HISAR SCHOOL

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“Globalization: Creating a Common Language”

Economics Committee

Seeking tax reform as a course to reducing global income inequality

HISAR SCHOOL JUNIOR MUN

RESEARCH REPORT

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Forum: Economics Committee

Issue: Seeking tax reform as a course to reducing global income inequality

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Introduction

As stressed in the International Monetary Fund's (IMF) Fiscal Monitor, a survey that analyzes the latest public finance developments and policies, rising income inequality is a critical problem in today's world. Past data shows that institutions, banks, finance incentives, and national policies play a big role in affecting income share as inequality has increased at different speeds across the world. Thus, with the rise of globalization, much fear among citizens emerged from excessive income inequality as the income gap between the rich and the poor expanded greatly in many countries. Lower economic growth that was caused by the inflated income inequality eventually led to political polarization, increased poverty, hunger, sickness and disintegration of individuals in certain countries all over the world. In countries such as the United States and Russia, for instance, wealth inequality rose significantly with the expansion of large private ownership and business, whereas Europe experienced more moderate levels of wealth inequality over the past decades. That being said, tackling global income and wealth inequality requires taking serious measures in national and global policies along with the reassessment of the current education system, wage settlement, and corporate governance.

In addition, one of the proven tools in the fair distribution of income and welfare is tax reform. Over the years, many policies that are apt to tax progressivity led to positive shifts in income inequality. That being so, delegates, your duty in the economics committee is to tackle income inequality in a global perspective while addressing particular concerns of tax reforms such as "the taxation of high net worth individuals; efficient business taxation; and the taxation of socially-harmful activities like smoking tobacco" (ICTD).

Definition of Key Terms

Tax: "Tax is an amount of money that you have to pay to the government so that it can pay for public services. When a person or company is taxed, they have to pay a part of their income or profits to the government. When goods are taxed, a percentage of their price has to be paid to the government."

Progressive tax: It takes more percentage of a larger income and less percentage of a smaller income. (Ex. Luxury cars are taxed more as rich people buy them)

Regressive tax: It takes a larger percentage of a lower-income and a smaller percentage of a higher income. (Ex: Tax on basic necessities, bad for poor people)

Wage: The amount of money that is regularly paid to employees for the work they've done.

Gross domestic product (GDP): “The total value of goods and services produced within a country in a year, not including its income from investments in other countries.”

Fiscal Policy: Government spending and tax policies to influence economic conditions of countries

Welfare: The welfare of a person or group is their health, comfort, and happiness.

Gini coefficient: “Measures the extent to which the distribution of income (or, in some cases, consumption expenditure) among individuals or households within an economy deviates from a perfectly equal distribution.”

General Overview

Over the past decades, the sum of inequality among and within nations, which is referred to as “global inequality” has decreased moderately yet it still remains high. The Gini coefficient, which is the statistical measure of income distribution, has been estimated to be around 0.65 for the entire world. Considering that a Gini coefficient of zero expresses perfect equality in income distribution, the current index of 0.7 is quite inflated for today’s world.

The story of global income inequality starts with one major event in history: industrial revolution. During the early 19th century, with the rise of the British industrial revolution, the financial gains directly benefited urban and rural class and the poor class didn’t get the gains. Within the rise of the revolution, up until the late 20th century, around 1975s, the income distribution expanded as gaps between national incomes widened, as the fast-developing economies of North America and Western Europe left other countries behind in the race. While some parts of the world were gaining much from pre and postindustrial advancements in technology, others could not benefit that much from the industrial revolution. “For example, in 1800, American purchasing power parity was twice that of China; by 1975 it was 30 times that of China” (WEF).

Until the 1920s, global inequality continued to increase rapidly as international businesses, financial manipulation, industrialization, and entrepreneurship passed the majority of new gains to the wealthiest people at that time. However, between the 1930s and 1980s, the picture of global income inequality shifted significantly. With social democracy getting more popular around the global north, higher taxes were pushed on the wealthiest people. As a result, the governments had more gains to pay for benefits and social programs for their citizens.

Global inequality level was highest in 1980, and since then, the trend has been declining moderately. Even though the inter-country inequality is not as high as before, within-country inequality has ,unfortunately, begun to move even higher. Various factors played a role in this rise such as but not limited to tax policy shifts from progressive to regressive, globalization, advancements in technology and lack of need for less skilled/educated human capital in certain areas.

