

Redistribution with Political Constraints: Legal Rules Compared to Taxes and Transfers

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ABSTRACT

A widely accepted result, associated with Louis Kaplow and Steve Shavell, is that it is more costly to use legal rules to redistribute income than to use the tax and transfer system (the income-tax-only result). An assumption behind this result is that if a legal rule is changed to alter its income-redistributive effects, the tax and transfer system will be adjusted to counteract the effects of those changes on the distribution of income. A number of commentators have questioned this assumption, suggesting that political constraints may limit the ability of the tax and transfer system to adjust to changes in legal rules. They conclude that legal rules should sometimes, or always, be designed to redistribute income. This Article addresses this critique.

It starts by examining whether, in the contemporary United States, the tax and transfer system adjusts as required by the income-tax-only result. The empirical problem is complex because there are many legal changes (often offsetting in their effects on inequality) as well as other changes in the economy in any given period. The tax and transfer system only needs to adjust to the aggregate effects for the income-tax-only result to hold. We do not need to see simple, direct correspondence between a legal change and a tax system change. Notwithstanding the empirical challenge, the evidence is strongly suggestive that the required tax and transfer system adjustments happen.

The Article then assumes to the contrary that the tax and transfer system adjustments do not happen and examines the implications. It argues that even so, we should not use legal rules to redistribute income for three reasons. First, any norm allowing the use of legal rules to redistribute would allow regressive as well as progressive legal rules. Second, if legal rules can be both regressive and progressive and the party controlling the legal system changes hands over time, the redistributive effects of legal rules will offset one another. When there are reversals of this sort, the

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redistributive effect is the net of the different legal rules while the efficiency costs are the sum of the efficiency costs of the different legal rules. As a result, the efficiency costs may be orders of magnitude higher than the efficiency costs of using the tax system. Finally, current institutions are well structured to design tax and transfer rules that redistribute income, but not for legal rules. Moreover, there are good reasons to believe that the United States will not develop the necessary institutions for designing redistributive legal rules. Combined, these three arguments imply that even if the tax and transfer system failed to adjust, we should still not use legal rules to redistribute income.

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I. INTRODUCTION

By some measures, income inequality is at levels not seen since the days of the robber barons, with the wealthy capturing an overwhelming share of our nation's output.¹ Inequality at this level is thought to cause a variety of harms, including distortions to the political process,² lower income growth for middle and lower-class households,³ reduced

1. See Thomas Piketty & Emmanuel Saez, *Income Inequality in the United States, 1913-1998*, 68 Q.J. ECON. 1, 11 (2003).

2. See LARRY M. BARTELS, *UNEQUAL DEMOCRACY: THE POLITICAL ECONOMY OF THE NEW GILDED AGE* 345 (2d ed. 2016).

3. See Paul Krugman, *Why We're in a New Gilded Age*, N.Y. REV. (May 8, 2014), <https://perma.cc/MVQ5-NS5S>.

mobility,⁴ lower social cohesion,⁵ and worse health outcomes.⁶ For these and other reasons, many people view income inequality as one of the central problems facing the United States.⁷

A central question for both law and policy is what to do to address rising income inequality. To the extent we believe that inequality is one of the most important problems facing our society, it is tempting to use all possible solutions, in the words of one scholar, to seek “a thousand points of equity.”⁸ This approach would include shifting legal rules away from the content they might otherwise have (e.g., their efficient or their otherwise fair content) so that they redistribute income. For example, we might make tort damages or levels of care dependent on income, enforce antitrust rules more vigorously when the harms affect poor consumers, or limit otherwise desirable immigration if it helps the rich. Contract enforcement might take the income levels of the parties into account. Perhaps the poor could be allowed to infringe on property rights held by the rich but not vice versa. The possibilities for attacking inequality using legal rules are endless.

In a series of articles, however, Louis Kaplow and Steven Shavell argued against this approach, not because they are opposed to redistribution but because they believe that redistribution is better done through the tax and transfer system.⁹ Although scholars have raised

4. See Raj Chetty et al., *The Fading American Dream: Trends in Absolute Income Mobility Since 1940*, 356 SCIENCE 398, 398–406 (2017).

5. See Robert Andersen, *Support for Democracy in Cross-national Perspective: The Detrimental Effect of Economic Inequality*, 30 RSCH. SOC. STRATIFICATION & MOBILITY 389, 399–400 (2012); see also Robert Andersen & Tina Fetner, *Economic Inequality and Intolerance: Attitudes toward Homosexuality in 35 Democracies*, 52 AM. J. POL. SCI. 942, 954 (2008).

6. See Pravin Matthew & Donka Mirtcheva Brodersen, *Income Inequality and Health Outcomes in the United States: An Empirical Analysis*, 55 SOC. SCI. J. 432, 436 (2018).

7. See generally, e.g., EMMANUEL SAEZ & GABRIEL ZUCMAN, *THE TRIUMPH OF INJUSTICE* (2019); JOSEPH E. STIGLITZ, *THE PRICE OF INEQUALITY: HOW TODAY’S DIVIDED SOCIETY ENDANGERS OUR FUTURE* (2012); George Packer, *The Broken Contract - Inequality and American Decline Essay*, 90 FOREIGN AFF. 20 (2011); Jacob S. Hacker & Paul Pierson, *Winner-Take-All Politics: Public Policy, Political Organization, and the Precipitous Rise of Top Incomes in the United States*, 38 POL. & SOC’Y 152 (2010); ROBERT H. FRANK & PHILIP J. COOK, *THE WINNER-TAX-ALL SOCIETY* (1995); RICHARD WILKINSON & KATE PICKETT, *THE SPIRIT LEVEL: WHY GREATER EQUALITY MAKES SOCIETIES STRONGER* (2011).

8. Zachary D. Liscow, *Redistribution for Realists*, 107 IOWA L. REV. 495, 501 (2022).

9. See, e.g., Louis Kaplow & Steven Shavell, *Why the Legal System Is Less Efficient than the Income Tax in Redistributing Income*, 23 J. LEGAL STUD. 667, 668–69 (1994) [hereinafter Kaplow & Shavell, *Why the Legal System is Less Efficient*]; Louis Kaplow & Steven Shavell, *Should Legal Rules Favor the Poor? Clarifying the Role of Legal Rules and the Income Tax in Redistributing Income*, 29 J. LEGAL STUD. 821, 823–25 (2000) [hereinafter Kaplow & Shavell, *Clarifying the Role of Legal Rules*]; Steven Shavell, *A Note of Efficiency vs. Distributional Equity in Legal Rulemaking: Should Distributional Equity Matter Given Optimal Income Taxation?*, 71 AM. ECON. REV. 414, 416–17 (1981). For

criticisms,¹⁰ the argument, sometimes referred to as the “income-tax-only argument,” is now accepted as the standard wisdom in economic approaches to law.¹¹

In the last several years, a number of commentators have raised a new criticism of the income-tax-only argument. The key claim made by these commentators is that the political (as opposed to legal or economic) assumptions in the income-tax-only argument are not realistic. In particular, the income-tax-only argument requires that the tax and transfer system be sufficiently responsive to inequality caused by legal rules that redistribution via legal rules is not necessary. (I will describe the precise nature of this requirement below.) These commentators argue that redistribution through the tax and transfer system is limited because of political constraints and, therefore, does not meet the responsiveness requirements. Because a precondition for the income-tax-only argument to apply is not met, we should reject the income-tax-only argument and seek to address income inequality by using redistributive legal rules.

Lee Fennell and Richard McAdams were the first to make this argument.¹² They argue that there are costs to enacting all legislation, including tax legislation. These political transactions costs make the tax

related literature, *see generally* Aanund Hylland & Richard Zeckhauser, *Distributional Objectives Should Affect Taxes but Not Program Choice or Design*, 81 SCANDINAVIAN J. ECON. 264 (1979); Louis Kaplow, *Public Goods and the Distribution of Income*, 50 EUR. ECON. REV. 1627 (2006); Louis Kaplow, *On the (Ir)Relevance of Distribution and Labor Supply Distortion to Government Policy*, 18 J. ECON. PERSPS. 159 (2004); Louis Kaplow, *On the Undesirability of Commodity Taxation even when Income Taxation Is not Optimal*, 90 J. PUB. ECON. 1235 (2006); LOUIS KAPLOW, *THE THEORY OF TAXATION AND PUBLIC ECONOMICS* (2011); Louis Kaplow, *Taxing Leisure Complements*, 48 ECON. INQUIRY 1065 (2010); Louis Kaplow, *Optimal Control of Externalities in the Presence of Income Taxation*, 53 INT’L ECON. REV. 487 (2012); David A. Weisbach, *Should Legal Rules Be Used to Redistribute Income?*, 70 U. CHI. L. REV. 439 (2003); David A. Weisbach, *Distributionally-Weighted Cost Benefit Analysis: Welfare Economics Meets Organizational Design*, 7 J. LEGAL ANALYSIS 151 (2015).

10. *See, e.g.*, Christine Jolls, *Behavioral Economics Analysis of Redistributive Legal Rules Symposium: The Legal Implications of Psychology: Human Behavior, Behavioral Economics, and the Law*, 51 VAND. L. REV. 1653, 1654–67 (1998); Kyle Logue & Ronen Avraham, *Redistribution Optimally: Of Tax Rules, Legal Rules, and Insurance*, 56 TAX L. REV. 157, 165–67 (2002); Ronen Avraham et al., *Revisiting the Roles of Legal Rules and Tax Rules in Income Redistribution: A Response to Kaplow and Shavell*, 89 IOWA L. REV. 1125, 1127–31 (2003); Richard S. Markovits, *Why Kaplow and Shavell’s Double-Distortion Argument Articles Are Wrong*, 13 GEO. MASON L. REV. 511, 519 (2004); Tomer Blumkin & Yoram Margalioth, *On the Limits of Redistributive Taxation: Establishing a Case for Equity-Informed Legal Rules*, 25 VA. TAX REV. 1, 2–3 (2005); Daphna Lewinsohn-Zamir, *In Defense of Redistribution through Private Law*, 91 MINN. L. REV. 326, 329–32 (2006); Richard L. Revesz, *Regulation and Distribution*, 93 N.Y.U. L. REV. 1489, 1492 (2018).

11. *See* Lee Anne Fennell & Richard H. McAdams, *The Distributive Deficit in Law and Economics*, 100 MINN. L. REV. 1051, 1062 n.32 (2015) (arguing that the income-tax-only argument is the standard wisdom and collecting sources).

12. *See* Fennell & McAdams, *supra* note 11, at 1063.

and transfer system insufficiently responsive to meet the requirements of the income-tax-only argument. That is, Fennell and McAdams view the income-tax-only argument as a Coasean argument that illustrates possibility in the absence of transactions costs. Actual policy, however, needs to take transactions costs, including political transactions costs, into account. Once we do so, legal rules should sometimes, and perhaps often, redistribute income.

Several years later, Alex Raskolnikov surveyed a broad swath of legal changes since around 1990 and concluded that many had bad distributive effects.¹³ He argues that the income tax system, however, was not adjusted to offset these effects. Like Fennell and McAdams, Raskolnikov concludes that the tax and transfer system is not sufficiently responsive to meet the requirements of the income-tax-only argument and, therefore, legal rules should be used to redistribute income.

Finally, Zachary Liscow argues that psychological effects, such as framing, cause people to prefer redistributing income through legal rules to redistributing the same amount through the tax system.¹⁴ To support this claim, he relies on surveys and experimental evidence of individual preferences regarding methods of redistribution. Because of these framing problems, the income-tax-only argument will not be as responsive to rising inequality as legal rules. He concludes that we should, therefore, use legal rules to address income inequality.

