Why Hasn't Democracy Slowed Rising Inequality?

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During the past two generations, democratic forms have coexisted with massive increases in economic inequality in the United States and many other advanced democracies. Moreover, these new inequalities have primarily benefited the top 1 percent and even the top .01 percent. These groups seem sufficiently small that economic inequality could be held in check by political equality in the form of "one person, one vote."

Indeed, the notion that inequality should be at least partially self-correcting in a democracy has a long pedigree in economic theory. In the canonical model of Meltzer and Richard (1981), increased inequality (in the form of median incomes falling relative to average incomes) leads the median voter to demand more redistribution, so that politics should limit after-tax and -transfer inequality. Redistribution is limited, however, by the consequences of how the higher rates of taxation reduce labor supply. A stripped-down version of this model, with similar implications, is the model developed by Bolton and Roland (1999), where redistribution is limited through deadweight loss in taxation. These early approaches (see also Romer 1975) assume that politics is majoritarian, equal (one person, one vote) and with full participation (all economic agents vote).

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Other authors, notably Benabou (2000), look at more complex and realistic environments where theory does not provide clear predictions. In economies where there are efficiency gains to redistribution, there may be more support for redistribution at low levels of inequality than at high levels. If the 1 percent is not exceptionally rich relative to the mean, the efficiency gains may offset additional taxes. But as the 1 percent get relatively richer, they turn against redistribution. In any economy, unequal turnout or political power can create a situation where the pivotal voter under majority rule may have income greater than the median. When a society has large numbers of relatively poor residents without voting rights, as arises with substantial immigration, redistribution will be limited even when all of the enfranchised participate fully (McCarty, Poole, and Rosenthal 2006). When these and other concerns are brought into play, many relationships between democracy and inequality are theoretically possible.

In this paper, we explore five possible reasons why the US political system has during the last few decades failed to counterbalance rising inequality.

First, both Republicans and many Democrats have experienced an ideological shift toward acceptance of a form of free market capitalism which, among other characteristics, offers less support for government provision of transfers, lower marginal tax rates for those with high incomes, and deregulation of a number of industries. Financial deregulation, in particular, has been a source of income inequality (Philippon and Reshef 2008). The mass public may well embrace such an ideological shift if rising inequality nonetheless "trickles down" to rising incomes and home ownership for all. In recent years, there has been a serious financial crisis, declining median incomes, and declining home ownership rates. This raises important questions as to why these ideological trends persist and remain politically powerful.

Second, immigration and low turnout of the poor have combined to make the distribution of voters more weighted to high incomes than is the distribution of households (McCarty, Poole, and Rosenthal 2006). Turnout, of course, can also be influenced by legal and administrative measures that make it relatively costly for the poor to vote.[1]

Third, rising real income and wealth has made a larger fraction of the population less attracted to turning to government for social insurance. When the insured consumption can be self-provided at relatively low risk, there will be less support for government insurance than when risk is high and private insurance markets are of dubious value. There is a telling contrast between Social Security, which provides old age payments for general consumption, and Medicare and the Patient Protection and Affordable Care Act of 2010, which cover unforeseen, potentially catastrophic, expenses for health care. Social Security does not have a strongly progressive tax and benefit structure. Attempts to increase progressivity by removing the cap on the payroll tax or taxing unearned income have little political traction. By contrast, the

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[1] See Alvarez, Bailey, and Katz (2008) for evidence on the disparate impact of recent tougher voter identification laws on the turnout of the poor.

Medicare tax on earned income was uncapped during the administration of George H. W. Bush and raised in the 2010 health care legislation. In addition, the Patient Protection and Affordable Care Act imposed a 3.8 percent tax on unearned income of high earners. Thus, public expenditure for high-risk health care consumption has expanded more than expenditure for other, less-risky, forms of old age consumption. Although the 1 percent might self-insure for health risks, the broader population has supported social insurance in this area.

Fourth, the rich have been able to use their resources to influence electoral, legislative, and regulatory processes through campaign contributions, lobbying, and revolving door employment of politicians and bureaucrats.

Fifth, the political process is distorted by institutions like gerrymandering that reduce the accountability of elected officials to the majority. Other political institutions, including a bicameral legislature with a filibuster, combine with political polarization to create policy gridlock, which in turn inhibits efforts to update social safety nets and regulatory frameworks in response to changing conditions.

An Ideological Shift and Greater Polarization

Since roughly 1980, the political system has polarized (McCarty, Poole, and Rosenthal 2006) with the ideological gap between Democrats and Republicans widening while moderates vanish from Congress. At the same time, the Republicans enjoyed increased electoral success. The Democratic control of the federal government initiated with Franklin Delano Roosevelt was broken. During the 34 years from 1981–2014, the Republicans will have held the presidency for 20 years and at least one house of Congress for 22 years. Except for a brief period in 2009, the Republicans have had the 41 votes needed to sustain a Senate filibuster.[2]

Our data source for liberal–conservative positions of members of Congress are the widely used DW-NOMINATE scores, based on roll call votes. The one-dimensional implementation of DW-NOMINATE (Poole and Rosenthal 1997; McCarty, Poole, and Rosenthal 1997; Poole 2005) assumes that legislators make choices between yea and nay outcomes on a roll call vote as a function of the distance between the legislator's "ideal point" on the liberal–conservative dimension and the locations of the outcomes. The "spatial utility" a legislator assigns to an outcome is a Gaussian function of the distance between the outcome and that legislator's ideal point on the liberal–conservative dimension. The total utility of the outcome is the spatial utility plus a random, normally distributed component. The legislators' "ideal points" and the outcome components are estimated simultaneously from roll call votes. The

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[2] In addition, a majority of the Supreme Court has been appointed by Republican presidents since 1970. Over time, some Republican Supreme Court appointees such as Earl Warren, John Paul Stephens, and David Souter often voted with Democratic appointees. However, there has been a conservative majority on the court since 1982 according to a scoring system developed by political scientists Andrew Martin and Kevin Quinn and available at http://www.targetpointconsulting.com/scotusscores-labels.html.