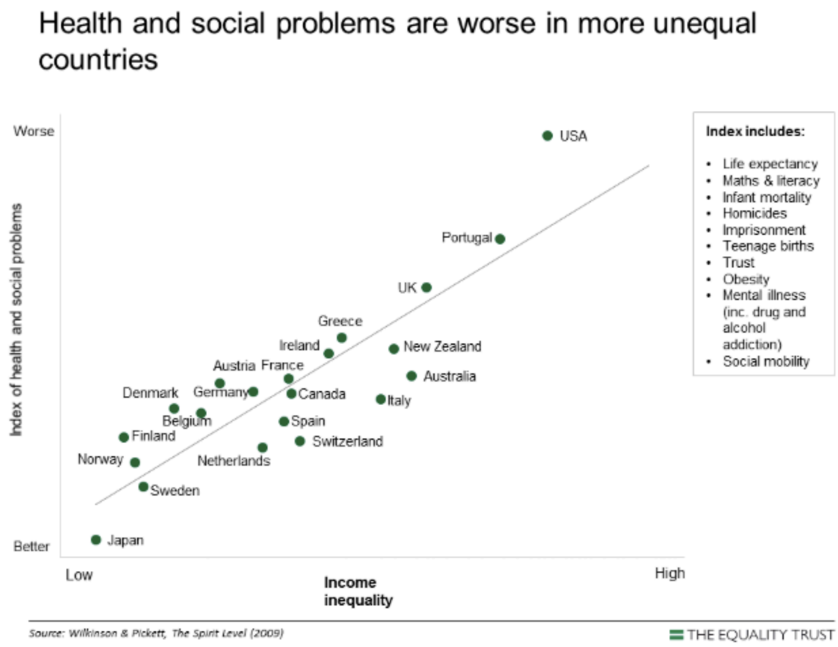


Figure 1: https://www.weforum.org/agenda/2015/09/5-reasons-why-we-need-to-reduce-global-inequality/

To sum up, excessive concentration of gains in the top wealthy and the disappearance of the middle class in developed countries pose serious threats in today's world. Moreover, national populism and patriotism as currently being witnessed in many developed countries such as the USA and UK (Brexit vote) are on the rise and these countries continue to push away from globalization and thus worsen the dynamic of the income distribution. That being said, rising inequality demands a great amount of political attention in order to promote further tax reforms and policy changes in the government agenda.

Major Parties Involved and Their Views

Nordic countries plus Switzerland

In these countries, the income inequality is below average and the employment rate is quite high. Governments of these countries favor household taxes that are proportional to household income, resulting in little distribution of tax and transfer system.

Eight European countries (Belgium, the Czech Republic, Estonia, Finland, France, Italy, the Slovak Republic and Slovenia)

Although income inequality in these countries is again below the OECD average, their employment rate is lower compared to the Nordic countries. Plus, the tax system is large and there is little wage dispersion.

Seven European countries (Austria, Germany, Greece, Hungary, Luxembourg, Poland and Spain) plus Japan and Korea

The income inequality and poverty rate are at or above the OECD average. The part-time labor is high whereas the overall employment rate is low in these countries. In addition, taxes and transfers are not highly progressive.

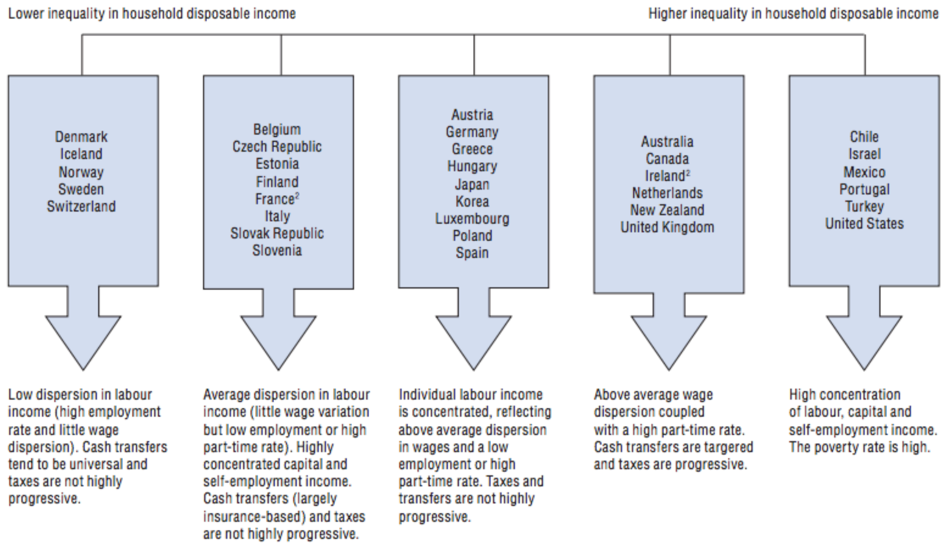
Five English-speaking countries (Australia, Canada, Ireland, New Zealand and the United Kingdom) and the Netherlands

