the federal architecture of

Income INEQUALITY

Draft 9/6/24

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*Income inequality is a national preoccupation, and the public’s imagination is captured by the astronomical incomes of Silicon Valley tech billionaires and Greenwich fund managers. But most people do not live in California or Connecticut, and many of the adverse effects of income inequality are local. Our preoccupation with national income inequality comes at the expense of attending to localized inequality and our national focus has potentially pernicious effects as policies that reduce national income inequality can paradoxically increase local income inequality. Using income tax return data, I show how recent proposals for student loan forgiveness and interest payment pauses have precisely this effect.*

*Understanding the moral significance of income inequalities across different contexts and levels of political organization requires a general account of how incomes are translated into the goods that affect individual status, well-being, and opportunity. This translation of income into power and consumption can be thought of as occurring through an architecture of “allocative fields,” which includes commodity markets and political entities such as states and counties. Toward this end, I propose a new composite measure of income inequality that accounts for the range of contexts where it matters. Viewing income inequality through this lens allows us to see new ways of addressing the adverse effects of income inequality, including accounting for distributional effects of federal policies at subnational levels, adopting a national priority for the poorest, and tinkering with the federal architecture of income inequality itself.*

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*We are told that, as he was crossing the Alps and passing by a barbarian village which had very few inhabitants and was a sorry sight, his companions asked with mirth and laughter, “Can it be that here too there are ambitious strifes for office, struggles for primacy, and mutual jealousies of powerful men?” Whereupon Caesar said to them in all seriousness, “I would rather be first here than second at Rome.”[[2]](#footnote-2)*

# Introduction

When it comes to income inequality, context is everything. Imagine that your family consists of two adults and one child in Madison County, Mississippi, population 110,000. You make $50,000 per year, which places you right in the middle of income distribution—you are richer than 54% of the households in Madison.[[3]](#footnote-3) But because Madison is an affluent county by Mississippi standards, your income is higher than 69% of households in the state. On the other hand, Mississippi is a poor state by national standards, so your income places you at the 57th percentile nationally. Yet again, and on the bright side, since the U.S. is such a rich country, your income makes you richer than 93% of the world.[[4]](#footnote-4) You are middle-income in Madison, affluent by Mississippi standards, middle-income by U.S. standards, and very rich when compared globally. Which reference point matters for shaping the experience of income inequality? They probably all do, to some degree. But local standards may matter most of all.

Consider how your income translates into the experience of inequality across contexts. You can afford a modest home in Madison and eat out once in a while. You are a relatively anonymous member of the community, respected but not pandered to by local government officials and leaders of local schools or community organizations. But you are an alumnus of the University of Mississippi, and you periodically return to Ole Miss to attend reunions and football games. When you do, you buy tickets to the games and hotel accommodations in Oxford that most fans in the state cannot afford and, while tailgating with your college roommates, you enjoy a feeling of easy superiority, knowing that you are a graduate of the most elite university in the state, the alma mater of 27 Rhodes Scholars and 10 governors. Although you are only a little engaged in state politics, even your modest political donations exceed those of most of the state’s population, and you have met both of your Senators and the Governor at fundraisers in Oxford over the years.

Although you and your family enjoy annual vacations throughout the Southeast, trips to major coastal destinations—New York, San Francisco, Los Angeles—have always seemed just a bit beyond your reach. The cost of travel, accommodations, restaurants, and many of the amenities would stretch your budget too far. And the burden of having to watch each of your expenditures so closely makes the prospect sound like not much fun. You are also aware that in many of those parts of the country, your home state is frequently the butt of jokes and is openly called a “dependent,” “taker,” or “moocher” state.[[5]](#footnote-5)

But you have travelled outside the country. Last year, you and your family spent a week in Costa Rica, enjoying luxurious accommodations in San Jose, a private travel guide, and feeling mostly unconstrained by cost in choosing restaurants. Your greater purchasing power is noticed by the locals, who regard their American visitors as “wealthy,” “powerful,” and (less flatteringly) as having “inflated egos.”[[6]](#footnote-6)

There are enormous differences in living standards and income inequality across counties, states, and countries. For example, if you lived in Blaine County, Idaho, in 2020, you lived in the most unequal county in the country, a county that was 39% more unequal than the United States as a whole.[[7]](#footnote-7) But you also lived in a state with less inequality than half of the states in the country, a state that was 5% *more* equal than the country as a whole.[[8]](#footnote-8) You would have lived in a relative unequal county, in an equal state, in an unequal country. By contrast, someone who lived in Orleans County, New York, lived in a county that was 21% more equal than the U.S.,[[9]](#footnote-9) but in a state that was 4% less equal than the U.S.[[10]](#footnote-10)

In the United States, media representation of income inequality is driven by narratives involving specific people—Jeff Bezos or Elon Musk—or archetypes—the financier or tech wizard—with whom most of us will never cross paths.[[11]](#footnote-11) They may live thousands of miles away and spend their money on completely different things than we do. It is much more likely that income inequality in our own neighborhoods is shaped by lawyers, doctors, and the owners of auto dealerships.

The national narrative of income inequality focuses attention on national solutions. This focus is evident in the national distributional tables that are used to evaluate the effects of policy proposals such as the adoption of a wealth tax,[[12]](#footnote-12) the taxation of capital income using mark-to-market accounting,[[13]](#footnote-13) and student debt relief.[[14]](#footnote-14) But if local inequality is at least as much of a problem as national inequality, then the effects of federal policies need to take this into account and a uniform national approach to income inequality is likely to be a poor fit for the problems of income inequality. This does not mean that national policies cannot address inequality at each level that it matters, but it does mean that a more nuanced approach is required.

For example, consider the federal income tax deduction for state and local taxes (SALT). Individuals who itemize their personal deductions may deduct state and local income and property taxes in computing their federal taxable income.[[15]](#footnote-15) Making state and local taxes deductible reduces their burden on individuals and makes it easier for states and localities to impose higher taxes. After all, taxpayers in high tax jurisdictions do not bear the full cost of those taxes because the SALT deduction transfers some of the costs to the federal government through lower federal tax collections.

In 2017, federal legislation placed a $10,000 cap on the SALT deduction.[[16]](#footnote-16) Since the SALT deduction is only available to people who itemize their personal deductions and grows with the amount of state and local taxes that an individual pays, it tends to benefit higher-income taxpayers in high-tax states. As a result, limiting the SALT deduction makes the federal income tax more progressive and reduces after-tax income inequality *on a national level*. However, consider the following: if the limit on the SALT deduction reduces the political feasibility of high state and local taxes such that they fall over time, the SALT limit could undermine state and local income redistribution. And in that case, the reduction in national inequality could come at the cost of an increase in state and local inequality.

This article analyses the political and social boundaries defining the spaces where income inequality matters. I explain how the problems arising from income inequality are fundamentally intertwined with the structure and allocation of economic and political authority within a federal system. The more power is exercised by the federal government, the more troubling is national inequality. The more power delegated to states and localities, the more important is state and local inequality. This means that reconfiguring the allocation of authority between the federal and state governments can diminish or exacerbate the ills of national income inequality.

I explain how measured income inequality can vary dramatically in a federal system at different levels of aggregation, and I document the recent history of national, state, and local income inequality in the United States. I then describe how attempts to remedy national inequality can adversely affect state and local inequality, and show some of these effects using several recent national policies pertaining to tax and student debt. Finally, I consider some ways that federal fiscal policy might respond to the problems of local income inequality. I propose to replace simple national inequality measures with an index that reflects the importance of local inequality. I argue that national policies should be guided by this more nuanced and useful measure of income inequality and that, very often, national policy should emphasize policies that redistribute from the richest to the very poorest.[[17]](#footnote-17) Focusing national efforts to reduce inequality on the very top and very bottom of the income distribution is the most reliable means of ameliorating inequality in a federal system.

The themes in this article are central to the scholarly literature on fiscal federalism.[[18]](#footnote-18) The robust conclusion from the existing literature is that income redistribution should be performed by national, rather than by local, governments.[[19]](#footnote-19) What often goes unnoticed is that this conclusion is premised on the idea that the national income inequality is what matters. When we foreground this assumption about the primacy of national inequality, it is intuitive that national solutions are preferable to local ones. Indeed, it would be astonishing if *local* fiscal tools were discovered to be the best way of addressing *national* inequality. I challenge the premise of these analyses by arguing that local inequality matters too, and it may even matter more than national inequality. Whether national, state, or local inequality is of greater concern depends on how political power and fiscal authority is allocated across these different levels of government in a federal system. The fact that local income inequality can be a problem does not imply that income redistribution should also be local, but it does require a more nuanced approach to addressing inequality at higher levels of government. As I will show, policies that reduce national income inequality can simultaneously increase local income inequality.

Other scholars have argued that local inequality matters. For example, the economist Mark Pauly has grounded the normative importance of local inequality in the altruism of people towards those who live closest to them.[[20]](#footnote-20) Status comparisons are also mostly local, with people caring about their relative position vis-à-vis their neighbors, not the whole world.[[21]](#footnote-21) But these accounts about the localism of altruism and status-comparisons are fairly particular, whereas I argue that they are examples of a more general category of locally-allocated goods. In this article, I suggest a general framework that describes the contexts within which income inequality is important by connecting income inequality among members of a group to the resources allocated in their political or economic contexts.

The distribution of income only affects the distribution of well-being after it has been refracted through the economic and political infrastructure of U.S. federalism and the U.S. economy. Income inequality matters little in some contexts and much more in others. Appreciating the benefits of reducing income inequality requires understanding the way that this architecture translates differences in income into differences in status, opportunities, and well-being. And reducing the adverse effects of income inequality can involve changing the architecture as well as reducing income inequality itself.

In Part I, I propose a framework for understanding the direct and collateral effects of income inequality within different contexts. The framework is built upon the idea of “allocative fields”—the different spheres of economic and political life characterized by the allocation of a different privilege, good, or opportunity on the basis of income. I argue that income inequality within each of these fields has varying degrees of normative significance, depending on the goods that are allocated within those spheres. I explain how different measures of income inequality do, or do not, capture the underlying values that motivate our inequality concerns, and I emphasize the value of accounting for inequality both within and between groups.

Part II reports new evidence about differences in the levels and trends in income inequality at the national, state, and local levels, painting a much more complex picture of inequality in the United States than is typically represented. I then analyze the effect of several recent federal policies to contrast the effect that they would have on national inequality with the effect that they would have on state and local inequality.

In Part III, I situate my approach within the fiscal federalism literature and consider the best way to address income inequality in a federalist system where income inequality at different levels of political and economic association has different welfare effects. To address local inequality at the national level, we must begin by incorporating local inequality measures in our distributional analyses. Toward that end, I propose a new composite measure of income inequality. I also emphasize the benefits of focusing on the well-being of the poorest members of society in enacting redistributive policies at the national level.

# I. Income Inequality in Context

## Why Income Matters

Before turning to the problems of income inequality, it is worth briefly summarizing why income is valuable. The answer may seem obvious, but being explicit about the fundamental goods that income helps realize is helpful to understanding the importance of income inequality in a federalist system, and how the features of our political and economic institutions and the arrangement of political authority interact with income inequalities. Before we consider what is objectionable about income inequality, we need to understand why income is valuable.

The economic definition of income is a broad conception that includes the value of a person’s consumption plus any increase in her net wealth over some time interval.[[22]](#footnote-22) This definition of income includes not only the cash wages someone is paid by their employer, but also any in-kind benefits. If your employer provides you with the free use of a company car, pays your health insurance premiums, or provides you with a free lunch at the company cafeteria, these, too, are income. Why? The goods and services that someone consumes are the kinds of things that generally make them better off. Having the use of a car means you do not have to walk everywhere, which is tiring and time-consuming. Health insurance facilitates access to medical care that can have important effects on the quality and length of your life. And, of course, everyone needs to eat.

But money is not like this, and neither are mere changes in the value of one’s property. The value of money is in what you can accomplish by transferring it, whether that be paying for a child’s college tuition, donating to charity, or spending it on indulgent meals or holidays. If no one were willing to exchange something of intrinsic value for money, then it would be worthless, like Monopoly money in a real economy. Ultimately, the value of money income bottoms out in people’s willingness to accept it in exchange for something of intrinsic value. Because of this, the value of money income depends on the configuration of the economy, the pervasiveness of markets, and the number of things that are for sale. The more goods are allocated by the market, the more valuable market income is to the person who has it, which means that moving the boundary between public/private methods of allocating goods and services affects the value of money income.

For example, a prohibition on private schools reduces the value of earning income to parents if they would have used that income to send their child to a private school or if they would have made a gift to friends or family so their children could attend a private school. The same is true of limits on political contributions. Direct limits on the contributions I can make to political candidates, or limits on the ability of candidates themselves to spend donated funds, reduces the ability of my income to help me realize my political goals or purposes. The logic is general: reducing the scope of markets reduces the power of money income to realize purposes and desires across the economy, and it reduces the value of income and the incentive to earn it. In the same way, increasing the prices of goods and services also reduces the usefulness of income. It is an individual’s *real* income—her nominal income adjusted for the cost of consumption—that affects her wellbeing.

In sum, the first reason money is valuable is because it can be exchanged for the kinds of things that people enjoy for their own sake. And since that ability depends on the ubiquity of markets for exchanging goods and services for money, the regulation of markets can have a direct impact on the value of an individual’s money income. There is a fundamental interdependence of the value of money income and the structure of the economy; the range of opportunities to exchange money for something else provides that value.

Income also confers social status and respect.[[23]](#footnote-23) People view the amount that others are willing to pay them for their services as a sign of respect that reflects their value. This relationship between income and status, whatever its historical roots, is a natural consequence of a market-oriented economy.[[24]](#footnote-24) Market logic tends to allocate greater financial rewards to people who are more productive, in the sense of doing work that is more highly valued by other people. In a competitive economy, individuals are paid based on the productivity of their labor, so the more productive an individual is, the higher her wage. The better one is at investing capital where it can earn the highest return, the higher one’s income. Income is how we keep score of the value (measured in market terms) of an individual’s labor, so there is a direct connection between income and status in a world where status is allocated based on how well one deploys resources to satisfy individual wants in the marketplace.[[25]](#footnote-25)

This is only a descriptive and contingent claim about how having a higher income tends to confer higher social status because of presumptions about how that income was earned. These presumptions may of course be false. One may have a high income for reasons that have nothing to do with contributions to the social product. One may work in an industry with large economic rents arising from monopoly. Income earned in the financial industry, from digital platform networks, or land speculation, may be perceived this way.[[26]](#footnote-26) One may have obtained one’s income through theft or fraud. Conversely, one may make large contributions to the social product in ways that are not remunerated in the market, such as by providing child-rearing or other caregiving activities, for instance.[[27]](#footnote-27)

Needless to say, even if income accurately measured contributions to the social product, it would be a dubious basis for creating a status hierarchy. The financial returns to one’s labor or capital are not an indicator of a timeless virtue. At best, they reflect how well one can deploy efforts and talents at satisfying other people’s desires. The returns on one’s labor depend on the goodness of this fit. The lawyer’s skills are well-remunerated in a society with extensive laws and regulations and restrictions to entry into the market for lawyers, but much less well-remunerated in a society where disputes are resolved by force or through some other non-legal method.

Distinguishing between these two sources of value for money income—exchangeability for consumption and signal of status—is important because the values derive separately from pre-tax and after-tax income. An individual’s income net of taxes and government transfers determines her ability to command resources in the market economy and to use it to realize her purposes. But it is an individual’s pre-tax income, the return on her labor and the deployment of her capital, that is an (imperfect) marker or signal of her contributions to the social product. Whether we tax LeBron James’s earnings at a 20% rate or a 50% rate will affect the resources available to him for realizing his desires in a market economy, but it does not affect the productivity of his labor or the status that is derived from it.[[28]](#footnote-28)

In reality, someone’s pre-tax income is generally not observable to other people. One enjoys (or suffers) feelings of respect (or disrespect) on account of one’s income, mostly in private. The outward markers of one’s income, which are necessary for social status signaling, are the ways that one spends one’s income. Conspicuous consumption, large public donations to charity, and generous gifts to family members are ways of communicating to others just how successful one has been in the market economy.[[29]](#footnote-29) For this reason, redistributive tax and transfer policy may still be effective in undermining the status hierarchy created by pre-tax incomes by limiting the availability of consumption signaling.

In principle then, reallocating the consumption value of income means changing the distribution of after-tax income, which can be accomplished through taxes and transfers as well as through rearranging the economy to change market returns. But reconfiguring the status hierarchy created by inequitable pre-tax incomes can only be accomplished through structural change to the economy that affect the “pre-distribution” of income—labor, trade, and antitrust policy, for example.

Summing up, we can observe that money income is a form of power that helps an individual realize a wide range of ends and purposes, including personal consumption of goods and services, supporting political candidates and causes, and transferring money to family and friends to allow them to realize their goals. The limits of this power are set by the pervasiveness of markets and the number of things that are for sale, because ultimately the value of money bottoms out in its use to acquire consumption.[[30]](#footnote-30) And earning a higher income in a capitalist economy confers another value. Because income roughly tracks contributions to the social product, and because social status and respect are allocated in part on the basis of these contributions, income tends to confer status.

It is worth emphasizing the contingency of all of this. If a greater share of consumption were allocated by non-market mechanisms, then money income would lose power as an all-purpose means of realizing one’s goals. And if there were limits on gratuitous transfers, to political candidates or parties for example, then money would also lose some of its power. And what about income as a signal of individual productivity and hence status? Regulatory interventions in the labor and capital markets that separate individual productivity from remuneration would reduce the usefulness of income as a signal of productivity. And, of course, if social status were based predominantly on something other than contributions to the social product, such as educational attainment or membership in an identity group, then the income-status link would be weakened.

Finally, it is important emphasize that income is only one factor affecting individual welfare, and that there are well known limitations of income as a proxy for wellbeing. Sen and Nussbaum’s capabilities framework, for example, which focuses on the meaningful abilities that people have to convert resources into the goods, potentials and functionings to which they aspire, is a much richer and more complete account of what matters.

Moreover, even to the extent that we are concerned with the access to material resources and command over market consumption, income is an imperfect measure. For one thing, income is measured imperfectly, with substantial amounts of economic income—from household production, for example—mostly outside of income accounting, and the attribution of business income is another challenge.[[31]](#footnote-31) Disagreements about the proper measurement of income are at the heart of recent scholarly debates about the evolution of income inequality over time.[[32]](#footnote-32) Moreover, income is measured periodically, and it varies considerable over the lifecycle. Income inequality driven by differences among working age adults is quite different than inequality driven by differences between working age adults and retirees. Lifetime wealth is presumably a better measure of the distribution of material resources for purposes of thinking about distributive justice.[[33]](#footnote-33)

## Why Local Income Inequality Matters

Before considering the level of political and economic organization in a federalist system at which income inequality matters most, we need to survey the reasons why it matters anywhere.[[34]](#footnote-34) To be clear, a discussion of the problems of income inequality provides only a partial assessment. The effects of income inequality are not thought to be universally bad. I ignore the process that generates income inequality. If income inequality results from a fair process, then fairness or justice might require inequality in outcomes. And income inequality is almost certainly necessary to provide people with the right incentives to deploy their labor and talents in a way that is socially beneficial.

So, although I will focus on the problems of income inequality, I want to emphasize that this is only a partial accounting. My focus is on the presence of income inequality among people competing over scarce resources, not the presence of income inequality among people engaged on the “supply side,” where the emergence of very high-end income inequality could be beneficial for everyone. To see the difference, consider how one’s relationship with Google co-founder Sergey Brin depends on the context. The enormous economic value created by Brin and Larry Page, and which is reflected in their enormous wealth, is shared by anyone who uses the Google search engine. In these cases, a rising tide lifts all boats, even if some rise more than others. But it is of course another thing to be bidding against Sergey Brin in an auction, or to be making campaign contributions in the same election, or to be buying real estate in the same local market. In these contexts, where a scarce good is being allocated on the basis of income and there is more of a zero-sum nature to the allocation, there is no rising tide. Since someone’s willingness to pay for goods or services is typically greater when their income is greater, then income inequality tends to result in inequalities in consumption allocated by the market.

Concerns about inequality, per se, can be difficult to disentangle from concerns about low absolute standards of living and poverty. To help focus on inequality itself, it will be useful to keep in mind the following thought experiment: consider a given distribution of wealth and imagine further increasing the wealth of the wealthiest members of society. To focus solely on the distributional consequences, assume that the procedure that leads to the increase in their wealth is just. What complaint could anyone have about this new state of affairs? Isn’t a world where some people are richer but no one is made poorer an unambiguous better world?

The issue is that the ability to convert cash income into the goods, services, privileges, and opportunities that affect individual well-being can depend not only on an individual’s own income, but also on the incomes of other people seeking to purchase the same goods or privileges. Most people are not participants in most markets most of the time. Jeff Bezos could, of course, purchase property in Madison County, Mississippi, but he probably has not. But if he and other very high-income individuals did enter the Madison real estate market, their purchases would likely exert a “pecuniary externality” on other would-be purchasers of property in Madison.

An externality in the law and economics literature refers to the negative (or positive) effect of one’s actions on the well-being of other people. A pecuniary externality refers to the effect of one’s personal consumption decisions on the price of some good. When demand for a good increases and the good is in limited supply, then the price of the good increases and the people who consume that good are worse off than they were before the price increase.[[35]](#footnote-35) This is the intuitive harm behind concerns about the effects of foreign real estate investment on local property prices and affordable housing,[[36]](#footnote-36) the effect of increased demand for quinoa on traditional consumers of the cereal,[[37]](#footnote-37) and so on. An increase in high-end income inequality can affect prices in any context where the good for sale is in relatively fixed supply; housing and political influence are leading examples.[[38]](#footnote-38)

One of the primary concerns about income inequality is its effect on politics. The concern is that people with higher incomes have greater access to, and influence over, government officials and, ultimately, the content of our laws.[[39]](#footnote-39) In the political arena, income inequality translates into inequalities in democratic participation, and ultimately inequalities in the representation of individual interests and values in our politics.[[40]](#footnote-40) There is evidence that increasing local income inequality can lead to greater political participation by the more affluent.[[41]](#footnote-41) If it’s not too cynical to do so, we might imagine that there is a market for influence in each political jurisdiction, with a fixed quantity of influence allocated according to donors’ financial contributions. Where this is true, an increase in high-end income inequality skews the limited supply of political influence in the direction of the wealthiest.