Figure 1
Party Means on Liberal–Conservative Dimension for the US House of Representatives, 1879–2012
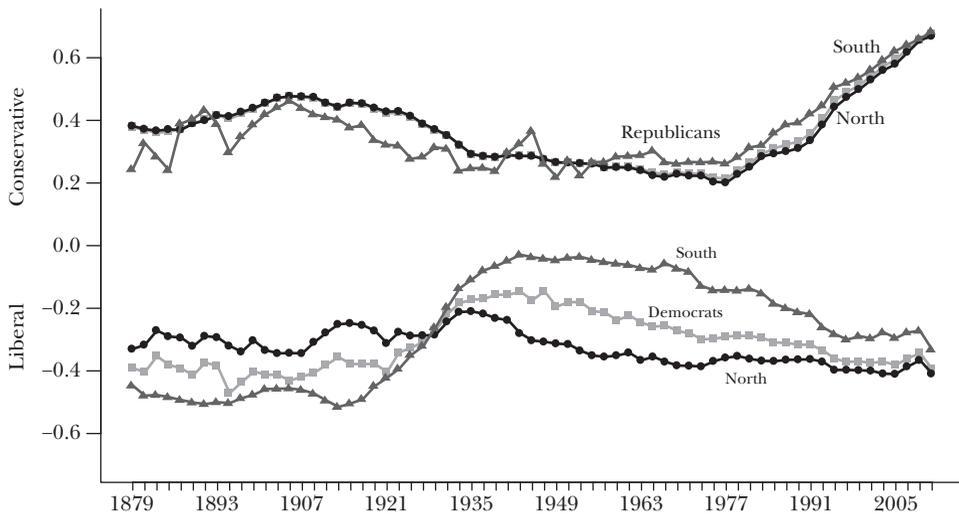
Source: Author's calculations using DW-NOMINATE scores of the liberal–conservative positions of members of Congress, which are based on roll call votes. For methodological details, see Poole and Rosenthal 1997; McCarty, Poole, and Rosenthal 1997; and Poole 2005.

average ideal point of a legislator is constrained to lie in a continuum from −1 (far left) to +1 (far right).

Polarization is measured as the distance between the average ideal point of Republican legislators and that of Democrats. (Results are similar for other measures of dispersion, such as the variance of ideal points.) Overlapping cohorts of legislators permit measurements that are comparable across time.[3]

As Figure 1 shows, most of the polarization for the House of Representatives has been produced by a rightward movement of Republicans. The pattern for the Senate is similar. More precisely, entering Republicans like Ted Cruz have tended to vote to the right of continuing members, and exiting members like Olympia Snowe have been relatively moderate. Republicans have become sharply more conservative. The slight liberal drift of the Democrats is compositional in nature. Moderate Democrats from the South have been replaced by conservative Republicans. The few remaining southern Democrats are now heavily African-American, representing minority-majority districts. The change has made for a smaller, more liberal group of southern Democrats. However, Democrats as a whole have not moved much to the left. Overall, entering and exiting Democrats have looked much like those that have continued to serve.

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[3] Legislator ideal points are restricted to linear trends throughout the legislator's career. For example, a legislator can trend from liberal to conservative but cannot go back and forth.

Our findings do not, however, suggest that the Democrats continue to support policies that would reduce inequality as much as they did in the New Deal. After all, nineteenth-century Democrats, centered on populist southern whites, supported railroad regulation and antitrust legislation, and in this sense were to the economic left of current Democrats. The Democratic party pushed through the financial regulation of the 1930s, while the Democratic party of the 1990s undid much of this legislation in its embrace of unregulated financial capitalism, including the Interstate Banking and Branching Efficiency Act of 1993, which eliminated previous restrictions on interstate banking and branching; the Gramm–Leach–Bliley Act of 1999, which repealed the 1933 Glass–Steagall Act that had separated commercial banking from other financial services; and the Commodity Futures Modernization Act of 2000, which prevented the Commodity Futures Trading Commission from regulating most over-the-counter derivative contracts, including credit default swaps.

There appears to have been a substantial change in how issues of market regulation and fiscal policy have mapped onto the relatively stable ideological positions of Democratic members of Congress. What makes a legislator liberal or conservative evolves over time. Part of the changed mapping is found in the Democrats' embrace of environmental protection, a public and normal good where demand is likely to increase with income. Similarly, in a quantitative analysis of party platforms, Geering (1998) has documented that the Democratic agenda has shifted away from general social welfare to policies that target ascriptive identities of race, ethnicity, gender, and sexual orientation.

The extent of political polarization, as measured by the average difference between the parties, is positively correlated with the extent of inequality. Figure 2 shows the dramatic increases in the difference between the mean Republican and the mean Democrat in the House. Again, results for the Senate are very similar. The figure also shows that polarization and income inequality track each other closely over the past 100 years; indeed, when this measure of political polarization is lagged ten years, thus making it a leading indicator, its correlation with the income share of the top 1 percent exceeds 0.9. [4]

This correlation raises questions of cause and effect. What causes increased political polarization? How might greater political polarization reduce the efforts of government to push back against greater income inequality? These are important questions for research. In later sections of this paper, we will discuss the arguments suggesting that lower support for policies that would influence inequality may result from an increase in polarization coupled with a greater adherence to free-market ideology, which is in turn supported by campaign contributions from the rich.

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[4] Polarization is not only a phenomenon at the federal level. Shor and McCarty (2011) show that many state legislatures are as polarized as Congress and have become more polarized over the last 15 years. Controlling for region, there is also a statistically significant cross-sectional correlation between state legislative polarization and the 80/20 wage ratio. Also see Garand (2010) for evidence that income inequality at the state level is correlated with the voting of US senators.

Figure 2

Top 1 Percent Income Share and Polarization in the US House of Representatives, 1913–2008
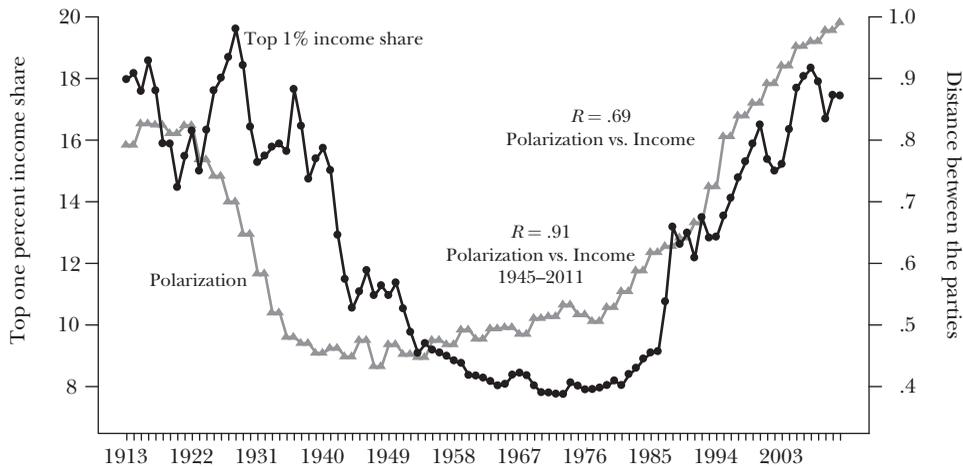
Source: Authors calculations using the polarization data described under Figure 1, and data on income from Piketty and Saez (2013).