These authors (collectively, the “critics”) conclude that legal rules *should* be used to redistribute income, depending on the critic, either some of the time or all of the time. They suggest that the income-tax-only conclusion should be reversed¹⁵ and its assumptions inverted¹⁶ in light of the political realities of addressing income inequality. Redistribution must be realistic, not done only in theory.¹⁷

My goal in this Article is to explore this criticism of the income-tax-only argument. This criticism puts politics into Kaplow and Shavell’s largely institution-free approach.¹⁸ The question is, to what extent, if at all, does the income-tax-only argument survive once we add politics?

13. See Alex Raskolnikov, *Distributional Arguments, in Reverse*, 105 MINN. L. REV. 1583, 1666 (2021).

14. See Liscow, *supra* note 8, at 525.

15. See Raskolnikov, *supra* note 13, at 1596.

16. See Lee Anne Fennell & Richard H. McAdams, *Inversion Aversion*, 86 U. CHI. L. REV. 797, 806 (2019) (suggesting that the assumption of distributive invariance should be inverted).

17. See Liscow, *supra* note 8, at 556.

18. See Kaplow & Shavell, *Why the Legal System is Less Efficient*, *supra* note 9, at 667–69. Kaplow and Shavell have an implicit institutional story, and that story was most likely not chosen without thought. As we will see, the implicit institutional setting is quite robust. Nevertheless, they have no explicit political institutions in their models.

Part II provides a brief overview of the income-tax-only argument. The argument should be relatively familiar to most readers, but understanding what it assumes is important. In particular, we need to know precisely what the income-tax-only argument requires of the tax and transfer system because that is the focus of the critics' arguments. Part II then provides more details on the criticisms that the argument has faced, focusing on the recent criticisms regarding political responsiveness.

Part III considers the question of whether the tax and transfer system is sufficiently responsive to meet the assumptions of the income-tax-only argument. The critics argue that it is not.

Part III starts by carefully stating what we should expect to observe in the data if the tax and transfer system meets or fails to meet the requirements of the income-tax-only argument. It shows that empirically verifying or refuting the assumptions in the income-tax-only argument is not straightforward and that none of the data the critics bring to the question refutes the assumptions about tax system responsiveness. It examines what we know about tax and transfer responsiveness. It shows that the tax system has been extremely responsive to changing inequality, changing in response to changing conditions. Over the last several decades, those changes have made the system markedly more progressive. While, for reasons I will discuss, there is no straightforward way to empirically guarantee that the tax and transfer system has been sufficiently responsive to meet the requirements of the income-tax-only argument, the data is strongly suggestive that it is.

Part IV assumes to the contrary, that the income tax is not sufficiently responsive to meet the requirements of the income-tax-only argument and examines the implications. That is, it grants the empirical claims made by the recent criticisms and asks whether the normative conclusions made by those criticisms follow. It argues that: (1) once we allow distributive preferences to be incorporated into legal rules, legal rules can be regressive as well as progressive; (2) the costs of using legal rules to redistribute may be much higher, indeed orders of magnitude higher, than the income-tax-only argument suggests; and (3) current institutions are not well-designed to promote redistribution through legal rules but are for the tax and transfer system and, moreover, there are good reasons to believe that this difference in institutional capacities will remain.

The conclusion from the analysis in Part IV is that even if the tax and transfer system was not sufficiently responsive to meet the requirements of the income-tax-only argument, it would still be a bad idea to try to use legal rules to address distributive concerns. We are more likely to get costly and regressive legal rules than we are to get well-designed, effective legal rules that reduce inequality. Combining Parts III and IV, there is little or no case for preferring the use of legal rules to address inequality instead

of the tax and transfer system once we add political constraints to the argument.

Before turning to the argument, I need to make an important caveat. The income-tax-only argument, in its original form, is framed as a theorem. It is proven mathematically. The critics' argument is that the assumptions of the theorem do not describe the current institutional structure in the United States. That is, the arguments are about the applicability of the income-tax-only theorem to a particular time and place, the contemporary United States, to, in the words of one critic, look for realistic means of redistribution.¹⁹

This Article takes the same stance as the critics. It focuses on how well the assumptions of the income-tax-only argument apply to the contemporary United States, including its tax and transfer system and its legal institutions. This means that we are no longer in the world of theorems. Instead of mathematical proofs, the goal is to look for general tendencies and to examine current (or near future) institutional structures. As a result, the conclusions are necessarily tentative. One can imagine other societies or times where these tendencies or institutional structures are different, in which case, the conclusions might also be different.

II. BACKGROUND

The income-tax-only argument has been widely discussed in the literature, so I provide only a brief overview here.²⁰ My focus is on the assumptions about the tax and transfer system.

Consider a legal rule that deviates from its otherwise desirable content because it attempts to redistribute income. The literature, following the example used in the original Kaplow and Shavell paper, often considers a tort rule that adjusts damages based on the income of the injurer. For example, rather than making all injurers pay damages equal to the harm they caused, rich injurers might be forced to pay damages equal to twice the harm they caused, and poor injurers half. The rule is inefficient

19. See Liscow, *supra* note 8, at 556.

20. See sources cited *supra* notes 9–10. Note that many descriptions of the income-tax-only argument are inaccurate. In particular, descriptions that claim it relies on a so-called “double distortion” are not accurate. See, e.g., David Gamage, On Double-Distortion Arguments, Distribution Policy, and the Optimal Choice of Tax Instruments 2 (Feb. 2, 2014) (unpublished manuscript), <https://perma.cc/759G-LCZQ>; see also Richard S. Markovits, *Why Kaplow and Shavell's Double-Distortion Argument Articles Are Wrong*, 13 GEO. MASON L. REV. 511, 550–55 (2004). While, in some sense, the double distortion explanation gives an intuition for the argument, the formal claim does not rely on counting distortions.

because rich people would take excessive care and poor people would take too little care, but it might redistribute income from the rich to the poor.²¹

The income-tax-only argument against this sort of redistribution has three steps:

Step one: Replace the redistributive tort rule with an efficient tort rule in which all injurers pay damages equal to the harm that they cause. Care levels would adjust to be more efficient, increasing total resources. The change, however, would be regressive.

Step two: To offset this regressivity, adjust the tax and transfer system so that the utility of individuals at each income level is held constant.²²

In the torts example, the adjustment to the tax and transfer system would require increasing taxes on the rich and reducing taxes (or increasing transfers) on the poor. With this adjustment, the progressivity of the combined tax and legal system would not change, which means that any disincentives caused by that progressivity, most importantly work incentives, would not change. That is, the level and the costs of redistribution are held fixed by the combination of steps one and two.

Because the tort system is now more efficient, however, total resources have increased. Utility for each individual is, by construction, held constant, which means that the increase in total resources must have been captured by the government through the changes to the tax and transfer system.

Step three: Adjust government policy to use those additional resources to make at least one person, and possibly everyone, better off. For example, the government could lower taxes, distribute the resources as cash grants, or increase spending on public goods.

The net effect of the three steps is a Pareto improvement. As a result, a system combining efficient legal rules and the tax and transfer system is Pareto superior to the redistributive legal rule. The conclusion is that legal rules should not be used to redistribute income.

This argument immediately attracted a host of criticisms. Most criticisms questioned whether the tax system adjustment in step two, even if it were to happen, would, in fact, hold everyone's utility constant. The core concern was that within an income class, people might be affected by the legal rule in different ways. For example, suppose that the legal rule under consideration governs trade in a particular good. Restricting trade in the good will raise its domestic price, helping workers who produce the

21. There are many reasons why the tort rule might not redistribute income. For example, the redistributive effects also depend on who the victims are. Effects will also depend on how the rule affects victim care levels.

22. Note that the income-tax-only argument refers to the entire tax and transfer system, not just the component labeled "tax." The same is true here. Any references to the income tax include a reference to the entire tax and transfer system.

good but hurting everyone else. People at the same income level may be helped (those who work in the protected industry) or hurt (those who purchase the now more expensive trade-restricted good). An income tax adjustment that applies to everyone at that income level cannot make everyone equally well off. It can only raise or lower the average income for people in that income class. Some will end up better off (those who work in the trade-protected industry), and others worse off (everyone else), even holding the average constant.

This concern, which is about heterogeneity within income classes, has been discussed extensively elsewhere.²³ The focus here is on a different potential problem with step two. The concern is not whether an income tax adjustment, if done, holds everyone's utility constant. The concern is that the income tax adjustment will not be done in the first place.²⁴ If there is no income tax adjustment, we risk making the legal rule less progressive (in step one) without an offsetting adjustment to the tax system (step two). The net result would be to reduce overall redistribution. There would be no Pareto improvement, and we cannot conclude that using the legal system to redistribute income is undesirable, at least not without substantially more analysis. I will call this the "step two will not happen" argument, or the "step two is not valid" argument (noting that the heterogeneity argument is also about step two but is a distinct concern).

The narrowest version of this argument, which is the core of Fennell and McAdams's article, is that there are costs to changing laws, including changing the tax system as required in step two. Bills must be drafted, hearings held, coalitions formed, resistance overcome, veto-gates avoided, and so forth. As a result, the tax system might not always, and instantly, adjust to offset the distributive effects of changes to legal rules. Akin to Coasean transactions costs incurred by private actors, there are political transactions costs to adjusting the tax and transfer system. If the tax system

23. See Kaplow & Shavell, *Clarifying the Role of Legal Rules*, *supra* note 9, at 827–28.

24. Note that in many places through their articles, the critics mix up the heterogeneity criticism and the "will not happen" criticism. Most of Raskolnikov's article mixes heterogeneity concerns with the "will not happen" criticism. For example, the trade, immigration, and other rules that he examines affect particular sectors of the economy rather than overall income inequality. A tax system that responded to income inequality induced by the trade, immigration, or other rules that he examines would still leave the heterogeneous effects of those rules.

Fennell and McAdams also argue that because individuals and groups fight to win distributive fights, it cannot be the case that the tax system adjusts to offset any distributive gains within the legal system. See Fennell & McAdams, *supra* note 11, at 1081. Why, after all, would a group fight for handouts if the handouts will then immediately be taken away by the tax system? But these lobbying efforts are for discrete sectors, such as public-school teachers or users of crack cocaine (to cite two examples that they use). The fights are about heterogeneity within an income class, not about whether the tax system can adjust to overall income changes.

does not adjust because of these costs, using the legal system to redistribute might be the best remaining option.

Taken narrowly, this argument must be correct. Between 1895 and 1913, the income tax was unconstitutional.²⁵ It was quite literally illegal to make the kind of adjustments envisioned in step two. As a result, during that time, it might have been optimal to use legal rules to redistribute income.

The question, however, is the extent to which the “step two will not happen” argument has policy relevance today. Is it true that today, as a practical matter, the income tax cannot or does not adjust to offset the distributive effects of legal rules, or more generally, to achieve the distributive goals that our nation sets for itself?

Fennell and McAdams argue that beyond a mere theoretical problem of transactions costs, the “will not happen” concern is empirically important today. To support this claim, they cite to an increase since 1974 in the after-tax U.S. Gini coefficient and to an increase in the after-tax 80/20 ratio (i.e., the share of income received by the top 20% relative to the share received by the bottom 20%), in both cases relying on OECD estimates.²⁶ They conclude that it is a *fact* that the tax and transfer system has not adjusted to offset the effects of regressive legal rules.²⁷

Raskolnikov also concludes that step two will not, and does not, happen. To support his argument, he examines a number of important legal changes over the last several decades, including trade, immigration, antitrust, labor, and environmental policies. In each case, he concludes that the policies had unexpected regressive effects. He then argues that these effects were not offset by *targeted* programs or *targeted* adjustments to the tax and transfer system. That is, Raskolnikov reads step two in the argument as requiring specific changes to the tax and transfer system rather than general changes. Finding few such targeted changes, he concludes that “Congress simply failed to offset distributional burdens through the legal system or the tax system. The tax-and-transfer adjustment assumption [step two in the terminology here] failed.”²⁸

Liscow comes to a similar conclusion, though he does so not by looking at how the tax and transfer system has changed over time, or for

25. See *Pollock v. Farmers' Loan & Tr. Co.*, 158 U.S. 601, 637 (1895) (holding that certain types of income taxes were unconstitutional because they were direct taxes that had to be apportioned among the states), *superseded by constitutional amendment*, U.S. CONST. amend. XVI.