Taxes are more progressive, meaning that the wealthy pay more tax than the poor in these countries compared to others in OECD. Yet except for the Netherlands, the household income inequality is high.

Chile, Israel, Mexico, Portugal, Turkey and the United States

The income distribution in these countries is quite high an low employment rate is evident excluding the United States. Tax systems are also small in many of these countries, as policy changes such as tax reforms tend to be less progressive in these nations. The income inequality rate is quite above the OECD average.

Figure 5.6. **Country groups with similar patterns of inequality**[1]



1. Country groups are derived from a cluster analysis of a set of 12 core income inequality indicators, with standardised values and unsquared Euclidean distance to measure differences between groups. Various alternative scenarios have been run. They suggest that the two groups to the right are very stable. The dividing lines between the three groups to the left are less sharp.
2. For France and Ireland, mid-2000s (instead of end-2000s) data have been used for the cluster analysis.

Source: Hoeller, P. *et al.* (2012), "Less Income Inequality and More Growth – Are they Compatible? Part 1. Mapping Income Inequality Across the OECD", *OECD Economics Department Working Papers*, No. 924, OECD Publishing.

Figure 2: https://www.oecd.org/eco/growth/49421421.pdf

The Organization for Economic Co-operation and Development (OECD)

OECD is an organization where 37 countries work together to promote policies that will stimulate economic growth and benefit the social wellbeing of the individuals. This forum analyzes data and statistics in order to predict future economic trends and seeks solutions for global concerns such as income inequality, poverty, and the gender wage gap.

Timeline of Events

The curve of global inequality and growth (1980–2016)

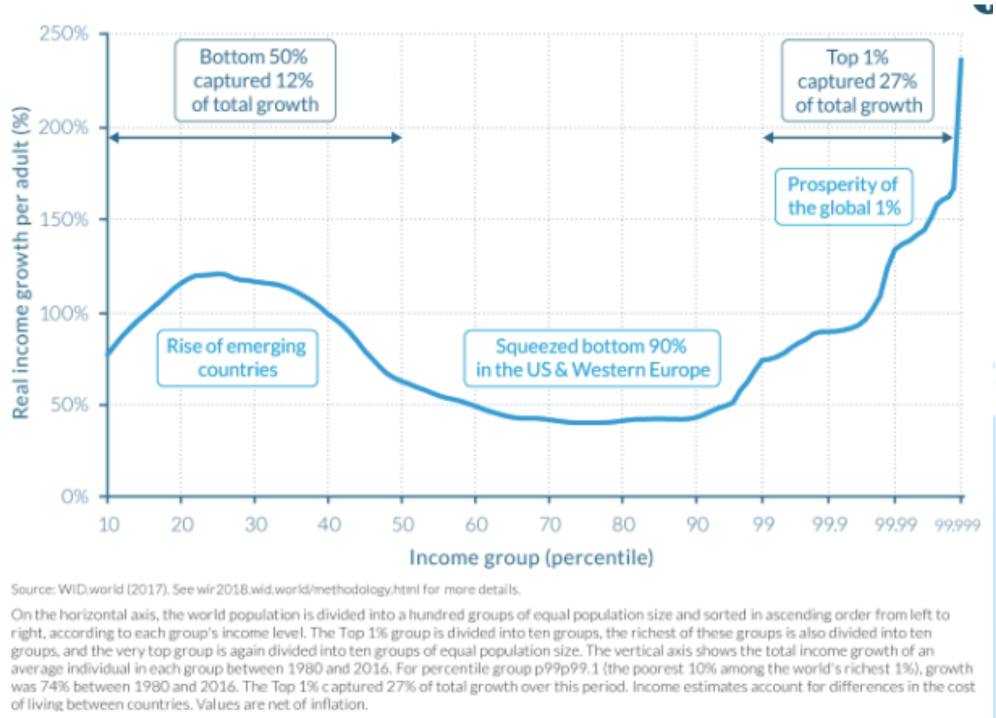


Figure 3: https://wir2018.wid.world/files/download/wir2018-summary-english.pdf

Top 10% income shares across the world (1980–2016)