But clearly, efforts to reduce inequality are not especially popular. For example, Barack Obama campaigned in 2008 and again in 2012 to raise marginal tax rates only on the relatively small slice of households earning over $250,000 and eventually in early 2013 accepted increases for only the tiny sliver of households (filing joint returns) at $450,000 and above. There has been no groundswell of political support for sharp reforms of the financial sector, nor for actions to reduce mortgage foreclosures substantially, nor for expanding investment in the human capital of children from low-income households.

It's important to remember that the left-to-right political spectrum described here involves many issues, not just economic ones. When Democrats have won elections, their victory has been due in large part to voters' concerns about issues other than redistribution to the poor. Such issues might include the environment, foreign policy (Iraq), and identity issues for women and the lesbian, gay, and transgender communities. Arguably, the electoral success of the Democrats in 2006 and 2008 owed more to the Bush administration's Iraq policy than to redistributive policies espoused by Democrats.

Voters and citizens also tend to make clear distinctions among the holders of wealth based on how it was acquired. To the extent that public furor is directed against the 1 percent, it is largely directed against the financial sector. We had Occupy Wall Street, but no Occupy Silicon Valley or Occupy Walmart. Political animus toward the 1 percent is largely directed at those perceived to have caused direct harm to the general public, like executives from major financial institutions and BP. Rage is accentuated when the malefactors are

Figure 3

Polarization in the House of Representatives, and Relative Wage and Education in Financial Services Sector, 1909–2006
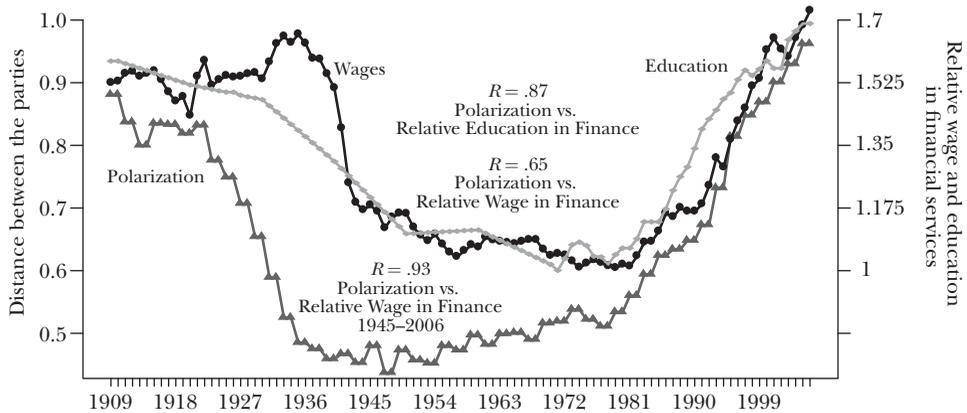
Source: Authors calculations using the political polarization data described under Figure 1, and financial data from Philippon and Reshef (2008).
Note: Figure 3 shows that political polarization in the US House of Representatives tracks wages and educational levels in the financial sector relative to the remainder of the economy.

perceived to benefit from taxpayer money, as in the TARP and AIG bailouts of 2008 (McCarty, Poole, and Rosenthal 2013). But there is no widespread sense that high incomes are illegitimate per se. Executive compensation went essentially unscathed in the Dodd–Frank financial regulation legislation passed in 2010. Entrepreneurial wealth derived from providing valued goods and services is admired, even revered.

Hard evidence on mass public attitudes toward the 1 percent is thin. But a 60 Minutes/*Vanity Fair* poll in July 2010 asked, "Which one of the following professions do you think most deserves the large salaries its members receive?" The responses from 1,167 telephone interviews were: Bankers, 12 percent; Professional athletes, 15 percent; Film stars, 9 percent, Lobbyists, 5 percent, Internet entrepreneurs, 33 percent; None of the above (an unsolicited, volunteered response), 14 percent; and Don't know/ No answer, 15 percent. In short, Internet entrepreneurs, who populate far more of the Forbes 400 wealthiest Americans than athletes, film stars, and lobbyists, are viewed as deserving. Even bankers, less than two years after the collapse of financial markets, found some support. The framing of the question limits what we can draw from the responses—"Who most deserves . . .?" allows for the interpretation that none deserve it very much. But at least we can say that these responses are hardly a smoking gun of widespread public resentment over rising income inequality.

However, there are some tantalizing linkages from our measure of political polarization to the financial sector. Figure 3 shows that political polarization tracks

Figure 4
Voter Turnout by Household Income and Citizenship, 2008 and 2010
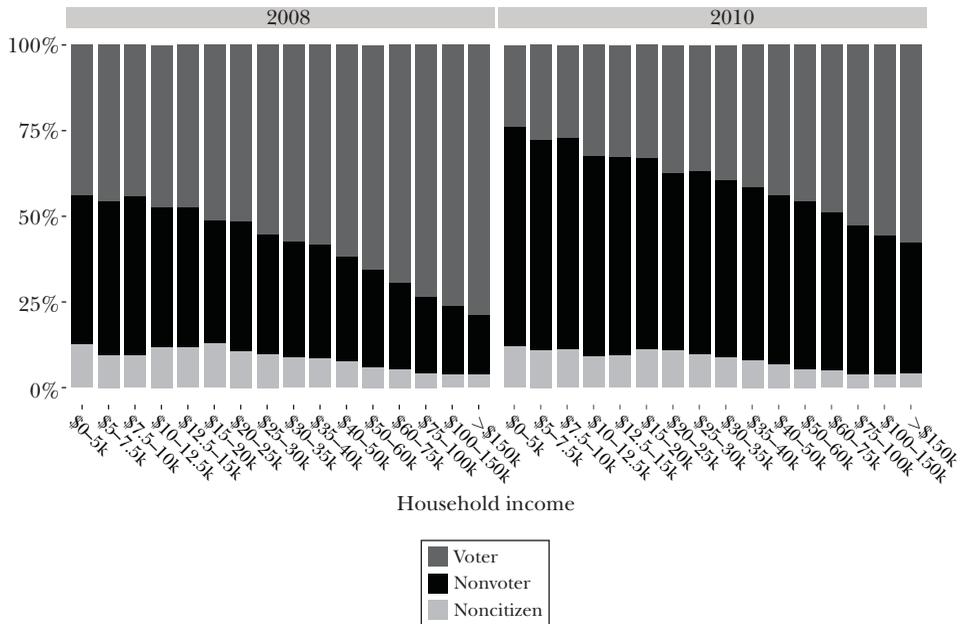
Note: Figure 4 shows the relationship between voter turnout and voter household income and citizenship for the 2008 presidential and 2010 midterm elections.

wages and educational levels in the financial sector relative to the remainder of the economy. (Again, the correlation of polarization between both of these series is maximized at 0.9 by lagging polarization by 10 years.) Philippon and Resheff (2008) in turn show that these financial variables go hand in hand with financial deregulation; that is, a deregulated financial sector attracts those with more educa-tion, who in turn are paid a higher wage. The top 1 percent contains a sizable share of individuals from the financial sector. Thus, a set of interconnections seem to exist here between political polarization, policy choices affecting the financial sector, and greater inequality as one outcome of those policy choices.