The housing market has been the other focus of economics research on the effect of inequality. Researchers have paid particular attention to how higher incomes at the top end of the income distribution affect housing prices for everyone else.[[42]](#footnote-42) Economic theory predicts that the results are straightforward in partial equilibrium, where higher incomes at the top end make the poor worse off (through higher housing expenditures or lower consumption), but the results in general equilibrium are more nuanced.[[43]](#footnote-43)

Housing supply is more or less fixed in the short-term. Increasing the availability of housing often requires contentious re-zoning as well as costly investments in new housing stock that take time to build. For this reason, the elasticity of housing supply is relatively small, although there is considerable variation across the country in housing supply elasticities.[[44]](#footnote-44) Empirically, there is evidence in the United States of a crowding effect of higher incomes on housing consumption by lower income households in tight housing markets, but not in markets where housing supply can adjust.[[45]](#footnote-45) There is also evidence from China that greater income inequality is associated with higher home prices.[[46]](#footnote-46) A few multi-country studies find that higher income inequality is associated with higher home prices and housing affordability issues for the poor.[[47]](#footnote-47)

But it is not only housing where income inequality can have adverse effects on the consumption of low-income households.[[48]](#footnote-48) The consumption patterns of higher-income households can also shape the local retail environment in ways that make lower-income households worse off. Consumption preferences vary with income,[[49]](#footnote-49) and stores favor wealthier consumer more in wealthy locations than in poorer locations, both in terms of their offerings and in the relative price they charge for good desired by high-income consumers.[[50]](#footnote-50) Professor Handbury finds that markets can be simultaneously relatively cheap for the rich and relatively expensive for the poor:

For example, a low-income household earning $25,000 a year faces 9 percent higher grocery costs in Bridgeport, CT, with per capita income $50,000, relative to Flint, MI, with per capita income below $25,000. But the same is not true for high-income households earning $200,000 a year whose grocery costs are 19 percent lower in Bridgeport than in Flint.[[51]](#footnote-51)

Because of the significant differences in regional cost of living by income group, Handbury argues that “ignoring intra-national price variation biases measures of real income inequality.”[[52]](#footnote-52) Consistent with Handbury’s evidence on differences in local cost of living by income group, Professors Diamond and Moretti find that lower-income households can enjoy much higher consumption levels in areas with lower mean incomes than in areas with higher mean incomes.[[53]](#footnote-53) By contrast, the consumption of higher-income households is not much affected by living in a more affluent area. They report that low-income households in the most affordable areas enjoy 95% more market consumption than low-income households in the most expensive areas.[[54]](#footnote-54) Much of the difference is attributable to the greater cost of housing in affluent areas, and the fact that housing makes up a greater share of the budget of low-income households than high-income households.[[55]](#footnote-55) As a result, consumption inequality increases with the local cost of living.[[56]](#footnote-56)

Diamond and Moretti find that differences in wages across regions compensate college-educated individuals—but not those with less education—for the local cost of living, which explain why less-educated households high cost areas have reduced consumption and greater financial distress.[[57]](#footnote-57) Since the presence of higher-income households alongside lower-income households drives up the cost of living in a way that is not fully compensated in wage-setting, Diamond and Moretti find that without geographical sorting the national mean difference in consumption between college graduates and those without a college degree would be 19% smaller.[[58]](#footnote-58) In other work, Professors Bertrand and Morse find that increases in high-end incomes in a state are correlated with increases in the consumer price index.[[59]](#footnote-59) And the consumption of high-income households may even influence the consumption preferences of lower-income households. There is evidence that increased exposure to high income households leads to increased consumption by the non-rich of more conspicuous consumption goods.[[60]](#footnote-60)

The economic logic of this contemporary work on negative consumption spillovers is reminiscent of the immiserizing growth literature, which analyzed the (mostly theoretical) possibility that export-led economic growth could leave a country worse off through a deterioration in the terms of trade.[[61]](#footnote-61) Standard models of economic growth predict that the growth improves the wellbeing of everyone in the economy. However, recent work by Daniel Murphy shows that the conditions under which economic growth—and higher incomes—for one segment of the population adversely affect the wellbeing of other groups are not so far-fetched.[[62]](#footnote-62) What is required is skill-biased technological change and some difference in the bundle of goods consumed by the rich and the bundle consumed by the poor. This can lead to a re-allocation of resources—land, labor and so on—from the sector that serve the poor to the sector that serves the rich, driving up prices and reducing availability of the goods consumed by the poor. Murphy then reports evidence that technological growth in the 20th century has indeed been biased toward the production of goods—computers and information technology—that are used disproportionately in the delivery of financial services, professional services and education, which are consumed by higher income households.

In a study of Remote Worker Relocation Programs, which provided cash incentives to attract remote workers, Hoyoung Yoo finds similar dynamics at work. He finds that the program had positive overall effects in the target cities through wages that compensated for increased rents and local goods prices, but that nonemployed and low-skilled renters in the tradable sector were adversely affected.[[63]](#footnote-63) There was an increase in local service sector employment and a decline in tradable sector employment as people moved sectors.[[64]](#footnote-64)

I have focused so far on the distributional effects of income inequality in politics and contexts where the consumption by the rich affects the consumption of the poor. But the literature documenting social and individual ills associated with income inequality is vast. For example, there are studies showing that income inequality is correlated with crime,[[65]](#footnote-65) poor health,[[66]](#footnote-66) social mistrust and anxiety about social status,[[67]](#footnote-67) and political polarization.[[68]](#footnote-68) The creation of a social hierarchy based on income can be costly, as people who are lower in the pecking order bear a badge of inferiority.[[69]](#footnote-69) Income can be an example of a so-called “positional good,” the benefit of which derives from one’s relative consumption as compared with a reference group.[[70]](#footnote-70) Some scholars argue that income inequality also reduces community solidarity, trust, and social cohesion.[[71]](#footnote-71) Michael Sandel argues that the perception that income inequality tracks merit helps reinforce a status hierarchy, which in turn justifies that income inequality.[[72]](#footnote-72)

Many of the ills associated with income inequality arise at the local level.[[73]](#footnote-73) Professor Ed Glaeser finds that unequal cities tend to have higher crime rates, higher rates of people reporting that they are unhappy, and lower growth rates of income and population.[[74]](#footnote-74) High local inequality is associated with lower intergenerational mobility,[[75]](#footnote-75) and outcomes for poor children are better in more equal neighborhoods.[[76]](#footnote-76) People tend to make local comparisons in income, envying their neighbors rather than people geographically further away.[[77]](#footnote-77) Social distance created by income inequality limits the formation of social ties in a neighborhood,[[78]](#footnote-78) ties which have benefits in terms of neighborhood satisfaction, working together to reduce crime, and cooperating politically.[[79]](#footnote-79) And yet, “almost all of the economic research on inequality has focused on countries rather than cities.”[[80]](#footnote-80)

Although I have focused on the adverse effects of local income inequality, there may also be benefits.[[81]](#footnote-81) Perhaps there are unmeasured positive spillovers resulting from charitable giving or trickle-down benefits from the spending of higher income individuals on lower-income residents. Local income diversity may increase support for redistribution by high-income individuals,[[82]](#footnote-82) improve local school quality.[[83]](#footnote-83) The purported benefits of mixed income housing have long guided housing policy, but the benefits may be overstated,[[84]](#footnote-84) and there is evidence of countervailing effects for low-income residents from “living in conditions of racial and class stigma” and that “Overwhelmingly, research findings indicated that mixed-income developments have not fostered positive social interaction across group lines.”[[85]](#footnote-85) There is not yet strong evidence of these effects or of their being of sufficient magnitude to outweigh the negative effects of local inequality. Nevertheless, future research may cause us to re-evaluate how we tradeoff inequality at the local level with inequality across regions. For my purposes, what is most important is the recognition that local inequality has independent significance, and that our concern with local income inequality will, in general, be different than our concern with inequalities between counties or between states. National income inequality measures conflate all of these, and in arguing for the independent significance of local inequality I mean to justify the need for a new composite measure of national income inequality that reflects these differences, which I propose in Part III.

In the next section, I offer a framework for thinking about the distributive effects of income inequality that generalizes beyond the particular features of localities, to help map the ways that income inequalities in the various spheres we simultaneously inhabit—which I call “allocative fields”—such as our counties and states of residence, directly affect both access to consumption in these spheres and also spill over to create inequalities in other areas.

## Allocative Fields

In this section, I describe a framework for assessing how income inequalities translate into differences in welfare. For the most part, the focus will be on the conditions under which inequality affects consumption. With that in mind, it is natural to ask whether my concerns would be addressed by shifting attention to consumption inequality rather than income inequality. Certainly, I think that consumption inequality should be paid greater attention than it currently receives. But income inequality matters beyond consumption inequality. One reason is that expenditures on family gifts, political donations, and non-profit contributions are not always included in accounting for consumption,[[86]](#footnote-86) despite conferring benefits on the donor. The second is that income that is saved can also confer power and influence on the earner, as when candidates for office jockey for donations. Focusing on the channels through which income inequality translates into differences in wellbeing, influence, and opportunity, rather than simply the measured consumption part of the outcome, can help identify ways of mitigating some of the worst effects of these differences.

The organizing framework I have in mind for thinking about the effects and tradeoffs of inequality in a federal system is one defined by the various contexts of our lives in which we interact with other people, and within which some good is allocated according to the members’ shares of some currency for allocation. In some cases, the context is a market. But taxing jurisdictions, political entities, and many other spheres of life fall under this general description. I use the term “allocative field” to cover all of them. An allocative field is defined by (1) a good, such as housing, healthcare, or political influence; (2) a currency according to which that good is allocated, such as money, educational attainment, or political connections; and (3) a collection of individuals or entities with endowments of the currency. A federal system is a particular arrangement of allocative fields, comprised of national, state and local governments within which political influence is allocated to their members.[[87]](#footnote-87)

Each of us simultaneously belongs to multiple allocative fields. Let’s focus first on fields that are political units. As I write this article, I am a resident of Charlottesville, Virginia, and the United States. I am subject to the laws made by each of these levels of government, and so I have a considerable interest in the laws and policies that they enact. I might, for example, favor lower federal and state income tax rates on the ordinary income earned by law professors, and I might prefer more restrictive local zoning rules that increase my home’s value. In my framework, influence over state and local income tax rates is the “good” allocated by the governments at those levels, and influence over zoning regulation is the “good” allocated by the city of Charlottesville.

I can vote for candidates for office in each of these governments. My vote counts the same as each other Charlottesville resident in Charlottesville elections, as each other Virginian in state elections, and as each other American in federal elections (apart from some of the peculiarities of the American system, such as the electoral college and U.S. Senate). If policy influence were allocated solely by vote, then there would no inequality among jurisdictional residents with respect to political influence.[[88]](#footnote-88) But—and if it’s not too cynical to say—policy influence is also allocated based on residents’ incomes, warped by actual—and perhaps even just potential—political contributions.

Because political influence is in limited supply—my elected representative can only return so many phone calls and take so many meetings—then increase in demand for political influence by other members of my political community will necessarily increase the price of political influence and make it more costly for me to get my representative’s attention. Where would that increase in demand for political influence come from? One possibility is that some particularly important issue has come into public view as a possible target of new regulation. For example, Charlottesville is currently considering a rezoning plan that would increase the building envelope throughout the city.[[89]](#footnote-89) I expect that there has been increased spending on local politics, particularly among those who think they would be most affected by the rezoning plan.

The other cause of an increase in demand for political influence is an increase in residents’ incomes. And for this purpose, it doesn’t matter much whether the increase in resident incomes is due to the increase in incomes of native residents or to the immigration of new, higher-income, residents. The more money that is chasing after political influence, the higher the price of that influence. Since aggregate income is greater at the state level than the local level, and greater at the federal level than the state level, the price of political influence generally increases at higher levels of political organization.

It is clear now how increasing incomes among other people in my political sphere can make me worse off, by increasing the price of political influence and allowing me to obtain less influence than I had before. And crucially, it matters whether the increase in incomes is among those at the lower or higher end of the income distribution. If the price of political influence is already greater than lower-income residents are willing to pay, then an increase in their incomes is unlikely to lead to much of an increase in demand for influence, as they spend their money on other necessities. But increasing income among residents who are already purchasing political influence will increase the price of influence.

This effect can be seen most starkly if we consider a case where influence is in completely fixed supply and is, essentially, auctioned off to the highest bidder. Consider an official who is willing to take only three meetings per evening with individual constituents. If access is determined based on residents’ incomes, and residents differ only in their incomes and not in their interest in local politics, then the official will take meetings with the three highest-income residents. And if the income of the richest resident were high enough, and political contributions could accommodate it, then the official might just decide to spend the entire evening with the one resident.

The limited supply of political influence is crucial to the way that increasing incomes among the richest has an adverse effect on those lower in the income distribution. Suppose that instead of selling political influence, the local government had to charge a modest fee for Zoom access to city council meetings to defer the cost of providing that online access. And suppose also that a local resident was livestreaming the city council meetings through her private channel, to which the public could subscribe for a modest fee. The government, in a form of competition with the local resident, cannot charge any more than the resident for online access to the meeting, and as long as the cost to the city of adding each Zoom participant is the same, increase in demand for city council meeting online attendance will have no effect on the price. In that case, increases in income inequality will have no effect on the price. So, we can see how within a political field, when the good being allocated is in relatively fixed supply, an increase in high end income inequality will tend to have an adverse effect on those lower down the income distribution by driving up the price of the goods they buy. Increases in high-end inequality can reduce the real incomes of lower-income households.[[90]](#footnote-90)

We can also begin to think about how increases in high-end inequality in one field might affect influence spending in other fields. Suppose that I participate in politics financially at the federal, state, and local levels, making financial donations to candidates and organizations at each level. How would I respond to an increase in high-end inequality at the national level, driven, for example, by extraordinary returns in the financial sector accruing mostly to the benefit of individuals in New York, Connecticut, and New Jersey?

The first effect, already discussed, is that the increase in high-end inequality will increase federal political spending. This influx of money will reduce the relative impact of my modest financial contributions and make it more expensive for me to purchase the same amount of political influence I had before. If the cost of meaningful financial political participation at the federal level is too great, I am likely to spend less on federal politics and more on other things. These other things may include spending on state and local politics, although this will depend on whether the policies that I can influence at the state and local substitute or complement the policies that I sought to influence at the federal level.

Suppose, for example, I am particularly concerned about the effects of globalization on the working class. At the federal level, I may have worked to oppose free trade agreements and support legislation for enhanced trade adjustment assistance. If high-income individuals generally support free trade, then an increase in high-end incomes that makes it impracticable for me to counter their political influence may cause me to redirect my spending to state politics, where I might lobby for more generous unemployment insurance or job retraining programs. Federal and state policies are rough substitutes in this case, in the sense that they both advance the interests of working-class households in my state. I can substitute political influence at the state level for political influence at the national level, however imperfectly. And, if I do, then increases in income inequality that drive up the price of political engagement at the federal level will have a spillover effect that increases the price of political engagement at lower levels of government, where policies are substitutes for federal policies.

Policies can also be complements, in the sense that one does not work well without the other. Suppose that I favor the devolution of law and policy to cities and counties, and so I am actively involved in making Virginia a “home rule state,”[[91]](#footnote-91) which would give municipal governments greater lawmaking authority than they currently do as a state with “Dillon’s Rule.”[[92]](#footnote-92) I am also actively involved in local politics, supporting candidates and helping to work on local legal reform—such as the imposition of new taxes—that could only become effective if Virginia becomes a home rule state. Suppose that an economic boom in Virginia drives a new class of high-income individuals interested in state politics, and that they prefer state control to the kind of devolution I favor.[[93]](#footnote-93) If the spending from the rise of this new class of high-income individuals drives me out of state politics, then it will also tend to discourage me from being involved in local politics, since my interest in local political influence was contingent on having influence over a state political issue.

We can sum up the main lessons of this exercise. An increase in high-end income inequality among members of a political field will tend to reduce the ability of lower-income individuals to access whatever good is being allocated in that field, and the effect will be greater when whatever is allocated within that field is in relatively fixed supply. The effect of high-end inequality in one political field will also spill over to other political fields, either increasing or decreasing individuals’ devotion of time and financial resources to those other fields, depending on whether the policies that are allocated there are substitutes or complements, and with larger effects when the goods in the new fields are in fixed supply.

Although the example I have used thus far focuses on political spending, it applies to markets for commodities as well. A market is an example of an allocative field that distributes a good or service according to the financial willingness-to-pay (the currency) of the market participants. In the case of our federal system, the structure of allocative fields is a set of three nested circles: Charlottesville within Virginia within the United States. We might add to our structure an allocative field comprised of owners of Charlottesville real estate, which includes non-resident investors. The relatively fixed supply of real estate in Charlottesville means that increases in high-end inequality among Charlottesville real estate buyers will tend to drive up home prices, which will have an adverse effect on me if I am a renter (although it may benefit me if I am a homeowner).

We can say that is a member of an allocative field when they actually exchange the currency of that field for a share (however small) of the good being allocated. Thus, anyone who votes in Charlotteville elections is in the field that allocates formal power to elect representatives in Charlottesville. But anyone who donates money to political candidates in Virginia is in the field that allocates the power to influence electoral outcomes in Virginia. Lurking in the shadows are those people who could become members of the field if circumstances changed—say, by their moving to Charlottesville, or if the price of making political contributions in Virginia fell—as well as the people at the margins who would exit the field if the cost of participation gets too high.

The determination of who is inside or outside a field is partly a result of individual preferences and the equilibrating process between prices and individuals’ search for the bundle of goods that best satisfies their preferences, but it is also a question of institutional design. Immigration rules influence who can becomes resident of the United States and on what terms. Residency rules determine the jurisdiction in which you can vote. Federal limits on political contributions from foreign nationals limit who can influence the outcomes of political elections, and federal campaign contribution limits are intended to level the playing field with respect to the income inequality of donors. Limits on foreign investment in U.S. real estate, and property taxes that discriminate against foreign owners, limit the participation of high-income individuals in local real estate markets.[[94]](#footnote-94)

The allocative field framework helps focus our attention on the contextual features that translate income inequality into inequalities in the distribution of the goods with intrinsic value. Consider that the amount of income inequality we have at a national level must be due to a combination of inequality within individual fields and inequality across fields.[[95]](#footnote-95) Is it better to have more within-county inequality and less inter-county inequality, or vice versa? Imagine two stylized extremes: a world where each county is perfectly representative of the national income distribution (“RepWorld”), and a world perfectly segregated between rich counties and poor counties (“SegWorld”).[[96]](#footnote-96) What are the consequences of the inequality in each case?

There is more reason to care about between-group inequality if counties compete in an allocative field—say, the state or federal legislatures—over scarce resources, such that there are interests shared by members of a county that are rivalrous to members of another county. If the greater income of the rich counties in SegWorld gave them disproportionate influence in legislatures, they may be able to help pass legislation that favors wealthier counties. For example, if wealthier counties were clustered in more urban locations, then the interest of urban residents might be privileged over the interests of more rural areas.

On the other hand, the greater amount of proximate individual inequality of RepWorld has its own set of issues within the allocative field of each county. Many of the ills of income inequality documented in Section B arise at the local level, within counties rather than between them. The increased local consumption expenditures of high-income residents may result in increased housing costs, shape a retail environment too costly for lower-income residents, influence commuting patterns and the availability of public transportation, and so on.

In the next section, I discuss several measures of income inequality, and what values they do and do not capture. For much of the empirical analysis in Part II, I use the Theil index of income inequality (explained below) primarily because it allows for the easy composition of national inequality into the part that is attributable to inequality across counties and the part that is attributable to inequality within counties.

## Measuring Income Inequality

The central concept reflected in most measures of income inequality is how closely the share of a group’s income tracks the share of the group’s population. As the income distribution deviates from one in which each group has the same equal share of the overall group’s income, society becomes more unequal. But there are a variety of plausible ways of ranking income distributions by how equal they are and each of them differ—sometimes subtly—in how different points in the income distribution affect these indices. If inequality is going to be normatively relevant to law and policy, then our measures must be responsive to the values that are at stake. In this section, I describe how certain common measures of inequality respond to changes in the income distribution.

