International Journal of Social Science and Economic Research

ISSN: 2455-8834

Volume:09, Issue:06 "June 2024"

Equity in The United States: Universal Pensions and Other Considerations

Arnav Sherpuri

Northern Valley Regional High School at Demarest

DOI: 10.46609/IJSSER.2024.v09i06.027 URL: https://doi.org/10.46609/IJSSER.2024.v09i06.027

Received: 26 June 2024 / Accepted: 10 July 2024 / Published: 15 July 2024

The central inquiry of this essay is to examine methods of income redistribution across the world and determine which of these would be a) effective, and b) viable when applied to the United States. We must also ascertain the relationship between income redistribution and economic growth, as this affects the viability of a given tool.

In order to do so, it is imperative to differentiate between the 4 general forms of income redistribution (Palme, 2006).

(i) Horizontal redistribution: Spreading income over the life-cycle of an individual

(ii) Vertical redistribution: Taking from the rich and giving to the poor

(iii) Risk redistribution (social insurance)

(iv) Perverse redistribution (negligible effect)

Horizontal redistribution most often takes the form of pensions, with risk redistribution closely imitating this, subsidizing healthcare and other benefits the way a pension serves to subsidise living costs. In contrast, vertical redistribution takes the form of higher marginal taxes, which gives rise to the possibly fallacious perception (which will be addressed later in this essay) that combatting inequality always takes a toll on economic growth. Regardless, it is pertinent to treat efficacy and viability as two separate questions.

The question of efficacy comes first. In attempting to perfect their social net, I believe the United States can certainly take cues from other countries, especially those that are known for having historically efficient social security systems. This group is composed of Sweden, Norway, Germany and Denmark.It was found that within these nations, public pensions accounted for the largest reduction in income inequality (Caminada, Goudswaard, Wang, 2013). Notably, in these countries, the pension takes a universal form, *similar* to the UBI (universal basic income) first suggested by Thomas Pence (King, Marangos, 2006), and it seems to demonstrate what the

ISSN: 2455-8834

Volume:09, Issue:06 "June 2024"

United States stands to gain by adopting one. The same study revealed that these countries ranked highest in terms of absolute fiscal redistribution between 1985 and 2005, a testament to its efficacy. The United States has correctly identified that it is necessary that a social insurance scheme must be targeted; one example of a means-tested (dispensing aid on the basis of need) social insurance program is Medicaid (Gruber, Moffitt, 2003). However, its fatal flaw is the assumption that it must be targeted with regards to social groups; failing to evaluate thefact that such an approach inevitably leads to religious, ethnic or class divisions, deepening inequality in contravention of its purpose; this is likely the root of the positive relationship between benefits provided to the impoverished and the level of inequality in a country (Korpi, Palme, 1998). Rather, as the case of Sweden shows (Palme 2006), a universal program functions best. It not only steers clear of this malaise, but leads to higher levels of adoption, increasing social and political acceptability. The group that is essential to the success of such a scheme is the middle class. Generally, countries with higher middle-class inclusions are more successful in enforcing feasible income safety nets (Nelson, 2003); by integrating them into the pension system, the number of involved stakeholders is increased tenfold, and the adage of strength in numbers rings truer than ever before.

It is essential to differentiate the form universal pensions take from a UBI. Proponents of a UBI advocate for cash handouts, whereas universal pensions take the form of *specific benefits, tailored with regards to recipient's needs*. A social policy like UBI that serves simply to provide basic security again leads to a stratification of social security, borne of the dependency that certain impoverished groups are more likely to have on it, entrenching the very issues it is designed to alleviate. For this reason, it is essential that a universal scheme be targeted, with regards to the way it is dispensed. Examples of the aforementioned targeted benefits include housing benefits for families with children, free childcare services for new mothers, veteran benefits, and so on.

Viability is another question altogether. Economic theory does tend to assert that a conflict between income equality and economic growth is inescapable (Okun, 1975), thus giving rise to the question of whether income redistribution, horizontal or vertical, can *ever* be economically viable. Several studies have found that raising marginal tax rates on high-income individuals tends not to raise additional tax revenues, but instead imposes substantial costs on the economy (Dahlby, Ferede, 2013); others postulatethat there is in fact, a non-sequential relationship (Milasi, Waldmann, 2018); yet another study found there to be no relationship whatsoever between equity and inequality (Stevans, 2012). The contradictoryideas surrounding this field make it difficult to derive a general relationship between equity and economic growth, warranting a case-by-case examination for each tool.

The effect of redistributory tools on economic growth can be evaluated by considering the nature

ISSN: 2455-8834

Volume:09, Issue:06 "June 2024"

of a tool in question. Employing horizontal redistribution as opposed to vertical redistribution avoids penalising the rich, oft considered the worst side effect of measures designed to reduce inequality. In the case of Scandinavia, I hypothesise economic growth is likely to be relatively unscathed by their vast pension system for several reasons, and in some cases may actually benefit from it. The system is largely horizontal, i.e., most individuals fund their own benefits, with the state simply acting as a fiduciary. A certain minority, such as the terminally homeless or unemployed are unable to provide for themselves, and as a result their benefits are paid for by higher tax rates on the rich, introducing a vertical element. This is, however, partially offset by the fact that the pension is universal, meaning those who pay higher marginal taxes as a result of it end up receiving a cashback of sorts. This push to reduce inequality may actually benefit economic growth (e.g., Germany) through the added political stability, increased size of workforce (since more mothers are enabled to work), and increased productivity that is brought about by equity (Lynch, 2021).