Voting Participation and Inequality

If those with lower incomes are less likely to vote, then the political system will be less responsive to a rise in inequality. The relationship between voter turnout and income (and citizenship) is shown in Figure 4 for the 2008 presidential and 2010 midterm elections. The data is drawn from the large samples in the November Current Population Survey, which asks questions on citizenship, turnout of citizens,

and household income.[5] In the figure, the dark grey bars at the top represent the voters; the black bars in the middle, nonvoting citizens; and the light grey bars at the bottom, noncitizens.

   Two effects are worth noting. First, higher fractions of the poor are noncitizens. Second, among the poor who are citizens, turnout is very low. Fewer than half the households with incomes under $15,000 reported voting in the presidential election of 2008, even though turnout of the poor increased over the 2000 level (shown in McCarty, Poole, and Rosenthal 2006, figure 4.1.) In contrast, over four-fifths of those with incomes over $150,000 reported voting. The contrast is greater for midterm elections. Turnout for the 2010 midterm election decreased only slightly from levels in 2008 for top incomes but decreased substantially for those with household incomes below $15,000 so that only about one-third of that group reported voting. In 2008, those reporting incomes above $150,000 represented 9.9 percent of the voters as against 8.0 percent of the voting age population. In 2010, the numbers were 9.6 and 7.4 percent.

   Schlozman, Verba, and Brady (2012) show that there is a significant socioeconomic skew to all forms of political participation with the exception of participating in a protest—an activity in which very few Americans participate. Voting tilts the policy scales in favor of top incomes. Another important distortion comes from campaign contributions, which we discuss in the next section.

Campaign Contributions and Political Outcomes

   Campaign contributions by individuals have grown over time, with 3,138,564 individuals making itemized contributions in 2012 compared to 224,322 in 1980. But this increased participation has also been marked by increased inequality in contributions. Figure 5 shows that the share of total income received by the top 0.01 percent of households is about 5 percent but that the share of campaign contributions made by the top 0.01 percent of the voting age population is now over 40 percent.[6]

   This change over several decades does not seem to be primarily driven by legal factors governing donations: broadly speaking, the legal framework for wealthy individuals to donate unlimited amounts was set in place decades earlier by

[5] There is overreporting of citizenship and turnout and probably underreporting of income. Ansolabehere and Hersh (2012) show that, in sample election surveys, turnout is heavily overreported and that the tendency to overreport is increasing in income. However, the same authors show that, for 2008, the Current Population Survey turnout rate among citizens is only 2 percent higher than the turnout of the Voting Eligible Population computed by McDonald (2011). Thus, overreport bias in the Current Population Survey appears unlikely to account for the strong differences shown in Figure 4.

[6] We have used the 0.01 percent rather than the 0.1 percent or the 1 percent because in 1982 less than 0.1 percent of the voting age population made itemized contributions. Although contributing has become more widespread, it has also become more concentrated, with the top 0.01 percent dominating total contributions.

Figure 5
Concentration of Income and Campaign Contributions in the Top 0.01 Percent of Households and Voting Age Population
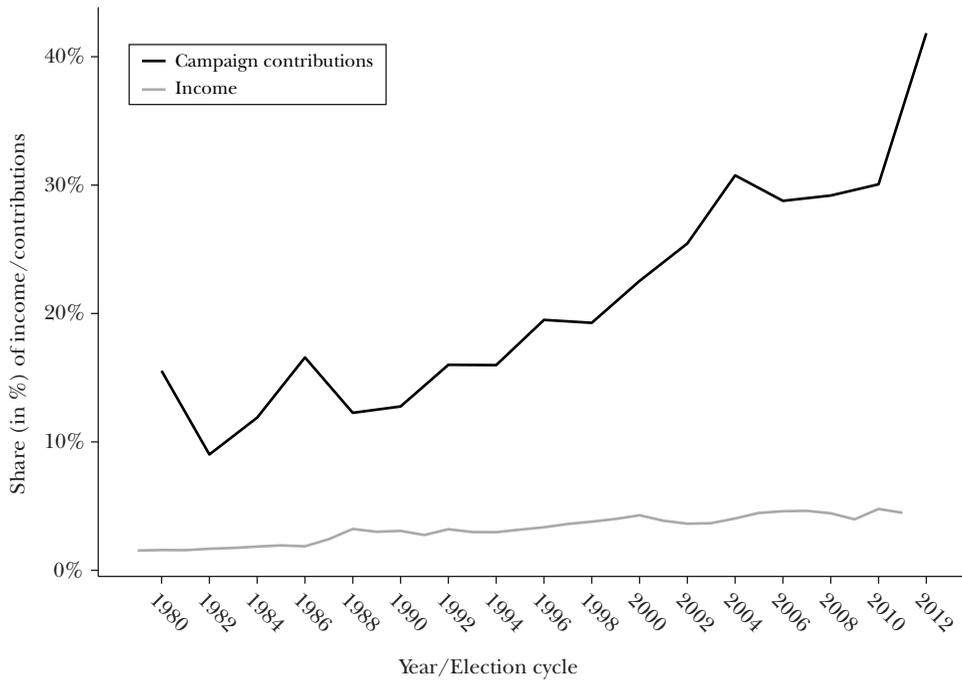
Source: For income data, Piketty and Saez (2013).
Notes: The dark line tracks the share of campaign contributions in all federal elections donated by the top 0.01 percent of the voting age population. The number of donors included in the 0.01 percent share of voting age population grew from 16,444 in 1980 to 24,092 in 2012. During the same period, the minimum amount given to be included in the top 0.01 percent grew in real terms from $5,616 to $25,000 (in 2012 dollars). The shaded line tracks the share of total income (including capital gains) received by the top 0.01 percent of households. The figure includes individual contributions to Super PACs and 527 organizations but excludes contributions to nondisclosing 501c(4) organizations, which are recorded to have spent approximately $143 million in 2010 and $318 million in 2012, much of which was raised from wealthy individuals. Were it possible to include contributions to nondisclosing 501c(4)'s, the trend line would likely be 1–2 percentage points higher in 2010 and 2012.