One way to describe income inequality among a group of people would be to simply measure the distance between the highest and lowest incomes in the group. The *range* of incomes in the group tells us something, but it also neglects much.[[97]](#footnote-97) Surely inequality should reflect something other than the incomes of two people. Most measures that are taken as plausible take account of each individual in the income distribution, and in particular they satisfy the “principle of transfers,” or what is sometime called the Pigou-Dalton condition. This principle requires that a transfer from someone who is richer to someone who is poorer (and which does not flip their order in the income distribution) reduce measured inequality and is generally regarded as an essential to a plausible inequality metric.[[98]](#footnote-98)

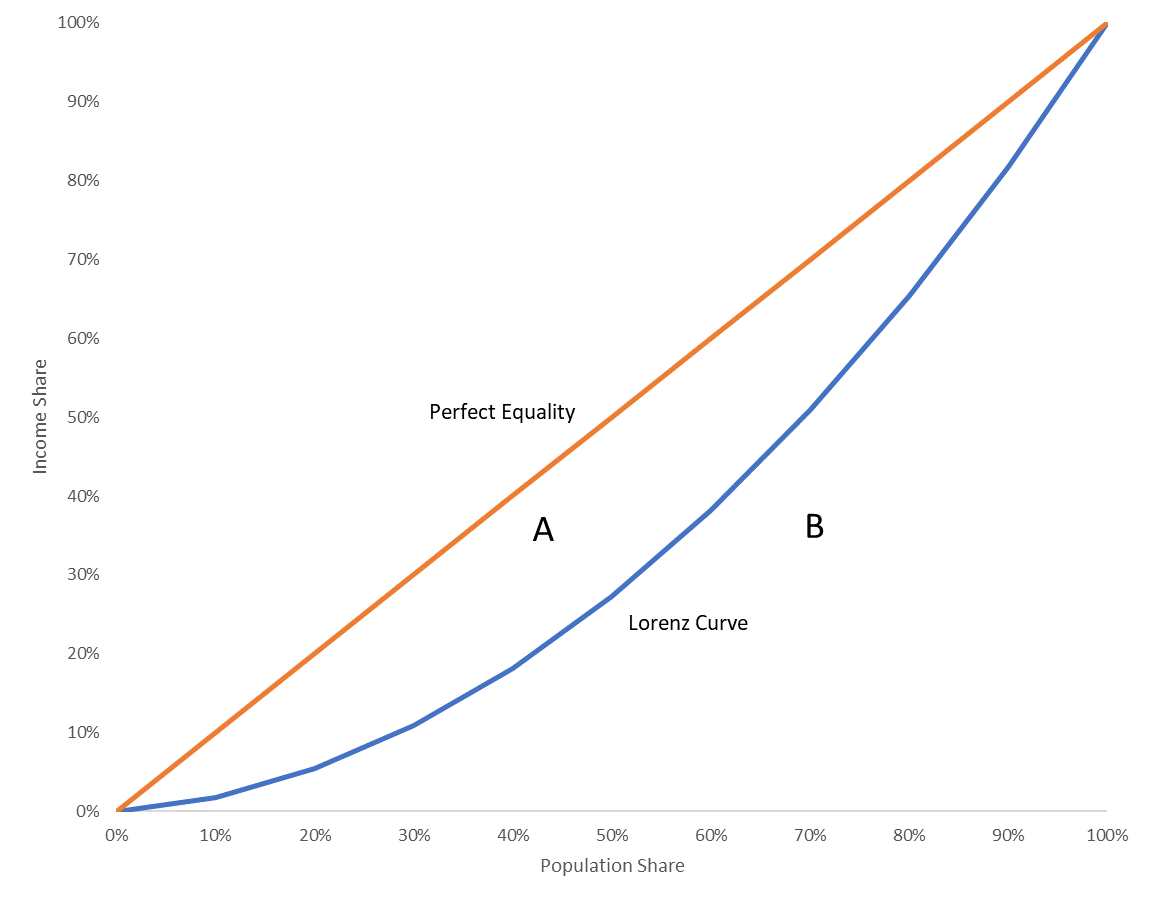
One such metric is the variance of the income distribution. The variance is calculated by taking the squared difference between each income and the mean for the entire group and averaging.[[99]](#footnote-99) Because differences from the mean are squared, difference in incomes further away from the mean have a larger effect than changes closer to the mean. As a consequence, redistributing income from a richer person to a poorer person lowers the variance wherever they are in the income distribution, thereby satisfying the Pigou-Dalton condition.[[100]](#footnote-100) The variance is mostly out of fashion as a measure of inequality, in part because it is not a relative measure of inequality; a proportional increase in the income distribution will result in an increase in the variance.[[101]](#footnote-101) By contrast, most measures frequently used today are independent of the mean and measure only relative inequality.

Consider the following three-person income distribution: $10,000; $50,000; and $500,000. Now imagine a tax policy that increases everyone’s after-tax income by 20%. The new income distribution is $12,000; $60,000; $600,000. The policy gave everyone the same percentage benefit but gave some more than others in absolute terms. The difference in the incomes of the richest and poorest people in the distribution has grown by $98,000. This will be reflected in the range and the variance, but not in relative measures of inequality. Disagreement about whether relative or absolute differences are more important can drive disagreements about the redistributive effects of policies and whether the label “progressive” is appropriate or not.[[102]](#footnote-102) For example, President Biden’s proposal to discharge student debt provided a greater benefit to higher-income households in absolute dollar terms, but a smaller benefit when measured as a proportion of household income.[[103]](#footnote-103) Because both relative and absolute income inequality may be normatively relevant in different contexts, I report estimates of national policies on local inequality using both measures in Part II.

The Gini coefficient is one of the most frequently used relative measures of income inequality. One advantage of the Gini coefficient is that it can be understood intuitively using the Lorenz curve, illustrated in Figure 1. Imagine a community of 100 people ordered from the lowest to the highest incomes and, as you progress from the poorest to the richest person, keeping track of the total share of the population and the total share of the community’s income that they represent. The Lorenz curve plots how the cumulative share of the community’s income increases with the cumulative share of the community’s population. Clearly, 0% of the population has 0% of the community’s income and 100% of the population has 100% of the community’s income. This means that the Lorenz curve must intersect with both the (0,0) and the (100,100) point on the graph.

If each person in the community had exactly the same 1/100 share of the community’s income, then each 1% increase in the cumulative population would result in a 1% increase in the income share, so a perfectly equal society would be represented by a straight line from (0,0) to (100,100). But, in anything other than a perfectly equal society, the Lorenz curve will lie below the line of perfect equality, because the poorest X% of the population will have less than X% of the overall income. The Gini coefficient is the ratio .[[104]](#footnote-104)

Figure 1: Lorenz Curve



The Gini coefficient satisfies the Pigou-Dalton condition, and its responsiveness to a transfer between two people depends on the number of people between them in the income distribution.[[105]](#footnote-105) As a result, the implicit weights given to individuals’ incomes depends on how much of the population is distributed between them.

Another popular measure of inequality has its roots in information theory. Theil’s “entropy measure” has a maximal value when income is equally distributed across the population, and like the Gini coefficient, it is grounded in the relationship between individual income shares and population shares. Figure 2 shows how the national Theil index and Gini coefficient tracked each other from 2010 - 2019.

The primary advantage of the Theil index is that it can be decomposed into constituent parts, so that the inequality of a group can be attributed to inequality within subgroups and inequality across those subgroups. This makes it an especially useful metric for looking at inequality in a federal system, where there are normative reasons to care about individual inequality within individual states and localities as well as inequality across those levels of government.[[106]](#footnote-106) For these reasons, much of the inequality analysis in Part II is conducted using Theil’s index.

Each of the inequality measures we have discussed so far is mostly descriptive in nature.[[107]](#footnote-107) Connecting the properties of each to underlying values is difficult to do, and it seems backwards to start with a quantitative inequality metric and then see what social welfare function might be consistent with that metric, rather than the other way around. The most popular index of inequality derived from a social welfare function was formulated by the economist Anthony Atkinson. The index satisfies a collection of desirable properties of inequality indices, including the Pigou-Dalton condition. The index is also typically invariant to proportional increases in income; if everyone’s income were multiplied by the same factor then the value of the index would not change. The social welfare function from which the index is derived takes the incomes of each person in the society and subjects them to concave transformations. This approach lends itself to the interpretation that the social welfare function is utilitarian, although other interpretations are possible.[[108]](#footnote-108)

Perhaps one of the most useful features of the Atkinson index is that it embeds a quantity known as the “equally distributed equivalent income” (EDEI). The EDEI for a given distribution of income is the specific amount of income which, if it were given to each person in society, would yield the same amount of social welfare as the actual distribution of income. Since the social welfare of each individual’s income is a concave function of their income, then the EDEI is less than the average amount of income in the population.

One nice feature of the Atkinson index is its closely analogous relationship to the way that economists are used to thinking about the evaluation of risky prospects. Imagine an investment that yields profits of $100 with probability and $200 with probability . This prospect has an expected value of , or $150. But if the utility of $200 is less than twice the utility of $100—which would be the case, if the individual has diminishing marginal utility of income—then the expected *utility* of the gamble, which is , is something less than $150. If, for example, the expected utility from the gamble is the same as the utility from $120 received with certainty, then $120 is the *certainty equivalent* for the gamble. The $30 excess of the expected value of the gamble over its certainty equivalent is the (absolute) risk premium. Whenever there is a positive risk premium, we say that the individual is risk averse.[[109]](#footnote-109)

Risk aversion has a natural counterpart in the Atkinson index. Imagine that instead of a risky gamble over the outcomes $100 and $200, we were considering the social desirability of an allocation of income: $100 to person A and $200 to person B. We may well value the $200 in person B’s hands at less than twice the amount by which we value the $100 in A’s hands. In that case, the average income from the distribution is $150, but the social welfare from the allocation is less than $150. If the social welfare from the unequal allocation is the same as the social welfare from $120 allocated to each person, then $120 is the EDEI. In the Atkinson index, a parameter determines inequality aversion just as a similar parameter determines risk aversion for individuals’ utility functions. And just as we speak of an individual’s risk aversion in terms of how much less the certainty equivalent is than the expected value of a gamble, we can also speak about inequality aversion in terms of how much less the EDEI is than the average income in society. The Atkinson index is written as follows:

where is simply the average income in the group. For example, if the average income is $100 and the EDEI is $80, then the Atkinson index is 0.2. This has the natural interpretation that society would be willing to sacrifice 20% of its income to implement an equal distribution of income rather than the unequal one.[[110]](#footnote-110)

It is important to emphasize that inequality imposes a social welfare penalty in Atkinson’s index because of the way that individual incomes are valued: i.e., after a concave transformation. Inequality aversion emerges as a property of the social welfare function just as risk aversion emerges for an individual who enjoys diminishing marginal utility of her own consumption. Income inequality does not itself cause any harms under this approach. This may be a little difficult to reconcile with many of the harms of inequality documented in Section B, such as crime, which may be caused by income disparities themselves.[[111]](#footnote-111)

I have emphasized in Section C how the problems of income inequality are contingent on the context and what is at stake. In certain fields, high-end income inequality does not impose negative pecuniary externalities and income inequality aversion may be low, whereas in the other fields inequality aversion may be much higher. The Atkinson social welfare function can still be useful in these different fields, but the parameter may vary.[[112]](#footnote-112) Atkinson himself raises the question of whether the assumptions embedded in his approach about invariance with respect to proportional increases in income make sense in other contexts, asking:

suppose that there has been a rise in the age-at-death at the bottom decile from age 50 to age 55 and that the rise at the top decile has been from 80 to 80 + X. What value of X would indicate that there had been no change in health inequality? A proportionate measure would indicate X = 8, but invariance with respect to equal absolute changes might seem more appropriate, indicating X = 5.[[113]](#footnote-113)

Thus, adapting the Atkinson index to different fields may require not only changing the parameter of relative inequality aversion, but in some cases, it may require changing the social welfare function to reflect aversion to absolute, and not only relative, inequality. Measures such as the standard deviation or variance might sometimes capture something normatively relevant that other measures do not.

For example, there is considerable evidence that satisfaction with one’s income depends on the incomes of one’s reference group and one’s relative position.[[114]](#footnote-114) As the incomes in that reference group increase, personal satisfaction declines. But do people pay more attention to relative or absolute inequality within their reference group? Recent research finds that that people care more about absolute than about relative inequality.[[115]](#footnote-115) Moreover, they care more about their relative position in a large reference group than in a small reference group.[[116]](#footnote-116)

I next turn to a description of the evolution of national, state, and local income inequality in the United States from 2010 - 2019. I also consider the local distributional effects of several national policies and, when I do, report estimates using both the Theil index of relative income inequality and the standard deviation of income, which reflects absolute levels of inequality.

# II. Income Inequality in the U.S. Federal System

In this Part, I document the evolution of state and local income inequality over time and compare it against the backdrop of national income inequality.[[117]](#footnote-117) After describing the data used in the analysis, I begin by describing how inequality has evolved at the national, state, and county levels. The analysis shows the substantial local variation in inequality both at particular points in time and across years. I then show how national policies can have widely disparate effects on state and local inequality. Subpart C considers four recently adopted or proposed federal policies and describes their distributional impacts on local income inequality, using both the mean-independent Theil index of income inequality and the standard deviation of incomes. Since these kinds of analyses are not typically done for federal policies, the exercise is revealing for what it shows about the effect of national policies on local inequality. And because both local and national income inequality matter, this evidence justifies a theoretical frame for federal policy in which both local and national effects are included, and motivates the composite measure of income inequality I propose in Part III.

## Data Description

The income inequality analysis in this Part uses publicly available federal income tax data from the Internal Revenue Service’s Statistics of Income (SOI) division.[[118]](#footnote-118) The tax data include aggregates from individual income tax returns, including the total number of returns, adjusted gross income and taxable income, and individual items of income and deduction. Since 2010, aggregates for each geographic unit have available for each of several levels of adjusted gross income (AGI): under $1; $1 to $25,000; $25,000 to $50,000; $50,000 to $75,000; $75,000 to $100,000; $100,000 to $200,000, and over $200,000.[[119]](#footnote-119)

The income data by AGI group since 2010 make it possible to calculate inequality measures for those years, albeit with some imprecision. The imprecision arises from the fact that individual incomes are grouped within the AGI bands described above. Within each band of AGI, the data include the number of tax returns and the average income within the band, but nothing at a more granular level. This means income inequality will be underestimated to the extent that there is inequality within each band. To improve the inequality estimates, I use the interpolation method suggested by Cowell & Mehta (1982),[[120]](#footnote-120) which treats the population of tax returns filers as uniformly distributed on either side of the mean within each AGI band. A second challenge with using the tax data is that the top AGI band includes all filers with AGIs above $200,000. I interpolate incomes in the top band by assuming that these incomes have a Pareto distribution and use the conditional mean in this band to interpolate incomes within the following additional bands: $200,000 to $400,000; $400,000 to $600,000; $600,000 to $800,000; $800,000 to $1,000,000; and above $1,000,000.

There are a few other shortcomings of using the aggregated tax data to calculate local inequality indices. For one, the data excludes low-income households who do not file income tax returns. For tax year 2020, this was estimated to be about 9 million people.[[121]](#footnote-121) To help mitigate this missing data problem, I use IRS estimates of the number of non-filers by state in 2020 and allocate them to counties based on the poverty rate in each county. In that year, the threshold for non-filing was $12,400 for individuals and $24,800 in the case of married couples filing jointly, which is reasonably close to the poverty thresholds for a one-person household and a three-person household with a child, which were $13,171 and $20,832 respectively.[[122]](#footnote-122)

Although tax data have limitations for estimating income inequality, they do have some advantages. The primary alternative data source used for producing inequality estimates is census survey data. The advantage of tax data as compared to the census data is that the income tax data are administrative data that are less subject to measurement error. Income data are also available on an annual basis and at subnational political units and can therefore be used to track changes in income over shorter time intervals in a federal system.

One of the most challenging aspects of income measurement—not unique to tax data— is the treatment of capital gains. Capital gains are only income when they are “realized,” such as when property is sold. But income that is realized in one year may have accrued over a much longer period of time. As a result, including all the capital gains in the year of realization will create misleading fluctuations in income from year to year. For example, imagine buying real estate for $200,000 in year 1. Suppose that the real estate increases in value by 10% per year and then is sold for $518,748 after ten years. For income tax accounting purposes, it will appear that the owner has no income in years 1 through 9 and has $318,748 of income in year 10. This is misleading because the income accrued at a steady rate over the prior decade.

Since capital income is only taxed when it is realized and realization is within the control of the taxpayer, selective realization of capital gains and losses is ubiquitous, and capital owners can strategically realize their capital income to minimize the tax due. For example, the amount of capital income realized nearly doubled from 1985 to 1986 as taxpayers anticipated an increase in capital income rates in 1987.[[123]](#footnote-123) For this reason, including realized capital gains in income can result in fluctuations in taxable income that have little to do with changes in income inequality. Figure 4 illustrates how national measures of income inequality track the realization of capital gains over time. As capital income is realized by higher-income taxpayers it generates a surge in measured inequality.

If taxpayers’ holding periods for capital assets were observable, then a reasonable approach would be to accrue the gain over the holding period in some fashion, but that information is not readily available. At the same time, omitting capital income altogether could also lead to very misleading estimates of inequality given how important it is both in absolute terms and because of its disproportionate ownership by higher-income taxpayers.[[124]](#footnote-124) For this reason, I include the capital gains component of AGI but use smoothing techniques in certain figures to show trends in the absence of large fluctuations from capital income realizations.

Finally, a word about the unit of analysis in this Part. I report estimates of income inequality at the national, state, and county levels. One reason for this is simply that the IRS tabulates income data at these levels. But there is a principled reason too: they are political units and therefore allocative fields within which income inequality translates into political inequality. This means that income inequality in these fields is meaningful. The IRS also report tax aggregates at the zip code level, but zip code boundaries do not generally track anything economically or social meaningful—they are not an allocative field. Of course, political units in our federal system are not the only allocative fields that matter. One could re-do the analysis in this Part focusing on local housing markets, or regional economies that cross county or even state lines.

## Income Inequality

Before turning to national and subnational inequality measures in the United States, it is interesting to place the United States’ experience of inequality in its global context. Figure 5 shows the evolution of the global Gini coefficient for the period from 1820 to 2018.[[125]](#footnote-125) The data series, calculated by economist Branko Milanovic, shows the dramatic increase in global income inequality from 1820 to 1950 associated with the industrial revolution and the “Rise of the West,” followed by continued increases in inequality until 1990, a period associated with the Cold War. In the last 30 years, there has been a stunning decline in inequality attributable to the “Rise of Asia,” particularly the explosive economic growth of China and India.

Rapidly increasing incomes in China and India since 1990 have caused global inequality to fall at the same time inequality within those countries has grown. While average income in India has more than doubled between 1990 and 2022,[[126]](#footnote-126) the share of income earned by the top 10% of the population increased from 24.4% to 57.1%.[[127]](#footnote-127) In China, the share of income earned by the top 10% increased from 30.9% in 1990 to 42.5% in 2018, as average income more than quadrupled.[[128]](#footnote-128) The dramatic reduction in global inequality is mostly an effect of shrinking between-country inequality and, in fact, inequality has increased significantly within the states that have been engines for the reduction in global inequality.

### National Inequality and Its Components

We now turn to the United States. To understand the statistical factors driving national income inequality, we begin by documenting some of the differential trends at the state level. Figure 6 shows both the evolution of the national Theil index from 2010 - 2019, as well as the evolution of the indices for Florida and Wyoming, the states with the biggest increases and decreases in inequality over the same time period.

One of the advantages of using the Theil index to measure inequality is that it allows for the decomposition of income inequality measured for one group into the parts that are attributable to its subgroups. For example, it is possible to estimate the share of national inequality that is attributable to inequality within counties, and the share that is attributable to inequality between counties. Figure 7 shows this decomposition over time. The solid green line plots the evolution of the national Theil index from 2010 - 2019, and the dashed and dotted lines show the portion of national inequality in each year that is attributable to within-county and between-county inequality, respectively.

Figure 7 shows that almost all national inequality is attributable to within-county inequality, which explains 93.9% of national inequality in 2019. The remainder is due to differences across counties in mean incomes. Figure 7 also illustrates that this relationship has been fairly stable over time.[[129]](#footnote-129) The within-county share of national inequality was 94.5% in 2010.

Which specific counties are most responsible for our national income inequality? Figure 8 shows a county-by-county map, illustrating the contributions of each county to the national Theil index in 2019. The counties contributing the most to national inequality are in dark blue, and the top 20 counties in terms of their contributions to national inequality are listed in Table 1. Contributions to national inequality depend both on the amount of within-county inequality and the county’s population, so it is unsurprising that the biggest contributors are large unequal counties in California, New York, Texas, and Illinois.

### Local Inequality

We turn now to a description of county-level income inequality and how inequality at that level has evolved over the last 10 years. One way of appreciating how much income distributions vary by county is simply to look at how much income is required to be near the top of each county’s income distribution. Figure 9 is a histogram showing the share of all U.S. counties by the income needed to be in the top 20% of incomes in that county in 2020. Data are from the 2020 American Community Survey from the U.S. Census.[[130]](#footnote-130) The histogram shows an approximately normal distribution, with most counties having a cutoff of between $75,000 and $125,000. However, there are counties where the cutoff for the top 20% is below $50,000, and others where it exceeds $250,000.[[131]](#footnote-131)

Figure 10 shows the Theil indices for U.S. counties in 2019, using the IRS tax data. The vertical black line indicates the Theil index for the United States as a whole. The vast majority of U.S. counties are more equal than the United States as a whole. This suggests that national inequality is driven largely by between-county inequality and some very large and unequal counties. Figure 11 shows the geographic distribution of this inequality, with the most unequal counties in dark blue. Although there is some spatial concentration of inequality in the Southeast, Texas, California, and the Northeast, there are unequal counties across the entire map.

Table 2 lists the twenty most-equal and the twenty least-equal counties, ranked by the Theil index. Of the most unequal counties in the country, seven are in Florida and five are in Texas.

The next couple of figures illustrate the change in local inequality over time. Figure 12 shows the geographic dispersion of changes in inequality from 2010 - 2019, with the counties marked in dark blue experiencing the biggest increase in inequality and the ones with the lightest shading experiencing the biggest decline in inequality over this period. Table 3 lists by name the twenty counties with the biggest decrease and the twenty counties with the biggest increase in inequality over the decade. Here we see that Blaine County, Idaho, is not only the fourth the most unequal county in the country but has also undergone one of the biggest increases in income inequality over the prior 10 years. This increase has not gone unnoticed, with local news reports commenting on the influx of high-income immigrants to the county from the West Coast and South America.[[132]](#footnote-132)

The charts in Figure 13 illustrate how much county inequality can vary within a state. Each chart illustrates, for one state, the evolution of inequality measured at the state level as well as the evolution of inequality for the county with the biggest increase in inequality and the county with biggest decrease (or smallest increase) in inequality in that state from 2010 - 2019. Table 4 lists the states with the biggest changes in inequality– during that period.