This hypothesis can be confirmed econometrically. The ideal income redistribution is where an income transfer of D is made from an individual with income X1 to an individual of lesser income X2 where the conditions $D > 0$ and $X2 \leq X1-D$ (Dalton, 1920); the purpose of an income redistribution tool is to promulgate income transfers that reduce the difference between two incomes thereby changing the income distribution of a given country.

Assume θ represents an income distribution histogram for a given country. Take a function f(X), composed of the values of deviation between a point X and X+H on θ, where H is a value approaching 0; when graphed, this function represents the various values of deviation between points on θ, that are spaced in infinitesimally small intervals.

$$\sum_{i=a}^{b} f(X) = f(y)$$

f(y) thereby represents the net value of deviation between A and B (the lowest and highest incomes on θ), at different points in time. By representing the net inequality in a given country at a given time as a singular numerical value, we can perform a regression analysis between several of these values (income distributions at various times) against economic growth, revealing the relationship between growth and equity.

For Sweden, Norway and Germany, it appears this hypothesis holds, as there is either no correlation between the two variables (Sweden, Norway), or a positive relationship in the case of Germany. In the case of Canada, the expected relationship is seen and the best explanation for this is that Canada employs a heavily vertical form of redistribution (Dahlby, Ferede, 2013), which

ISSN: 2455-8834

Volume:09, Issue:06 "June 2024"

likely hurts innovation and therefore efficiency, lending more support to implementation of horizontal redistribution.

Country	Correlation (+/-)	P-value
Sweden	+	>0.05
Norway	-	>0.05
Germany	+	0.021
Canada	-	0.0012

Source: Own data (raw data sourced from Luxembourg Income Study, FRED)

Thus, enacting the aforementioned universal pension in the United States may bring about increased levels of equality, while leaving economic growth intact, and is likely to increase political stability and re-establish the middle class which has been declining since the 2010s (Wolfson, Foster 2009). Scandinavia and Germany certainly provide undeniable evidence that it has been both effective and viable. There are those who fear that the unique nature of the United States economy makes it incompatible with federal inequality reduction campaigns. This can be refuted with several facts; taxation levels are only slightly lower, and its economy is in the same phase of development. Other factors which have been found to cause inefficiency in redistribution include higher state-level poverty rates, lower employment-to-population ratios (Petach, 2022), and while there is lower overall employment (62% vs 69%) in the United States, it enjoys lower levels of poverty (12.2% vs 15%).

In conclusion, I believe a universal, targeted pension scheme, similar to *Pensionmyndigheten (Sweden)*and *Rentenversicherung (Germany)*, is the best income redistribution method scheme to adopt from abroad. Its nature is likely to satisfy the increasingly prevalent calls for the implementation of a UBI (Johnson, Johnson, Nettle, Saxe, 2021), parallelly meeting the unique needs of the United States; besides being easily integrable with existing forms of income redistribution, it has shown itself to function constructively whilst aiding the economy.

References

(i) Atkinson, A. B. (1970). On The Measurement of Inequality. *Journal of Economic Theory*, *2*, 1-5.

(ii) Dahlby, B., & Ferede, E. (2013). Income Inequality, Redistribution and Economic Growth. *University of Calgary, The School of Public Policy Publications*, *6*(25).

(iii) Dalton, H. (1920). The Measurement of the Inequality of Incomes. *The Economic Journal*, *30*(119). https://www.jstor.org/stable/2223525

(iv) Foster, J. E., & Wolfson, M. C. (2009). Polarization and the decline of the middle class: Canada and the U.S. *The Journal of Economic Inequality*, *8*, 247-273.

(v) Gruber, J., & Moffitt, R. A. (2003). Means-Tested Transfer Programs in the United States. *National Bureau of Economic Research*.

(vi) King, J. E., & Marangos, J. (2006). TWO ARGUMENTS FOR BASIC INCOME: THOMAS PAINE (1737-1809) AND THOMAS SPENCE (1750-1814). *History of Economic Ideas*, *14*(1), 55-71.

(vii) Korpi, W., & Palme, J. (1998). The Paradox of Redistribution and Strategies of Equality: Welfare State Institutions, Inequality, and Poverty in the Western Countries. *American Sociological Review*, *63*(5).

(viii) Lynch, R. (n.d.). The economic benefits of equal opportunity in the United States by ending racial, ethnic, and gender disparities. In *Inequality & Mobility*. (Excerpted from *Washington Centre for Equitable Growth*, 2021, June,)

(ix) Milasi, S., & Waldmann, R. J. (2017). Top Marginal Taxation and Economic Growth. *Applied Economics*, *50*(19), 2156-2170. https://doi.org/10.1080/00036846.2017.1392001

(x) Palme, J. (2006). Income distribution in Sweden. *The Japanese Journal of Social Security Policy*, *5*(1).

(xi) Petach, L. (2022). A Tullock Index for Assessing the Effectiveness of Redistribution. *Public Choice*, *191*(1-2), 137-159. https://doi.org/10.1007/s11127-022-00957-7

(xii) Saxe, R., Nettle, D., Johnson, E., & Johnson, M. (2021). Why has the COVID-19 pandemic increased support for Universal Basic Income? *Humanities and Social Sciences Communications*.

(xiii) Stevans, L. K. (2012). Income Inequality and Economic Incentives: Is there an Equity–Efficiency tradeoff? *Research in Economics*, *66*(2), 149-160. https://doi.org/10.1016/j.rie.2011.10.003

(xiv) Wang, C., Caminada, K., & Goudswaard, K. (2013). Income redistribution in 20 countries over time. *International Journal of Social Welfare*.