Buckley v. Valeo (424 US 1 [1976]). Rather, it reflects the rising wealth of the super-rich and an increased willingness to spend large sums on elections.

One stark indication of increased willingness to spend comes from a comparison of the largest individual contributors in federal elections over time. In 1980, the top contributor was Cecil R. Haden, owner of the tugboat operator Bay-Houston Towing, who gave $1.72 million (in 2012 dollars), nearly six times the amount given by the next largest contributor. In 2012, the two largest donors were Sheldon and Miriam Adelson, who gave $56.8 million and $46.6 million, respectively. Other members of the Forbes 400 accompany the Adelsons; 388 current members are on record as having made political contributions. They account for 40 of the

155 individuals who contributed $1 million or more to state and federal elections during the 2012 election cycle.

Another wealthy group is represented by a sample of 4,493 board members and chief executive officers from Fortune 500 firms. More than four in five in this group reported contributions in federal elections, a proportion that looks even higher when observing that many noncontributors are foreign nationals and are prohibited by law from contributing to US political campaigns. Overall, the corporate sample gave over $170 million during the 2012 election cycle. These contributors have given a lifetime average over the period 1979–2012 of $172,513 per individual and a lifetime median of $30,359. While these numbers are miniscule compared to philanthropic giving, the participation rate of the nation's wealthiest individuals is quite astounding when one considers that less than 4 percent of citizens have given in amounts large enough to be itemized. (Small contributions—less than $500 to a candidate before 1990, and $200 since then—are not reported on Federal Election Commission disclosure forms.)

Consistent with Figure 5, there appears to be a growing reliance on the top 0.01 percent of donors. Democrats as well as Republicans rely on big donors. The sources of contributions to Democrats are shown in Figure 6. The Democrats have come to rely, increasingly, on contributions from individuals, particularly big money. Contributions from organized labor, never dominant, have fallen in importance.[7] The relative proportions of funds raised by Democrats from the top 0.01 percent and from organized labor provide a telling comparison. The top 0.01 percent, whose donations had been roughly on par with those of labor during 1980s and early 1990s, outspent labor by more than a 4:1 margin during the 2012 election cycle. While Republicans had a slight advantage in fundraising from the top 0.01 percent during the 1980s, this trend had reversed by the mid-1990s, with Democrats raising more than Republicans from the top 0.01 percent in six out of eight election cycles between 1994 and 2008. Only in the last two election cycles did Republicans regain the advantage in fundraising from the top 0.01 percent.[8] While it is difficult to gauge the effect of the Democrat's reliance on contributions from the wealthy, it does likely preclude a strong focus on redistributive policies.

For individual campaign donors, we have explored who gives how much to whom in terms of the ideology of the donors and candidates. We measure the ideology of donors and candidates jointly in an estimation procedure (for details, see Bonica 2013a, 2013b) reasonably analogous to DW-NOMINATE estimation (see Figures 1–3) for roll call data. Campaign finance scores reported here are based on individual contributions in federal races. Similar results for candidates are also obtained by using PAC ("political action committee") contributions with controls

[7] For a contrary view on the importance of the decline of contributions from labor, see Hacker and Pierson (2010).

[8] In 2012, 62 percent of contribution dollars raised from the top 0.01 percent went to Republicans, accounting for 40 percent of the party's total campaign dollars.

Figure 6
Democratic Fundraising Sources
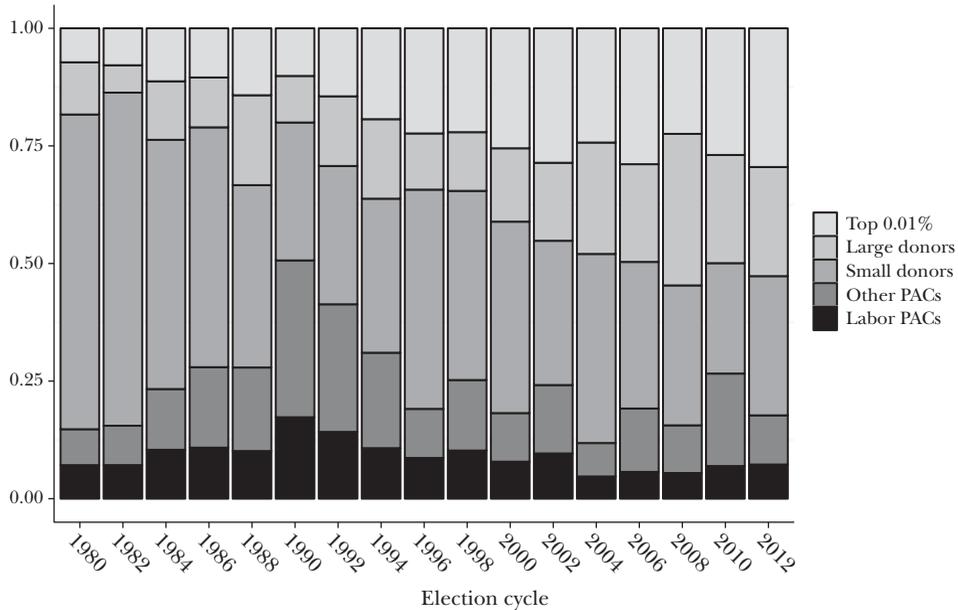
Sources: The Federal Election Commission and the Internal Revenue Service.
Notes: Includes funds raised by federal candidates, national party committees, Super PACs, federal-oriented 527s, and other independent groups aligned with the Democratic Party (for example, Priorities USA Action and the MoveOn.org 527). The amounts from labor and other PACs include direct contributions to candidates and committees, soft-money contributions to national party committees (prior to 2004), and independent expenditures (including those made through 527s) to support Democrats or oppose Republicans in the general elections. The total amounts raised from individuals are divided into three categories. The first category includes all donations made by individuals included in the top 0.01 percent of donors in the voting age population, similar to Figure 5. The category labeled "Large Donors" includes all individual donors that gave more than $1,500 (in 2012 dollars) during the election cycle but not enough to be included in the top 0.01 percent. The category labeled "Small Donors" includes contributions from donors giving less than $1,500 during the election cycle plus the total funds raised in nonitemized amounts. The cutoff at $1,500 approximates the inflation-adjusted $500 minimum donation required for disclosure in 1980.

