeling cuts across party lines, with 91 percent of Democrats, 84 percent of independents and 73 percent of Republicans agreeing.[27] The rising levels of inequality in Arkansas are a red flag signaling a decrease in the equality of opportunity that is so valued in this country. Much of the structural changes need to occur at the national level but there are several important steps to take at the state level.

1. **Correct an imbalanced, "upside down" tax system so that everyone, including the top income earners, pays their fair share in state and local taxes.** Currently low-income earners in Arkansas pay twice as much as high-income earners as a share of their income.[28] That's upside down. The Arkansas state income tax system needs to be more progressive so that high-income earners pay their fair share and provide a stronger foundation for a tax system that can support investments in all of its residents. Creating steeper and more significant differences in state income tax brackets will also help level the playing field for Arkansans. Reducing the generous exemptions for capital gains taxes, which mostly benefit the rich, will also help shrink the income gap.

2. **Enact a state earned income tax credit (EITC).** Tax credits like the federal EITC help struggling families now and also increase the chances of success for future generations. Enacting a similar state-level tax credit will help combat the problems associated with low wages and assets faced by many Arkansans. A Center on Budget and Policy Priories report shows "the children of families with more income from refundable tax credits will do better in school, and they are likelier to attend college and also likely to earn more as adults."[29]

3. **Invest in programs that increase mobility.** It is crucial to the future of Arkansas that we continue to invest in education for all citizens. The Economic Mobility Project 2013 found that "having college degrees significantly increased households' median income and wealth levels and boosted mobility prospects."[30] Family assets also increase the opportunities for mobility, so it is important to look into programs such as homeownership support that increase these assets.

4. **Raise and index the minimum wage.** Arkansas workers are losing their stake in the success of the businesses they contribute to. Employees are becoming more and more productive, but they aren't seeing their paychecks increase. Economists estimate that if minimum wage had kept up with increases in worker productivity since the late 1960s, our current minimum wage would be $16.54.[31] A worker should be paid fairly for what he or she produces, and that paycheck should be periodically increased to keep up with rising prices. The minimum wage has not only failed to keep up with worker productivity, it hasn't even kept up with inflation. Because of inflation, the 2011 federal minimum wage is 12.1 percent lower than it was in 1967."[32] By raising and indexing the minimum wage we can ensure that the average employee doesn't get left behind.

5. **Reinforce the unemployment insurance system.** The unemployment insurance system counteracts the detrimental effects of liquid asset poverty by creating a financial safety net during times of unemployment. This increases the ability to establish wealth, and thus, mobility.

Notes

[1] This assumes a 2,080 hour work year.
[2] A significant improvement here indicates moving up at least 10 percentiles, for example from the bottom 20 percent of earners to the bottom 30 percent of earners.
[3] http://www.irs.gov/uac/SOI-Tax-Stats---Historic-Table-2
[4] http://www.cbpp.org/files/11-15-12sfp.pdf
[5] http://www.cbpp.org/files/11-15-12sfp.pdf
[6] http://www.census.gov/hhes/www/income/data/statemedian/
[7] http://www.cbpp.org/cms/?fa=view&id=255
[8] http://www.cbpp.org/cms/?fa=view&id=255
[9] http://1.usa.gov/K8WXBt
[10] http://www.census.gov/hhes/www/income/data/statemedian/
[11] http://www.census.gov/hhes/www/income/data/statemedian/
[12] http://www.cbpp.org/files/11-15-12sfp.pdf
[13] Lardner, James, and David A. Smith. Inequality Matters: The Growing Economic Divide in America and Its Poisonous Consequences. New York: New, 2005. Print.
[14] http://www.pewstates.org/research/data-visualizations/economic-mobility-of-the-states-85899381539
[15] http://www.pewstates.org/research/data-visualizations/economic-mobility-of-the-states-85899381539
[16] http://www.pewstates.org/research/analysis/economic-mobility-and-the-american-dream-where-do-we-stand-in-the-wake-of-the-great-recession-85899378421
[17] http://www.pewstates.org/research/reports/pursuing-the-american-dream-85899403228
[18] http://citizensfirst.org/about-us/legislative-priorities/achievement-gap/Achievement%20Gap.pdf
[19] http://citizensfirst.org/about-us/legislative-priorities/achievement-gap/Achievement%20Gap.pdf
[20] http://scorecard.assetsandopportunity.org/2013/measure/liquid-asset-poverty-by-race
[21] http://citizensfirst.org/about-us/legislative-priorities/achievement-gap/Achievement%20Gap.pdf
[22] http://www.irs.gov/uac/SOI-Tax-Stats---Historic-Table-2
[23] http://elsa.berkeley.edu/~saez/saez-UStopincomes-2012.pdf
[24] http://www.taxpolicycenter.org/numbers/Content/PDF/T09-0492.pdf
[25] http://www.cbpp.org/files/11-15-12sfp.pdf
[26] http://www.pewstates.org/research/analysis/economic-mobility-and-the-american-dream-where-do-we-stand-in-the-wake-of-the-great-recession-85899378421
[27] http://www.pewstates.org/research/analysis/economic-mobility-and-the-american-dream-where-do-we-stand-in-the-wake-of-the-great-recession-85899378421
[28] http://www.itep.org/
[29] http://www.cbpp.org/cms/?fa=view&id=3793
[30] http://www.pewstates.org/research/data-visualizations/faces-of-economic-mobility-85899503593
[31] http://www.cepr.net/index.php/blogs/cepr-blog/the-minimum-wage-and-economic-growth
[32] http://www.epi.org/publication/declining-federal-minimum-wage-inequality/