## Local Effects of Federal Policies

In this section, I revisit certain federal policies proposed or adopted in the last five years to estimate their effects on local income inequality. In each case, policy analysts evaluated the distributional effects of the policies at a national level but provided no similar analyses for state or local income distributions. My analysis illustrates the widely disparate effects that national policies can have on inequality at different levels of political organization and shows that policies that reduce national income inequality can increase local inequality. Depending on the weight that one assigns to inequality at these different levels, an assessment of the distributional effects of the policy could be dramatically changed as compared with what one might conclude from a myopic focus on the national level.

The analysis helps illustrate the complexity of addressing income inequality where it matters. The fiscal federalism literature typically concludes that the central government should be responsible for income redistribution. My theoretical account of why local inequality matters does not imply that redistribution should also be local, although it does justify reconsidering the conventional wisdom on that point. It may be possible to account for the effects of national policies on state and local inequality through more granular distributional analysis and fine-grained policies. A one-size fits all redistributive policy is likely to be inadequate if one takes seriously the normative significance of local inequality. And there may be other avenues for improving on a nationally uniform approach. I consider some of those possibilities in Part III.

### Bernie Sanders’s Tax Plan

Senator Bernie Sanders of Vermont ran for the Democratic nomination in the 2020 presidential primary election. A prominent political progressive, his campaign proposals for tax reform included increasing corporate taxes, raising income and payroll taxes for high-income taxpayers, and adding a wealth tax on very high-income individuals. The Tax Policy Center (a joint center of the Urban Institute and the Brookings Institution) estimated the revenue and distributional effects of the tax increases.[[133]](#footnote-133) The provisions were estimated to generate $580 billion in 2021 alone and $9.9 trillion from 2021 to 2030.[[134]](#footnote-134)

Across the national income distribution, Senator Sanders’s proposal would impose taxes that increased both proportionally and in absolute terms as a share of the taxpayer’s income. Because the taxes would increase more than proportionately with income across the whole income distribution, relative inequality measures—which includes most inequality indices, such as the Gini coefficient and the Theil index—would fall as a result.

Figure 14 is a histogram showing the effect of the Sanders tax plan on county inequality indices. The vertical black dashed line shows the effect on the national inequality index. The chart shows that not only would the Sanders tax plan reduce inequality at the national level, but that it would also reduce inequality in each county: the effect of the tax plan on county-level inequality is always negative.

The fact that the Sanders plan raised taxes more than proportionally with income means that it was guaranteed to have a negative effect on income inequality everywhere, albeit to differing degrees.

Figure 15 shows that the plan would reduce the standard deviation of income in each county, as well as the standard deviation of the national income distribution.

Sanders’ plan would have cut national income inequality—measured using the Theil index—by 10%. This effect can be decomposed into the effect on within- and between- county inequality. Both would have fallen, but the Sanders plan would have had an even larger effect (in absolute terms) on within-county inequality.

### Tax Cuts and Jobs Act

The second set of tax reforms I consider are those made by the so-called Tax Cuts and Jobs Act of 2017 (TCJA). Whereas the Sanders’s campaign tax proposals would have increased taxes across the board both in absolute terms and proportionally with income, the TCJA reforms cut taxes across the income distribution. Again, I used distributional estimates generated by the Tax Policy Center to calculate the effects on local income inequality.[[135]](#footnote-135)

Figure 16 shows the effects of TCJA on county Theil indices, and again the effect on the national index is indicated with the vertical black dashed line. Not only does the simulation show that the effect of TCJA would be to increase national inequality, but it would increase inequality in nearly every county. There are a couple of stray counties to the left of 0, where TCJA would have reduced inequality measured with the Theil index, but virtually the entire mass is in the positive region. My simulation shows that TCJA would also increase national and county income inequality measured by using the standard deviation of income. Figure 17 shows the distribution of these effects. Overall, I estimate that TCJA increased national income inequality by roughly 1%, with a larger absolute effect on within-county inequality than between-county inequality.

### Student Loan Debt Forgiveness

The Sanders tax plan and the TCJA are pretty thoroughgoing progressive and regressive tax reforms. The direction of their effects on inequality are the same on both the national and local levels, using both relative indices such as the Theil index and the standard deviation. It is nevertheless striking that the policies had such variable effects on local inequality across different counties.

An interesting policy for comparison is one form that student loan debt forgiveness might have taken under President Biden. In this simulation, I use estimates generated using the Penn Wharton Budget Model of the national distributional effects of $50,000 in student debt relief, not subject to any caps or phaseouts by borrower income.[[136]](#footnote-136) Ultimately, the Biden administration proceeded with a debt forgiveness plan that is more nuanced, but I use this hypothetical alternative for illustrative purposes.[[137]](#footnote-137)

Early student loan debt forgiveness proposals were controversial in part because of disagreement about their distributional effects. This disagreement took different forms, but one interesting and relevant point of disagreement relates to the measurement of inequality. Measured as a percentage of income, student loan debt forgiveness under these proposals would have been progressive—decreasing as a share of income—but it would have conferred greater benefits in absolute terms on higher income taxpayers who had more debt.[[138]](#footnote-138)

This difference can be seen in a comparison of Figure 18 and Figure 19. Figure 18 shows that the policy would have reduced inequality measured using the Theil index both nationally and in each county. But Figure 19 shows that the policy would increase inequality both nationally and in almost every county as measured using the standard deviation of income. I also estimate that student debt forgiveness would reduce national income inequality, with a larger effect on within-county inequality than between-county inequality.

### Student Loan Interest Pause

The final illustrative example considers the pause on student loan repayments implemented by the Biden administration in March 2020.[[139]](#footnote-139) The case is an interesting one, because it illustrates a national policy that reduces inequality at the national level, yet it reduces income inequality for some counties and actually increases it for others.

Figure 20 shows the effects of the loan repayment pause on national and local income inequality measured using Theil indices. The national effect is a reduction in income inequality, with a larger effect on within-county inequality than between-county inequality (in absolute terms). But there is a substantial mass of counties to the right of 0 in the histogram, showing that there are many counties where the policy would increase local income inequality. Cases like this force us to confront the question of which level of income inequality matters more, and what if anything should be done to address the difference between the national and local effects.

The effects of the loan repayment pause on income inequality measured using the standard deviation are almost uniformly positive. Figure 21 shows that the policy would increase the standard deviation of income in virtually all counties in the U.S.

# III. Addressing Local Income Inequality

The first two parts of this paper have been theoretical and descriptive. I have argued that the normative importance of income inequality is in large part due to the way that it is translated into the unequal allocation of goods—consumption, social status, influence, security, and power—across a range of allocative fields. Income inequality matters little in fields and much more in others. I have argued that subnational political units such as states and counties are fields where income inequality is particularly important, and I have shown that national redistributive policies can have widely variable effects on localities, sometimes even exacerbating local income inequality.

In this Part, I turn to the normative question: If local income inequality is important but national policies can be a poor fit, what can be done? What can the allocative fields framework, and the empirical evidence provided in Part II, do to guide policies that address income inequality where it matters?

## Local Redistribution

This Article is a contribution to the literature on fiscal federalism, which explores the assignment of revenue collecting and spending responsibilities to different levels of government in a federal system. Much of the work in this area appears in the economics literature and is concerned primarily with the economic efficiency of different arrangements of political and economic authority between levels of government.[[140]](#footnote-140) Two questions in particular have been the focus of work in this area: which level of government—national or local—should finance and provide public goods, and which level of government should perform the redistributive function of fiscal policy? The theoretical analysis of these two questions grapples with two features of a federal system: differences among people in their desire for different public goods and mobility across jurisdictions.

When it comes to public good provision, the conventional wisdom is that public goods are best provided by local governments. The reason for this is simple and arises from individual heterogeneity in tastes for public goods. People with children generally want good schools. People without children don’t care nearly as much. People who enjoy the outdoors want well-maintained public parks. People who prefer the cinema care less. And so on. Given the differences in the amount and kind of public goods that people want to enjoy, it is better to allow local governments to choose the public goods on offer so they can cater to their local clientele.[[141]](#footnote-141) In equilibrium, there will be some jurisdictions that collect more in taxes and provide better schools or better parks, and other jurisdictions that collect less in taxes and provide fewer public goods. People will sort themselves among the different local jurisdictions according to their tastes for public goods.

The result of this sorting process is homogeneity within local jurisdictions, whereby people who value good schools will live in the jurisdictions that provide them and people who care less about public goods will cluster in jurisdictions that provide lower taxes and fewer public goods.[[142]](#footnote-142) The alternative, setting the level and mix of public goods at the national level, means choosing a bundle of goods that will not be ideal for nearly anyone. Local tailoring of public good provision is much more efficient.[[143]](#footnote-143)

Wallace Oates summarizes this insight with what he refers to as the “decentralization theorem”:

under certain prescribed (sufficient) conditions, a varied pattern of local outputs in accordance with local tastes will be Pareto superior to an outcome characterized by a centrally determined, uniform level of output across all jurisdictions. The proposition itself is trivially obvious, but what goes into it is less so. In particular, the theorem presumes that the alternative to local provision is a centrally determined, uniform level of public outputs.[[144]](#footnote-144)

The last sentence is provocative. To the extent that the central government is itself able to provide different public goods in different regions, then the case for the superiority of local public good provision is weakened.[[145]](#footnote-145)

Whereas geographic mobility facilitates efficient sorting of individuals’ across jurisdictions according to their taste for public goods, and thereby makes it attractive to allocate public good provision to subnational governments, it tends to have the opposite effect on the optimal assignment of the redistributive function.[[146]](#footnote-146) One of the most robust results from the early literature on the fiscal federalism is that income redistribution should be done by the central, or national, government.[[147]](#footnote-147)

The logic for why redistribution is best carried out by a national—rather than subnational—government is easy to understand and depends on mobility.[[148]](#footnote-148) Redistributive taxation means taking from high-income individuals and giving to low-income individuals. When a national government weighs the benefits of redistribution against the costs, the costs include the various ways that high-income individuals will engage in unproductive tax avoidance activities rather than pay the tax. When a subnational government weighs the benefits of local redistribution against the costs, it has two more costs to worry about than the national government does: the cost of high-income taxpayers leaving the jurisdiction and low-income taxpayers entering the jurisdiction.

Once these migration dynamics are taken into account, the cost of any redistributive policy becomes greater than it otherwise would be because there will be fewer high-income households to pay into the redistributive program and more low-income households receiving benefits.[[149]](#footnote-149) Because these costs are higher, local governments will engage in less redistribution than they otherwise would.[[150]](#footnote-150)

The prescription to reserve redistribution only to the national government is a strong one. Since this conclusion is premised on the migratory responses of taxpayers in response to local redistribution, there is a large empirical literature studying the magnitude of these migratory effects that I do not attempt to summarize here. Very recent work finds that the adoption of state incomes taxes, particularly in the post-war period, did lead to significant out-migration, particularly among middle- and high-income households,[[151]](#footnote-151) and that more recent attempts to tax high income households in California also had an economically meaningful effect on out-migration.[[152]](#footnote-152) On the other hand, some scholars read the empirical literature and conclude that the effects on out-migration of redistributive taxes are modest, and that the much mor important margin of tax avoidance is income shifting.[[153]](#footnote-153) Another margin of adjustment that is becoming increasingly important with the rise of remote work is the withdrawal of labor from the taxing jurisdiction by non-resident workers.[[154]](#footnote-154)

An important contribution at the overlap of the fiscal federalism work on public goods and redistribution is by Mark Pauly, who argued that local redistribution is itself a sort of public good.[[155]](#footnote-155) Pauly argued that when the motivation for redistribution flows from the fact that the rich care about the well-being of others, and that their concern for others is spatially-based so that they care more about the poor in close proximity to them, then there is a case for local redistribution.[[156]](#footnote-156) Following the logic for the decentralization of public good provision, he argues that national redistribution only creates inefficiencies by preventing local tailoring of redistributive policy.[[157]](#footnote-157) When “true” public goods are added to the taste for local redistribution, then there are forces pushing in opposite directions, with the taste for redistribution pushing towards more mixed communities and the taste for public goods pushing towards more homogeneous communities, where the true public goods can be efficiently provided.[[158]](#footnote-158)

Burbidge and Myers show that *only* when subnational governments have the same taste for redistribution can it be efficient to localize redistribution. The reason again is migration, because differences in local tastes for redistribution create incentives for people to move for reasons unrelated to their productivity and thereby distort the distribution of the working population across the country.[[159]](#footnote-159) The mere fact of local differences in tastes that justifies localism in the true public good context does not—in their model—justify it in the redistribution context.[[160]](#footnote-160)

Professor Wildasin analyzes the spillover effects of locally redistributive policy when there is a national labor market. In that case, migration influences pre-tax wages in other jurisdictions. Strikingly, Wildasin finds that when the central government optimally subsidizes these spillover effects, the equilibrium level of redistribution in each jurisdiction is identical. What varies instead is the *subsidy rates* across jurisdictions, with higher subsidies going to jurisdictions with weaker redistributive preferences.[[161]](#footnote-161) When inter-state transfers are set optimally, they simply replicate the outcome with centralized redistribution. It appears that all roads lead to centralized redistribution.

In practice, redistribution occurs at both the national and local levels, and there are several points of contact between them. Legal scholars working on fiscal federalism have given a lot of attention to the federal income tax deduction for state and local taxes (SALT).[[162]](#footnote-162) Since the SALT is an itemized deduction that mostly only benefits higher income taxpayers, it encourages state and local governments to increase spending[[163]](#footnote-163) and impose higher taxes on higher-income households—i.e., make their income tax more progressive—than they otherwise might. This interdependence of federal, state and local tax policy choices suggests, first, that the myopic focus in distributional tables on the federal tax structure is partial and misleading.[[164]](#footnote-164) The distributional consequences of limiting or repealing the federal SALT deduction should take into account the likely effects on state taxes since it is the combined effect of these taxes that determines the material resources available to households for consumption, and the empirical evidence is clear that such effects exist.[[165]](#footnote-165)

Since the SALT deduction is available only to those who itemize their deductions, and are typically higher-income taxpayers, the deduction particularly encourages progressive subnational taxes.[[166]](#footnote-166) Howard Chernick reports that “[a] five percentage point increase in the percentage itemizing (about 16 percent) would increase net progressivity by six percentage points, or about ten percent.”[[167]](#footnote-167) And so, even to accurately measure *national* income inequality, we should take into account the interdependence of federal and state taxes.

But the subnational tax policy effects of the SALT deduction are apt vary widely depending on factors such as the distribution of incomes within each jurisdiction. Some states and localities will increase the progressivity of their tax system while others will not, and so the SALT deduction almost certainly changes the mix of within- and between- jurisdiction inequality in the country. I am not aware of any empirical research on this question, and so we can at best speculate. Since the SALT deduction only benefits itemizers, it seems plausible that jurisdictions with more itemizers—those with higher incomes—will be more like to increase the progressivity of their local tax system because of the deduction. And so, one might guess that the SALT deduction would have an ambiguous effect on within-county inequality (as localities captured some of the benefits of the federal deduction through higher local taxes), but cause a reduction in between-county inequality, as higher-income counties increase their local taxes.

[[168]](#footnote-168)

There are other points of contact between the federal and state and local tax systems as well. For example, forty-three states have income taxes,[[169]](#footnote-169) but Professor Mason has argued that because state income tax bases tend to mirror the federal income tax base, they import national policy choices and undermine the possibility of fiscal decentralization to achieve federalism values.[[170]](#footnote-170) Moreover, she argues that federal taxation regulates conduct that has historically been the province of the states, further threatening federalism values.[[171]](#footnote-171) For another example, Professor Daniel Hemel argues that the Supreme Court’s federalism jurisprudence forces the federal government to collect more in taxes (and the states to collect less in taxes) than they otherwise might, which results in a more progressive tax system overall because of the progressivity of federal income tax law.[[172]](#footnote-172)

The effect of local redistributive efforts on other jurisdictions through migration is just one example of the spillover effects that state policies can have on other states and the federal government. Managing these spillover effects efficiently is one of the key organizing principles for fiscal federalism analysis. As Professors Besley and Coates put it: “heterogeneity and spillovers are correctly at the heart of the debate about the gains from centralization.”[[173]](#footnote-173)

When a local government imposes a tax on residents, there are migration spillover effects on other states’ workforces and a positive “fiscal externality” on states through the changed composition of their tax base.[[174]](#footnote-174) These are horizontal fiscal externalities. If the local tax is imposed on the same base as a federal tax—the income tax, for example—then then there is a negative vertical fiscal externality from the imposition of the tax, as federal tax receipts fall as people act to avoid the new local tax.[[175]](#footnote-175)

Given the recurring concern with spillover effects in this literature—spillovers of public goods, fiscal externalities, and redistributive policies—from one locality to another, it unsurprising that there may be a role for a compensatory transfer scheme between states that internalizes these spillovers. Related to this function, and in light of concerns about inequality between states themselves,[[176]](#footnote-176) there may also be a role for making equalization payments between states.[[177]](#footnote-177) Brian Highsmith has observed that, given the fact of economic segregation, rising individual income inequality aggravates inter-jurisdiction inequality,[[178]](#footnote-178) and that enlarging the size of tax jurisdictions can facilitate redistribution that would otherwise be unavailable if the rich self-segregate. This line of reasoning seems to provide yet another justification for redistribution by the central government, which has the maximal tax jurisdiction.

The fiscal federalism literature typically assumes that social welfare is defined nationally. As Professors Ladd and Doolittle put it, centralization of redistribution

proceeds from the presumption that the welfare level in any particular jurisdiction ought to reflect the redistributive preferences and attitudes of residents throughout the country, not just those within the local jurisdiction. Implicit in this presumption is either the assumption that the concern of local voters for the poor extends to poor people living elsewhere in the country, or alternatively, the value judgement that, regardless of their actual views, people ought to be concerned about the poor in other states because poverty is a national problem.[[179]](#footnote-179)

In the next section, I consider some of the implications of moving towards a conception of national welfare as an aggregate of local welfare measures.

## National Redistribution

I have argued that inequality matters at the local level. A change in the income of a resident in one jurisdiction is likely to have a greater effect on social welfare in the subnational jurisdiction in which they live than in other jurisdictions, and the social welfare function should reflect this.[[180]](#footnote-180) Focusing only on the distributional effect of policies on the national income distribution can lead to misleading conclusions about whether the policy increases or reduces income inequality in the places that it matters.

For example, imagine again that the United States was comprised of two kinds of counties: high-income counties comprised of bankers, tech executives, and a handful of the very highest-earning doctors and lawyers, and middle-income counties with everyone else. Imagine that doctors and lawyers have the lowest incomes in the high-income counties and the highest incomes in the middle-income counties. A policy that transferred wealth from the bankers to the doctors and lawyers will register as a decrease in income inequality using any metric that satisfies the Pigou-Dalton condition. But to the extent that local inequality matters, then whatever reduction there is in inequality in the high-income counties needs to be weighed against the increase in income inequality in the middle-income counties. And if local inequality is all that matters, then it might be that the transfer should register as an increase in inequality overall, and therefore as a reduction in national social welfare.

If local inequality is normatively important—and I argue that it is—then the appropriate national social welfare function should be comprised, at last in part, of local social welfare functions.[[181]](#footnote-181) In this section, I provide one illustration of what it could mean to move from a national social welfare function to one that simply sums the local social welfare functions. The result in this one case is that a redistributive policy that would be desirable under a national social welfare function becomes undesirable when local inequality is all that matters.

Figure 2 below shows a hypothetical income distribution. The distribution is log-normal. The average income in this distribution is $75,741. If we assume that social welfare is defined over the entire distribution of incomes using the Atkinson index with a parameter of inequality aversion equal to 1, then the equally distributed equivalent income (EDEI) is about $70,000. The value of the national Atkinson index is 0.076. This means that if society were presented with a redistributive policy that equalized everyone’s income, *and only the national income distribution mattered*, then society would be willing to implement the policy as long as the efficiency cost of the policy sacrificed no more than 7.6% of national income.

Figure 2: Hypothetical Income Distribution

A graph of income and income

Description automatically generated

Now imagine that there are three regions, and that the national income distribution is partitioned equally between the three regions so that there is a low-income, a medium-income, and a high-income region. Suppose that the people in each region have the same redistributive preferences (represented by an Atkinson social welfare function with inequality aversion parameter of 1), but that they care only about inequality within their region.

The mean income in the low-income region is $46,191 and the EDEI is $45,246 (an Atkinson index of 0.020). In the middle-income region, the mean income is $70,280 and the EDEI is $69,944 (an Atkinson index of 0.005). In the high-income region, the mean income is $110,756 and the EDEI is $108,096 (an Atkinson index of 0.024). The nationally redistributive policy will be socially preferred to the existing distribution only in the low-income and the middle-income regions. The EDEI in the high-income region is far in excess of $70,000.

Are there transfers between regions that would make the redistributive policy preferable to the status quo in all regions? If we implement the policy and give each person $70,000, then the maximal transfer that can be made from the low-income region that will still leave them better off than before the policy change is $34,754. The middle-income region is roughly indifferent between implementing the national policy or not, so it neither needs a transfer nor is willing to make one to enact the policy. The EDEI in the high-income region means that they require a transfer of $38,096 to accept the redistributive policy. This is more than the low-income region is willing to pay. Moving from inequality to equality is socially preferred under a national social welfare function, but not if local income inequality is all that matters.

This is only an example, and there are changes to the example that would cause local policy preferences to align with national preferences. We have assumed complete economic segregation across the three regions. If each region were representative of the national income distribution, then each region would have the same EDEI of $70,000 and the redistributive policy would be socially preferred in all regions. And it becomes easier to implement a nationally redistributive policy as the amount of inequality aversion in each region increases, relative to national inequality aversion.

