Pulling Apart

Wisconsin's Growing Income Inequality

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Center on Wisconsin Strategy
Wisconsin Council on Children & Families

Research Methodology for Pulling Apart

Pulling Apart: Wisconsin's Growing Income Inequality is based on *Pulling Apart, a State-by-State Analysis of Income Trends* published by the Center on Budget and Policy Priorities and the Economic Policy Institute.

Pulling Apart, a State-by-State Analysis of Income Trends assesses how families at different income levels in each state have fared over the past two decades, this report measures income inequality at three points in time: the early 1980s, the early 1990s, and the early 2000s. These periods reflect comparable points in the economic cycle — namely, when the economy was in a recession. All families are ranked by family income (adjusted for family size) and then divided into five groups (or "quintiles"), each containing the same number of persons. The average income of families in each quintile is then calculated for each of the three time periods.

The data source for this analysis is the Bureau of the Census's March Current Population Survey — a survey of a nationally representative sample of households conducted every year. The survey provides information on family income, which includes not only wages and salaries, but also other sources of cash income such as interest income and cash benefits, including veterans' assistance, welfare payments, and child support income. The starting point is the official Census definition of cash income. This analysis then uses additional Census Bureau data to construct a more comprehensive measure of income. The measure used here accounts for the impact of the federal tax system (including the Earned Income Tax Credit) and the cash value of food stamps, subsidized school lunches, and housing vouchers. Income from capital gains is also included. The incomes shown are adjusted for inflation and expressed as their value in 2002 dollars.

This study is based on three year averages of income data for each of the states. The use of three year averages is necessary in order to have a large enough sample to accurately estimate average income for each of the five income groups for each state.

This Analysis Understates Growth in Inequality

For two main reasons, the results understate the magnitude of growth in inequality over the last two decades. First, the Census Bureau data do not capture trends among the top one percent of families. Data from other sources such as the Congressional Budget Office show that the growth in the incomes of the top quintile was especially rapid at the very top of the income scale. Second, this analysis found higher income growth for the bottom fifth than other studies of the last two decades. This results from the starting point for this trend over time — the average incomes for 1980, 1981 and 1982. These were particularly bad years for low-income families as they were hit harder by the economic downturn of the early 1980s than by subsequent recessions. The fact that we're starting our analysis of income growth from this uniquely low base means that we are likely to record particularly strong growth rates for the lowest-income families.

To read the complete national study published by the Center on Budget and Policy Priorities and the Economic Policy Institute study please visit www.epi.org/content.cfm/studies_pulling_apart_2006.

Pulling Apart

Wisconsin's Growing Income Inequality

Inequality continues to grow in the United States, producing an ever-widening chasm between the rich and the poor. Though consistently more equal than other states, Wisconsin does not stand apart from this trend. Indeed, over the last two decades, Wisconsin's richest residents experienced dramatic increases in income, while gains for middle and lower income Wisconsinites were sluggish. In this report, we provide an overview of recent analysis by the Economic Policy Institute and the Center on Budget and Policy Priorities. Their report, *Pulling Apart, a State-by-State Analysis of Income Trends*, shows that from the early 1980s (1980–82) to the early 2000s (2001–03), the average real income of the lowest-income families in Wisconsin grew by just 14 percent, while the average real income of the highest-income families grew nearly four times as fast, up 48 percent.

Pulling Apart, a State-by-State Analysis of Income Trends, released January 26, 2006 by the Economic Policy Institute and the Center on Budget and Policy Priorities, analyzes trends in income and inequality within each state over the last two decades. Using Current Population Survey data from the U.S. Census Bureau, they track earnings changes for households (two or more related people living together) in each income "quintile" (20 percent) of the state's population. Here we focus on their results for Wisconsin.