26. See Fennell & McAdams, *supra* note 11, at 1079.

27. See *id.* (“[C]onsider . . . the fact that the tax and transfer system has not generally adjusted over time to correct for changes [in legal rules].”).

28. Raskolnikov, *supra* note 13, at 1624 (“Part II revealed that a wide range of national policies likely created unintended burdens. This Part shows that the U.S. government did little to mitigate them.”).

that matter, at data about any other existing policies.²⁹ Instead, he argues based on experimental or similar evidence that: (1) people tend to view policies in different areas (e.g., trade, immigration, torts, tax, and so forth) as separate silos, largely unconnected to one another; and (2) within the tax policy silo, people do not like very much redistribution because they believe that they (and others) deserve their pre-tax income. Instead, they have preferences, based on notions of fairness, for redistribution through legal rules.³⁰

We can think of this argument as a framing argument. With taxes, people think that the government is taking away something that is theirs. People earn their market income, and the government then takes a share. Many people resist this. When the government uses legal rules to redistribute, people never get the money in the first place. They “earn” their after-redistribution amount rather than their pre-redistribution amount. As a result, they do not resist this form of redistribution as much as they resist redistribution via the tax and transfer system.

Fennell and McAdams also make framing arguments to support the “will not happen” conclusion.³¹ Among other things, they discuss salience and cognitive biases that may make it difficult to enact tax legislation to offset the effect of legal rules and argue that preferences for fairness may make redistribution relatively less difficult.

All three critics conclude, although in various formulations, that step two will not happen, at least not always or completely. A separate question is what follows if step two does not always and completely occur to offset

29. Liscow does include one sentence citing a single source regarding how the tax system has responded to changes to overall inequality. *See* Liscow, *supra* note 8, at 522 n.129.

30. Liscow’s evidence for this claim, however, is weak. He cites a survey that he suggests shows that the public supports more equality but at the same time does not support highly progressive taxation. *See* Liscow, *supra* note 8, at 498, 549 (citing RSCH. CTR., THE GENERATIONAL GAP IN AMERICAN POLITICS 18 (2018), <https://perma.cc/N5VR-VVB2>). The survey shows no such thing. The question on the relevant page of the survey, page 18, appears to ask whether the respondent believes that the economic system unfairly favors powerful interests (we are not provided with the actual questions). *See id.* Someone may answer yes to this on the belief that various legal rules such as the antitrust rules have not been efficiently enforced. There is no reason to believe that survey respondents are sensitive to the nuances legal scholars make to distinguish efficiency from fairness. Indeed, many respondents may believe that efficient enforcement of various laws is fair.

Liscow also includes the following fairness preferences as important to the choice of whether to use legal rules or the income tax to redistribute income: (i) people’s lack of acceptance of a philosophical argument made by Liam Murphy and Thomas Nagel that people do not own their own earnings; (ii) a belief that higher market returns are deserved, (iii) desert-based attitudes; (iv) a study of two hypothetical jazz singers where people think that the one who has a better genetic endowment should keep her earnings notwithstanding equal effort; and (v) a survey asking about how much hypothetical people should pay for a public good. *See* Liscow, *supra* note 8, at 516–23.

31. Fennell & McAdams, *supra* note 11, at 1093–1106.

changes in inequality due to changes in legal rules. Before turning to this latter question, I first examine what we know about whether we can expect step two to happen.

III. IS THE TAX AND TRANSFER SYSTEM RESPONSIVE TO CHANGES IN LEGAL RULES?

In this Part, I examine the data on changes to the tax and transfer system over time to try to understand whether, and to what extent, the system is responsive to the distributive effects of changes to legal rules. What do the data tell us about the validity of step two and the “will not happen” argument?

A. The Empirical Challenge

Before turning to the data, we need to clarify what we should expect to observe in the data to either verify or refute step two. There are four significant problems that make it difficult to obtain clear conclusions.

An initial problem is that for conceptual clarity, the income-tax-only argument separates out a series of steps, but some of those steps, in practice, are likely to be combined into a single policy. That makes observing each individual step difficult or impossible.

In particular, recall the three hypothetical steps in the income-tax-only argument: (1) a shift from an inefficient legal rule to an efficient legal rule; (2) a shift to the tax and transfer system to hold utility at each income level at the pre-step one level; and (3) distribution of the gains produced from steps one and two. Steps two and three are both changes to the tax and transfer (and possibly spending) systems. The income-tax-only argument separates them for conceptual clarity, but when the government changes the tax and transfer system, there is no reason that it would follow this breakdown rather than combining and simultaneously enacting the net of steps two and three.

A combined steps two and three, however, need not be distribution neutral because step three involves a distribution of a surplus. The surplus can be distributed to increase, reduce, or hold constant the pre-change level of inequality, as the government sees fit. As a result, the single policy change that combines steps two and three may not seem to meet the requirements of step two taken alone because it is not distribution-neutral. Nevertheless, the combined steps two and three policy could be completely consistent with the income-tax-only argument. As a result, observing an increase in after-tax and transfer inequality in the data does not tell us that step two does not happen.

Second, while the income-tax-only argument considers a single, hypothetical legal rule and a corresponding tax change, in practice, it would apply to the aggregate distributional effects of large groups of legal

rules. In a country the size of the United States, there are thousands of legal changes every day, once one counts federal, state, and local court decisions, decisions by other types of tribunals, administrative rulemakings, guidance documents, changes to statutes and municipal codes, and so forth. Each of these changes to the legal system potentially changes the distribution of income. The income-tax-only argument does not require separate changes to the tax and transfer system to respond to each change in a legal rule. Instead, for step two to be valid, the tax and transfer system need only regularly respond to net changes in inequality.

For example, suppose that a tort rule changes, transferring \$100 from the wealthy to the poor, and, at the same time, a contracts rule changes, transferring \$70 from the poor to the wealthy. We do not need separate \$100 and \$70 tax changes for the income-tax-only argument to be true. A single tax change offsetting the net \$30 transfer from the wealthy to the poor due to these two legal changes would be sufficient.

This means that we cannot expect to look at the data and find one-for-one changes to legal rules and changes to the tax system, which is how the model is framed.³² Instead, we should see aggregate changes to the tax system to respond to aggregate net changes due to legal rules.

Third, and for similar reasons, the tax and transfer system only needs to respond to net legal changes over a reasonable period of time rather than every day, hour, or second. If the contract law change hypothesized above happens the next day, rather than the same day as the tort law change, we should not expect the tax law to separately respond to each. We do not need the tax law to make a \$100 transfer from the poor to the wealthy to offset the torts rule and then the next day make a \$70 transfer from the wealthy to the poor to offset the contracts rule. Instead, periodic tax law changes that respond to the aggregate effect of legal rules are sufficient for step two to be valid.

There is no bright line telling us the right period for tax system adjustments. The question is practical rather than theoretical. No adjustment for long periods of time would be inconsistent with the income-tax-only argument. Requiring changes to the tax and transfer system every day, week, or month, however, does not seem necessary.

Finally, and perhaps most importantly, there are good reasons to believe that a substantial fraction of the change in inequality over the recent past has been due to non-legal factors. For example, technological changes that increase the returns to high-skilled labor or the rise of China

32. Raskolnikov's claim that the tax and transfer system did not respond to the various legal changes he examined makes this mistake. He looks only at specifically targeted changes to the tax and transfer system and doesn't find any. *See* Raskolnikov, *supra* note 13, at 1624. The lack of specifically targeted changes to the tax and transfer system, however, does not tell us that step 2 did not happen.

and other trading partners may have been responsible for a large fraction of increases in inequality over the last several decades.³³ Nothing in the income-tax-only argument requires that the tax and transfer system respond to these changes, which means that an increase in after-tax and transfer inequality is not inconsistent with step two. Conversely, the tax and transfer system might respond only to these non-legal causes of changes to inequality, failing to adjust to increases in inequality due to changes in legal rules. In reality, changes to the tax and transfer system likely respond to aggregate changes in inequality. Moreover, Congress need not specifically designate the cause of a change in inequality when it adjusts the tax system. As a result, there is no way to separate legal and non-legal causes of changes to the tax system.

To summarize, over any reasonable period, there are thousands of changes to the legal system, many with offsetting effects on inequality. There are also underlying changes to the economy that change the level of inequality. Changes to the tax and transfer system likely respond to aggregate effects. And to the extent that the tax and transfer system responds to aggregate effects, it does so periodically, considering the effects over time. Finally, the breakdown of the steps in the income-tax-only argument is hypothetical, designed to clarify thinking rather than to

33. The question of what has caused the change in pre-tax-income is the subject of much current research, in part because the answer is vital to determine which public policies best respond to inequality. We can crudely group the possibilities into two categories: (1) changes to legal rules such as deregulation, a stagnant minimum wage, laws governing unionization, immigration, trade laws, and antitrust, have increased the market power of rapacious employers, suppressing wages at the low end while increasing the returns to capital held by the rich, and (2) the demand for skills driven by technological change has outpaced the supply for skills, thereby increasing the price of high-skilled labor relative to low-skilled labor. If for example, the demand for workers with a college education goes up because of a change in technology, wages for those with a college education will go up until the supply of educated workers adjusts. Because the supply of educated workers changes only slowly—only a fraction of workers enter or leave the workforce each year—there can be long periods where technological change leads to an increase in inequality. This latter story is known as the Race between Education and Technology or RBET. See CLAUDIA GOLDIN & LAWRENCE F. KATZ, *THE RACE BETWEEN EDUCATION AND TECHNOLOGY* 287 (2010); see also Jan Tinbergen, *Substitution of Graduate by Other Labour*, 27 *KYKLOS* 217, 224 (1974).

While there is surely an element of both and the debate among experts in the area is ongoing, there are reasons to believe that RBET is the central cause of the growth in inequality in pre-tax earnings. RBET is able to explain long run changes in earnings in the United States in ways that the legal rules story cannot. See Daron Acemoglu & David Autor, *What Does Human Capital Do? A Review of Goldin and Katz's The Race between Education and Technology*, 50 *J. ECON. LITERATURE* 426, 427 (2012). A more recent review of the RBET model, however, suggests that its explanatory power has been lower over the period from 2000 to 2017 than it was in previous periods. See David Autor et al., *Extending the Race Between Education and Technology*, 110 *AEA PAPERS & PROC.* 347, 351 (2020). This Article suggests that during the period between 2000 and 2017, within skill-group differences (e.g., wage differentials within the group of college graduates) became relatively more important. See *id.*

model how policy is actually implemented, which means that we cannot expect to separately observe step two.

Combined, these problems make empirically verifying or refuting step two difficult. It may not be possible to make valid statements to the effect that it is a fact that step two is false,³⁴ or the converse, that we know step two is true. Nevertheless, I will argue below that the evidence on changes to the tax and transfer system strongly suggests that the tax system responds roughly in ways that step two imagines. That is, while we cannot know for sure, the evidence we have is far more consistent with step two being valid than the converse. Moreover, some versions of the “step two will not happen” argument, such as the transactions costs argument, can be firmly rejected.