### A Composite Measure of Income Inequality

If we take seriously the risk of household migration, the importance of local income inequality would suggest that more of the redistributive fiscal function should be assigned to state and local governments. Lower federal taxes or more generous federal deductions for state and local taxes, for example, would increase the tax capacity of subnational governments. But migration probably does create a constraint, and so we need to return to thinking about the role of the federal government in addressing local inequality. State and local governments do not have the ability to simply adjust their redistributive policies to fully compensate for the effects of federal tax and transfer programs and implement their optimal amount of income inequality. But if federal policy is to try and accommodate state and local redistributive preferences, a necessary first step is to report information about the distributional effects of national policies at state and local levels.

In this section I propose a measure of national income inequality that is a composite of income inequality measures across allocative fields, beginning first with the political fields at the state and county level. I construct my inequality index following Anand and Sen,[[182]](#footnote-182) who construct a multidimensional poverty index that is a weighted mean of the primitive indices, and Persky and Tam (1990), who construct a national Gini coefficient that is a weighted sum of local Gini coefficients.[[183]](#footnote-183) Let the composite national income inequality index be defined as follows:

The variables are measures of average within-county, within-state, and within-nation income inequality. Thus, the overall within-county inequality measure is calculated as a weighted average of the inequality index across all counties: , where is an inequality index based on household incomes in county . The weights may be either county share of national income or share of the national population. The average within-state inequality measure is a weighted average inequality index across all 50 states: , where is an inequality index based on the household incomes within state and the weight is the state’s share of either the national population or national income. Finally, the national index of inequality is given by . The weights are policy preference parameters that represent the relative importance income inequality at each level of aggregation.

This flexible representation of income inequality has several desirable features. First, it allows for income inequality to enter the composite index separately at the county, state, and national levels reflecting the fact that inequality matters independently in each. The weights require explicit consideration of how to trade off inequality across partitions of the US population. Second, the indices , could be any of the commonly used measures of income inequality in the literature, such as the Gini coefficient, the Atkinson index, or variance. If absolute inequality is more important within states and relative inequality is more important within counties, then could be the variance or standard deviation and could be the Gini coefficient or Theil index. Moreover, if the Atkinson index is used to measure inequality at both the state and the county levels the parameter of inequality aversion could be different at these two different levels of aggregation, reflecting the possibility that localities are willing sacrifice a greater share of local income to achieve local equality at than they would be willing to sacrifice to achieve equal state incomes.

The composite income inequality index incorporates income inequality measures at only the county, state, and national levels, but it can be generalized to include inequality in other allocative fields in which income inequality matters. For example, component indices could include income inequality within regional housing markets, school districts, or congressional districts, or it could include inequality between, say, urban and rural areas. In its general form, the composite income inequality index is written as the weighted mean of order of indices, each of which is defined within an allocative field:

I propose that federal policies should be assessed in terms of their effects on this measure of composite income inequality. To the extent that we care about income inequality, we should care about it in the contexts that it matters and in the form that it matters. This may mean that we account for absolute inequality in some contexts and relative inequality in others and may mean that we care more about local income inequality than national income inequality—although we care about them both.

Accounting for income inequality where it matters most can change our assessments of the desirability of federal policies. For example, consider again the student interest pause considered in Part II and illustrated in Figure 20. The policy reduces measured national inequality by roughly 1%, but it has varied effects on within-county inequality, actually increasing local inequality in some instances. If we evaluate the effect of the interest rate pause using the composite income inequality measure and assume that within-county inequality weighted by county income is all that matters, then the effect of the interest rate pause is to reduce inequality by only 0.04%.

### A National Priority for the Poorest

I have shown in Part II the wide range of effects that a nationally redistributive policy might have on local inequality. I proposed in the previous section that national policies account for these subnational effects using a composite income inequality index, but there is also a class of redistributive policies that always (weakly) reduce inequality at all levels of geography: these are transfers from the wealthiest individuals in society to the poorest. Since the richest households nationally must always be richest households in any subnational jurisdiction, then increasing taxes on these households will not only reduce national income inequality, but it will also reduce local inequality in some subnational jurisdiction. And for symmetric reasons, using the revenue from a tax on the richest to increase incomes of the poorest households in the United States will *also* reduce inequality not only at the national level but also at every subnational geography where the poorest live.

My focus in this section will be on the reasons why it makes sense to focus on the very poorest Americans for redistribution from the richest for the purpose ofreducing inequality at the national level. I do not provide an all-things-considered assessment of the desirability of a transfer from the richest to the poorest. I do not discuss, efficiency, for example. Since, under certain assumptions, the highest-income individuals in society are also the most productive, then there is a larger efficiency loss to be reckoned with by redistributing from top earners on account of their tax-avoidance responses. My focus is only on the distributional side of things, and my reasons for focusing on redistribution to the very poorest can be thought of as factors weighing in the balance against other incentive-based considerations.

One might think that it does need not arguing that redistribution should focus on the poorest among us, except that is not what we typically do. As Professor Kleiman has observed, the earned income tax credit—which is the largest federal cash transfer to low-income households—leaves out the very poorest.[[184]](#footnote-184) Many tax and transfer proposals, described by their proponents as “progressive,” confer greater benefits on higher income individuals than the poorest individuals. Consider, for example, the effect of the student loan interest pause documented in Part II. Some scholars argue that our preoccupation with income inequality has caused us to neglect poverty.[[185]](#footnote-185) In this section, I argue that focusing on poverty at the federal level is the best means of addressing inequality at all levels.

The first reason for focusing federal redistribution to the poorest households is that doing so is *certain* to reduce income inequality in all political and economic fields. Reducing the ceiling and raising the floor is, in fact, the only way to be certain that national policy is not increasing inequality anywhere. Thus, a national priority for the poorest avoids any unintended perverse consequences of national redistributive policies.

Not only is a priority for the poorest certain to reduce income inequality in all political and economic fields, but it does so maximally. Redistributing income to the poorest members of society has a bigger effect in reducing all measures of inequality using most any plausible metric, including the Gini coefficient, the variance, and the Theil index. Under most social welfare functions, a redistribution to the poorest will lead to the biggest increase in social welfare and if the social welfare function is given a welfarist or utilitarian interpretation, then a transfer to the poorest will also have the biggest effect on aggregate utility.

A national priority for the poorest may have also have other benefits in terms of income segregation and migration. As discussed above in the literature on fiscal federalism, migration limits the efficacy of locally redistributive efforts, but it also facilitates the sorting of people into groups with similar tastes for public goods, enabling the efficient provision of those goods.

There is a very large literature on the determinants of migration,[[186]](#footnote-186) and the decision is correlated with personal characteristics such as race, age,[[187]](#footnote-187) education, family structure, employment status, and poverty.[[188]](#footnote-188) Local tax and spending policies also matter.[[189]](#footnote-189) For low-income households, the ability to migrate to other “high opportunity” neighborhoods can be an important factor for children’s outcomes,[[190]](#footnote-190) and migration is an important channel by which labor moves to its most productive use.[[191]](#footnote-191)

But moving is expensive, and there has been a decline in migration within the United States from 3% in 1981 to 1.5% in 2016.[[192]](#footnote-192) One estimate of the typical costs of moving between states is $34,248.[[193]](#footnote-193) And moving into high-income areas has been made more difficult by escalating home prices,[[194]](#footnote-194) perpetuating regional income segregation.[[195]](#footnote-195) Raising the incomes of the poorest would help them access economically-integrated neighborhoods while making fewer demands on local public services.

How does inequality itself affect migration? Theoretical work on the relationship between inequality and migration suggests that an in increase in income inequality is associated with an increase in income segregation,[[196]](#footnote-196) particularly segregation by the richest.[[197]](#footnote-197) The same work shows that increases in inequality make people more dissatisfied with their neighborhoods and hence more likely to move.[[198]](#footnote-198) Empirical work tends to bear this out. There is evidence that people tend to move out of neighborhoods when they are outliers; they tend to leave neighborhoods the further their household income is from the median, and they tend to move into neighborhoods where their income is close to the median.[[199]](#footnote-199) Nationally redistributive policies that target the poorest by taxing the richest will reduce this measure of social distance at the top and the bottom end, perhaps reducing the incentive to emigrate at both ends.[[200]](#footnote-200)

There is reason to think compressing local income distributions will lead to less pressure to emigrate by those at the top and the bottom, because people care about social distance from their neighbors. At the same time, an individual’s rank in the local income distribution is also a factor affecting their desire to migrate. Although people tend to seek neighborhoods of people with similar social status, middle and high-income households tend to avoid neighborhoods where they would be below the median income, and high-income households are attracted to neighborhoods where their incomes are much higher than the median.[[201]](#footnote-201) Another benefit of focusing redistributive efforts on the poor is that they would not induce exit by status-conscious high-income households, because the local median income is unlikely to change.

## Renovating the Architecture

There are a variety of ways that fiscal policy can be responsive to within- and between- jurisdiction income inequality, in addition to those discussed above. National policy could also make greater use of place-based subsidies,[[202]](#footnote-202) and state limits on local fiscal autonomy could be relaxed. Another possibility is to index federal taxes for local costs of living. Federal taxes are imposed on nominal, not real, incomes so that someone making $150,000 in a low-cost area pays a higher effective tax rate than someone making the same amount in a high-cost area.[[203]](#footnote-203) If people could move easily from high-cost to low-cost areas then real effective tax rates should roughly equalize across the country, but the resulting allocation of labor is away from high productivity locations. [[204]](#footnote-204) By one estimate, the failure to index transfers approximately $270 billion each year from high-wage areas to low-wage areas.[[205]](#footnote-205) Another report concludes that by failing to index “the nation is not only redistributing income from the prosperous to the poor, but from the middle-income residents of high-cost states to the middle-income residents of low-cost states.”[[206]](#footnote-206) As a political matter, however, indexing has always been a non-starter. As Tax historian Joe Thorndike puts it, such a law “might as well be called the Bicoastal Elite Tax Relief Act.”[[207]](#footnote-207)

I argued in Part I that evaluating income inequality among a collection of people should be done by explicit reference to the features of the economic, political, or social field that they occupy. If income is the basis for allocating a good in that field and the good is in relatively fixed supply, then two things follow. First, income inequality will translate into inequality in the allocation of that good. Second, income inequality in that field may have collateral effects on the allocation of goods in other fields, as people adjust their spending on substitutes and complements.

Thinking about the problems of income inequality within a framework of allocative fields reveals the several ways of mitigating the adverse distributional effects of income inequality. The first and most obvious approach is to reduce the amount of income inequality itself. The scholarly and political work under this approach is ongoing. I have highlighted some of the important nuances that need to be considered when federal policy is used for this purpose, and I have offered a composite income inequality measure to guide national policy toward that end and argued specifically for a national priority for the poorest. Another possibility is to tinker with the allocative fields themselves.

One avenue in this approach is to change the currency by which we allocate important goods in fixed supply within a field. If money is “kept out of politics,” and political influence is allocated on the basis of only votes, then income inequality cannot easily translate into inequalities in political influence. And public provision of goods such as housing and medical insurance, for example, would weaken the link between income inequality and the allocation of housing.

A second possibility focuses on restricting entry into the field. Consider political spending. The market for influence over state and local electoral outcomes and political influence is not limited to only those people who live in the jurisdiction. People from other political jurisdictions can spend money to influence the local politics, partially nationalizing the population of people whose incomes are relevant and widening the range of relevant incomes. Limits on local political spending by nonresidents could reduce income inequality in the political field.

A third avenue within this approach is to reallocate policymaking powers across federal, state, and local governments. For policies that have more of a zero-sum nature, or those with respect to which the rich are likely to have very different preferences than everyone else, it would be better to delegate these to lower levels of political organizations where income inequality is typically more attenuated. For policies involving true public goods, it might be perfectly fine to allocate these in a national market where high-end income inequality is less likely to harm low-income households.

The allocative fields framework introduces these changes in our legal and political system as possibilities for mitigating the adverse distributional effects of income inequality. And the framework works hand-in-hand with the composite measure of income inequality; reducing the relative importance of income inequality in a particular allocative field will reduce the weight that is given to that field in the index. More generally, it puts the problem of income inequality into its larger context, raising institutional questions such as how to decide which level of government should perform which function, how protectionist we should be in setting boundaries around our markets and political institutions, and what is the optimal use of market allocation mechanisms.

# Conclusion

I have argued that local income inequality matters, independently and in addition to the inequality at the state and national level, for reasons that have to do with how we allocate goods of various kinds based on the federal structure of U.S. government and the boundaries of the market economy. I have demonstrated that national attempts to address national income inequalities can have various and even perverse effects at subnational levels.

There is no easy fix. The independent importance of local inequality resurrects the case for local redistribution, but the limits of local redistribution remain. Federal fiscal policy can help, and toward that end I propose a composite measure of income inequality and an emphasis on prioritizing redistribution to the very poorest, which can ensure that redistributive efforts are inequality-reducing *everywhere*.

\* \* \*

# Appendix A: Figures and Tables

Figure 3: National Gini Coefficient and Theil T Index

A graph of a graph showing the value of a company

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Figure 4: National Inequality and Capital Gains Realizations

A graph of a graph with numbers and lines

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Figure 5**:** Global Inequality[[208]](#footnote-208)

A graph with a red line

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Figure 6: National Theil and Top State Risers and Fallers

A graph of a graph showing the number of state decline

Description automatically generated with medium confidence

Figure 7: National Inequality Decomposition

A graph with green line and blue line

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Figure 8: County Contributions to National Inequality

A map of the united states

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Table 1: Top Contributing Counties to National Inequality 2019

|  |  |  |
| --- | --- | --- |
| US Theil Contribution | County | State |
| 0.034 | Los Angeles County | CA |
| 0.033 | Miami-Dade County | FL |
| 0.019 | New York County | NY |
| 0.018 | Cook County | IL |
| 0.017 | Harris County | TX |
| 0.016 | King County | WA |
| 0.014 | Maricopa County | AZ |
| 0.014 | Orange County | CA |
| 0.013 | Santa Clara County | CA |
| 0.013 | Middlesex County | MA |
| 0.012 | Palm Beach County | FL |
| 0.010 | San Diego County | CA |
| 0.009 | Clark County | NV |
| 0.009 | Dallas County | TX |
| 0.009 | Westchester County | NY |
| 0.009 | Fairfield County | CT |
| 0.009 | San Mateo County | CA |
| 0.008 | Nassau County | NY |
| 0.008 | Norfolk County | MA |
| 0.007 | St. Louis County | MO |
| 0.007 | Kings County | NY |

Figure 9: 80th Income Decile Cutoff by County - 2020

A blue graph with numbers

Description automatically generated

Figure 10: Theil Indices by County - 2019

A graph of a graph

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Figure 11: Theil Indices by County - 2019

A map of the united states

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Table 2: 20 Most and 20 Least Equal Counties - 2019

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
| **Most Unequal** | | |  | **Most Equal** | | |
| Theil Index | County | State |  | Theil Index | County | State |
| 2.922 | Tom Green County | TX |  | 0.341 | Trimble County | KY |
| 2.264 | Miami-Dade County | FL |  | 0.338 | Beaver County | OK |
| 2.210 | La Salle County | TX |  | 0.338 | Red Lake County | MN |
| 2.201 | Blaine County | ID |  | 0.338 | Calhoun County | AR |
| 1.838 | Indian River County | FL |  | 0.338 | Cotton County | OK |
| 1.776 | Karnes County | TX |  | 0.336 | Lewis County | KY |
| 1.722 | Charleston County | SC |  | 0.336 | Little River County | AR |
| 1.681 | Routt County | CO |  | 0.336 | Cass County | IL |
| 1.567 | Eddy County | NM |  | 0.330 | Lassen County | CA |
| 1.520 | Potter County | TX |  | 0.327 | Lincoln County | NV |
| 1.479 | Reeves County | TX |  | 0.327 | Pulaski County | MO |
| 1.478 | Charlottesville city | VA |  | 0.323 | Vinton County | OH |
| 1.458 | Martin County | FL |  | 0.320 | Sullivan County | MO |
| 1.392 | Palm Beach County | FL |  | 0.317 | Long County | GA |
| 1.363 | Collier County | FL |  | 0.316 | Morgan County | OH |
| 1.362 | Union County | SD |  | 0.315 | Johnson County | NE |
| 1.357 | Red River Parish | LA |  | 0.306 | Geary County | KS |
| 1.350 | Pitkin County | CO |  | 0.304 | Oliver County | ND |
| 1.333 | Norfolk County | MA |  | 0.288 | Eureka County | NV |
| 1.291 | Taylor County | GA |  | 0.248 | Greenlee County | AZ |

Figure 12: Change in County Theil Indices

A map of the united states

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Table 3: 20 Counties with Biggest Increase/Decrease in Inequality 2010 - 2019

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
| **Biggest Increase in Inequality** | | |  | **Biggest Decrease in Inequality** | | |
| Theil | County | State |  | Theil | County | State |
| 2.277 | Tom Green County | TX |  | -0.583 | Pettis County | MO |
| 1.103 | Miami-Dade County | FL |  | -0.591 | Real County | TX |
| 1.042 | Blaine County | ID |  | -0.604 | Gray County | TX |
| 1.039 | Karnes County | TX |  | -0.652 | Midland County | TX |
| 1.012 | Charleston County | SC |  | -0.669 | Bandera County | TX |
| 0.881 | Reeves County | TX |  | -0.688 | Wichita County | KS |
| 0.840 | La Salle County | TX |  | -0.785 | Goshen County | WY |
| 0.718 | Routt County | CO |  | -0.876 | Zavala County | TX |
| 0.615 | Columbia County | NY |  | -0.957 | Frio County | TX |
| 0.527 | Reagan County | TX |  | -0.975 | Pennington County | MN |
| 0.519 | Albany County | NY |  | -1.014 | Grant County | KY |
| 0.507 | Indian River County | FL |  | -1.016 | Fulton County | GA |
| 0.502 | Newport County | RI |  | -1.035 | Yazoo County | MS |
| 0.499 | Dunn County | ND |  | -1.086 | Red River County | TX |
| 0.492 | Putnam County | TN |  | -1.114 | Crosby County | TX |
| 0.468 | Orange County | NC |  | -1.115 | Teton County | WY |
| 0.449 | New Kent County | VA |  | -1.669 | Kent County | MI |
| 0.435 | Dixie County | FL |  | -1.885 | Clayton County | IA |
| 0.430 | Colorado County | TX |  | -2.962 | Aurora County | SD |
| 0.423 | Martin County | TX |  | -3.218 | Bee County | TX |

Figure 13: Evolution of State Inequality and Counties with Biggest Increase/Decrease in Inequality

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Table 4: States with the Biggest Changes in Inequality 2010 - 2019

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| **Biggest Increase in Inequality** | |  | **Biggest Increase in Inequality** | |
| Theil | State |  | Theil | State |
| 0.318 | FL |  | -0.030 | IL |
| 0.258 | SC |  | -0.031 | DE |
| 0.234 | NV |  | -0.044 | SD |
| 0.167 | UT |  | -0.055 | AK |
| 0.152 | AZ |  | -0.069 | MN |
| 0.149 | WA |  | -0.097 | NY |
| 0.147 | MA |  | -0.172 | CT |
| 0.140 | HI |  | -0.178 | GA |
| 0.092 | NC |  | -0.194 | MI |
| 0.088 | VT |  | -0.199 | WY |

# Appendix B: Simulated Policy Effects

Figure 14: Effect of Sanders Tax Plan on County Theil Indices

A graph of a person

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Figure 15: Effect of Sanders Tax Plan on Standard Deviation of Income

A graph with numbers and a line

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Figure 16: Effect of TCJA on County Theil Indices

A blue graph with black text

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Figure 17: Effect of TCJA on County Standard Deviation of Income

A graph of a number of blue and black lines

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Figure 18: Effect of Student Debt Forgiveness on Theil

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Figure 19: Effect of Student Debt Forgiveness on Standard Deviation of Income

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Figure 20: Effect of Student Loan Interest Pause on County Theil Indices

A graph of a blue line

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Figure 21: Effect of Student Loan Interest Pause on County Standard Deviation of Income

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Description automatically generated