for standard covariates such as incumbency and seniority. Figure 7 shows how the top 0.01 percent of donors and smaller donors distribute their donations in terms of the ideology of candidates (including losing candidates). To further explore the ideological leanings of the wealthiest members of the business community, we include a third density of donations from a group composed of the Forbes 400 list of wealthiest Americans and of directors and executives of Fortune 500 companies. In addition to the ideological distribution of dollars allocated by each group of donors, the figure displays the estimated ideal points for several well-known politicians and the 30 richest Americans that have made contributions. The vertical lines

Figure 7

The Ideological Distribution of Dollars from Small Donors and the Top 0.01 Percent
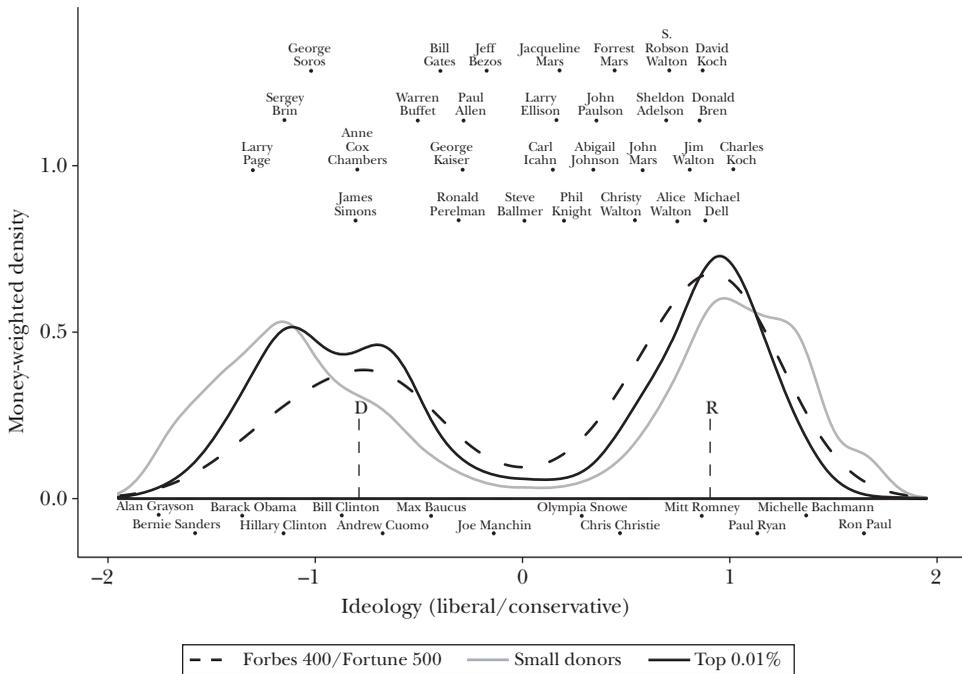
Source: Authors calculation's using "CF" scores, as described in Bonica (2013b), as measures of candidate and contributor ideology. Data on political contributions are from the Federal Election Commission.
Notes: While the DW-NOMINATE scores range from –1 to 1, the Bonica CF scores range from –2 to 2. The kernel densities show the distribution of candidate ideal points weighted by the total amounts raised from small donors (defined as donors giving $500 or less during a two-year election cycle), from the top 0.01 percent of donors, and a group of the very wealthy donors composed of members of the Forbes 400 and directors and CEOs of Fortune 500 firms. The densities are based on contributions made to candidates for federal office from 2004 to 2012. The names above the density plots mark the estimated ideal points of the 30 richest Americans that have made contributions. In order to aid in interpreting the scale, the ideal points for several well-known politicians are included below the densities (read along the *x*-axis only; the varying heights of these points do not mean anything). The vertical bars show the average positions of Democratic and Republican candidates.

in the figure show the mean positions of Democratic and Republican members of Congress during the period.

Although contributions from the Forbes 400/Fortune 500 skew somewhat to the right, a sizable percentage of their contribution dollars go to support candidates who are left of center. In coding their positions, there are three channels for placing these wealthy individuals in the moderate category. First, the individual might donate nearly exclusively to moderates of one of the two major parties. Second, the individual might spread contributions across moderates in both parties. Third, the contributions could be dispersed across the ideological spectrum. The third channel is unimportant empirically. As a rule, individual donors

exhibit high levels of partisanship in their giving patterns, and the super-rich are no exception. The vast majority have given at least 90 percent of their contribution dollars to one or the other party. Of those who split their contributions between parties, most give predominantly to the moderate wings of both parties. As such, the bimodal density of contribution dollars reflects the ideological diversity in the contributors, rather than individuals purchasing access or otherwise acting strategically in ways that cause them to disperse their contributions widely. The level of ideological diversity is apparent in the estimated ideal points of the 30 richest Americans, which are displayed above the densities. Only three of the 30—George Soros, Larry Page, and Sergey Brin—would be placed in the "progressive" wing of the Democrats. Similarly, only one of the 30, Charles Koch, is to the right of the mean Republican member of Congress. Nonetheless, the densities in Figure 7 are bimodal, with the big contributions appearing as moderate only in the limited sense that they are less polarized than the small contributions.

The ideological diversity of corporate elites is not simply a function of firm-specific incentives that would cause a firm to stake out an ideological position. Bipartisan boardrooms are the norm. One way a firm maintains political access is to have both high-profile Democratic donors and high-profile Republican donors within the firm. A consequence of the ideological diversity of the corporate community is to help keep the political financing system competitive for both parties, while at the same time ensuring that firms remain well connected in both parties. Among the directors of JPMorgan Chase, to cite a typical example, are Crandall Bowles, former chair and chief executive officer of Springs Global and wife of Erskine Bowles, and James Bell, a former Boeing Co. executive. Crandall Bowles and James Bell have ideal points as far left as Bill and Hillary Clinton. The board also contains former ExxonMobil chief executive officer Lee Raymond and former Johnson & Johnson chief executive officer William Weldon whose positions are as far right as Paul Ryan. JPMorgan Chase chief executive officer Jamie Dimon is moderate left.

We have seen that the 30 richest Americans are diverse but relatively moderate. This observation is echoed in comparing the ideological densities of contribution dollars from Forbes 400/Fortune 500 individuals and small donors. While the contributions from the Forbes 400/Fortune 500 go disproportionately to candidates who are interior to the party means, contributions from small donors go disproportionately to candidates on the ideological extremes. The distribution of contributions from the top 0.01 percent of the voting age population is more extreme than the Forbes 400/Fortune 500 but less extreme than the small donors.