B. A Peek at the Data

There are three suggestive pieces of evidence that the tax and transfer system responds roughly the way that is imagined in step two: (i) the tax and transfer system changes with great frequency, which belies concerns that transactions costs limit the ability of the tax and transfer system to adjust; (ii) when the tax and transfer system changes, a central concern is the effect on the distribution of income, which means that Congress is taking into account the various sources of inequality and making a judgment about how to address them on a regular basis; and (iii) as pre-tax income inequality has increased over the last 40 to 50 years, the tax and transfer system has become markedly more redistributive. Because of the empirical challenges highlighted above, we cannot draw firm conclusions. These facts are nevertheless consistent with a responsive tax and transfer system that regularly adjusts to changes in inequality, including changes in inequality due to changes in legal rules.

1. Frequent Changes

As noted, a key argument that step two will not happen is that it is costly to change the tax and transfer system. Because change is costly, we might expect the tax and transfer system to be less than fully responsive to legal changes.

One way to determine if this argument is correct is to see how often the tax and transfer system changes. If the transactions costs of changing the tax and transfer system are high, we should see only infrequent changes. Conversely, if we see frequent changes, we can conclude that the transactions costs must be low.

In fact, the income tax and the transfer system change with great frequency. According to the Urban-Brookings Tax Policy Center, in the

34. See, e.g., Fennell & McAdams, *supra* note 11, at 1079.

40-year period from 1980 to 2019, there were 62 *major* income tax laws passed by Congress.³⁵ Each of these laws contained dozens or even hundreds of individual changes to the tax system. Most, and possibly all, of these hundreds of changes to the tax system had distributive effects.³⁶ Some of these laws, such as the 1986 Tax Reform Act, involved major rewrites of the tax system, including rewrites that changed much of its basic structure.

Other counts put the number of changes at much higher levels. In 2008, the National Taxpayer Advocate found that between 2001 and 2008, the tax system changed 3,250 times, with more than 500 changes in 2008 alone.³⁷ In 2012, the chairman of the Senate Finance Committee, Max Baucus, found that in the prior 26 years (that is, since 1986), the tax system had been changed 15,000 times.³⁸ Whether the right count is 62 major changes or 15,000 smaller changes, these counts show that the tax system changes all the time.

Moreover, these counts do not include changes to the transfer system, such as the Welfare Reform Act of 1996, the Affordable Care Act (enacted in 2009), or the numerous smaller changes (including the numerous state law changes, such as the state Medicaid or unemployment rules). I am not aware of a recent survey counting changes to the transfer system parallel to the studies of changes to the tax system, most likely because the transfer system is made up of many diverse programs, making a count of changes difficult. A New York Times article from 2023 lists 27 changes made to the transfer system in a matter of months to respond to the 2020 pandemic.³⁹ Earlier work examining changes to the welfare system concluded that “[t]he system of public assistance in the United States is constantly evolving.”⁴⁰

Combined, the data show that the tax and transfer system is adjusted multiple times each year. This is not consistent with a view of the tax and transfer system that is largely static, failing to respond to changes in the

35. The Urban Institute and Brookings Institution’s Tax Policy Center has a list of major enacted tax legislation. Between 1980 to 2019 they list 62 major pieces of enacted tax legislation. *See Laws & Proposals*, TAX POL’Y CTR., <https://perma.cc/WHT8-J435> (last visited July 21, 2024).

36. Note that this is true even if the change didn’t affect the rate structure. Changes to the tax base can have as profound distributive effects as changes to the nominal rates.

37. *See* 1 NAT’L TAXPAYER ADVOC., 2008 ANNUAL REPORT TO CONGRESS 4 (2008).

38. *See* Senator Max Baucus, Keynote Address at Bipartisan Policy Center: A Tax Code for the 21st Century (June 11, 2012), in *Baucus Announces Goals for New Tax Code for New Era*, SENATE COMM. FIN. (June 11, 2012), <https://perma.cc/62Q7-K8UM>.

39. *See* Claire Cain Miller & Alicia Parlapiano, *The U.S. Built a European-Style Welfare State. It’s Largely Over.*, N.Y. TIMES (May 11, 2023), <https://perma.cc/3BWM-HMPA>.

40. Rebecca M. Blank, *Trends in the Welfare System*, in WELFARE, THE FAMILY, AND REPRODUCTIVE BEHAVIOR: RESEARCH PERSPECTIVES 33, 33 (Robert A. Moffitt, ed., 1998).

distribution of income. In particular, the evidence rejects transactions costs concerns. Whatever the transactions costs are of adjusting the tax and transfer system, they cannot be high in a system that is adjusted almost constantly.

2. Attention to Distribution

A second piece of evidence on whether step two happens is that when these frequent changes to the tax and transfer system are made, their effects on inequality and the distribution of income are almost always a first-order concern. Sometimes Congress's goal might be to make the system more regressive, offering tax cuts to the wealthy or reducing transfers to the poor. Other times, Congress might want to make the system more progressive. Regardless, the distributional effects of the changes to the tax and transfer system are front and center.

The distributional effects of tax law changes are put front and center through what are known as distributional tables. The Treasury Department typically produces these tables when the President proposes a tax law change.⁴¹ As tax law changes are considered by Congress, the Joint Committee on Taxation produces its own distributional tables, using a related but distinct methodology.⁴² Separately, the Congressional Budget Office publishes an annual report on the distribution of federal taxes.⁴³ And in addition, think tanks in Washington often produce their own estimates as bills work their way through Congress.⁴⁴ That is, at least annually, and for essentially every tax bill introduced, Congress has in front of it at least one and possibly two, three, or more tables describing the distributional effects of the change to the tax system.

Note, importantly, that the distributional tables include the effects on inequality of changes to legal rules. They are “all in” estimates, in the

41. See JULIE-ANNE CRONIN, U.S. TREASURY DISTRIBUTIONAL ANALYSIS METHODOLOGY 2–4 (2022) (describing Treasury's methodology for producing distributional tables).

42. Revenue estimates for each tax bill are required by law. Distributional tables are produced by the Joint Committee on Taxation upon request of a member of Congress. See *Revenue Estimating*, JOINT COMM. ON TAX'N, <https://perma.cc/K8ZW-XZMZ> (last visited Aug. 16, 2024). Nevertheless, they are effectively always produced. See generally JOINT COMM. ON TAX'N, MODELING THE DISTRIBUTION OF TAXES ON BUSINESS INCOME (2013); JOINT COMM. ON TAX'N, METHODOLOGY AND ISSUES IN MEASURING CHANGES IN THE DISTRIBUTION OF TAX BURDENS (1993); Edward D. Kleinbard, Chief of Staff, Joint Comm. On Tax'n, Reading JCT Staff Distribution Tables: An Introduction to Methodologies and Issues, Keynote Address to the 21st Annual Institute on Current Issues in International Taxation in Washington, D.C. (Dec. 9, 2008) (describing the Joint Committee on Taxation's methodology).

43. See generally CONG. BUDGET OFF., THE DISTRIBUTION OF HOUSEHOLD INCOME AND FEDERAL TAXES, 2020 (2023).

44. See, e.g., *Analysis of the Tax Cuts and Jobs Act*, TAX POL'Y CTR, <https://perma.cc/4RJ2-U9QG> (May 8, 2020).

sense that they measure existing inequality and changes to inequality from the proposed tax law change. Existing inequality is in part affected by legal rules, which means that the effects on inequality due to legal rules are part of the baseline estimate. For example, if trade liberalization has caused an increase in inequality, that increase in inequality will show up in the distributional tables. As a result, when Congress considers the distributional effects of the tax system, it is including the effects on inequality due to legal rules.

Writing in 1995, Michael Graetz addressed the effect of these distributional tables (along with revenue estimates) on tax legislation.⁴⁵ He concluded that distributional tables were “outcome-determinative.” To my knowledge, that has not changed in the 30 years since Graetz made this observation.⁴⁶

Supporting this line of reasonings, over the last 40 to 50 years, commentators and Congress itself have frequently fought over how these tables are produced, a testament to their importance. For example, during the debate over the 2017 Tax Cuts and Jobs Act, analysts on the left and right strenuously fought over whether cutting the corporate tax would help wealthy owners of capital or workers. The Council of Economic Advisors argued that most of the benefit of cutting corporate taxes would accrue to workers, which meant the proposed corporate tax cut was progressive.⁴⁷ Others, such as experts at the Urban-Brookings Tax Policy Center, argued that the benefits would accrue to owners of capital, making corporate tax cuts regressive.⁴⁸ These sorts of debates are central to tax legislation.

Combining these first two points, the idea that the tax system is static and does not respond to changes in underlying inequality is demonstrably incorrect. It is constantly adjusted with great attention to the distribution of income.

45. See Michael Graetz, *Paint-by-Numbers Tax Lawmaking*, 95 COLUM. L. REV. 609, 612 (1995).

46. To illustrate, the 2017 Tax Cut and Jobs Act was, as usual, accompanied by distributional tables as it worked its way through Congress. See generally JOINT COMM. ON TAX'N, JCX-68-17, DISTRIBUTIONAL EFFECTS OF THE CONFERENCE AGREEMENT FOR H.R. 1, THE “TAX CUTS AND JOBS ACT” (2017). In addition, there have been many analyses of its effect by academics and think tanks. See *Analysis of the Tax Cuts and Jobs Act*, supra note 44; see also William Gale et al., *Effects of the Tax Cuts and Jobs Act: A Preliminary Analysis*, BROOKINGS (June 14, 2018), <https://perma.cc/4F5L-EHNF>; Aparna Mathur & Cody Kallen, *Distributional Impacts of the Tax Cuts and Jobs Act*, 74 NAT'L TAX J. 721, 721 (2021).

47. See Kevin Hassett, Chairman, Council of Econ. Advisors, Prepared Remarks Before the Tax Policy Center Tax Foundation (Oct. 5, 2017).

48. For responses to the CEA, see Howard Gleckman, *Will A Corporate Wage Cut Really Increase US Jobs and Wages?*, TAX POL'Y CTR. (Oct. 5, 2017), <https://perma.cc/ECT5-5C72>; see also Larry Summers, *Hassett's Flawed Analysis of Trump's Tax Plan*, LARRY SUMMERS (Oct. 17, 2017), <https://perma.cc/X422-Y64V>.

3. Increase in Redistribution

What has been the net effect of all these changes to the tax system? Estimating the extent that the tax and transfer system redistributes is a surprisingly difficult task. Problems include how to account for changing household composition over time, how to estimate hidden income, such as income hidden by tax shelters, how to distribute indirect taxes, such as the corporate tax, and how to account for tax-deferred income, such as pensions. These seemingly technical problems can have large effects on the estimates.

There is a sizable literature debating various problems and techniques for estimating the effects, and there remains a great deal of uncertainty notwithstanding extensive study.⁴⁹ In recent work, Thomas Coleman and I looked at every study since 2013 that estimated changes in the progressivity or redistributive effects of the tax and transfer system.⁵⁰ Given the substantial uncertainty in estimating the effects of taxes because of the factors just mentioned, our goal was to find results that were robust across studies and methodologies. Starting with a complete list of published studies on the topic, we then eliminated studies that did not meet basic credibility requirements or did not make their data available (so that we could use the data to make comparisons).