1. \* Nancy L. Buc ‘69 Research Professor of Democracy and Equity, University of Virginia School of Law. Thanks to Ryan Bubb, Conor Clarke, Dhammika Dharmapala, Daniel Hemel, Rich Hynes, Ruth Mason, Sai Prakash, Paul Stephan, Rory Van Loo, and participants at the UVA Tax Invitational, the Columbia Law School Tax Policy Colloquium, and the Annual Meeting of the American Law & Economics Association for helpful comments and conversations. I’m grateful to Leslie Ashbrook and Li Zhang for research assistance and Billi Jo Morningstar for editorial help. [↑](#footnote-ref-1)
2. 7 Plutarch, *Caesar*, *in* Plutarch’s Lives 443, 467-69 (Bernadotte Perrin trans., Harvard Univ. Press 1919), <https://www.loebclassics.com/view/plutarch-lives_caesar/1919/pb_LCL099.467.xml> (last visited Nov. 6, 2023). [↑](#footnote-ref-2)
3. This is limited to households that filed an income tax return in 2020. [↑](#footnote-ref-3)
4. *How Rich Am I?*, Giving What We Can, <https://howrichami.givingwhatwecan.org/how-rich-am-i> (last visited Nov. 6, 2023). [↑](#footnote-ref-4)
5. Justin H. Vassallo, *The Danger of Discussing ‘Maker and Taker’ States*, Am. Prospect (Dec. 10. 2021), https://prospect.org/politics/danger-of-discussing-maker-and-taker-states/; John Tierney, *Which States are Givers and Which are Takers?*, Atlantic (May 5, 2014), https://www.theatlantic.com/business/archive/2014/05/which-states-are-givers-and-which-are-takers/361668/. [↑](#footnote-ref-5)
6. *What do Ticos Really Think About Foreigners in Costa Rica?*, Tico Times (June 27, 2014), https://ticotimes.net/2014/06/27/what-do-ticos-really-think-about-foreigners-in-costa-rica. [↑](#footnote-ref-6)
7. The Gini coefficients of the United States and Blaine County, respectively, were 0.588 and 0.821. The difference between the two, as a share of the national Gini coefficient, was 0.39. [↑](#footnote-ref-7)
8. The Gini coefficient of Idaho was 0.5648, which is 4% less than the national Gini coefficient (0.588-0.5648)/0.588. [↑](#footnote-ref-8)
9. The Gini coefficient of Orleans County was 0.464, which is 21% less than the national Gini coefficient (0.588-0.464)/0.588. [↑](#footnote-ref-9)
10. The Gini coefficient of New York was 0.616, which is 4% more than the national Gini coefficient (0.616-0.588)/0.588. [↑](#footnote-ref-10)
11. *See, e.g*., Jesse Eisinger et al., *The Secret IRS Files: Trove of Never-Before Seen Records Reveal How the Wealthiest Avoid Income Tax*, ProPublica (June 8, 2021), <https://www.propublica.org/article/the-secret-irs-files-trove-of-never-before-seen-records-reveal-how-the-wealthiest-avoid-income-tax> (highlighting low taxes paid by Elon Musk and Jeff Bezos); Jeff Sparrow, *The Grotesque Inequality Embodied by Musk, Bezos and Zuckerberg is a Threat to Democracy*, Guardian (Nov. 17, 2022), https://www.theguardian.com/commentisfree/2022/nov/18/the-grotesque-inequality-embodied-by-musk-bezos-and-zuckerberg-is-a-threat-to-democracy. [↑](#footnote-ref-11)
12. *See, e.g*., Arun Advani, Helen Hughson & Hannah Tarrant, *Revenue and Distributional Modelling for a UK Wealth Tax*, 42 Fiscal Stud. 699 (2021). [↑](#footnote-ref-12)
13. *See, e.g*., Eric Toder & Alan D. Viard, *Replacing Corporate Tax Revenues with a Mark-to-Market Tax on Shareholder Income*, 69 Nat’l Tax J. 701 (2016). [↑](#footnote-ref-13)
14. *See, e.g*., Douglas W. Elmendorf, Jason Furman, William G. Gale, & Ben Harris, *Distributional Effects of the 2001 and 2003 Tax Cuts: How Do Financing and Behavioral Responses Matter?,* Brookings Inst. (June 30, 2008) https://www.brookings.edu/articles/distributional-effects-of-the-2001-and-2003-tax-cuts-how-do-financing-and-behavioral-responses-matter/. [↑](#footnote-ref-14)
15. I.R.C. § 164(a)(1), (3). [↑](#footnote-ref-15)
16. I.R.C. § 164(b)(6). [↑](#footnote-ref-16)
17. The same analysis here could be applied to any nationally redistributive policies, such as those implemented by consumer or competition law. *See, e.g.,* Rory Van Loo, *Broadening consumer law: Competition, protection, and distribution*, 95 Notre Dame L. Rev. 211 (2019). [↑](#footnote-ref-17)
18. A related literature adopts a development perspective on cities and considers the limits created by mobility on cities’ ability to engages in redistributive policies. *See, e.g.,* Richard C. Schragger, *Is a progressive city possible: reviving urban liberalism for the twenty-first century*, 7 Harv. L. & Pol’y Rev. 231 (2013); Richard C. Schragger, *Mobile capital, local economic regulation, and the democratic city*, Harv. L. Rev. 482 (2009). [↑](#footnote-ref-18)
19. *See* Mark V. Pauly, *Income Redistribution as a Local Public Good*, 2 J. Pub. Econ. 35, 57 (1973). [↑](#footnote-ref-19)
20. *Id*. For a discussion of this argument and its relevance to SALT deductibility, *see* Louis Kaplow, *Fiscal Federalism and the Deductibility of State and Local Taxes under the Federal Income Tax*, 82 Va. L. Rev. 413 (1996). [↑](#footnote-ref-20)
21. Joseph Persky & Mo‐Yin Tam, *Local Status and National Social Welfare*, 30 J. REG’L SCI. 229 (1990). Beliefs about the importance of income inequality are shaped by local conditions. Scott L. Minkoff & Jeffrey Lyons, *Living With Inequality: Neighborhood Income Diversity and Perceptions of the Income Gap*, 47 Am. Pol. Rsch. 329, 329 (2019) (“[T]hose who are exposed to more income diversity near their homes perceive larger gaps between the rich and everybody else, and are more likely to believe that the gap should be smaller. Moreover, this effect appears to be especially pronounced among those with lower educational attainment and at either end of the income spectrum.”). [↑](#footnote-ref-21)
22. Henry C. Simons, Personal Income Taxation: The Definition of Income as a Problem of Fiscal Policy 50 (1938) (“income is ‘the algebraic sum of (1) the market value of rights exercised in consumption and (2) the change in the value of the store of property rights between the beginning and end of the period in question.’). [↑](#footnote-ref-22)
23. *Cf*. Amy E. Mickel & Lisa A. Barron, *Getting “More Bang for the Buck”: Symbolic Value of Monetary Rewards in Organizations*, 17 J. Mgmt. Inquiry 329, 331 (2008) (citing Terence R. Mitchell & Amy E. Mickel, *The Meaning of Money: An* *Individual-Difference Perspective,* 24 Acad. Mgmt. Rev. 568 (1999) (money has symbolic value for achievement and recognition, status and respect, freedom and control, and power)). [↑](#footnote-ref-23)
24. However, income may negatively correlate with professional status if it compensates people for taking less “honorable” jobs. Adam Smith, An inquiry into the nature and causes of the wealth of nations: Volume One (1776) (“The wages of labour vary with the ease or hardship, the cleanliness or dirtiness, the honourableness or dishonourableness of the employment…Honour makes a great part of the reward of all honourable professions. In point of pecuniary gain, all things considered, they are generally under-recompensed”). [↑](#footnote-ref-24)
25. Income is only one factor in what sociologists refer to as “socioeconomic status.” Other factors include education and the prestige associated with one’s occupation. Social status can depend on any number of things, including kinship relationships, race, caste and ethnicity, and other inherited characteristics. [↑](#footnote-ref-25)
26. Cf. Mariana Mazzucato, Josh Ryan-Collins & Giorgos Gouzoulis, *Mapping Modern Economic Rents: The Good, the Bad, and the Grey Areas*, 47 Cambridge J. Econ. 507 (2023). [↑](#footnote-ref-26)
27. Cf. Nancy Folbre & Julie A. Nelson, *For love or money—or both?*, 14 J. Econ. Persps. 123 (2000). [↑](#footnote-ref-27)
28. It may affect how much he works, but not his productivity. [↑](#footnote-ref-28)
29. For evidence that the income elasticity of a good depends on its public visibility *see* Ori Heffetz, *A Test of Conspicuous Consumption: Visibility and Income Elasticities*, 93 Rev. Econ. & Stat. 1101 (2011). [↑](#footnote-ref-29)
30. For this reason. David Weisbach has argued that a consumption tax ultimately reaches the benefits of income. David A. Weisbach, *The Case for a Consumption Tax*, 110 Tax Notes 1357, 1357-59 (2006) (“Power and prestige from savings come from the ability to direct the money, from the possibility of future consumption...Taxing that future consumption reduces the power and prestige from savings”). [↑](#footnote-ref-30)
31. Conor Clarke & Wojciech Kopczuk, *Business income and business taxation in the United States since the 1950s*, 31.1 Tax Pol’y & the Economy 121 (2017). [↑](#footnote-ref-31)
32. See infra note 114. For a recent discussion, see Conor Clarke & Wojciech Kopczuk, *Measuring Income and Measuring Inequality*, WashU Law and Columbia Economics Mimeo (2024) [↑](#footnote-ref-32)
33. For a recent discussion of the importance of the relevant accounting period, *see* Daniel Shaviro, *Ten Observations about Income Inequality* (June 20, 2024). Available at SSRN: https://ssrn.com/abstract=4871782 or [http://dx.doi.org/10.2139/ssrn.4871782 at 11](http://dx.doi.org/10.2139/ssrn.4871782%20at%2011). [↑](#footnote-ref-33)
34. For an overview of the relationship between income inequality and psychological health and stress, *see* Richard Wilkinson & Kate Pickett, The Inner Level: How More Equal Societies Reduce Stress, Restore Sanity and Improve Everyone’s Well-Being (2019). [↑](#footnote-ref-34)
35. Of course, the seller of the commodity may be made better off by being able to receive a higher price for the good. This depends on competition on the supply side. [↑](#footnote-ref-35)
36. Andrew T. Hayashi & Richard M. Hynes, *Protectionist Property Taxes*, 106 Iowa L. Rev. 1091 (2020). [↑](#footnote-ref-36)
37. Long Yu, *Superfoods’ Dark Side: Increasing Vulnerability of Quinoa Farmers in Bolivia*, Global Food, Health, & Soc’y (Jan. 22, 2019), https://web.colby.edu/st297-global18/2019/01/22/superfoods-dark-side-increasing-vulnerability-of-quinoa-farmers-in-bolivia/. In places where quinoa is produced, the increase in global quinoa consumption can redound to the benefit of producers and their neighbors. Jeremy Cherfas, *Your Quinoa Habit Really Did Help Peru’s Poor. But There’s Trouble Ahead*, NPR (Mar. 31, 2016), https://www.npr.org/sections/thesalt/2016/03/31/472453674/your-quinoa-habit-really-did-help-perus-poor-but-theres-trouble-ahead. [↑](#footnote-ref-37)
38. There is also significant inequality in nutrition, with most of the difference due to differences in preferences. Hunt Allcott, Rebecca Diamond, Jean-Pierre Dubé, Jessie Handbury, Ilya Rahkovsky & Molly Schnell, *Food Deserts and the Causes of Nutritional Inequality*”, 134 Q. J. Econ. 1793 (2019) (“households in the top income quartile buy groceries that are 0.56 standard deviations more healthful than the bottom income quartile…exposing low-income households to the same products and prices available to high-income households reduces nutritional inequality by only about 10%, while the remaining 90% is driven by differences in demand.”) [↑](#footnote-ref-38)
39. *See, e.g*., John Harwood, *5 Reasons Why Income Inequality has Become a Major Political Issue*, CNBC (June 5, 2019), https://www.cnbc.com/2019/06/05/5-reasons-income-inequality-has-become-a-major-political-issue.html (“Rising wealth confers political power, and it has allowed economic winners to further reward themselves through government policies. . . . The same goes for policies at private institutions.”). [↑](#footnote-ref-39)
40. Branko Milanović, Global Inequality: A New Approach for the Age of Globalization (2016). [↑](#footnote-ref-40)
41. James Szewczyk & Melody Crowder-Meyer, *Community Income Inequality and the Economic Gap in Participation*, 44 Pol. Behav. 479 (2022). [↑](#footnote-ref-41)
42. *See, e.g*., Janna L. Matlack & Jacob L. Vigdor, *Do Rising Tides Lift All Prices? Income Inequality and Housing Affordability*, 17 J. Hous. Econ. 212 (2008) (“In tight housing markets, the poor do worse when the rich get richer. In slack markets, at least some evidence suggests that increases in others’ income, holding own income constant, may be beneficial”); Jacob L. Vigdor, *Does Gentrification Harm the Poor?,* Brookings-Wharton Papers on Urb. Affs., 2002, at 133. [↑](#footnote-ref-42)
43. Matlack & Vigdor, *supra*. [↑](#footnote-ref-43)
44. Anthony W. Orlando & Christian L. Redfearn, *What’s Lost in the Aggregate: Lessons from a Local Index of Housing Supply Elasticities* (2018). For factors driving these elasticities, see Albert Saiz, *On Local Housing Supply Elasticity* (July 31, 2008), https://ssrn.com/abstract=1193422. [↑](#footnote-ref-44)
45. Matlack & Vigdor, *supra* note 41 at [] (“in tight housing markets, greater inequality…predict[s] higher rent payments and greater crowding for households headed by a high school dropout. These effects are uniformly weaker in areas with above-average vacancy rates.”). [↑](#footnote-ref-45)
46. Chuanchuan Zhang, *Income Inequality and Access to Housing: Evidence from China*, 36 China Econ. Rev. 261 (2015); Chuanchuan Zhang, Shen Jia & Rudai Yang, *Housing Affordability and Housing Vacancy in China: The Role of Income Inequality*, 33 J. Hous. Econ. 4 (2016). *But see* Niku Määttänen & Marko Terviö, *Income Distribution and Housing Prices: An Assignment Model Approach*, 151 J. Econ. Theory 381 (2014); M.U. Özmen, M.K. Kalafatcılar & E. Yılmaz, *The Impact of Income Distribution on House Prices*, 19 Cent. Bank Rev. 45 (2019). [↑](#footnote-ref-46)
47. Thomas Goda, Chris Stewart & Alejandro Torres García, *Absolute Income Inequality and Rising House Prices*, 18 Socio-Economic Rev. 941 (2019); Caroline Dewilde & Bram Lancee, *Income Inequality and Access to Housing in Europe*, 29 Eur. Socio. Rev. 1189 (2013). For a study finding a negative effect of inequality on home prices over a longer horizon, *see* Abebe Hailemariam, et al., *Income Inequality and Housing Prices in the very Long‐Run*, 88 S. Econ. J. 295 (2021). [↑](#footnote-ref-47)
48. Dirk Krueger & Fabrizio Perri, *Does Income Inequality Lead to Consumption Inequality? Evidence and Theory*, 73 Rev. Econ. Stud. 163 (2006) (arguing that income volatility generate thicker credit markets which allow for better consumption smoothing). Meyer and Sullivan also find support for this general conclusion over a longer time horizon. Bruce D. Meyer & James X. Sullivan, *Consumption and Income Inequality in the US Since the 1960s*, Nat’l Bureau Econ. Rsch. No. w23655 (2017). *But see* Mark Aguiar & Mark Bils, *Has Consumption Inequality Mirrored Income Inequality?,* 105 Am. Econ. Rev. 2725 (2015) (after correcting for measurement error, consumption inequality tracks income inequality more closely). *See* generally Orazio P. Attanasio & Luigi Pistaferri, *Consumption Inequality*, 30 J. Econ. Persps. 3 (2016). Consumption and income inequality can follow very different trends. For example, during the period spanning 2000 - 2011 in the United States, income inequality grew but consumption inequality first rose then fell again to below its 2000 level. Bruce D. Meyer & James X. Sullivan, *Consumption and Income Inequality and the Great Recession*, 103 Am. Econ. Rev. 178 (2013). [↑](#footnote-ref-48)
49. Jessie Handbury, *Are Poor Cities Cheap for Everyone? Non‐Homotheticity and the Cost of Living Across US Cities*, 89 Econometrica 2679 (2021) (“I show that product variety is skewed towards the income-specific tastes of local consumers.”) [↑](#footnote-ref-49)
50. Handbury, *supra* note 48. [↑](#footnote-ref-50)
51. Handbury, *supra* note 48. [↑](#footnote-ref-51)
52. Handbury, *supra* note 48. [↑](#footnote-ref-52)
53. Rebecca Diamond & Enrico Moretti, *Where is Standard of Living the Highest? Local Prices and the Geography of Consumption*, Nat’l Bureau Econ. Rsch. No. w29533 (2021). [↑](#footnote-ref-53)
54. *Id*. [↑](#footnote-ref-54)
55. *Id*. [↑](#footnote-ref-55)
56. *Id*. (“consumption inequality within a commuting zone increases significantly with cost of living.”) [↑](#footnote-ref-56)
57. *Id*. (“low-income households in expensive commuting zones have a higher incidence of financial distress than low-income households in a affordable commuting zones”). [↑](#footnote-ref-57)
58. *Id*. [↑](#footnote-ref-58)
59. Marianne Bertrand & Adair Morse, *Trickle-Down Consumption*, 98 Rev. Econ. Stat. 863, 864 (2016). Maria Charles & Jeffrey D. Lundy, *The Local Joneses: Household Consumption and Income Inequality in Large Metropolitan Areas*, 34 Rsch. Soc. Stratification & Mobility 14 (2013) (in metro areas with high inequality, there is more spending on shelter and food in particular). David M. Frankel & Eric D. Gould, *The Retail Price of Inequality*, 49 J. Urb. Econ. 219 (2001) (absence of lower-middle income households tend to results in higher retail prices). [↑](#footnote-ref-59)
60. Bertrand & Morse, *supra* note 65. (“Holding their own current income constant, nonrich households that are exposed to higher top income levels in their market spend a higher share of their income.”) [↑](#footnote-ref-60)
61. Jagdish Bhagwati, *Immiserizing growth: A geometrical note*, 25.3 Rev. Econ. Stud. 201 (1958); H. Johnson, *Economic expansion and world trade*, 23 Manch. Sch. 95 (1955). [↑](#footnote-ref-61)
62. Daniel Murphy, *Welfare consequences of asymmetric growth*, 126 J. Econ. Behavior & Org. 1 (2016). [↑](#footnote-ref-62)
63. Hoyoung Yoo, *The Welfare Consequences of Incoming Remote Workers on Local Residents*, Available at SSRN 4907833 (2024). [↑](#footnote-ref-63)
64. Id. The arrival of remote workers can have significant effects on home prices. John A. Mondragon & Johannes Wieland, *Housing demand and remote work*. NBER No. w30041 (2022) (“We show that the shift to remote work explains over one half of the 23.8 percent national house price increase over this period [from 2019-2021].”). [↑](#footnote-ref-64)
65. *See, e.g*., Jongmook Choe, *Income Inequality and Crime in the United States*, 101 Econ. Letters 31 (2008); Jesse Brush, *Does Income Inequality Lead to More Crime? A Comparison of Cross-sectional and Time-series Analyses of United States Counties*, 96 Econ. Letters 264 (2007); Morgan Kelly, *Inequality and Crime*, 82 Rev. Econ. Stat. 530 (2000); Thomas D. Stucky, Seth B. Payton & John R. Ottensmann, *Intra- and Inter-Neighborhood Income Inequality and Crime*, 39 J. Crime & Just. 345 (2016); Ted Enamorado et al., *Income Inequality and Violent Crime: Evidence from Mexico’s Drug War*, 120 J. Dev. Econ. 128 (2016). [↑](#footnote-ref-65)
66. Kate E. Pickett & Richard G. Wilkinson, *Income Inequality and Health: a Causal Review*, 128 Soc. Sci. & Med. 316 (2015). *But see* Adam Wagstaff & Eddy Van Doorslaer, *Income Inequality and Health: What Does the Literature Tell Us?*, 21 Ann. Rev. Pub. Health 543 (2000); Paula K. Lorgelly & Joanne Lindley, *What is the Relationship Between Income Inequality and Health? Evidence from the BHPS*, 17 Health Econ. 249 (2008); Jennifer M. Mellor & Jeffrey Milyo, *Income Inequality and Health Status in the United States: Evidence from the Current Population Survey*, J. Hum. Res. 510 (2002). [↑](#footnote-ref-66)
67. Nicholas R. Buttrick & Shigehiro Oishi, *The Psychological Consequences of Income Inequality*, 11 Soc. & Personality Psych. Compass e12304 (2017); Simone M Schneider, *Why Income Inequality is Dissatisfying—Perceptions of Social Status and the Inequality-Satisfaction Link in Europe*, 35 Eur. Socio. Rev. 409 (2019). [↑](#footnote-ref-67)
68. James C. Garand, *Income Inequality, Party Polarization, and Roll-Call Voting in the US Senate*, 72 J. Pol. 1109 (2010); Hernan Winkler, *The Effect of Income Inequality on Political Polarization: Evidence from European Regions, 2002–2014*, 31 Econ. & Pol. 137 (2019). *But see* Bryan J. Dettrey & James E. Campbell, *Has Growing Income Inequality Polarized the American Electorate? Class, Party, and Ideological Polarization*, 94 Soc. Sci. Q. 1062 (2013). [↑](#footnote-ref-68)
69. One’s relative socioeconomic position is associated with myriad outcomes. *See, e.g.,* Ying-Chih et al., *A Multilevel Analysis of Neighborhood and Individual Effects on Individual Smoking and Drinking in Taiwan*, 7 BMC Pub. Health 151 (2007) (being relatively advantaged can be protective of alcoholism); Adrian Aguilera, Yan Leykin, Nancy Adler & Ricardo F. Muñoz, *Assessing the Impact of Relative Social Position and Absolute Community Resources on Depression and Obesity Among Smokers*, 50 Am. J. Cmty. Psych. 211 (2012) (being relatively advantaged can be protective of depression). *But see*, Amanda L. Roy, Erin B. Godfrey, & Jason R.D. Rarick, *Do We Know Where We Stand? Neighborhood Relative Income, Subjective Social Status, and Health*, 57 Am. J. Cmty. Psych. 448, 449 (2016) (for low-income people, being in a high-income neighborhood is protective of physical and mental health.) [↑](#footnote-ref-69)