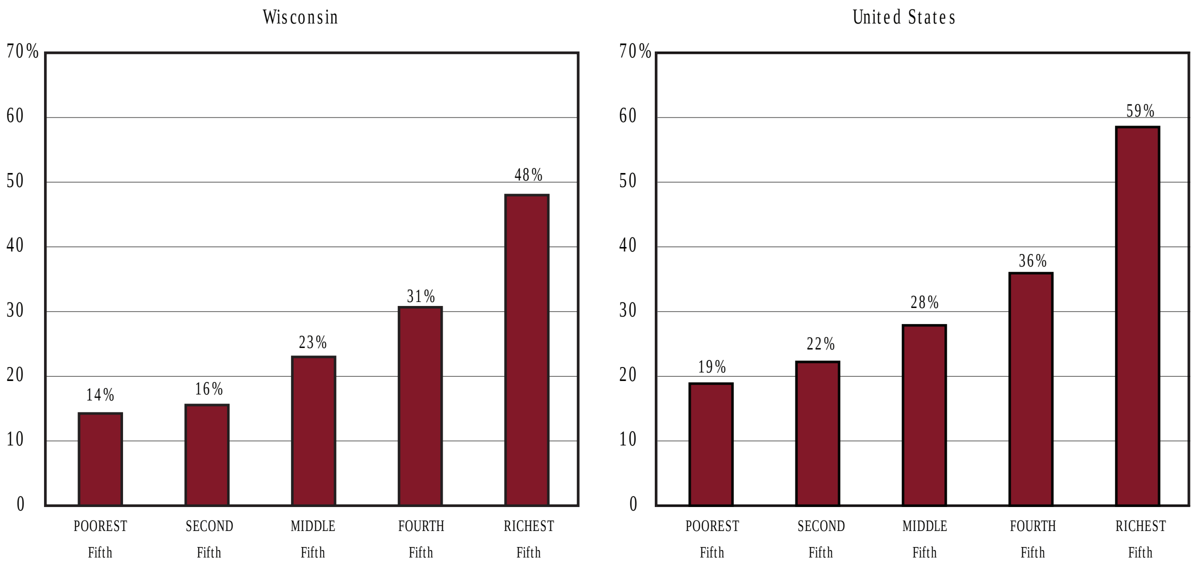
Figure 1 summarizes the income trends for Wisconsin and the United States. Growing inequality is clear across the income spectrum. Wisconsin's poorest residents have gained the least income over the past two decades, and our richest residents have made the greatest strides forward in income. In the last twenty years, economic growth has not lifted the fortunes of all equally. Up until the early 1980s, economic growth secured income growth for families across the spectrum. The current inequality trend directly contradicts the pattern for previous generations in this state and nation.

Wisconsin has traditionally prided itself on its relatively high level of equality, and it still can. Even with this growth in inequality, only three states have a more equal distribution of income. But over the past two decades, the benefits of the state's economic growth have been increasingly concentrated on our wealthiest residents. Our proud legacy of equality, and the joint commitment to building a strong state which that equality helped undergird, is in serious and troubling decline. Together, we need to pursue strategies to ensure that WIsconsin's economic growth is more widely shared. As the national authors point out:

> Halting and then reversing this trend is the only fair path. A widening gulf between the rich on the one hand and the poor and middle class on the other hand can reduce social cohesion, trust in government and other institutions, and participation in the democratic process. Growing income inequality also has widened discrepancies in political influence — a particular problem given political candidates' heavy dependence on private contributions. This may have contributed to the increase in the number of Americans who feel that their elected officials do not care much about the views of ordinary citizens.

Figure 1

Pulling Apart
Income Change Early 1980s to Early 2000s, by Income Quintile



Source: *Pulling Apart*, Economic Policy Institute and Center on Budget and Policy Priorities, 2006.