Most studies did not make their data available, and a small handful did not meet our credibility requirements. This left us with three studies or series of studies: the annual studies of the distribution of federal taxes by the Congressional Budget Office,⁵¹ a 2018 paper by Thomas Piketty, Emmanuel Saez, and Gabriel Zucman,⁵² and a 2024 paper by Gerald

49. Key recent contributions include Thomas Piketty et al., *Distributional National Accounts: Methods and Estimates for the United States*, 133 Q.J. ECON. 553 (2018); Gerald Auten, *Recent Research on Income Distribution: An Overview of the Field*, 15 CAPITALISM & SOC'Y 3 (2021); Gerald Auten & David Splinter, *Top 1 Percent Income Shares: Comparing Estimates Using Tax Data*, 109 AEA PAPERS & PROC. 307 (2019); Gerald E. Auten & David Splinter, *Income Inequality in the United States: Using Tax Data to Measure Long-Term Trends*, 132 J. POL. ECON. 2179 (2024) [hereinafter Auten & Splinter, *Income Inequality in the United States*]; Jeff Larrimore et al., *Recent Trends in US Income Distributions in Tax Record Data Using More Comprehensive Measures of Income Including Real Accrued Capital Gains*, 129 J. POL. ECON. 1319 (2021); Jeff Larrimore et al., *Accounting for Income Changes over the Great Recession Relative to Previous Recessions: The Impact of Taxes and Transfers*, 68 NAT'L TAX J. 281 (2015); Philip Armour et al., *Deconstructing Income and Income Inequality Measures: A Crosswalk from Market Income to Comprehensive Income*, 103 AM. ECON. REV. 173 (2013).

50. See Thomas Coleman & David A. Weisbach, *How Progressive is the U.S. Tax System?* (Univ. of Chi. Coase-Sandor Inst. for L. & Econ., Working Paper No. 991, 2023).

51. See *The Distribution of Household Income in 2020*, CONG. BUDGET OFF. (Nov. 2023), <https://perma.cc/EP7K-K2QN>.

52. See generally Piketty et al., *supra* note 49.

Auten and David Splinter.⁵³ We attempted to make apples-to-apples comparisons of their conclusions by examining their underlying data. To ensure that our search criteria did not exclude contrary results, we also surveyed all other studies on the issue in the last ten years (though we continued to exclude studies that used outlier methodologies).

The conclusion of this effort was straightforward, though surprising: there is strong agreement that the tax and transfer system redistributes substantially more now than it did in the past. That is, the net result of the frequent changes mentioned above has been an increase in the redistributive effect of the tax and transfer system.

To illustrate, Table 1 summarizes the Auten and Splinter results.⁵⁴ It shows the percent change in pre-tax income and after-tax and transfer income for the period between 1979 and 2014 for the entire U.S. economy and selected subgroups. If there had been no change in a given measure (e.g., pre-tax income) during the 35-year period that is covered, the growth rate would be the same across all subgroups. Therefore, we can read across each line to see whether and how much income inequality grew for each measure over this period.

Table 1: Growth in Real Per-Capita Income, 1979-2014

	Average	0-50th	50-90th	90-99th	Top 1%
Pre-tax/Pre-Transfer	70.9	26.9	63.3	93.2	157.1
Pre-tax/After-Transfer	80.2	58.5	71.2	95.7	156.8
After-tax and transfer	70.9	59.3	68.8	83.2	104.6

53. See generally Auten & Splinter, *Income Inequality in the United States*, *supra* note 49.

54. Table 1 is from computations using the Auten and Splinter data found in Xi Song et al., *Three Myths About US Economic Inequality and Social Mobility*, 15 CAPITALISM & SOC'Y 1, 5 (2021).

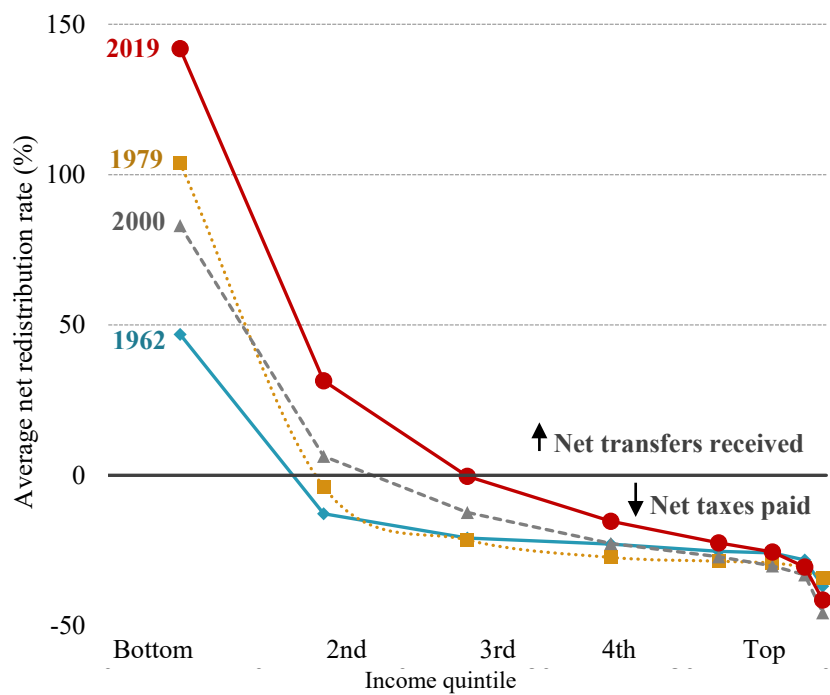
As can be seen, the growth in pre-tax income (top row) was highly skewed toward the top: as we move to the right, the growth rates get larger with the top 1% growing 157% during this period compared to only about 27% for the bottom half of households. Comparing the top line to the bottom line shows the extent to which the tax and transfer system moderates these effects. The tax and transfer system substantially reduces, but does not eliminate, the growth in inequality during that time. The growth rate for the bottom 50th percentile more than doubles because of taxes and transfers. The group between the 50th and 90th percentile stays roughly the same. The top 1% has its growth rate cut by a third. There is still an increase in inequality, but it is substantially muted by taxes and transfers. Moreover, the urban legend of the top 1% capturing all of the gains is false. There was substantial growth in the bottom and the middle percentiles.

The data just presented tells us the extent of current redistribution. It does not tell us how much redistribution has changed over time. Figure 1, which is taken from the same Auten and Splinter study, gives one estimate of changes over time. It shows the average rate of redistribution for different income groups and time periods.⁵⁵

Looking at the bottom quintile, we can see that the average rate of redistribution increased dramatically from 1962 to 2019, with a current average net tax rate of about negative 150%. That is, households in the bottom quintile now receive a net subsidy of almost 150% of their earnings, compared to a net subsidy of about 50% in 1962. The data at the top are harder to see in this figure because they are compressed, but the underlying data show that the net tax rate at the top went up from 34.4% in 1979 to 40.9% in 2019, a modest increase. Focusing on the super-elite, the 0.01%, their net tax rate went up from 39% in 1979 to almost 48% in 2019. Overall, tax rates went up at the top and down (i.e., more transfers) at the bottom. The system has become much more progressive.

55. See Auten & Splinter, *Income Inequality in the United States*, *supra* note 49, at 2215. The average rate of redistribution is defined as difference between pre-tax and transfer and after-tax and transfer income, as a fraction of pre-tax and transfer income. See *id.* at 2214.

Figure I: Auten and Splinter (Fig 8) Estimates of Redistribution



Other studies using different methodologies confirm these results.⁵⁶ Most importantly, every study we examined found a substantial increase in transfers to people at the bottom of the income distribution. They vary to some extent on how much taxes changed on the top 1% or smaller slices. Looking at aggregate measures, they all find a substantial increase in the amount of redistribution.

That the tax and transfer system has become markedly more redistributive does not alone establish that step two is valid. It does, however, show that Congress responds to underlying changes in inequality, which is consistent with step two. It refutes the view that step two must be invalid because the tax and transfer system is not responsive.

56. See Jesse Bricker et al., *Measuring Income and Wealth at the Top Using Administrative and Survey Data*, BROOKINGS PAPERS ON ECON. ACTIVITY, Spring 2016, at 261, 306–07; Richard V. Burkhauser et al., *Recent Trends in Top Income Shares in the United States: Reconciling Estimates from March CPS and IRS Tax Return Data*, 94 REV. ECON. & STAT. 371, 381–82 (2012); CONG. BUDGET OFF., *THE DISTRIBUTION OF HOUSEHOLD INCOME*, 2019 31–32 (2022), <https://perma.cc/5EEA-6SS6>; James Elwell et al., *Income Growth and Its Distribution from Eisenhower to Obama: The Growing Importance of In-Kind Transfers (1959–2016)* 31–33 (Nat'l Bureau of Econ. Rsch., Working Paper No. 26439, 2019).

C. Summary

Combining these points, we can conclude the following:

(1) The tax and transfer system changes multiple times a year, with great attention to the distributive effects of the changes. Whatever the transactions costs are of changing the tax and transfer system, they are not sufficiently high to prevent frequent changes.

(2) The tax and transfer system redistributes substantially more now than it did 40 or more years ago. Whether it redistributes enough depends on one's views about the costs of inequality and the costs of reducing inequality, but the tax and transfer system cannot be dismissed out of hand as an ineffective tool that does not respond to increases in underlying inequality. Instead, the tax and transfer system is highly responsive to underlying changes in equality. That is, the evidence is strongly suggestive that step two in the income-tax-only argument is valid.

(3) Nevertheless, there is no way to disaggregate the data to determine whether the tax and transfer system is, in fact, responding as required by the income-tax-only argument. While it is not correct to say that step two is invalid or false, at least without any modifiers, we cannot be sure that it is true. The data, however, are more consistent with it being true or mostly true.

IV. IMPLICATIONS IF THE TAX SYSTEM DOES NOT FULLY ADJUST

While I believe that the best reading of the evidence is that the tax system is responsive to changes in inequality (inclusive of changes in inequality due to changes in legal rules), assume that one accepts the critics' claim. In particular, assume that the tax and transfer system does not respond to changes in legal rules with sufficient regularity or that it does not sufficiently offset the effects of changes to legal rules for step two to be fully valid. The question is whether it follows that one should use the legal system to redistribute income.

There may be no single answer to this question that applies across all times and locations. Legal and tax systems vary, as do the institutions that determine the content of legal and tax systems. My goal is to find general norms or approaches to the problem to apply to the United States with its current (or possibly near future) institutions. In particular, I will assume, consistent with the evidence presented above, that the tax system changes all the time and that it can and often does redistribute more if pre-tax inequality increases, but that these changes are insufficient to meet the requirements of step two.

Fennell and McAdams are the most cautious in offering an answer to whether the legal system should be used to redistribute income. They argue that legal scholarship should change how it frames issues of

distribution (which they call messaging) to acknowledge the possibility that redistribution via legal rules might be desirable.⁵⁷ They also suggest where the burden of proof should lie in making claims about these issues.⁵⁸ Finally, they suggest that courts and other legal actors take a great deal of care when thinking about redistributing via legal rules because of the possibility that the tax system will offset the redistributive effects.⁵⁹

At the other end of the spectrum, Liscow would have laws always and everywhere seek to redistribute income through what he calls a thousand points of equity.⁶⁰ To achieve this, he suggests that Congress pass an “Economic Equity Framework Act[,]” which would require agencies to interpret statutes to achieve economic equity (which I take to mean redistribute income) in ways consistent with statutory purposes.⁶¹

Raskolnikov is in the middle but closer to Fennell and McAdams. He would look for laws where the efficiency benefits are small or dubious but that have bad distributive effects.⁶² For example, many professional licensing regimes have dubious efficiency benefits and may also be regressive. These kinds of laws might be appropriate targets for addressing distributive concerns. In addition, he suggests slowing the implementation of laws that are likely to be overall beneficial but that have uncertain distributive effects as a way of easing distributive burdens.⁶³

I will suggest here that even if one assumes slow and imperfect offsetting, the best norm is that legal rules should not be used to redistribute income. One should be attentive to institutional structure, as Fennell and McAdams suggest, and should be cautious about enacting rules with dubious efficiency gains and bad distributional effects, as Raskolnikov suggests. Nevertheless, there should be a strong norm against seeking to redistribute using legal rules.