70. Fredrik Carlsson, Olof Johansson‐Stenman & Peter Martinsson, *Do You Enjoy Having More Than Others? Survey Evidence of Positional Goods*, 74 Economica 586 (2007) (income is a positional good)*; cf.* Michael Schneider, *The Nature, History and Significance of the Concept of Positional Goods*, 45 Hist. Econ. Rev. 60 (2007). There is evidence that positional goods are more important to people in states with greater income inequality. Lukasz Walasek & Gordon. D.A. Brown, *Income Inequality and Status Seeking: Searching for Positional Goods in Unequal U.S. States*, 26 Psych. Sci. 527 (2015). [↑](#footnote-ref-70)
71. Anthony M. Annett, Cathonomics: How Catholic Tradition can Create a More Just Economy 193 (2022). [↑](#footnote-ref-71)
72. Annett, *supra* note 71; Michael J. Sandel, *How Meritocracy Fuels Inequality—Part I The Tyranny of Merit: An Overview*, 1 Am. J. L. & Equality 4 (2021); *see also* Michael Young, The Rise of the Meritocracy (2011). [↑](#footnote-ref-72)
73. There may be some benefits to local inequality; for example, there may be positive spillover effects from economic mixing, such as the transfer of skills. However, beneficial inequalities in pre-tax incomes do not imply beneficial inequalities in after-tax incomes. [↑](#footnote-ref-73)
74. Edward L. Glaeser, Matt Resseger & Kristina Tobio, *Inequality in Cities*, 49 J. Reg’l Sci. 617 (2009). [↑](#footnote-ref-74)
75. Raj Chetty, Nathaniel Hendren, Patrick Kline & Emmanuel Saez, *Where is the Land of Opportunity? The Geography of Intergenerational Mobility in the United States*, 129 Q. J. Econ. 1553 (2014). [↑](#footnote-ref-75)
76. Raj Chetty & Nathaniel Hendren, *The Impacts of Neighborhoods on Intergenerational Mobility II: County-Level Estimates*, 133 Q. J. Econ. 1163, 1163 (2018) (“Counties with less concentrated poverty, less income inequality, better schools, a larger share of two-parent families, and lower crime rates tend to produce better outcomes for children in poor families.”). [↑](#footnote-ref-76)
77. Edward L. Glaeser, Matt Resseger & Kristina Tobio, *Inequality in Cities*, 49 J. Reg’l Sci. 617 (2009) (citing E.F.P. Luttmer, *Neighbors as Negatives: Relative Earnings and Well-Being*, 120 Q. J. Econ. 963 (2005)). [↑](#footnote-ref-77)
78. John R. Hipp & Andrew J. Perrin, *The Simultaneous Effect of Social Distance and Physical Distance on the Formation of Neighborhood Ties*, 8 City & Cmty. 5, 20 (2009) (“our findings suggest that wealth differences affect the degree of social interaction between residents *within* relatively small neighborhoods”). [↑](#footnote-ref-78)
79. *Id*. [↑](#footnote-ref-79)
80. Glaeser et al., *supra* note 76. [↑](#footnote-ref-80)
81. Local income inequality may lead to higher public expenditures. Leah Boustan, Fernando Ferreira, Hernan Winkler & Eric M. Zolt, *The Effect of Rising Income Inequality on Taxation and Public Expenditures: Evidence from U.S. Municipalities and School Districts, 1970–2000*, 95 Rev. Econ. & Stat. 1291 (2013). Increases in income inequality are also associated with charitable giving. A. Abigail Payne & Justin Smith, *Does Income Inequality Increase Charitable Giving?*, 48 Canadian J. Econ. 793 (2015). *But see* Nicolas J. Duquette, *Inequality and Philanthropy: High-income Giving in the United States 1917–2012*, 70 Expl. Econ. Hist. 25 (2018). [↑](#footnote-ref-81)
82. Juliana Londoño-Vélez, *The impact of diversity on perceptions of income distribution and preferences for redistribution*, J. Pub. Econ. 214 (2022); Minkoff & Lyons, *supra* note []. For an alternative (to proximity-based altruism) explanation of the effect of labor market segmentation on lower support for redistribution *see* James Alt & Torben Iversen, *Inequality, labor market segmentation, and preferences for redistribution*, 61.1 Am. J. Pol. Sci. 21 (2017). [↑](#footnote-ref-82)
83. Richard D. Kahlenberg, *Socioeconomic School Integration*, 85 N.C. L. Rev. 1545 (2007). [↑](#footnote-ref-83)
84. Diane K. Levy, Zach McDade & Kassie Bertumen, *Mixed-Income Living: Anticipated and Realized Benefits for Low-Income Households*, 2 Cityscape 15 (2013) (“Compared with the hypothesized benefits, the actual benefits from living in mixed-income developments or income-diverse areas have been limited for low-income households.”) [↑](#footnote-ref-84)
85. Amie Thurber, Claire Riehle Bohmann & Craig Anne Heflinger, *Spatially integrated and socially segregated: The effects of mixed-income neighbourhoods on social well-being*, 55.9 Urb. Stud. 1859 (2018). [↑](#footnote-ref-85)
86. *See, e.g.,* Orazio Attanasio, Erik Hurst & Luigi Pistaferri, *The Evolution of Income, Consumption, and Leisure Inequality in the United States, 1980–2010*, in Improving the measurement of consumer expenditures 100 (2014) (“Finally, and somewhat more arbitrarily, we exclude contributions and donations to charities”). *But see* Mark Aguiar & Mark Bils, *Has Consumption Inequality Mirrored Income Inequality?*, 105 Am. Econ. Rev. 2725 (2015) (including cash expenditure data from consumer expenditure survey data). [↑](#footnote-ref-86)
87. Brian Highsmith uses the term “fiscal unit” to describe the geographic unit scope of taxation. Brian Highsmith, *The Implications of Inequality for Fiscal Federalism (Or Why the Federal Government Should Pay for Local Public Schools)*, 67 Buff. L. Rev. 407, 408 (2019). [↑](#footnote-ref-87)
88. I acknowledge, but bracket for the purposes of this discussion, the many and unequal limits on equal participation in voting. [↑](#footnote-ref-88)
89. Jason Armesto, *Charlottesville leaders, residents split over zoning rewrite*, Daily Progress (Aug. 29, 2023), available at https://dailyprogress.com/news/charlottesville-leaders-residents-split-over-zoning-rewrite/article\_dd551078-438e-11ee-bdb2-4fdd9ce2c945.html [↑](#footnote-ref-89)
90. On the effect of local costs on real income inequality, *see, e.g.,* David Albouy, Gabriel Ehrlich & Yingyi Liu, *Housing Demand, Cost-of-Living Inequality, and the Affordability Crisis*, Nat’l Bureau Econ. Rsch. No. w22816 (2016) (“nationally rising rents over time have increased real-income inequality considerably”). On the effects of housing costs on measured real wage inequality, *see* Enrico Moretti, *Real Wage Inequality*, 5 Am. Econ. J.: Applied Econ. 65 (2013). Professor Diamond finds that the inequality in wellbeing between college and high school educated individuals is greater than that implied by the wage gap. Rebecca Diamond, *The Determinants and Welfare Implications of US Workers’ Diverging Location Choices by Skill: 1980–2000*,106 Am. Econ. Rev. 479 (2016). [↑](#footnote-ref-90)
91. Cf. David J. Barron, *Reclaiming Home Rule*, 116 Harv. L. Rev. 2255 (2003). [↑](#footnote-ref-91)
92. Cf. Osborne M. Reynolds, Jr., Local Government Law 150-52 (5th ed. 2019). [↑](#footnote-ref-92)
93. This is politically salient with the proliferation of state preemption laws. Richard C. Schragger, *The Attack on American Cities*, 96 Tex. L. Rev. 1163 (2018). [↑](#footnote-ref-93)
94. *See* Ashley Deeks & Andrew Hayashi, *Tax Law as Foreign Policy*, 170 U. Pa. L. Rev. 275 (2021); Andrew T. Hayashi & Richard M. Hynes, *Protectionist Property Taxes*, 106 Iowa L. Rev. 1091 (2020). [↑](#footnote-ref-94)
95. I assume that the fields are a partition of the entire country. [↑](#footnote-ref-95)
96. Assume that there are the same number of people in each county. [↑](#footnote-ref-96)
97. Much of this summary is adapted from the discussion in Amartya Sen & James Foster, On Economic Inequality (1973). [↑](#footnote-ref-97)
98. This also requires that the two do not change rank ordering in the income distribution. [↑](#footnote-ref-98)
99. Let be the income of the individual and be the mean income in population of individuals. The variance is . [↑](#footnote-ref-99)
100. Sen & Foster, *supra* note 95. [↑](#footnote-ref-100)
101. The coefficient of variation normalizes the standard deviation (the square root of the variance) by the mean, thereby ensuring that a comparison of income distributions is based on their relative income variation. The coefficient of variation is . [↑](#footnote-ref-101)
102. Professor David Kamin has written about the importance of connecting different measures of progressivity explicitly to theories of distributive justice. David Kamin, *What Is a Progressive Tax Change: Unmasking Hidden Values in Distributional Debates*, 83 N.Y.U. L. Rev. 241 (2008). [↑](#footnote-ref-102)
103. *See* *infra*, Part II. [↑](#footnote-ref-103)
104. The Gini coefficient is also one half of the relative mean difference in incomes. Sen & Foster, *supra* note 95. Formally, this is . [↑](#footnote-ref-104)
105. Sen & Foster, *supra* note 95 at 33 (“[T]he implicit welfare function underlying the Gini coefficient is a rank‐order‐weighted sum of different persons’ income shares.”) [↑](#footnote-ref-105)
106. Theil’s T can be written at where is the income share of person . [↑](#footnote-ref-106)
107. Yoram Amiel, John Creedy & Stan Hurn, *Measuring Attitudes Towards Inequality*, 101 Scandinavian J. Econ. 83 (1999) (experimental subjects’ judgments are better captured by the Gini coefficient or Atkinson’s index than constant absolute inequality aversion). [↑](#footnote-ref-107)
108. For a recent application of this index and discussion, *see* Prasad Krishnamurthy, *Forgiving Student Loans: Progressivity, Inequality, and Welfare* (May 2, 2023), https://papers.ssrn.com/sol3/papers.cfm?abstract\_id=4436493. [↑](#footnote-ref-108)
109. If the size of the premium is constant regardless of the scale of the bet, then the individual is said to have constant absolute risk aversion (CARA) preferences. [↑](#footnote-ref-109)
110. As the coefficient of inequality aversion increases, less weight is attached to higher incomes. John Creedy, *The Atkinson Inequality Measure and Inequality Aversion* 3 (Victoria Bus. Sch. Working Paper in Pub. Fin., Paper No. 01/2019, 2019), <https://www.wgtn.ac.nz/__data/assets/pdf_file/0006/1863762/WP-01-2019-The-Atkinson-Inequality-Measure-and-Inequality-Aversion.pdf> (“[I]t is possible for a change in a tax and transfer system to be judged as inequality increasing or decreasing, depending on the degree of relative inequality aversion.”) [↑](#footnote-ref-110)
111. An alternative approach models inequality as producing a negative externality. Morten Nyborg Støstad & Frank Cowell, *Inequality as an Externality: Consequences for Tax Design* (Aug 9, 2022), https://papers.ssrn.com/sol3/papers.cfm?abstract\_id=4185685. [↑](#footnote-ref-111)
112. Anthony B. Atkinson, *On Lateral Thinking*, 9 J. Econ. Inequality 319 (2011). [↑](#footnote-ref-112)
113. Atkinson, *supra* note 101 (“following Kolm, we would assume constant absolute inequality aversion, and replace the constant elasticity form of j(h) by an exponential form”). [↑](#footnote-ref-113)
114. Daniel Miles & M. Maximo Rossi, *Learning about one’s relative position and subjective well-being*, 39 Applied Econ. 1711 (2007); Gordon DA Brown, Jonathan Gardner, Andrew J. Oswald & Jing Qian, *Does Wage Rank Affect Employees’ Well‐Being?*, 47 Industrial Relations: A J. Econ. & Soc’y 355 (2008). For theoretical work based on utility from relative status, *see* Andrew E. Clark & Andrew J. Oswald, *Comparison-Concave Utility and Following Behaviour in Social and Economic Settings*, 70 J. Pub. Econ. 133 (1998); David Neumark & Andrew Postlewaite, *Relative income concerns and the rise in married women’s employment*, 157 J. Pub. Econ. 157 (1998). [↑](#footnote-ref-114)
115. Jeremy Celse, *An Experimental Investigation of the Impact of Absolute and Relative Inequalities on Individual Satisfaction*, 18 J. Happiness Stud. 939 (2017). [↑](#footnote-ref-115)
116. Jeremy Celse, *Do You Enjoy Having More Than Others or More Than Another? Exploring the Relationship Between Relative Concerns and the Size of the Reference Group*, 138 Soc. Indic. Res. 1089 (2018). [↑](#footnote-ref-116)
117. In all cases, incomes are measured before taxes and transfers. [↑](#footnote-ref-117)
118. In using tax data I follow recent work measuring income inequality at a national level. See, e.g., Thomas Piketty & Emmanuel Saez, *Income inequality in the United States, 1913–1998*, 118.1 Q. J. Econ. 1 (2003); Thomas Piketty, Emmanuel Saez & Gabriel Zucman, *Distributional national accounts: methods and estimates for the United States*, 133.2 Q. J. Econ. 553 (2018); Gerald Auten & David Splinter, *Income inequality in the United States: Using tax data to measure long-term trends*, 132.7 J. Pol. Econ. (2024). [↑](#footnote-ref-118)
119. Beginning in 2012, the $1 to $25,000 income category has been broken into two categories. This disaggregation allows for more precise inequality estimates, but to facilitate comparisons over a longer time horizon, I decided to use the categories that existed in 2010 and 2011 throughout the entire time period. [↑](#footnote-ref-119)
120. Frank A. Cowell & Fatemeh Mehta, *The Estimation and Interpolation of Inequality Measures*, 49 Rev. Econ. Stud. 273 (1982). [↑](#footnote-ref-120)
121. I.R.S. News Release IR-2020-214 (Sept. 17, 2020), https://www.irs.gov/newsroom/irs-releases-state-by-state-breakdown-of-nearly-9-million-non-filers-who-will-be-mailed-letters-about-economic-impact-payments. [↑](#footnote-ref-121)
122. https://www.irs.gov/newsroom/irs-provides-tax-inflation-adjustments-for-tax-year-2020 ; *Poverty Thresholds*, U.S. Census Bureau, https://www.census.gov/data/tables/time-series/demo/income-poverty/historical-poverty-thresholds.html (last updated Sept. 12, 2023). [↑](#footnote-ref-122)
123. Timothy Dowd & Robert McClelland, *The Bunching of Capital Gains Realizations*, Tax Pol’y Ctr., Feb. 7, 2017, at 4, https://www.taxpolicycenter.org/publications/bunching-capital-gains-realizations/full. [↑](#footnote-ref-123)
124. The Tax Foundation reports that there was $944 billion in realized capital gains in 2018, representing 4.58% of GDP. *Federal Capital Gains Tax Collections*, *Historical Data (1954-2018)*, Tax Found. (Apr. 26, 2021), https://taxfoundation.org/data/all/federal/federal-capital-gains-tax-collections-historical-data/. [↑](#footnote-ref-124)
125. Branko Milanovic, *The Great Convergence: Global Equality and Its Discontents*, Foreign Affs. (June 14, 2023), https://www.foreignaffairs.com/world/great-convergence-equality-branko-milanovic. [↑](#footnote-ref-125)
126. Average income per adult grew from € 2,517 to € 8,313 between 1990 and 2022. *India*, World Inequality Database, https://wid.world/country/india/ (last visited Nov. 8, 2023). [↑](#footnote-ref-126)
127. *India*, World Inequality Database, https://wid.world/country/india/ (last visited Nov. 8, 2023). [↑](#footnote-ref-127)
128. Income per adult grew from € 3,092 to € 16,333 between 1990 and 2018. *China*, World Inequality Database, https://wid.world/country/china/ (last visited Nov. 8, 2023). [↑](#footnote-ref-128)
129. Over this period, the share of national inequality due to between-county inequality is relatively stable. Gaubert et al. find that variance in income inequality has grown since the 1970s. Cecile Gaubert et al., *Trends in US Spatial Inequality: Concentrating Affluence and a Democratization of Poverty*, 111 AEA Papers & Proc. 520 (2021). Consistent with this, I find an increase in the standard deviation of county Gini coefficients from 0.043 to 0.045 from 2010 to 2019. [↑](#footnote-ref-129)
130. U.S. Census Bureau; American Community Survey, 2020 American Community Survey 5-Year Estimates. [↑](#footnote-ref-130)
131. The cutoff is truncated at $250,000 in the census data. [↑](#footnote-ref-131)
132. Tony Tekaroniake Evans, *Blaine County’s Wealth Gap, Cultural Diversity are Increasing*, Idaho Mountain Express (Nov. 2, 2022), https://www.mtexpress.com/wood\_river\_journal/special\_sections/blaine-county-s-wealth-gap-cultural-diversity-are-increasing/article\_10adbd56-4a7c-11ed-8123-8b7a6a29399d.html. [↑](#footnote-ref-132)
133. *An Analysis of Senator Sanders’s Tax Proposals*, Tax Pol’y Ctr. (Mar. 19, 2020), https://www.taxpolicycenter.org/publications/analysis-senator-sanderss-tax-proposals. [↑](#footnote-ref-133)
134. *Id.* [↑](#footnote-ref-134)
135. *Distributional Analysis of the Conference Agreement for the Tax Cuts and Jobs Act*, Tax Pol’y Ctr. (Dec. 18, 2017), https://www.taxpolicycenter.org/publications/distributional-analysis-conference-agreement-tax-cuts-and-jobs-act/full. [↑](#footnote-ref-135)
136. *Forgiving Student Loans: Budgetary Costs and Distributional Impact*, Penn Wharton Budget Model, Aug. 23, 2022, https://budgetmodel.wharton.upenn.edu/issues/2022/8/23/forgiving-student-loans. [↑](#footnote-ref-136)
137. Press Release, U.S. Dep’t of Educ., Biden-Harris Administration Announces and Additional $9 Billion in Student Debt Relief (Oct. 4, 2023), https://www.ed.gov/news/press-releases/biden-harris-administration-announces-additional-9-billion-student-debt-relief. [↑](#footnote-ref-137)
138. Sylvain Catherine & Constantine Yannelis, *The Distributional Effects of Student Loan Forgiveness*, 147 J. Fin. Econ. 297 (2023); Adam Looney, *Student Loan Forgiveness is Regressive Whether Measured by Income, Education, or Wealth: Why Only Targeted Debt Relief Policies Can Reduce Injustices in Student Loans* (Brookings Hutchins Ctr. Working Paper, Paper No. 75, 2022), https://www.brookings.edu/wp-content/uploads/2022/01/WP75-Looney\_updated\_1.pdf; Prasad Krishnamurthy, *Forgiving Student Loans: Progressivity, Inequality, and Welfare* (May 2, 2023), https://papers.ssrn.com/sol3/papers.cfm?abstract\_id=4436493. [↑](#footnote-ref-138)
139. *Federal Student Loan Payment Pause: Budgetary Effect and Distributional Impact*, Penn Wharton Budget Model, Feb. 3, 2023, https://budgetmodel.wharton.upenn.edu/estimates/2023/2/3/federal-student-loan-payment-pause. I use the distributional estimates of the “current law” alternative. [↑](#footnote-ref-139)
140. Much of this discussion is based on what Wallace Oates refers to as the “first generation” fiscal federalism literature. This literature also recognizes a primary role for national government in macroeconomic policy. Wallace E. Oates, *Toward a Second-Generation Theory of Fiscal Federalism*, 12 Int’l Tax & Pub. Fin. 349, 351 (2005). [↑](#footnote-ref-140)
141. Some public goods may have positive (negative) spillover effects on other jurisdictions, in which case there may be a role for a central government to subsidize (tax) the provision of that good. [↑](#footnote-ref-141)
142. The sharp prediction about sorting by income levels is not borne out in practice, a fact that can be explained by heterogeneity in redistributive preferences. Dennis Epple & Glenn J. Platt, *Equilibrium and Local Redistribution in an Urban Economy When Households Differ in Both Preferences and Incomes*, 43 J. Urban Econ. 23 (1998). [↑](#footnote-ref-142)
143. For evidence about this “Tiebout hypothesis” *see* Paul W. Rhode & Koleman S. Strumpf, *Assessing the Importance of Tiebout Sorting: Local Heterogeneity from 1850 to 1990*, 93 Am. Econ. Rev. 1648 (2003). [↑](#footnote-ref-143)
144. Wallace E. Oates, *Toward a Second-Generation Theory of Fiscal Federalism*, 12 Int’l Tax & Pub. Fin. 349, 351 (2005). [↑](#footnote-ref-144)
145. For example, the central government could create place-based subsidies. For recent work in this area, see, e.g., Michelle D. Layser, *How Place-Based Tax Incentives Can Reduce Geographic Inequality*, 74 Tax L. Rev. 1 (2020); Cecile Gaubert, Patrick Kline & Danny Yagan, *Place-Based Redistribution*, Nat’l Bureau of Econ. Rsch. Working Paper No. 28337, (2021); Enghin Atalay, et al., *Micro-and Macroeconomic Impacts of a Place-Based Industrial Policy*. NBER No. w31293. (2023). [↑](#footnote-ref-145)
146. Professor Brooks emphasizes that progressive taxes have an insurance function as well as a redistributive function, suggesting that there may be a limited role for states in redistribution but that the insurance role should be federal. John R. Brooks II, *Fiscal Federalism as Risk-Sharing: The Insurance Role of Redistributive Taxation*, 68 Tax L. Rev. 89 (2014). [↑](#footnote-ref-146)
147. John Ashworth, Bruno Heyndels & Carine Smolders, *Redistribution as a Local Public Good: An Empirical Test for Flemish Municipalities*, 55 Kyklos 27, 27 (2002) (“The fiscal federalism literature provides a framework for assigning responsibilities to different levels of government. The orthodox view is that income redistribution should be centralised.”). *See* Helen F. Ladd & Fred C. Doolittle, *Which Level of Government Should Assist the Poor?*, 35 Nat’l Tax J. 323 (1982) (confirming the view that the federal government should take primary responsibility for the poor). [↑](#footnote-ref-147)