While Forbes 400/Fortune 500 individuals are more moderate than small donors, their contributions tilt toward Republicans. The top 0.01 percent of donors give pretty evenly to Democrats and Republicans. Why are big donors a bit less polarized than other donors? With regard to the left, the answer seems straightforward: those who are left and rich still have a limited tolerance for redistribution. For the right, the answer seems a bit more complicated. The wealthy are often more pro-business than pro-market (a distinction explored by Zingales 2012), and are often not anti-statist.

This section has emphasized political spending in the form of campaign contributions. We should also note that even more is spent on lobbying. While a good deal of lobbying reflects corporate competition—for example, will Citicorp or Wells Fargo be allowed to purchase Wachovia—much of it gets directed in ways that increase inequality. One example is the persistence of the carried interest provision for hedge funds, often championed by liberal Democrat Senator Charles Schumer of New York. Another is the subprime mortgage origination industry, which was defended by lobbyists and does not seem to have helped the poor. Black homeownership rates in 2012 have fallen back to their level in the mid-1990s (McCarty, Poole, and Rosenthal 2013). Originators do seem to have benefited. Igan, Mishra, and Tressel (2009) have shown that the bulk of the lobbying on subprime was carried out by financial institutions that offered the riskiest products and that turned out to be most likely to fail.

We would also be amiss not to emphasize the role of the revolving door between politics and the private sector as another nontrivial form of political expenditure. For example, Robert Rubin, Treasury Secretary under Clinton, went to Citicorp from the US Treasury. The recently confirmed Obama Treasury Secretary, Jack Lew, after serving during the Clinton administration and doing a highly compensated stint at New York University, was chief operating officer of Citicorp from 2006 to 2008. One view is that these people are dedicated public servants who sacrifice financial gain to serve the American public. The other is that the revolving door, even with the best of intentions, clouds their decision making. Revolving door jobs, lobbying, and campaign contributions by the rich, when coupled with free market ideological proclivities in the voting population, are likely to have abetted the increase in inequality.

We might wonder what these individuals receive for their contributions? A decade ago, Ansolabehere, de Figueiredo, and Snyder (2003) asked in this journal, "Why is There So Little Money in U.S. Politics?" They concluded that money was largely directed at ideological consumption rather than buying political benefits; for an opposite view, see Gordon, Hafer, and Landa (2007). The question we focus on is a little different: Why have total contributions and the share of total contributions from the top .01 percent risen so much in the last few decades? One possibility is that campaign contributions are just another fad for the rich in the twenty-first century. Standard economic arguments are that rational people won't make large contributions in the hope of different policy outcomes for the same reason that rational people will not expect their personal vote to influence the outcome of elections.[9] However, when contributions become very large, then the notion that your contributions will be completely overshadowed by others may

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[9] There is, moreover, an ongoing academic debate about the effect of campaign spending on electoral outcomes. For the no-effect position, see Levitt (1994). For an opposing view, see Erikson and Palfrey (2000). We simply ask the reader to do the thought experiment as to what American politics would look like if one party were permitted no expenditure on polling, data analysis, grass roots organization, and television advertising.

not be as true. Large contributors may also be serving as "bundlers" (fundraisers who solicit checks from other individuals and then pass the checks along to candidates and committees), similar to the collective funding of industry lobbies such as the American Bankers Association. Contributions may help carry the day on very specific issues that relate to income inequality—like the provisions that allow the "carried interest" income received by private equity investors to be taxed at a lower capital gains tax rate rather than the higher marginal income tax rate.

More broadly, there does seem to be evidence that members of Congress represent the views of their high-income constituents much more than those of low-income ones (for example, Bartels 2008).[10] Gilens (2012) presents considerable evidence showing that the policy outputs of the US national government are far more responsive to preferences of high-income voters, especially in policy domains where the opinions of rich and poor diverge. When the rich and poor (90th and 10th percentile incomes) disagree more than 10 percentage points on a policy question, the odds of a policy change are completely unresponsive to views of the poorer voters. But if 80 percent of high-income voters support the change, it has a 50 percent chance of passing compared to only a 32 percent chance of passing with 80 percent support from the poor.[11]

Political Institutions and Reactions to Inequality

The United States is more majoritarian (winner takes all) in its political institutions than many nations, but also has a higher degree of inequality, which suggests the possibility that less-majoritarian systems may in fact have less inequality. Empirically, the use of proportional representation—in which at least some members of the legislature are chosen in proportion to the vote of an area, not in elections in single-person districts—correlates with lower levels of economic inequality. Austen-Smith (2000) and Iversen and Soskice (2006) match this stylized fact in theoretical models. Although the proposed mechanism varies, the central insight is that plurality rule (where the candidate with the most votes wins) is conducive to two-party political systems (Duverger 1954). In turn, political bargaining in two-party systems tends to privilege coalitions of the middle and upper classes against the poor. A related institutional distinction compares parliamentary regimes, which lack a strong separation of powers between the legislative and executive branch

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[10] The Bartels (2008) claim is based on correlating DW-NOMINATE scores with public opinion data. The claim, however, has been criticized on methodological grounds by Bhatti and Erikson (2011). Using much larger sample sizes, Tausanovitch (2011) confirms the Bartels claim but then argues that the poor are nonetheless represented. His argument is that even if the DW-NOMINATE scores correlate more highly with the expressed preferences of those with high incomes, the scores also respond to the proportion of poor constituents. Resolving the representation controversy is undoubtedly complicated by the fact, documented above, that the rich are a very heterogeneous group.

[11] He does find however that the gap in responsiveness of the preferences of the rich and poor is largest on noneconomic issues such as abortion and homosexuality, areas in which high-income voters tend to take the liberal positions.

(because the executive is selected by the party with a majority in the legislative branch), to presidential-congressional ones, with separation of powers. Here the theoretical analysis of Persson, Roland, and Tabellini (2000) points to less redistribution in presidential-congressional regimes like the United States.

It is an open question as to the robustness of the conclusions of various theoretical models of the politics of inequality. In at least some cases, the theoretical predictions are not robust to changes in assumptions. For example, Olszewski and Rosenthal (2004) show that political coalitions and after-tax outcomes can shift dramatically in certain models when a quasi-linear utility function is replaced by a Cobb–Douglas utility function.

In the past, most political economy models that depart from majoritarian settings imposed some form of compromise bargaining in the political process (for some different approaches, see Baron and Ferejohn 1989; Alesina and Rosenthal 1995; Grossman and Helpman 1999). However, as compromise has been expunged from the Washington political dictionary, political science models of policy formation have largely turned to *pivot* models following the seminal work of Krehbiel (1998). Pivot models embed the institutional structure of the political system of the federal government. In order to change policy from the status quo, legislation must pass over hurdles that include passage by simple majority in both Houses of Congress, the 60 votes needed to shut down possible filibusters in the Senate, and the two-thirds majorities in both houses needed to override vetoes by the president, followed by challenges in the courts and possible foot-dragging or noncompliance in the states. Models of these institutional processes identify the actors whose support is necessary for policy change. These actors are known as *pivots*. Potential pivots include the median representative in the House (or perhaps, the median member of the majority party), the filibuster pivot in the Senate, and veto override pivots in both houses. At a given time, which of the potential pivots will be the pivotal legislator depends on the distribution of liberal–conservative preferences in the two chambers. The internal rules of the two Houses of Congress also constitute hurdles.

