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How Republican Approaches to Social Spending Increase Income Inequality in the United States

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Political parties in control of government can modify social spending in ways that either increase or decrease inequality in America. According to the conventional wisdom, social spending goes up when Democrats are elected to office, leading to reduced inequality. But this is only part of the story, because it ignores alternative kinds of social expenditures and the role of the Republican Party and other conservatives in shaping social policy. Republicans, it turns out, also tend to increase federal social spending – on policies that benefit the privileged.

Both political parties, not just Democrats, have incentives to increase federal social spending because many Americans, including most Republican voters, demand that the federal government play an active role in the provision of social benefits and services. For the GOP, the challenge is how to meet such expectations in ways that align with an avowed small-government philosophy. The solution for many Republicans has been to create and expand tax subsidies (also called tax expenditures) for social spending by businesses, individuals, and other private interests, while cutting back on direct public spending. Good examples include tax breaks received by employers who provide private health insurance plans and tax exclusions to citizens who donate to charities and nonprofits. Such tax reductions amount to transfers of resources to the rich largely at the expense of tax revenues that could pay for broad-based public social benefits that help the middle and working classes. With few exceptions, income inequalities increase as a result of such transfers.

Different Versions of the Welfare State

How does the Republican welfare state differ from the Democratic one? The traditional Democratic social welfare state is well known. Between the 1930s and the 1960s, Democrats created Social Security, Medicare, and Medicaid along with a number of other public social spending programs. These programs disproportionately give federal assistance to vulnerable populations such as the elderly, the unemployed, and the working class; and they tend to decrease income inequalities.

An alternative welfare state has been built through the tax code largely as a political response to the success of traditional Democratic public programs. Starting in the 1970s, Republican leaders realized that attacks on Social Security and Medicare along with a balanced budget philosophy were costing them votes at the ballot box. The Republican Party, along with some conservative Democrats, began to promote government-subsidized private-sector social programs as viable political alternatives to popular social programs. Republicans offered new and expanded tax subsidies for private social programs like “401k” retirement savings programs or Health Savings Accounts (where people set aside money to pay for health expenses). This strategy created incentives for citizens to use such private alternatives to public social insurance and at the same time reduced political pressures to raise public revenues to expanded public forms of retirement insurance, health insurance, and other social-welfare programs. Republicans and other supporters of tax subsidies were able to sell increases in tax subsidies to their constituents as either government support for private-sector policy solutions or tax relief. In short, tax expenditure programs for social purposes allowed the Republican Party to meet demands for government social assistance while furthering conservative goals of cutting taxes and direct government spending.

The Tax Subsidy Approach to Social Welfare Increases Income Inequality

The shift toward tax expenditures rather than direct public spending – and the proliferation of tax expenditure programs – has contributed to rising economic inequality, in a number of ways:

- Most tax subsidy programs provide disproportionate financial assistance to the wealthiest citizens. For example, tax expenditure programs for private retirement plans provide more federal money to the wealthiest one percent of families than they do to the entire middle class.

- Tax breaks for privately delivered or managed services and benefits subsidize large pharmaceutical companies, financial institutions that sell retirement plans, private health insurers, and large corporations that offer employer-managed benefits to employees.

- Typically, increases in private tax subsidies are paid for with cuts to public social programs that disproportionately help poor and vulnerable populations.

My research assesses the overall, cumulative effect of increased reliance on tax subsidies for social-welfare purposes, an approach supported by many Republicans and some Democrats in recent decades. Since the 1970s, the data show that an increase in the proportion of tax subsidies within overall social spending has increased income inequality.

How Policies Could be Redesigned

Two changes could curtail the federal government's tendency to use the tax code to boost the privileged.

- Instead of continuing the current practice of counting tax subsidies as off-budget expenditures, these subsidies could be registered as budget costs – as recommended by the General Accounting Office, the Congressional Budget Office, and former Chairman of the Federal Reserve Board Alan Greenspan. This would give citizens and the media a more complete picture of the costs, purposes, and beneficiaries of all kinds of social programs.

- Social programs pursued through the tax code could use refundable tax credits instead of deductions or exclusions of income from taxation. For example, both Democrats and Republicans have proposed expanding the Earned Income Tax Credit to include single workers. If deductions and exclusion were transferred into refundable credits, many more workers and families of modest means would get larger tax refunds. Potentially, this approach to helping working people could gain more support from the American public than the expansion of "welfare programs" that arouse racial and class resentment.

Read more in Christopher Faricy, *Welfare for the Wealthy: Parties, Social Spending, and Inequality in the United States* (Cambridge University Press, 2015).

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