Increasing Inequality from the Late 1970s

Trends in average real (inflation adjusted) income for each fifth of the income distribution provide a good yardstick for measuring inequality. The national story of increasing inequality is well documented and is illustrated in Figure 1: from the early 1980s to the early 2000s, the average real income of the poorest fifth of families grew by $2664, or 19 percent. (Throughout the report, all income values are inflation adjusted and expressed in 2002 dollars.) Over that same period, the richest fifth of families experienced a 59 percent income increase ($45,101 annually). At the very top of the income distribution the story is more extreme; income rose by 85 percent for the richest five percent.

Wisconsin mirrors these national trends (Figure 1 and Table 1). From the early 1970s to the early 2000s, the average real income of Wisconsin families in the bottom fifth of earnings grew only 14 percent (or $2519) to $20,197. At the same time, families in the top income quintile saw their average income rise 48 percent ($36,000), to $110,653. The average income of the top five percent of the state's residents has grown to $174,919.

Income trends at the middle of the income distribution in Wisconsin are a bit better than those at the bottom, but still less than half the gains at the top. For the middle fifth of families, real income grew 23 percent (up $9,343) to $49,327. Middle income families made progress, but the state's richest families sprinted forward.

Figure 2 shows the increases in income inequality in Wisconsin for all income quintiles. Most disturbing, the picture shows increasing inequality in the last ten years, in spite of the strength of Wisconsin's economy in the 1990s.

Table 1

Wisconsin Family Income Trends

Average Family Income Early 1980s to Early 2000s

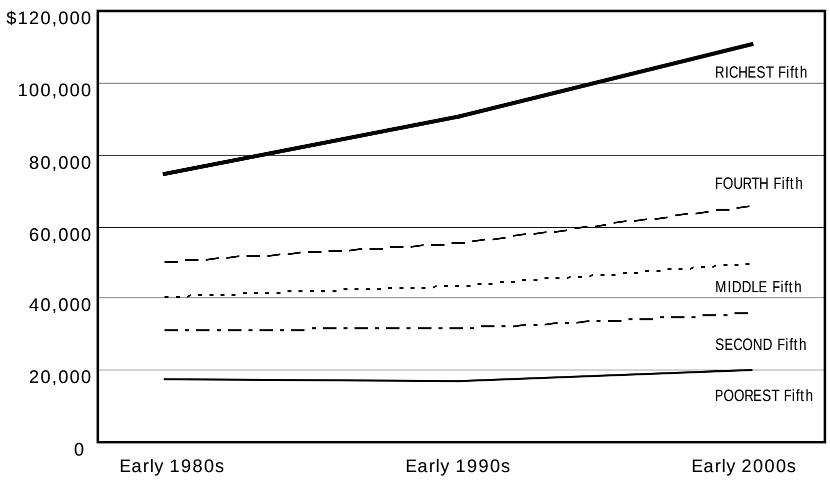
	Early 1980s	Early 1990s	Early 2000s	Percent Change, 1980s–2000s	Percent Change, 1990s–2000s
Richest Fifth	74,653	90,472	110,653	48%	22%
Middle Fifth	39,984	43,201	49,327	23	14
Poorest Fifth	17,677	17,213	20,197	14	2

Source: *Pulling Apart*, Economic Policy Institute and Center on Budget and Policy Priorities, 2006.

Figure 2

Average Wisconsin Family Income Late 1970s to Late 1990s, by Income Quintile

(2002 Dollars)



Source: *Pulling Apart*, Economic Policy Institute and Center on Budget and Policy Priorities, 2006.