I make three arguments in support of this conclusion. First, I consider what I will call the neutrality argument, namely that if legal rules can be used to increase redistribution they can also be used to reduce redistribution. They can be regressive as well as progressive. It is unlikely that allowing only progressives to use legal rules to redistribute would be a stable equilibrium. Second, the costs of using legal rules to pursue distributive aims are likely to be much higher than the income-tax-only argument suggests because of what I call reversals. Finally, the United

57. See Fennell & McAdams, *supra* note 11, at 1113–15.

58. See *id.* at 1116–17 (suggesting that the burden of proof be on those who claim that the tax system is categorically better and on those who claim particular redistributive legal rules can improve welfare).

59. See *id.* at 1117–20.

60. See Liscow, *supra* note 8, at 535–36.

61. *Id.* at 537–39.

62. See Raskolnikov, *supra* note 13, at 1647.

63. See *id.* at 1647–50.

States lacks the institutional expertise needed to effectively design redistributive legal rules and, for good reasons, is unlikely to develop the institutional capacity.

A. Neutrality and the likelihood of regressive legal rules

Most critics of the income-tax-only result (generally, not just the three criticisms focused on here) assume that giving legal decision-makers the ability to redistribute would mean more redistribution and less inequality. Liscow's thousand points of equity assumes that each point of equity, each legal rule, is progressive.⁶⁴ Fennell and McAdams refer to the distributive *deficit* in law and economics, implying that there is not enough redistribution.⁶⁵

Redistributive legal rules, however, can be regressive as easily as they can be progressive. Using legal rules to pursue distributive aims may mean less redistribution and more inequality. The question is, if we relax the income-tax-only result, which will we get: more progressive legal rules or more regressive legal rules? To answer this question, consider four possible norms governing the use of legal rules to redistribute:

(i) Legal rules may not be used to redistribute income; instead, only the tax system may be used this way.

(ii) Legal rules may be used to redistribute income (downward) by progressives or those who want more redistribution; conservatives or those who want less redistribution may not use legal rules to achieve their goals.

(iii) Legal rules may be used to redistribute income (upward) by conservatives or those who want less redistribution; progressives or those who want more redistribution may not use legal rules to achieve their goals.

(iv) Everyone is encouraged to use legal rules to redistribute income.

The critics seem to believe that if we relax the income-tax-only result, society will settle on the second option, that only progressives may use legal rules to achieve their distributive aims. As far as I can tell, this assumption is undefended, and the possibility of the third (only conservatives may use legal rules to redistribute) or the fourth (both sides may use legal rules to redistribute) options are never considered.

While social norms can develop in many ways, it is hard to see the second option—only progressives can use the full toolkit to achieve their goals while conservatives agree to limit their arsenal—could be an equilibrium. Why would conservatives or those who want less redistribution accede to such a norm? Indeed, I have trouble even articulating an argument for such a norm. It is no more appropriate to say

64. See Liscow, *supra* note 8, at 556–57.

65. See Fennell & McAdams, *supra* note 11, at 1053.

that legal rules should be used to redistribute income when progressives like the views of the politicians doing the redistributing, but not when they do not, than it would be to suggest touchdowns count for nine points when one team scores and five points when the other does. Liscow's argument implies we should have a thousand points of inequity. Fennell and McAdams should conclude that law and economics have a distributive excess.

The same is true for the third option, that conservatives can use legal rules to redistribute while progressives cannot. Progressives would not agree to this equilibrium for the same reasons conservatives would not agree to the reverse.

As a result, the only likely equilibria that both progressives and conservatives would likely agree to are the first (nobody uses legal rules to redistribute) or the last (everyone does). The question, therefore, comes down to which equilibrium, "nobody does" or "everybody does," is better.

B. Reversals

Given this choice, there are good reasons to prefer the "nobody does" norm over the "everyone does" norm. A key problem with the everyone does norm is what we might call reversals.

Reversals arise when the person or entity deciding on the content of a legal rule changes. Sometimes, a legal decision-maker may want a progressive legal rule. Other times, a legal decision-maker may want a regressive legal rule. In our democracy, there are regular changes in the party that controls each of our legal institutions, which means that the views of legal decision-makers change all the time. That means that with an "everybody does" norm, the distributive policy embedded in legal rules will reverse over time, and then reverse back, or move in both directions at the same time, and so on.

Reversals generate high costs with few benefits. If, over time, legal rules are balanced in their redistributive effects—some legal rules are progressive and some regressive—we get no redistribution but overall inefficiency. For example, one party might enact a progressive antitrust rule when it is in power. The other party might offset that progressivity by enacting a regressive trade rule, followed by the first party enacting a progressive labor law, and so on. The distributive effect of the overall legal system is the net of these changes. The efficiency cost, however, is the sum of the efficiency costs of each individual change.

For example, suppose that there are 100 legal rules, and 55 of them are inefficient but progressive and 45 are inefficient but regressive. The net is ten progressive legal rules. We get some additional redistribution. The cost, however, is 100 legal rules that are inefficient. The costs are ten times as high as just redistributing directly via the tax system (and, in fact,

more than ten times as high because of the inherent inefficiency of using legal rules to redistribute as illustrated by the income-tax-only argument). If the balance in the example were 50.5 to 49.5, we would net one legal rule that is redistributive for 100 inefficient legal rules, which means that the costs of using legal rules would be at least 100 times as high as using the tax system.

If legal rules are allowed to be used to pursue distributive aims (and, as assumed, the tax system is limited), it is hard to see how to stop reversals. Each side would want to use the tools at hand to pursue their distributive aims. Power changes hands regularly. The result is offsetting legal rules with a high overall level of inefficiency and limited redistribution (with the net redistribution possibly regressive).

Saying the efficiency costs are high is abstract and not easy to internalize. The widely-used example of a redistributive tort rule does not give sufficient context to understand the costs. That is, saying that rich people pay higher damages and poor people pay lower damages, in the somewhat rare event that they are defendants in a tort suit, does not give any sense of what the efficiency costs might be.

It is, I believe, worth a short detour to get a sense of what those costs may be.⁶⁶ Daniel Hemel, in a recent paper, explored precisely this issue and provided a number of examples. Hemel's key insight is that the outcome of using legal rules to redistribute depends on whether the efficient legal rule is regressive or progressive.⁶⁷ If the efficient legal rule is regressive in the sense that rich people benefit from the rule more than poor people, redistributing using that rule means making it weaker, and that may produce undesirable outcomes.

Air pollution rules provide a good example. Reducing air pollution has enormous efficiency benefits. According to a 2017 Lancet report, the United States has invested about \$65 billion in air pollution control since 1970 and received benefits of about \$1.5 trillion, or 23 times the cost.⁶⁸ Globally, the benefits may be even higher. On average, air pollution cuts lifespans by 2.2 years, but in northern India, it cuts lifespans by an astounding 8.5 years.⁶⁹

66. Of the critics, only Raskolnikov identifies actual legal rules that he believes might be used to redistribute. *See* Raskolnikov, *supra* note 13, at 1646–47. If the other critics do not like the examples identified here, they should identify which legal rules they think should be used to redistribute. Moreover, if their prescription is to redistribute anywhere we can—a thousand points of equity—it is hard to see how they can exclude these examples.

67. *See* Daniel Hemel, *Regulation and Redistribution with Lives in the Balance*, 89 U. CHI. L. REV. 649, 656 (2022).

68. *See* Philip J. Landrigan et al., *The Lancet Commission on Pollution and Health*, 391 LANCET 462, 463 (2018).

69. *See Air Quality Life Index*, EPIC, <https://perma.cc/XCE6-XHAH> (last visited July 15, 2024).

Suppose we want to use air pollution laws to redistribute. Reducing air pollution, on average, helps the poor more than the rich, but at the same time, it appears that the poor bear a higher portion of the costs of the reductions. As a result, the best estimates we currently have are that on net, air pollution laws are regressive, even if enormously cost-beneficial.⁷⁰

Because air pollution laws are regressive, using them to redistribute means making them weaker. Allowing more air pollution deviates from the efficient rule in a progressive fashion, making the overall system more progressive. The cost is more air pollution, leading to shorter, less healthy lives.⁷¹

The same appears to be true of vehicle safety regulations. Hemel analyzes the rearview camera rule to illustrate the likely effects.⁷² After extensive review, Hemel concludes that the regulation benefits wealthy households and hurts low-income households. It is cost-beneficial but regressive. As with air pollution rules, using the rearview camera rule (and possibly many other vehicle safety rules) to redistribute means weakening or possibly eliminating the rule. We would get less safety and more deaths if we seek to make vehicle safety rules progressive.

A final example is immigration. The benefits of immigration appear to be large, both to the receiving nation (i.e., the United States) and, especially, for the immigrants.⁷³ The distributive effects depend on how immigration affects wages. Crudely, high-skilled immigrants compete with domestic high-skilled workers, lowering their wages, and similarly for low-skilled immigrants.⁷⁴ Thus, the distributional effects of immigration depend on the balance of high-skilled and low-skilled immigration. Current estimates are that immigration to the United States has, since 1980, been distributionally neutral, neither increasing nor reducing inequality because it has been balanced between high-skilled and low-skilled immigrants.⁷⁵

70. See Richard J. Lazarus, *Pursuing Environment Justice: The Distributional Effects of Environmental Protection*, 87 NW. U. L. REV. 787, 800 (1992); see also Hemel, *supra* note 67, at 706–07.

71. One could try to jigger the rules so that they maintain their level of protection but become more progressive. As Hemel points out in the context of automobile safety rules, this is likely to be difficult.

72. See Hemel, *supra* note 67, at 684–95.

73. See NAT'L ACADS. OF SCIS., ENG'G, & MED., *THE ECONOMIC AND FISCAL CONSEQUENCES OF IMMIGRATION* 317 (2017). The effects on the sending nation are more complex.

74. The effects are likely more subtle because it can depend on whether immigrants act as a complement or a substitute for domestic labor, and that might depend on particular job markets.

75. See Giovanni Peri, *Immigrants, Productivity, and Labor Markets*, 30 J. ECON. PERSPS. 3, 10 (2016). Note that immigration also increases demand for goods and services, so it does not overall lower wages. If immigration is unbalanced, however, it can lower wages in particular sectors.

Using immigration laws to redistribute would likely mean changing who can immigrate to the United States. In particular, the United States would be less able to accept low-skilled, poor immigrants. Instead, immigration policy would be skewed toward accepting high-skilled immigrants who would compete with high-skilled natives. Whether this is attractive depends on views about the role of immigration in the United States, but it is arguably contrary to key progressive values, the values that would support a more progressive legal system under the critics' arguments.

To pursue redistribution via legal rules, progressives would have to accept policies like these. At the same time, they may achieve little in terms of actual redistribution because of reversals: conservatives would pursue offsetting policies. The net effect is high-efficiency costs, harming many people, and little gain.

By contrast, the “nobody does” norm has none of these effects. The costs of redistributing are limited to the direct costs of using the tax system. Moreover, our society would not be forced to bear the real costs of inefficient legal rules.

C. Institutions

Using legal rules to redistribute requires institutions, such as courts, the President, or Congress, to enact and enforce those rules. Any claim that legal rules should be used to redistribute instead of the tax system, therefore, requires a comparison of the relative institutional capacity of the legal and tax systems.⁷⁶ This Section begins this task.

