EPI ACTION

Working families need an end to wage suppression more than new tax cuts

Donald Trump seems to float a new tax cut every week he claims will help working families—most recently proposing to make tips, overtime earnings, and Social Security benefits tax-exempt. This new playbook is obviously a cynical ploy given that Trump as president *specifically* undermined tipped workers, overtime earners, and Social Security recipients. But most importantly, these ideas do nothing to fix the biggest problem U.S. workers have faced in recent decades—that employers have managed to hijack policies across a range of issues areas to help them suppress wage growth.

Since 1979, this wage suppression has cost middle-income workers dearly: for somebody earning the median wage and working full time, year-round, their annual earnings would be $19,000 higher today if wages had risen in line with overall economic growth. This cost dwarfs other economic pressures in their lives: Even if we cut the taxes these workers pay to zero, their income would rise by *less than a third* of what wage suppression has taken from them.

One way to see this is that productivity—the amount of income generated in an average hour of work in the economy—has risen by 1.4% per year since 1979, but pay for the 80% of workers who are not managers in the economy has risen by just 0.6% per year. In other words, while ordinary workers got less than half of their fair share of the income generated by productivity growth over this period, highly paid workers and corporate shareholders made out like bandits.

Have taxes added to this pressure on family incomes? Not even a little. In fact, between 1979 and 2019, the average federal tax rate for households with children in the middle-fifth of the income distribution fell significantly, from 17.6% to 12.3%. This fall happened during both Republican and Democratic administrations. If we cut federal taxes still owed by these middle-fifth families in 2019 *all the way to zero*, this would raise annual earnings of full-time, full-year wage earners by less than $6,000—not even a third of what wage suppression took from them.

If policymakers want to provide transformative help to middle-income families, enacting policies to fight this wage suppression should be front and center. These policies exist and they work, but they do not get near the attention they deserve. Key among these policies are: consistently maintaining very low rates of unemployment, increasing legal protections for workers trying to organize unions and negotiate first contracts, raising the shamefully low federal minimum wage, and policing labor markets to spot and end employer attempts to short-circuit the value of competition for workers' wages (the recent FTC ruling banning noncompete agreements—currently held up by the court system—is an excellent example).

Taxes can't be zero for everybody—not even for most

And, of course, not everybody can pay zero taxes. Yes, we should ask significantly more from the richest households, but Social Security, Medicare, Medicaid, the Affordable Care Act, and public investments are extraordinarily valuable to middle-class households—and we need contributions from these households to help pay for them.

For candidates like Trump, the pressure that the "tax cuts for everybody" strategy will put on these programs is part of the appeal. Take his proposal to cut taxes on tips. Workers in the bottom half of the income distribution (which includes most tipped workers) pay far more in payroll taxes (like those used to fund Social Security and parts of Medicare) than in income taxes. If he is only talking about exempting income taxes, then this will have incredibly limited reach—the average income tax rate for households with children in the middle-fifth of the income distribution is less than 1%. If he exempts payroll taxes too, this would broaden the reach, but because Social Security benefits are linked to lifetime contributions, this would cut their future Social Security benefits.

Even the proposal to exempt Social Security benefits from taxation threatens the long-run viability of the program. There is *already* highly preferential tax treatment for Social Security benefits—about 60% of recipients do not pay taxes on them. For those who do pay taxes on Social Security benefits, this money is specifically earmarked to go into the Social Security Trust Fund (SSTF) and finance benefits. This is a non-trivial source of financing for the Social Security program, accounting for over $50 billion in income for the SSTF. It is just one of many ways that the Social Security program is progressive—providing universal benefits but which are greater for those in the most need.

Tax rates should depend on ability to pay—not loopholes and accountants

Finally, all of these *ad hoc* tax cuts targeted to gain political favor are exactly what led to our tax code being so complicated and unfair in maddening ways. One goal of tax policy should simply be that *your tax rate should depend on your level of income*—not the way you earned your income (or what your accountants tell you to call your income).

If, say, a plumber working as a W-2 employee for a company makes $60,000 a year in wages, they should not pay higher taxes than a plumber who classifies themselves as an independent contractor and makes $60,000 in business income. But that's exactly what our current tax code allows today (so long as the second plumber shells out money for a clever accountant—foregoing much of the potential gain to them of this tax avoidance). And if we introduce more tax preferences for tip and overtime income and so on, then our tax code will continue to get more complex and more arbitrary about who is rewarded and why.

In short, the proposals to exempt tip and overtime income and Social Security benefits from taxes are half-baked political opportunism. Today's working families deserve more serious ideas that target the real pressure on their living standards—wage suppression that has been abetted by policymakers far too often in recent decades.