Of course, the membership of the US Congress is not simply determined by popular majorities, which leads to additional hurdles. Article V of the US Constitution has one unamendable provision that gives each state two votes in the Senate, without regard to population. The provision creates a situation in which some senators represent far fewer people than others. A pivot hurdle on the Affordable Care Act was Ben Nelson, the Democratic senator furthest to the right. Nelson is from Nebraska, which has its two of the 100 senators but only three of the 435 representatives. Majority representation in the House is distorted by geographic sorting of the population and, to a lesser extent, by gerrymandering that favors the Republicans. Gerrymandering explanations are rampant in the media but they should not be exaggerated. Democrats lost the House in 2010, but they won it with the same apportionment in 2006 and 2008. While gerrymandering has a Republican bias, it does not seem to contribute to polarization. Both geographic sorting and gerrymandering are discussed in more detail in McCarty, Poole, and Rosenthal (2009).

Multiple pivots imply that status quo policies may become gridlocked. The range of gridlocked policies expands theoretically, and has also expanded empirically, as polarization of legislative preferences increases. Expanded polarization has resulted in diminished legislative output (McCarty, Poole, and Rosenthal 2006, pp. 177–183).

Even if gridlock is sometimes overcome, policy change will need to be moderated to attract the support of critical pivots. In the first two years of the Obama presidency, for example, the stimulus package, the Patient Protection and Affordable Care Act, and the Dodd–Frank Act all passed. However, each piece of legislation was sharply limited by the need to obtain 60 votes to avoid a Senate filibuster. All three initially passed the Senate with exactly 60 votes. To obtain passage of the stimulus bill, the administration needed to cut $200 billion of assistance to state and local governments. Among the many concessions made in Dodd–Frank, a tax on banking transactions was removed to obtain the pivotal vote of Republican Senator Scott Brown of Massachusetts (McCarty, Poole, Romer and Rosenthal 2010). The Patient Protection and Affordable Care Act did raise certain taxes on those with high incomes, but in many ways it was constructed to appease insurance and pharmaceutical companies. Taxes were also increased on high incomes in the "fiscal cliff" legislation of 2012, but rates remain well below the levels in effect before the Reagan presidency. Moreover, this legislation ended payroll tax cuts that had provided low-income tax relief during the Great Recession. In the 2010 midterm elections, the Republicans regained control of the House of Representatives. The pivot was thus shifted from the relatively moderate 60th (from the left) position in the Senate to the quite conservative House median. The 2012 tax legislation reflected this shift.

Legislative gridlock also allows policies to drift. In principle, this effect could increase or decrease inequality. For example, an unindexed minimum wage falls in real terms if not updated by law. In contrast, unindexed income tax rates lead to "bracket creep" and higher taxes as inflation gradually pushes incomes into higher tax brackets. But in practice, indexing seems to have been applied more often where it prevents the rich from suffering the effects of a drifting policy: income tax brackets are indexed for inflation, but minimum wages are not.

Gridlock may also produce bureaucratic drift: those who are regulated can turn to a variety of different regulators at the federal level, as well as in the states and the courts, and when the legislature is gridlocked, these regulators become freer to pursue their own policy objectives without fear of legislative override (Ferejohn and Shipan 1990). This dynamic was very important in financial deregulation (McCarty, Poole, and Rosenthal 2013). For example, the barriers between commercial banking, investment banking, and insurance enshrined in Glass–Steagall were whittled to nearly nothing by regulators and court decisions well before Congress officially repealed the law. Regulatory conflict between the Federal Reserve, the Office of the Comptroller of the Currency, and the FDIC also facilitated lobbying as a gridlocked Congress first took two years from the financial crisis to enact Dodd–Frank and then produced a bill with substantial regulatory discretion (Bair 2012). Financial

industry lobbyists have to date been very successful in modifying and delaying new rules, many of which are still being written. But legislative polarization makes it exceedingly unlikely that Congress will be able to revisit Dodd–Frank and correct its shortcomings or overturn regulatory decisions.

Conclusion: Politics and Reacting to Inequality

Economists may be inclined to downplay the role of politics and public policy in generating and perpetuating inequality. Of course, economic shifts like globalization, technological shifts like information and communications technology, and social changes like the greater propensity of high-income earners to marry each other can lead to increases in inequality. But these changes are not orthogonal to political decisions that are taken—or decisions not taken.

For example, Piketty and Saez (2003) suggest that sharp changes in income inequality have been driven by destruction of assets in economic depressions and wars and by changes in fiscal policy. The economic policies that abet and respond to depressions are the subject of political processes, while "war is the continuation of politics by other means" (von Clausewitz 1832 [2009]). Open immigration policies, as argued by some economists like Borjas (1999), may increase inequality. The influence of globalization reflects political decisions about the free movement of goods and services. Globalization of financial services allows the wealthy to benefit from tax avoidance strategies by moving funds abroad or not bringing them home, depending on the policies embedded in the US tax code and the enforcement vigor of the IRS. The pace of technological development is intertwined with public policies related to innovation and intellectual property, and the applications of technology are intertwined with how, often slower-moving, regulatory agencies struggle to keep pace. The complexity in derivatives that emerged, with its disastrous consequences for the global economy, required both explicit acquiescence by the government in the form of legislation such as the Commodity Futures Modernization Act of 2000 and implicit acquiescence in the failure to exercise supervision. The deregulation and lack-of-regulation of the financial sector in the 1990s and early 2000s helped to shape the practices and compensation in that industry.

Thus, our general argument is that politics and public policy need to be considered explicitly in any discussion of the causes and consequence of inequality. The feedback from politics can also arise as a result of laws that were frozen in place, or that were never enacted. Top marginal tax rates in the United States declined sharply from the 1960s through the 1980s, but since then have fluctuated only mildly. US spending programs are increasingly focused on the elderly rather than on broader assistance to those of working age or those with low incomes. Overall, the kinds of government policies that could have ameliorated the sharp rise in inequality have been immobilized by a combination of greater polarization, lack of voter participation, feedback from high-income campaign contributors, and political institutions that must overcome a series of key pivots before making significant changes.

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