There are many aspects to choosing the appropriate institutions for determining whether and how legal rules should redistribute income and how they interact with the tax system. I limit myself in this Article to examining whether different possible institutions have, or could, develop the expertise needed to design redistributive tax or legal rules. Other important considerations not addressed here include how democratic accountability affects the choice of institutions and whether different institutional designs affect the resulting level of redistribution.

A key problem in designing tax or legal rules that redistribute income is determining how much redistribution a given tax or legal rule accomplishes. Unfortunately, this is not straightforward. The reason is that the nominal incidence of a tax or a legal rule does not tell us who bears the

76. The literature contains little or no discussion of institutional choices and how those choices affect the ability of redistributive legal rules to achieve their goals. Fennell and McAdams list examples of possibly redistributive legal rules by courts, agencies, and legislatures, but do not discuss which of these institutions should be the primary focus of redistribution using legal rules. *See* Fennell & McAdams, *supra* note 11, at 1065–69. Later, however, they appear to default to courts as the legal decision maker. *See id.* at 1118–19.

costs or gets the benefit. To illustrate, suppose you are purchasing a pack of gum at a corner store for \$1 and the tax on the sale is \$0.10. If the retailer has to remit the tax, we might naively think that the tax makes the retailer worse off by the amount of the tax. They get \$1 from you but only keep \$0.90 because they must send \$0.10 to the government. If, however, the retailer is able to charge you \$1.10, the retailer is not worse off after paying the tax, it has \$1, just as in the case without the tax. Instead, you are worse off because now you must pay \$1.10 for that same pack of gum that you previously could have purchased for \$1. In effect, you pay the tax even though the retailer is the one who sends the check to the government. If the retailer charges somewhere between \$1 and \$1.10, then both you and the retailer bear part of the cost of the tax.

The same is true of all taxes. Employers “pay” half of Social Security taxes, but most analysts view the tax as borne by workers—their pay goes down by the employer’s share of the tax.⁷⁷ Corporate taxes are “paid” by corporations, but since corporations are not people, they cannot bear the tax. Instead, it must be borne by investors, employees, or customers, or some combination of the three.

Legal rules have the same problem. The legal literature often refers to it as the “contracting around” problem: attempts to redistribute via legal rules where the parties interact, whether through private contracts or markets, can and often will simply be offset by changes to contract terms or prices.⁷⁸ For example, a change in the rules governing product liability may be passed on to consumers through higher prices. A change to the rules governing housing, such as a habitability requirement, may simply increase rents or reduce the supply of housing. The minimum wage may nominally increase wages but employers may offset that cost by reducing hours so that on net, employees bear the cost.

Determining incidence, and, as a result, the redistributive effect of a tax or legal rule is difficult. It requires modeling the relevant policy and empirically estimating the reactions to the policy. In the simple example of the tax on gum, it may be a matter of estimating supply and demand elasticities to determine how gum purchases respond to price changes. In more complex cases such as the minimum wage, estimating the effects may require understanding many complex factors, the structure of various labor markets, how the minimum wage affects wages of non-minimum wage workers, the quality (as well as the quantity) of work offered, and

77. For a general introduction to the problem of tax incidence, see Don Fullerton & Gilbert E. Metcalf, *Tax Incidence*, in 4 HANDBOOK OF PUBLIC ECONOMICS 1787 (Alan J. Auerbach & Martin S. Feldstein eds., 2002).

78. See, e.g., A. MITCHELL POLINSKY, AN INTRODUCTION TO LAW AND ECONOMICS 122–23 (5th ed. 2018); Richard Craswell, *Passing on the Costs of Legal Rules: Efficiency and Distribution in Buyer-Seller Relationships*, 43 STAN. L. REV. 361, 398 (1991).

the price of goods produced by minimum wage workers (and who buys those goods). In fact, after decades of close study, we still do not know the distributional effects of the minimum wage.⁷⁹ It could be that raising the minimum wage helps low-wage workers, but it is equally or more likely that it hurts them. Without knowing the answer to this question, an institution deciding whether to use the minimum wage to redistribute would not know what to do. Increasing the minimum wage might be a good way to help low-income workers, but so might reducing it.

The tax system has, over the last 50 years and possibly longer, developed an extensive infrastructure to answer these questions.⁸⁰ There are now at least three offices in the government with responsibility for estimating the distributive effects of tax laws: the Office of Tax Analysis in the Treasury Department, the Joint Committee on Taxation in Congress, and the Congressional Budget Office, also in Congress. Each of these offices employs a large professional staff devoted to estimating the distributive effects of proposed tax legislation.

For example, the Joint Committee employs 27 economists (in addition to lawyers and other staff). These economists provide revenue estimates and distributional tables for all tax legislation.⁸¹ They use models built up over decades, often in consultation with outside experts. The economists in the Office of Tax Analysis perform similar but independent analyses.⁸² The third office, the Congressional Budget Office, does not provide distributional analyses of pending tax legislation. Instead, it provides an annual estimate of the distributive effect of federal taxes, often focusing on important taxes enacted that year.⁸³

All of these publications allow assessment of how well the tax system addresses inequality and how that has changed over time. Moreover, all

79. The literature is extensive. *See, e.g.*, David Card & Alan B. Krueger, *Minimum Wages and Employment: A Case Study of the Fast Food Industry in New Jersey and Pennsylvania*, 84 AM. ECON. REV. 772, 792 (1994); Thomas MaCurdy, *How Effective Is the Minimum Wage at Supporting the Poor?*, 123 J. POL. ECON. 497, 534–36 (2015); Peter Harasztosi & Attila Lindner, *Who Pays for the Minimum Wage?*, 109 AM. ECON. REV. 2693, 2724–25 (2019); Jeffrey Clemens, *How Do Firms Respond to Minimum Wage Increases? Understanding the Relevance of Non-Employment Margins*, 35 J. ECON. PERSPS. 51, 68–69 (2021).

80. Some of this infrastructure was put in place in the 1974 Budget Act was a key to developing this infrastructure. *See* Congressional Budget and Impoundment Control Act of 1974, Pub. L. No. 93–344, 88 Stat. 297 (1974) (codified at 2 U.S.C. §§ 601–688).

81. *See* sources cited *supra* note 42.

82. *See generally* CRONIN, *supra* note 41.

83. *See generally* CONG. BUDGET OFF., *supra* note 43. The Congressional Budget Office estimates are found here: *Income Distribution*, CONG. BUDGET OFF., <https://perma.cc/FP9T-Q3GR> (last visited Aug. 16, 2024). The Treasury's also publishes annual estimates of the tax burden (as opposed to the effects of particular legislation). *See Office of Tax Analysis*, U.S. DEP'T OF TREASURY, <https://perma.cc/UKP2-8J6B> (last visited Aug 16, 2024).

three offices regularly publish papers explaining their methodology for estimating the distributional effects of the tax system. This allows the public, including outside experts, to comment on the methodologies and to understand the underlying assumptions.⁸⁴

In addition to these government offices, a number of private entities estimate the distributional effects of tax changes. For example, the Brookings-Urban Tax Policy Center uses a large-scale microsimulation model to estimate the distributional effects of taxes.⁸⁵ It has put out estimates every year since its founding and often puts out estimates of pending legislation during the legislative process. The National Bureau of Economic Research has a model, known as TaxSim. TaxSim can be, and is, used by experts to estimate the progressivity of the income tax.⁸⁶ Private researchers, such as academics, also regularly estimate the distributive effects of different types of taxes and of the overall tax and transfer system.⁸⁷

In short, the ecosystem for estimating the distribution of the tax burden and its effects on inequality is vast, comprising numerous experts both in and outside of government. The government reports are central to the tax legislative process.

There is a reason for all this expertise. The distributional effects of the tax system are central to its design. If we did not care about distributive effects, we could simply ask each individual to pay their pro rata share of federal spending, in what is known as a head tax. We use an income tax rather than a head tax because we want the tax burden to be fair, in the sense of having an appropriate distributional burden. Distributive issues, therefore, are at the core of the tax system.

84. See generally CRONIN, *supra* note 41. The Treasury provides updates to its methodology here: <https://perma.cc/SXW4-KYWX>. The Joint Committee's methodology is found here: SUMMARY OF ECONOMIC MODELS AND ESTIMATING PRACTICES OF THE STAFF OF THE JOINT COMMITTEE ON TAXATION, JOINT COMM. ON TAX'N (2011), <https://perma.cc/547P-GJ7D>. For a description of the development of the Joint Committee's methodology, see generally Thomas A. Barthold, *Measuring the Burden of Tax Changes: What Do We Tell Congress?*, 86 PROC. ANN. CONF. ON TAX'N HELD UNDER AUSPICES OF NAT'L TAX ASS'N-TAX INST. AM. 164 (1993).

85. *Brief Description of the Tax Model*, TAX POL'Y CTR. (Mar. 9, 2022), <https://perma.cc/8HZW-MWRR>.

86. See *Elasticity of the US Federal Personal Income Tax 1960 – 2015*, NAT'L BUREAU OF ECON. RSCH., <https://perma.cc/5BEN-QS6V> (Aug. 2016). The NBER uses a progressivity measure known as the elasticity of the income tax, which measures how much, in percentage terms, taxes go up, when income goes up by a percent.

87. The Auten and Splinter estimates are an example. See generally Auten & Splinter, *Income Inequality in the United States*, *supra* note 49. (Both Auten and Splinter are in the government, Auten in the Office of Tax Analysis and Splinter in Joint Tax, but the paper represents their individual views, not the views of their respective offices). The well-known estimates by Emmanuel Saez and Thomas Piketty of inequality and tax progressivity are another example. See generally Piketty & Saez, *supra* note 1.

The institutional structure surrounding the legal system is a stark contrast: it simply does not exist. There are no equivalents to the Congressional Budget Office, the Joint Committee on Taxation, or the Treasury Office of Tax Analysis, that provide regular, thorough, and well-documented distributional analyses of major legal rules.

To illustrate, consider two canonical cases from the first year of law school, *Williams v. Walker-Thomas Furniture*⁸⁸ and *Javins v. First National Realty Company*.⁸⁹ These two cases, according to one commentator, are among “the few cases that [have] stimulated sustained scholarly analysis of the distributive consequences of attempting to help the poor by regulating their consumer ‘choices.’”⁹⁰ If one is going to think about attempts to redistribute via legal rules, these two cases will be central.

Williams held that cross-collateralization agreements for consumer lending could be invalidated as unconscionable.⁹¹ Legal scholars immediately understood the contracting around problem with *Williams*. Some scholars argued that the rule hurt rather than helped poor consumers.⁹² Other scholars have disputed this analysis using behavioral economics⁹³ or by arguing that the sellers of the consumer goods in that case were oligopolists and, therefore, were likely to absorb the costs of those clauses.⁹⁴

The debate over unconscionability rules is extensive. Depending on who you ask, it is either resolved one way or the other, or remains in dispute. Regardless, two points stand out. One is that whatever the general merits of these clauses, their distributive effect almost surely depends on the particular structure of a market and the relevant elasticities. Yet the debate has been largely theoretical. We have little or none of the empirical information needed to evaluate the effects in the wide variety of markets that they may apply in. Second, in stark contrast to the tax system, there is no institutional apparatus for measuring these effects. A judge deciding whether a particular cross-collateralization clause should be invalidated would have no way of knowing whether doing so helps or hurts the poor.