Wisconsin's Income Inequality Catching Up to Neighboring States

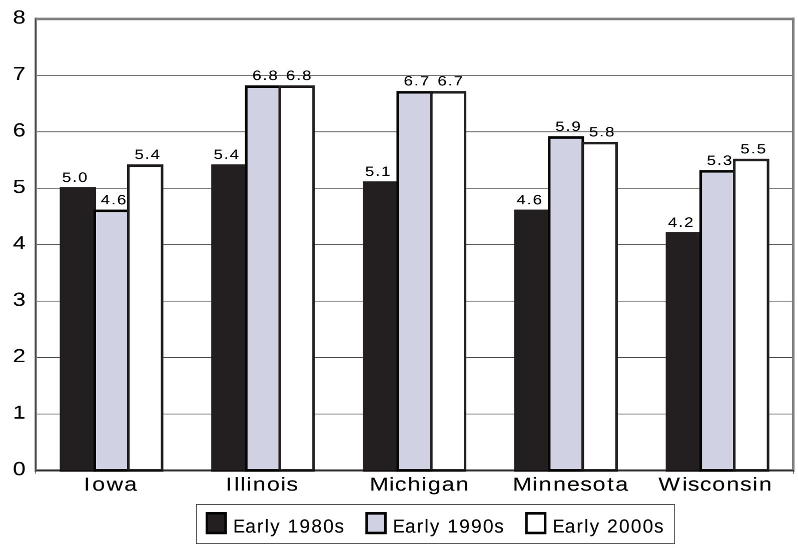
Wisconsin has traditionally had among the lowest levels of income inequality in the nation. Even after posting increases in inequality over the last twenty years, only three states have more equal income distribution. This is good news.

While Wisconsin has historically been a national leader in terms of income equality, the recent trends have narrowed the Wisconsin advantage over neighboring states. Figure 3 shows the ratio of the income of the richest fifth of families to the poorest fifth of families. In the early 1980s, Wisconsin and Minnesota posted the most equal income distribution, with the income of the richest fifth of families at just over four times the income of the poorest fifth of families. At that time, Illinois posted the most unequal income distribution; their richest families brought in 5.4 times the income of the poorest families in the state. Inequality has grown throughout the Midwest, and Wisconsin is no exception.

Figure 3

Inequality in the Midwest

Ratio of Richest to Poorest Income Quintiles



Source: *Pulling Apart*, Economic Policy Institute and Center on Budget and Policy Priorities, 2006.

Causes of the Growing Income Inequality

Across the nation, wage inequality is the single most important cause of increasing income inequality. Wages of those at the bottom of the income distribution have fallen or grown sluggishly over the last generation. Wage increases have been concentrated on those with the highest wages in the first place. Additionally, wage disparity between races and people of different educational levels is growing.

Wages in Wisconsin are also becoming more unequal, both within and between groups. *The State of Working Wisconsin, 2004* (Center on Wisconsin Strategy), shows that in 2003 the median wages of college graduates were much higher than those of high school graduates. This gap has markedly increased since 1979. For men, the wage differential was better than 40 percent in 2003, up from less than 14 percent in 1979. For women, this differential was 41 percent in 2003, compared to 29 percent in 1979. Wage inequality by race in Wisconsin is considerable as well. In 2003, white men's median wages were 45 percent higher than black men's. For women, the corresponding gap was 19 percent.

The increase in wage inequality within and between groups has been substantial, and a number of factors are to blame. As the EPI/CBPP report points out:

> Several factors have contributed to increasing wage inequality, including long periods of high unemployment, globalization, the shrinkage of manufacturing jobs and the expansion of low-wage service jobs and immigration, as well as the lower real value of the minimum wage and fewer and weaker unions. These factors have led to an erosion of wages for workers with less than a college education. ... More recently, even those with a college education have experienced real wage declines, in part due to the bursting of the tech bubble in high-wage industries, but also due to the downward pressure on wage growth from offshore competition.

These trends have been as clearly documented for Wisconsin as they have for the nation (see *The State of Working Wisconsin, 2004*). While immigration has had less influence here than in some other states, the expansion of low wage service jobs and the decline in union density — Wisconsin union membership fell from 24 percent of the labor force in the early 1980s to just 16 percent in 2003 — have certainly contributed to the increase in wage inequality.

Income disparity also results from the growing importance of income derived from capital, such as rental income, interest, dividends and capital gains. Because a small — and well-off — portion of the population holds assets, increasing returns to those assets pushes income inequality up.