148. Fiscal decentralization could also change the growth rates of national and local economies. Empirical evidence in this area is mixed. *Compare* Hamid Davoodi & Heng-fu Zou, *Fiscal Decentralization and Economic Growth: A Cross-Country Study*, 43 J. Urban Econ. 244 (1998) *with* Ulrich Thiessen, *Fiscal Decentralisation and Economic Growth in High‐Income OECD Countries*, 24 Fiscal Stud. 237 (2003). For theory, see Wallace E. Oates, *Fiscal Decentralization and Economic Development*, 46 Nat’l Tax J. 237 (1993); Jan K. Brueckner, *Fiscal Federalism and Economic Growth*, 90 J. Pub. Econ. 2107 (2006). [↑](#footnote-ref-148)
149. For empirical evidence that mobility decisions of the poor are influenced by local redistributive policy, *see* Paul E. Peterson & Mark Rom, *American Federalism, Welfare Policy, and Residential Choices*, 83 Am. Pol. Sci. Rev. 711 (1989). [↑](#footnote-ref-149)
150. Charles C. Brown & Wallace E. Oates, *Assistance to the Poor in a Federal System*, 32 J. Pub. Econ. 307 (1987). Professor Liscow argues that federal funding of schools (or redistribution generally) reduces the incentive for the rich to move. Zachary D. Liscow, *The Efficiency of Equity in Local Government Finance*, 92 N.Y.U. L. Rev. 1828 (2017). [↑](#footnote-ref-150)
151. Traviss Cassidy, Mark Dincecco & Ugo Antonio Troiano, *The introduction of the income tax, fiscal capacity, and migration: evidence from US States*, 16.1 Am. Econ. J.: Econ. Pol’y 359 (2024) (“We show that the introduction of the income tax in the post–World War II era induced significant out-migration to states that did not have the income tax… middle- and high- earning households were the most likely to leave after the income tax was introduced.”) [↑](#footnote-ref-151)
152. Joshua Rauh & Ryan Shyu, *Behavioral responses to state income taxation of high earners: evidence from California*, 16.1 Am. Econ. J.: Econ. Pol’y 34 (2024). (“for those earning over $5 million, the rate of departure spiked from 1.5 percent after the 2011 tax year to 2.125 percent after the 2012 tax year, with a similar effect among taxpayers earning $2 million–$5 million in 2012.”). [↑](#footnote-ref-152)
153. Galle et al. think it is feasible because the empirical case for mobility is weak. Brian D. Galle, David Gamage & Darien Shanske, *Money Moves: Taxing the Wealthy at the State Level*, Cal. L. Rev. (Forthcoming, 2024). [↑](#footnote-ref-153)
154. David R. Agrawal & Kenneth Tester, *State Taxation of Nonresident Income and the Location of Work*, 16.1 Am. Econ. J.: Econ. Pol’y 447 (2024). [↑](#footnote-ref-154)
155. Pauly, *supra* note []. [↑](#footnote-ref-155)
156. There is some evidence that people are more supportive of redistribution when they are in closer proximity to the beneficiaries of that redistribution. John Ashworth, Bruno Heyndels & Carine Smolders, *Redistribution as a Local Public Good: An Empirical Test for Flemish Municipalities*, 55 Kyklos 27 (2002) (more taste for redistribution in smaller political units); Joel H. Suss, *Higher Income Individuals Are More Generous when Local Economic Inequality is High*, 18 PLoS ONE e0286273 (2023) (higher income individuals are more generous when local income inequality is high); *cf.* Clayton P. Gillette, *Local Redistribution, Living Wage Ordinances, and Judicial Intervention*, 101 Nw. U.L. Rev. 1057 (2007). [↑](#footnote-ref-156)
157. Pauly, *supra* note []. [↑](#footnote-ref-157)
158. Jan K. Brueckner & Kangoh Lee, *Spatially-Limited Altruism, Mixed Clubs, and Local Income Redistribution* (Univ. of Ill., Urbana-Champaign, Bureau of Econ. & Bus. Rsch. Faculty Working Paper, Paper No. 1406, 1987). The effect of local heterogeneity on redistributive preferences is mixed. *Compare* Erzo F.P. Luttmer, *Group Loyalty and the Taste for Redistribution*, 109 J. Pol. Econ. 500, 519 (2001) (“support for redistribution declines as [racial] heterogeneity increases”), *with* Leah Boustan, Fernando Ferreira, Hernan Winkler & Eric M. Zolt, *The Effect of Rising Income Inequality on Taxation and Public Expenditures: Evidence from U.S. Municipalities and School Districts, 1970–2000*, 95 Rev. Econ. & Stat. 1291 (2013) (increasing income inequality can increase support for public goods). Luttmer finds that there is a strong effect of exposure to welfare recipients on support for welfare, but that there is also strong racial group loyalty, so that support for welfare increases as the share of welfare recipients from one’s own race increases. Luttmer, *supra*. [↑](#footnote-ref-158)
159. John B. Burbidge & Gordon M. Myers, *Redistribution Within and Across the Regions of a Federation*, Canadian J. Econ. 620 (1994). [↑](#footnote-ref-159)
160. *See* Brueckner & Lee, *supra* note 155. [↑](#footnote-ref-160)
161. David E. Wildasin, *Income Redistribution in a Common Labor Market*, 81 Am. Econ. Rev. 757 (1991). Professor Kades proposes a federal income tax credit that phases out with income to undo state tax regressivity. Eric Kades, *Giving Credit Where Credit is Due: Reducing Inequality with a Progressive State Tax Credit*, 77 La. L. Rev. 359 (2016). [↑](#footnote-ref-161)
162. For recent commentary, *see, e.g.,* Daniel J. Hemel, *Easy on the SALT: A Qualified Defense of the Deduction for State and Local Taxes* (October 28, 2017). University of Chicago Coase-Sandor Institute for Law & Economics Research Paper No. 826, U of Chicago, Public Law Working Paper No. 652, Available at SSRN: https://ssrn.com/abstract=3061096 or <http://dx.doi.org/10.2139/ssrn.3061096>; Brian Galle, *Federal Fairness to State Taxpayers: Irrationality, Unfunded Mandates, and the Salt Deduction*, 106 Mich. L. Rev. 805 (2008); Daniel Hemel, *The Death and Life of the State and Local Tax Deduction*, 72 Tax L. Rev. 151 (2019). [↑](#footnote-ref-162)
163. Bruce Bartlett, *Reagan’s Tax Revolution: Ending the Free Ride for State and Local Taxes*, June 14, 1985, available at https://www.heritage.org/taxes/report/reagans-tax-revolution-ending-the-free-ride-state-and-local-taxes [↑](#footnote-ref-163)
164. Patrick Driessen writes that the SALT deduction is “shown myopically in typical distribution tables.” Patrick Driessen, *A progressive case for a federal salt deduction*, Tax Notes (May 27, 2024). Metcalf acknowledges that “Focusing on the distribution in isolation may not provide a complete picture of the distributional impact of ending deductibility. To the extent that state and local spending is directed toward services disproportionately utilized by lower income households, the regressivity of the deduction may be overstated.” Gilbert E. Metcalf, *Assessing the Federal Deduction for State and Local Tax Payments*, 64:2 Nat’l Tax J. 565, 566 (2011). For a study of the distribution of the federal SALT deduction at the local level, complicating the conventional view that the deduction just favors “blue states”, *see* Manoj Viswanathan, *Hyperlocal Responses to the SALT Deduction Limitation*, 71 Stan. L. Rev. Online 294 (2018). On the distributional effect at the state level, as favoring the rich and rich states, see Bartlett, *supra*. [↑](#footnote-ref-164)
165. *See, e.g.,* Martin S. Feldstein & Gilbert E. Metcalf, *The effect of federal tax deductibility on state and local taxes and spending*, 95.4 J. Pol. Econ. 710 (1987); Douglas Holtz-Eakin & Harvey S. Rosen, *Tax Deductibility and Municipal Budget Structure*, In Rosen, Harvey S. (ed.), Fiscal Federalism: Quantitative Studies, 107-136 (1988); Mary N. Gade & Lee C. Adkins, *Tax Exporting and State Revenue Structure*, 43.1 Nat’l Tax J. 39 (1990). [↑](#footnote-ref-165)
166. Gilbert E. Metcalf, *Tax exporting, federal deductibility, and state tax structure*, 12 J. Pol’y Analysis & M’gmt 109 (1993). Ending deductibility may make states move from deductible taxes to nondeductible fees and taxes. Metcalf, *supra* note 164; Bradley T. Heim & Yulianti Abbas, *Does Federal Deductibility Affect State and Local Revenue Sources*, 68.1 Nat’l Tax J. 33 (2015) (More sales taxes when they become deductible.) Howard Chernick, *On the Determinants of Subnational Tax Progressivity in the U.S.*, 58.1 Nat’l Tax J. 93, 108 (2005) (“The magnitude of the effect implies that eliminating or curtailing the deductibility of state and local taxes would substantially reduce the progressivity of subnational tax system.”) In one recent study, David Coyne finds that a 1 percent rise in tax price lowers the local use of deductible taxes by about 3.5 percent... It finds an associated change in local expenditures of about -2.1 percent.” David Coyne, *Unmasking Local Fiscal Responses to Federal Tax Deductibility*, 70.2 Nat’l Tax J. 223, 227 (2017). Coyne also finds that cuts in deduction would not disproportionately harm counties with more poor residents. Id. at 225. [↑](#footnote-ref-166)
167. Chernick, *supra* note 166 at 108. The deduction is regressive at the federal level but supports progressive taxes at the subnational level. Metcalf, *supra* note 164 at 588. [↑](#footnote-ref-167)
168. Professor Stark argues that the SALT deduction encourages local tax progressivity, but that it would be better for redistribution to take place at the federal level as the fiscal federalism literature counsels. Kirk J. Stark, *Fiscal Federalism and Tax Progressivity: Should the Federal Income Tax Encourage State and Local Redistribution*, 51 UCLA L. Rev. 1389 (2004). Professor Gladriel Shobe argues that the SALT encourages economic segregation. Gladriel Shobe, *Subsidizing Economic Segregation Through the State and Local Tax Deduction*, 11 U.C. Irvine L. Rev. 539 (2020). Professor Hemel argues in support of the SALT deduction as a “subsidy for civic institutions that strengthen the democratic fabric.” Daniel Hemel, *The Death and Life of the State and Local Tax Deduction*, 72 Tax L. Rev. 151, 152 (2019); *see also* Andrew Hayashi, *Christianity and the Liberal(ish) Income Tax*, Notre Dame J. L. Ethics & Pub. Pol’y (forthcoming 2024). [↑](#footnote-ref-168)
169. Timothy Vermeer, *State Individual Income Tax Rates and Brackets for 2023*, Tax Found. (Feb. 21, 2023), https://taxfoundation.org/data/all/state/state-income-tax-rates-2023/. [↑](#footnote-ref-169)
170. Ruth Mason, *Delegating Up: State Conformity with the Federal Tax Base*, 62 Duke L.J. 1267 (2013). Nevertheless, Professor Mason concludes that administrative and compliance benefits make it unlikely for this to change anytime soon. On conformity issues with tax elections, *see* Heather M. Field, *Binding Choices: Tax Elections & Federal/State Conformity*, 32 Va. Tax Rev. 527 (2013). Professor Shaviro argues that states should be encouraged to share the tax base with the federal government and that their discretion should be limited to rate-setting. Daniel Shaviro, *An Economic and Political Look at Federalism in Taxation*, 90 Mich. L. Rev. 895 (1992). [↑](#footnote-ref-170)
171. Ruth Mason, *Federalism and the Taxing Power*, Calif. L. Rev. 975 (2011). [↑](#footnote-ref-171)
172. Daniel J. Hemel, *Federalism as a Safeguard of Progressive Taxation*, 93 N.Y.U. L. Rev. 1 (2018). [↑](#footnote-ref-172)
173. Timothy Besley & Stephen Coate, *Centralized Versus Decentralized Provision of Local Public Goods: A Political Economy Approach*, 87 J. Pub. Econ. 2611 (2003). [↑](#footnote-ref-173)
174. For the role of block grants to help with distorted migration patterns, see Frank Flatters, Vernon Henderson & Peter Mieszkowski, *Public Goods, Efficiency, and Regional Fiscal Equalization*, 3 J. Pub. Econ. 99 (1974). [↑](#footnote-ref-174)
175. Robin Boadway, Maurice Marchand & Marianne Vigneault, *The Consequences of Overlapping Tax Bases for Redistribution and Public Spending in a Federation*, 68 J. Pub. Econ. 453 (1998). Professors Gamage and Shanske call this effect “tax cannibalization.” David Gamage & Darien Shanske, *Tax Cannibalization and Fiscal Federalism in the United States*, 111 Nw. U. L. Rev. 295 (2017). [↑](#footnote-ref-175)
176. Robert A. Schapiro, *States of Inequality: Fiscal Federalism, Unequal States, and Unequal People*, 108 Calif. L. Rev. 1531 (2020). [↑](#footnote-ref-176)
177. *See, e.g*., Kirk J. Stark, *Rich States, Poor States: Assessing the Design and Effect of a U.S. Fiscal Equalization Regime*, 63 Tax L. Rev. 957 (2010). For a paper on theories supporting federal aid to states, see David A. Super, *Rethinking Fiscal Federalism*, 118 Harv. L. Rev. 2544 (2005). But on the effects of equalization payments in inefficiency, see Michael Smart, *Taxation and Deadweight Loss in a System of Intergovernmental Transfers*, 31 Canadian J. Econ. 189 (1998). [↑](#footnote-ref-177)
178. Brian Highsmith, *The Implications of Inequality for Fiscal Federalism (Or Why the Federal Government Should Pay for Local Public Schools)*, 67 Buff. L. Rev. 407 (2019). Highsmith asserts that “consumption choices are not bound to a specific geographic area—and the cumulative economic effects of inequality are thus uncertain with respect to geography” but that they are “certainly biased in the direction of concentration.” *Id.* at 417. Although Highsmith’s intention is to “shift away from *centralization* debate…and towards the size of the fiscal unit,” the implication of his argument would seem to be that the best fiscal unit for redistribution is the central government. *See id.* at 420*.* [↑](#footnote-ref-178)
179. Ladd & Doolittle, *supra* note 149 at 328. [↑](#footnote-ref-179)
180. Having a below-average income in one’s reference group negatively affects well-being. Ada Ferrer-i-Carbonell, *Income and Well-being: An Empirical Analysis of the Comparison Income Effect*, 89 J. Pub. Econ. 997 (2005). [↑](#footnote-ref-180)
181. Professors Persky and Tam have proposed a national social welfare function that reflects a weighted average of local inequality measures. Joseph Persky & Mo‐Yin Tam, *Local Status and National Social Welfare*, 30 J. Reg’l Sci. 229 (1990). [↑](#footnote-ref-181)
182. S. Anand & A.K. Sen, *Concepts of Human derivation and poverty: a multidimensional perspective*, United Nations: Poverty and Human Development: Human Development Papers (1997). Following Anand and Sen, we can observe a couple of properties of the composite inequality index. First, it is between the lowest and the highest values of the component indices, and as , it approaches the maximum component index. The index is homogeneous of degree 1 in the component indices and it is increasing at an increasing rate in each individual index. The constant elasticity of substitution between subindices is . [↑](#footnote-ref-182)
183. Persky & Tam, *supra* note 174. In motivating their local social welfare functions, they consider only local status comparisons. [↑](#footnote-ref-183)
184. Ariel Jurow Kleiman, *Low-End Regressivity*, 72 Tax L. Rev. 1 (2018). [↑](#footnote-ref-184)
185. *Cf*. David Kamin, *Reducing Poverty, Not Inequality: What Changes in the Tax System Can Achieve*, 66 Tax L. Rev. 593 (2013); Martin Feldstein, *Reducing Poverty, Not Inequality*, 137 Pub. Interest 33 (1999). [↑](#footnote-ref-185)
186. *Cf*. Brian Cushing & Jacques Poot, *Crossing Boundaries and Borders: Regional Science Advances in Migration Modelling*, 83 Papers in Reg’l Sci. 317, 320 (2004) (“the literature’s broad consensus is that migration results from forward-looking behaviour that aims to maximise an individual or household’s expected well-being over some time horizon by means of relocation”). [↑](#footnote-ref-186)
187. Christian Bayer & Falko Juessen, *On the Dynamics of Interstate Migration: Migration Costs and Self-Selection*, 15 Rev. Econ. Dynamics 377, 378 (2012). [↑](#footnote-ref-187)
188. Cushing & Poot, *supra* note 169 [↑](#footnote-ref-188)
189. Cushing & Poot, *supra* note 169 at 321. [↑](#footnote-ref-189)
190. Geographic location has important effects on social mobility. Raj Chetty & Nathaniel Hendren, *The Impacts of Neighborhoods on Intergenerational Mobility I: Childhood Exposure Effects*, 133 Q.J. Econ. 1107 (2018). Geographica mobility for low-income households is aided by financial and home search assistance. Peter Bergman, Raj Chetty, Stefanie DeLuca, Nathaniel Hendren, Lawrence F. Katz & Christopher Palmer, *Creating Moves to Opportunity: Experimental Evidence on Barriers to Neighborhood Choice* (Nat’l Bureau of Econ. Rsch., Working Paper No. 26164, 2023). [↑](#footnote-ref-190)
191. George J. Borjas, Stephen G. Bronars & Stephen J. Trejo, *Self-Selection and Internal Migration in the United States*, 32 J. Urban Econ. 159 (1992). [↑](#footnote-ref-191)
192. Tamim Bayoumi & Jelle Barkema, *Stranded!: How Rising Inequality Suppressed US Migration and Hurt Those “Left Behind*, (IMF Working Paper No. WP/19/122, 2019). For a discussion, *see* David Schleicher, *Stuck! The Law and Economics of Residential Stagnation*, 127 Yale L. J. 78 (2017). [↑](#footnote-ref-192)
193. Christian Bayer & Falko Juessen, *On the Dynamics of Interstate Migration: Migration Costs and Self-Selection*, 15 Rev. Econ. Dynamics 377, 378 (2012). [↑](#footnote-ref-193)
194. Bayoumi & Barkema, *supra* note 183. [↑](#footnote-ref-194)
195. Peter Ganong & Daniel Shoag, *Why has Regional Income Convergence in the US Declined?*, 102 J. Urban Econ. 76 (2017) (increase in home prices in high-income areas has reduced the return to migration for lower-income workers). [↑](#footnote-ref-195)
196. People seek out others of similar incomes, races and ethnicities. Don E. Albrecht & Sean-Shong Hwang, *Neighborhood Selection and Residential Segregation*, 61 Socio. Inquiry 199 (1991). The effects of racial preferences on patterns of residential segregation vary by income and education. William A.V. Clark, *Changing Residential Preferences Across Income, Education, and Age: Findings from the Multi-City Study of Urban Inequality*, 44 Urb. Affs. Rev. 334 (2009). People become more willing to move into integrated neighborhoods as their income and education increase, although African-Americans prefer not to be a racial minority. William A.V. Clark, *Changing Residential Preferences Across Income, Education, and Age: Findings from the Multi-City Study of Urban Inequality*, 44 Urb. Affs. Rev. 334 (2009). [↑](#footnote-ref-196)
197. Mustafa Yavaş, *Dissecting Income Segregation: Impacts of Concentrated Affluence on Segregation of Poverty*, 43 J. Mathematical Socio. 1 (2019). [↑](#footnote-ref-197)
198. Yavaş, *supra* note 188. [↑](#footnote-ref-198)
199. Sako Musterd et al., *Adaptive Behaviour in Urban Space: Residential Mobility in Response to Social Distance*, 53 Urb. Stud. 227 (2016). For supporting evidence, see Wouter PC van Gent et al., *Sociocultural, Economic and Ethnic Homogeneity in Residential Mobility and Spatial Sorting Among Couples*, 51 Env’t & Plan. A: Econ. & Space 891 (2019). *But see* William AV Clark, Rachel Ong Viforj & NT Khuong Truong, *Neighbourhood Selection and Neighbourhood Matching: Choices, Outcomes and Social Distance*, 59 Urb. Stud. 937 (2022) (people don’t move to improve match). [↑](#footnote-ref-199)
200. Income segregation increased in the 1980s and then tapered from 1990 - 2014. There has also been an increase in geographic segregation by education. Ning Jia, Raven Molloy, Christopher Smith & Abigail Wozniak, *The Economics of Internal Migration: Advances and Policy Questions*, 61 J. Econ. Lit. 144 (2023) [↑](#footnote-ref-200)
201. George Galster & Lena Magnusson Turner, *Status Aversion, Attraction and Discrepancy as Drivers of Neighborhood Selection*, 18 City & Cmty. 937 (2019). On the role of status in choosing neighborhoods, *see* George Galster & Lena Magnusson Turner, *Status Discrepancy as a Driver of Residential Mobility: Evidence from Oslo*, 49 Env’t & Plan. A: Econ. & Space 2155 (2017). [↑](#footnote-ref-201)
202. For a critique and suggestions, *see, e.g.,* Deanna S. Newton, *Closing the Opportunity Gap*, 102 N.C. L. Rev. 1159 (2023). [↑](#footnote-ref-202)
203. But see tax equity act 2009-cola adjustments. [↑](#footnote-ref-203)
204. David Albouy, *The unequal geographic burden of federal taxation*, 117.4 J. Pol. Econ. 635, 636 (2009). [↑](#footnote-ref-204)
205. *Id.* at 636-7. [↑](#footnote-ref-205)
206. *Id.* at 636 (citing the 2006 Tax Foundation Report). The deduction for SALT mitigates some of this effect. [↑](#footnote-ref-206)
207. See also https://www.nytimes.com/2011/11/12/your-money/taxes/tax-burdens-tilt-coastal-and-systems-fairness-is-debated.html [↑](#footnote-ref-207)
208. Branko Milanovic, *The Great Convergence: Global Equality and Its Discontents*, Foreign Affs. (June 14, 2023), https://www.foreignaffairs.com/world/great-convergence-equality-branko-milanovic. [↑](#footnote-ref-208)