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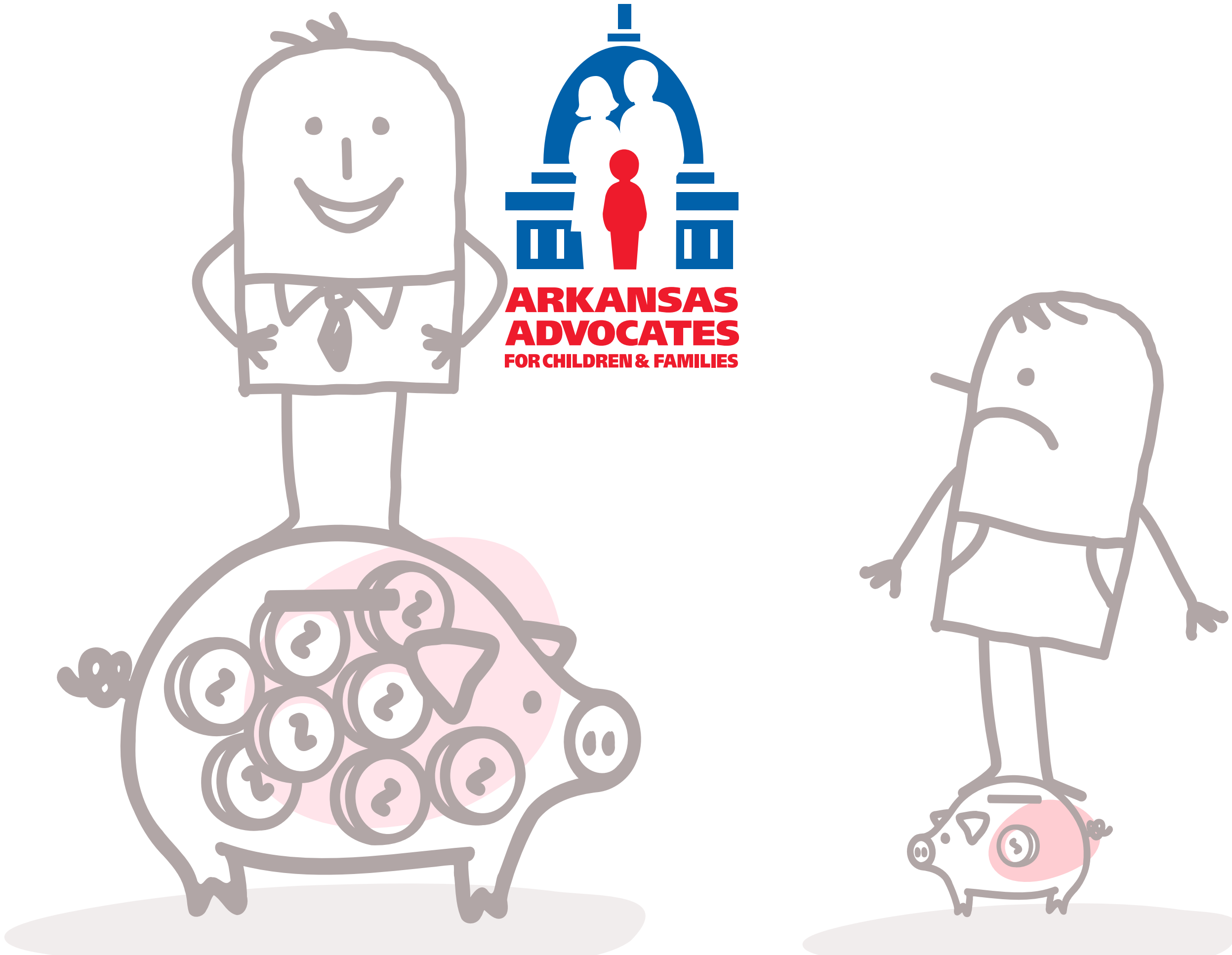

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