Black/White Inequality Extremely High in Wisconsin

The income disparity between the rich and the poor in the state is among the smallest in the nation. But that does not mean that Wisconsin has strong equality on all measures. In fact, our black/white inequality is consistently among the worst in the nation. The State of Working Wisconsin, 2004 identified a series of indicators where Wisconsin posts shocking levels of racial disparity. Indicators showing strong black/white disparity include poverty, child poverty, unemployment, education, and incarceration.

In July of 2005, an online journal, *The Black Commentator*, named Wisconsin the worst state in the nation for blacks.

Wisconsin Can Choose a Different Course

Wisconsin's economy has consistently been one of the most equal in the nation, and this is a source of pride for state residents. This report makes clear that Wisconsin remains among the most equal states in the nation, but our inequality is fading.

While there is no magic bullet to rectify the situation — any more than there was a single cause — a number of steps can be taken to put Wisconsin on a course of continued high levels of economic equality.

Build the Skills and Education of Wisconsin's Workforce

Employers in the state frequently speak of the need to tap into an increasingly skilled workforce. Likewise, many workers have to retool their skills and knowledge to match the changing nature of existing and newly created jobs. State and local governments in Wisconsin can help workers and employers alike by increasing the focus within the workforce development system on educational attainment and skill development.

Education and skill development can improve wages, productivity, and the state's competitive position.

Wisconsin can help lower income adults advance their education and improve their chances of climbing the economic ladder — and at the same time help employers find badly needed skilled workers — by:

- increasing need-based financial aid for higher education to cover increasing tuition;
- maintaining a strong vocational education system, and ensuring that the system is a key partner in the state's workforce development system;
- putting a much greater emphasis on the most effective education and job training services within the W-2 program;
- ensuring that a significant proportion of Workforce Investment Act resources go toward training in skill shortage areas; and
- increasing state investment in basic adult literacy for the workplace and our communities.

Make Work Pay and Support Working Families

State government can help lessen the burden of income inequality by carefully structuring benefits to lower-income families to ensure that work pays. Wisconsin has historically been relatively generous in the benefits it provides and has been a leader in developing policies to make work pay. For example, Wisconsin was one of the first states to establish a refundable earned income tax credit for working parents. Yet the tax and benefits structure in Wisconsin makes it difficult for low-income families to work their way out of poverty. In fact, Wisconsin's poverty rate is actually growing faster than any other state in nation according to the most recently available US Census Bureau data.

Wisconsin's Governor recently proposed an "Affordability Agenda" which includes a "Living Wage Tax Credit" to help families who work full-time escape the grasp of poverty and to help families pay for health insurance, heating bills and education. It is an important agenda aimed at helping low and middle-income residents work and learn their way out of poverty. Such an agenda deserves attention and consideration from the legislature.

A study by the Public Policy Forum (*Making Work Pay in Wisconsin: An Update,* August, 2000) examined the impact of state benefit and tax policies on low-income families in Wisconsin. The report concluded that the combined effects of taxes, loss of benefits such as food stamps, and increased co-payments for child care make it very difficult for parents to climb the economic ladder out of poverty. In conjunction with exploring and pursuing recent proposals such as the Governor's "Affordability Agenda", the state should examine the relationships between public assistance programs and strive to find ways to ensure that low-income parents get ahead as they earn increased wages or work longer hours.

Continue to Modernize the Unemployment Insurance System

Unemployment insurance (UI) can be a critical safety net for laid-off workers. Its importance has grown for low-wage workers, now that the former welfare system has been largely dismantled. However, only about 53 percent of unemployed workers in Wisconsin receive any UI benefits. Many low-income workers are ineligible because their jobs are more commonly intermittent, seasonal, and part-time, and less likely to qualify for benefits.