Javins is similar. In that case, the court imposed an implied warranty of habitability on rental apartments. As with *Williams*, analysts early on

88. See *Williams v. Walker-Thomas Furniture Co.*, 350 F.2d 445 (D.C. Cir. 1965).

89. See *Javins v. First National Realty Corporation*, 428 F.2d 1071 (D.C. Cir. 1970).

90. Duncan Kennedy, *The Bitter Ironies of Williams v. Walker-Thomas Furniture Co in the First Year Law School Curriculum*, 71 BUFF. L. REV. 225, 228–29 (2023).

91. See *Williams*, 428 F.2d at 449–50.

92. See Richard A. Epstein, *Unconscionability: A Critical Reappraisal*, 18 J. L. & ECON. 293, 304–05 (1975).

93. See Oren Bar-Gill, *The Behavioral Economics of Consumer Contracts Exchange*, 92 MINN. L. REV. 749, 801–02 (2008).

94. See Kennedy, *supra* note 90, at 245–54.

recognized the contracting around or incidence problem.⁹⁵ Bruce Ackerman argued that the rule helped renters while Neil Komesar argued that Ackerman's assumptions were invalid.⁹⁶ Other scholars weighed in.⁹⁷ A recent review, however, found that "little empirical research has been conducted to inform either position The absence of empirical evidence . . . leaves lawmakers in the dark."⁹⁸

Williams and *Javins* were court decisions. Perhaps agencies are a better forum for redistributive legal rules than courts because they have technical staff who might be able to perform the necessary analysis.

To this end, the Office of Management and Budget (OMB), in a revision of Circular A-4, suggests an increase in the use of distributional analyses when performing cost-benefit analyses of regulations.⁹⁹ It provides very little guidance, however, on when to perform such analysis, holding:

Reasonably available methodologies and data, as well as input from experts and the public, can inform an agency's determination as to whether production of a distributional analysis is practical, appropriate, consistent with law, and will produce relevant and useful information in a specific context.¹⁰⁰

Notably, this guidance makes no reference to whether or how an agency regulation may interact with the tax system.

What are the "reasonably available methodologies" referred to by Circular A-4? One might have hoped to find these methodologies in the section entitled "Producing a Distributional Analysis."¹⁰¹ But this section merely suggests identifying a baseline, estimating the effects of the regulation on relevant groups relative to the baseline, and preferring monetized over non-monetized estimates. Importantly, OMB created no institutional structure for performing distributional analyses, again a stark contrast to the tax system.

95. See Bruce Ackerman, *Regulating Slum Housing Markets on Behalf of the Poor: Of Housing Codes, Housing Subsidies and Income Redistribution Policy*, 80 YALE L.J. 1093, 1108 (1971).

96. See Neil K. Komesar, *Return to Slumville: A Critique of the Ackerman Analysis of Housing Code Enforcement and the Poor*, 82 YALE L.J. 1175, 1186-92 (1973).

97. See Craswell, *supra* note 78, at 380-85 (agreeing with Ackerman); Charles J. Meyers, *The Covenant of Habitability and the American Law Institute*, 27 STAN. L. REV. 879, 903 (1975) (agreeing with Komesar).

98. See Matthew Desmond & Monica Bell, *Housing, Poverty, and the Law*, 11 ANN. REV. L. & SOC. SCI. 15, 22 (2015).

99. See OFF. OF MGMT. & BUDGET, CIRCULAR NO. A-4, REGULATORY ANALYSIS 61 (2023).

100. *Id.* at 62.

101. *Id.* at 64.

Economists have also analyzed the incidence of various legal rules. For example, there is an extensive literature on the minimum wage. Its effects remain uncertain, likely depending on local market structures.¹⁰² Immigration¹⁰³ and trade rules¹⁰⁴ have also attracted significant attention. The attention paid by academic economists to distribution in these areas is on par with (though less than) the attention paid to issues of distribution for the tax system. Unlike the tax system, however, there is no institutional structure for incorporating academic research into legislative proposals.

What would it take to develop an institutional capacity for analyzing the distributive effects of legal rules that is anywhere near the capacity we have for analyzing the tax system? Developing the current institutional structure for analyzing taxes took decades. Even if the problem of analyzing the incidence of legal rules were similar to that of tax, and we were to start developing that structure immediately, it would likely take a similar amount of time to develop those capacities for legal rules (though perhaps an institutional structure for analyzing legal rules could learn from what was done in tax, so it could be done more quickly).

The problem, however, is more difficult in the context of legal rules than it is in tax. To the extent that legal rules are enacted by courts, it would be difficult or even impossible to develop the necessary institutions, at least while retaining the current structure of the judicial branch. Judges decide cases, and judges have no training in analyzing the distributive effects of their decisions. Most judges, at least as they are currently selected, would not have the capacity to ever do such analyses. They went to law school to avoid math.

Even if judges were competent to assess the distributive effects of their individual decisions, judges make largely uncoordinated decisions. This means that judges with different preferences and different understandings of the incidence of legal rules will all try to impose their views, often offsetting one another. All of these offsets act as a kind of reversal: we get inefficient decisions and no net distributive benefit. The court system is the least likely institution to make good distributional choices.

102. See sources cited *supra* note 79.

103. See *generally* Peri, *supra* note 75.

104. For a survey, see Lorenzo Caliendo & Fernando Parro, *Trade Policy*, in 5 HANDBOOK OF INTERNATIONAL ECONOMICS 219 (Gita Gopinath et al. eds., 2022). The classic argument that trade negatively impacts the earnings of low-skilled workers in the United States is Wolfgang F. Stolper & Paul A. Samuelson, *Protection and Real Wages*, 9 REV. ECON. STUD. 58 (1941); Ariel Burnstein & Jonathan Vogel, *International Trade, Technology, and the Skill Premium*, 125 J. POL. ECON. 1356 (2017); Justin Caron et al., *Per Capita Income and the Demand for Skills*, 123 J. INT'L ECON. 103306 (2020); Javier Cravino & Sebastian Sotelo, *Trade Induced Structural Change and the Skill Premium*, 11 AM. ECON. J.: MACROECONOMICS 326 (2019).

The executive branch is a better target for adding the institutional capacity needed to estimate the distributive effects of legal rules. It employs many people with the technical expertise to analyze distributive issues and issues regulations that cover a wide swath of the economy. The President has a degree of centralized control over agencies, allowing coordination across agencies, thereby reducing reversals or offsets.

There are reasons to believe, however, that even with concerted effort, the executive branch would never develop the capacity to understand the distributive effects of legal rules in the way that it has for tax rules.

One reason is that there are thousands of legal rules that potentially have distributive effects, while the tax system, as sprawling as it is, is relatively compact. Possibilities are as diverse as immigration, trade, labor, criminal law, zoning and housing rules, antitrust, and licensing. The entities implementing those legal rules are dispersed throughout the government, while there is a single entity charged with implementing the tax system. As a result, developing a similar institutional capacity for legal rules would be a much larger undertaking than for tax.

One possibility to prevent this duplication is centralizing distributional analyses in one office. The Office of Management and Budget is the obvious choice, though a new office, the Office of Distributional Analyses could be created. Regardless, under this model, the centralized office would perform the necessary analyses for agencies as needed.

Centralizing the distributional analysis across the entire executive branch, however, would be difficult or perhaps impossible. Agencies have the front-line responsibility for designing regulations. If they are to take distributional issues into account when designing regulations, they would need to have the ability to consider distributional effects during the design phase. This likely means that agencies need to have the relevant capacity in-house, consider multiple options, modify those options in response to distributional analyses, and so forth. This may be one of the reasons that new Circular A-4 leaves distributional analyses to agencies rather than centralizing it in OMB. Centralizing this design-level function in OMB would be a substantial shift in who chooses the content of a regulation.

A second reason that it is unlikely that we would develop the necessary institutional capacity for analyzing the distributive effects of legal rules is that distributional issues are usually second order for legal rules. The primary issue in the design of any legal rule is the substantive issue that the rule governs: safety, pollution, information provision, and so forth. This means that any agency deciding on the content of a legal rule will primarily focus its expertise on the subject matter at issue. For example, the EPA necessarily will focus its attention on studying the

environment rather than the distributional effects of its rules. Agencies that regulate safety, such as DOT and OSHA will necessarily focus their attention on safety. This is not true of taxation, where the distributive effects are one of the primary issues.

Third, because of the problem of reversals discussed above, the institutional capacity needed to generate a given amount of redistribution via legal rules may be orders of magnitude higher than for tax. In the example above, 100 legal rules were enacted to get a small amount of redistribution because most of the legal rules offset one another. The institutional capacity to estimate the distributive effects would likewise be 100 times that needed for a tax rule. That is, rather than analyzing the distributive effects of each legal rule, the tax system can just aggregate everything that affects the distribution of income and consider it all at once.

Finally, in many cases, the problem of estimating the distributive effects of a legal rule will be much more difficult than estimating the distributive effects of a tax law. Taxes primarily affect prices and price effects can be fed directly into the standard supply and demand analysis that determines incidence. Legal rules are usually aimed at something other than price. For example, they may determine the quality of a product that can be sold, the type of technology that must be used to produce a product, or the terms of a contract. It is far more difficult to estimate the incidence of these kinds of changes.

In short, it is possible that the executive branch, likely through OMB, could develop the institutional capacity to evaluate the distributional effects of legal rules similar to the capacity that it currently has in tax. For the reasons just discussed, it would, however, be a heavy lift.

The final possibility is that Congress could develop the necessary capacity to evaluate the distributive effects of the legal rules that it passes. It could create entities similar to the Congressional Budget Office and the Joint Committee on Taxation but that analyze the distributive effects of legal rules rather than taxes. Just as tax bills generally are accompanied by distributional tables, the “Congressional Distribution Office” could produce distributional tables for other forms of legislation.

Such an office would face many of the same problems as an executive branch office. More importantly, it is hard to understand why creating such an office would be a good idea. Instead of passing a redistributive legal rule, Congress could pass an efficient legal rule and at the same time make a modification to the tax system as suggested by the income-tax-only argument. That is, unlike the judiciary and the executive branch, Congress can change the tax laws when it wants.

D. Summary

While as discussed in Part II, the evidence suggests that the tax system responds to changes in the distribution of income (including changes due to legal rules), this Part examined the implications of a belief that it only responds slowly and imperfectly. The conclusion is that even under this assumption, using legal rules to redistribute income is unlikely to be desirable.

V. CONCLUSIONS

This Article considered whether and to what extent political or other constraints on the tax system refute the income-tax-only argument. The claim that it examined is that for various reasons, the political system will not adequately redistribute through the tax system, and, as a result, legal rules should also be used to redistribute income.

I have examined the two elements of this claim. First, I looked at how responsive the tax system is. I found that the tax system changes all the time, with major tax laws enacted at a rate of more than 1.5 times per year over the last 40 years and minor changes made thousands of times each year. The result of these changes is that the tax and transfer system has become substantially more progressive. This evidence refutes a bald claim that the tax system does not or cannot adjust in ways suggested by the income-tax-only argument and is strongly suggestive that the income tax responds as required by the income-tax-only argument.

Second, I looked at whether the legal system can be effective at redistributing income. The conclusion from that analysis is that most elements of the legal system are ill-suited for redistributing income. The costs of using the legal system are likely to be high, and the end result may be an overall more regressive system rather than a more progressive system as theorized by the critics. Moreover, the legal system lacks the institutions necessary to effectively design redistributive legal rules, and for good reasons, is unlikely to develop that capacity.

Putting these together, the argument for using legal rules to redistribute income because of potential limitations on the ability of the tax and transfer system to do so is weak to non-existent. There could be circumstances where a nation would want to use legal rules to redistribute income. The United States between 1895 and 1913 might be an example because it was unconstitutional to have an income tax during that period. In the contemporary United States, however, it is hard to imagine circumstances where using legal rules to redistribute would be preferred to amending the tax and transfer system.