To Wisconsin's credit, we have done a better job than many other states in extending benefits to low-wage workers. In a recently released report card on the UI systems in all 50 states, Wisconsin received a passing grade overall, but failed one of the five general categories studied: the unemployed who are only available for part-time work do not qualify to receive UI, in spite of the fact that UI taxes are being applied to their salaries (*Failing the Unemployed: A State by State Examination of Unemployment Insurance Systems*, Emsellem, et. al., March 2002).

Improvements that should be considered by Wisconsin's Unemployment Insurance Advisory Council include:

- expanding eligibility to individuals available for only part-time work or work on specific shifts;
- correcting an inequity in the state law authorizing benefit extensions during periods of high unemployment, which excludes about half the potentially eligible workers; and
- providing dependent allowances (as 12 states already do) that help support income of unemployed parents and their families.

Reform Regressive Taxes

Perversely, state and local taxes in Wisconsin increase income inequality rather than reduce it. Analysis of the burden of the combined package of Wisconsin taxes property, sales and excise, and income shows Wisconsin's tax structure to be almost regressive *(Who Pays? A Distributional Analysis of the Tax Systems in All 50 States*. Institute on Taxation and Economic Policy, 2003). The higher your income, the lower the portion of income paid for taxes.

In Wisconsin in 2002, the richest one percent of taxpayers paid 8.1 percent of their income in state and local taxes, the least by far of any income group, and only 5.9 percent after deducting from their federal taxes. By contrast, the poorest 20 percent of taxpayers paid 10.2 percent in state and local taxes in 2002, and middle-income taxpayers paid the most, 11.9 percent. The poorest 20 percent gain nothing from federal offset; the middle quintile gains 0.6 percent, lowering their final tax liability to 11.3 percent.

Even though the state's income tax structure is progressive (with lower incomes paying a lower portion of their income in tax), the state's sales and property taxes are quite regressive. A recent study by the Center on Budget and Policy Priorities concluded that Wisconsin's taxes have become more regressive since the early 1990s because the tax cuts have been in the more progressive taxes and the tax increases have been in regressive taxes such as gas, cigarette and sales taxes (*The Rising Regressivity of State Taxes,* December 27, 2001).

One progressive element of the state tax system is the Homestead Tax Credit, which helps lessen the burden of property taxes for many low-income homeowners and renters. However, the maximum credit has not been increased since 1991, allowing inflation to substantially erode the program. The state could also do a better job of informing families with children that they are eligible for the credit. Wisconsin should index the credit for inflation and continue working to improve outreach.

Finally, there are other tax system characteristics that place an undue burden on the poor while offering benefits to the rich, including our treatment of capital gains and the exclusion of services from sales tax. The distribution of the entire package of taxes needs to be examined, as part of a comprehensive review of the adequacy and equity of state and local taxes.

Raise the Minimum Wage and Index it to Keep up with Inflation

The state's minimum wage rose to $6.50 per hour at the beginning of 2006. These increases put money in the pockets of low-wage workers and help to lift incomes of the state's poorest residents. By raising the minimum wage, Wisconsin joined 17 states and the District of Columbia.

Without federal or state increases, inflation erodes the value of the minimum wage leaving minimum wage workers further behind each year. Indexing the minimum wage for the state, so that it keeps up with inflation, is one way to ensure that costs and minimum wage workers incomes rise together. Already four other states have indexed their minimum wage to inflation.

Conclusion

Wisconsin's growth and prosperity are not being equally shared. The rewards of prosperity have been concentrated on the richest 20 percent of families. As a state, this should be of substantial concern, not only because of the slow growth in incomes for the remaining eighty percent of families, but also because increasing disparity comes with substantial social costs.

To prevent a deepening divide between the rich and poor in our state, Wisconsin should pursue a number of strategies:

- Building the skills and education of Wisconsin's workers
- Making work pay and supporting working families
- Continuing to modernizing the unemployment insurance system
- Reforming regressive taxes
- Raising the minimum wage and indexing it to inflation

Taking these steps would help keep Wisconsin's economy growing, and ensure that all residents of the state would benefit from that growth.

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