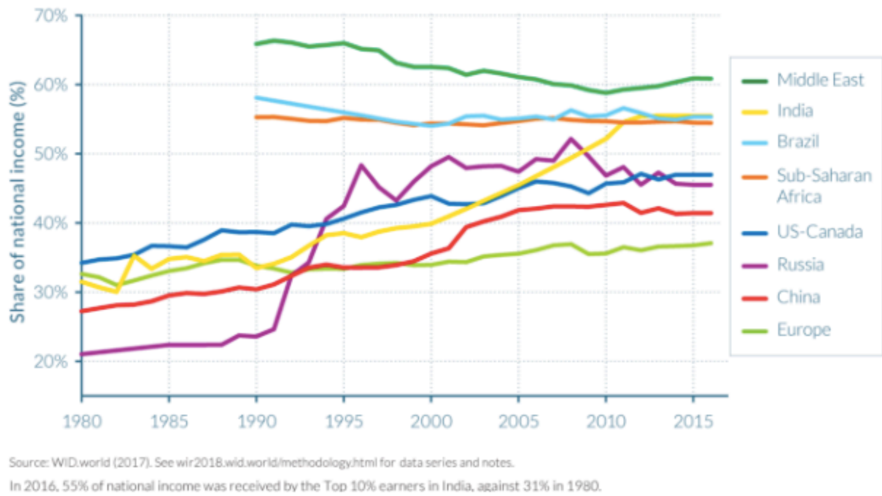


Figure 4: https://wir2018.wid.world/files/download/wir2018-summary-english.pdf

Treaties and Events

World Economic Forum in Davos 2018

"The body that organizes the Davos event said rising inequality was not an "iron law of capitalism", but a matter of making the right policy choices" (Guardian).

Overview of the Davos summit 2018 January: https://www.weforum.org/agenda/2018/01/davos-2018-biggest-stories/

Oxfam International Report for Inequality Crisis 2018

According to the Oxfam report, "The world's eight richest billionaires control the same wealth between them as the poorest half of the globe's population" (Guardian). Plus, while 3.7 billion people had no gains from economic growth, 82% of the wealth directly went to the wealthiest 1% of the population (WEF).

Link to the report: https://d1tn3vj7xz9fdh.cloudfront.net/s3fs-public/file_attachments/bp-reward-work-not-wealth-220118-en.pdf

World Inequality Lab's Report 2018

This report shows how global income inequality has declined modestly over the years since 1980, yet at different speeds. Using estimates and statistics for future growth, this report shows that the middle class has been shrunk and highlights the importance of national policies such as tax reforms to narrow the gap between the rich and the poor.

Link to the report: https://wir2018.wid.world/files/download/wir2018-summary-english.pdf

Evaluation of Previous Attempts to Resolve the Issue

Back in 2010, the government of Ecuador implemented minimum "dignity wage" which provides workers the basic expenses of living. This new minimum wage exercise benefited many workers over the years resulting in a lower unemployment rate in Ecuador compared to many other countries in Latin America, which also helped to decline the rate of income inequality.

In January 2018, Iceland became the first country to legally impose equal pay between men and women. The government of Iceland plans to eliminate the gender wage gap by 2020 as they believe this gap is a major obstacle in front of income equality among individuals. This new attempt hopefully will become a new European and even global model to demonstrate the possibility of eliminating the gender wage gap.

Moreover, many developed countries and multinational corporates are too focused on delivering extremely high returns on wealthy businessmen and chief executives that more poor-middle class people are becoming less tolerant to top rich. In addition, the rise of Donald Trump and Brexit aggravated much chaos among citizens as their lack of trust for these governments led to more anxiety for the rising income inequality and some unfavorable populist national policies.

Possible Solutions

One of the ways to reduce global income inequality is by enforcing new tax reforms. Considering that in rich countries the top 1% is capturing most of the income, it will be a reasonable policy to increase the tax rate imposed on individuals with the highest income.

Another crucial solution will be investing in human capital. By expanding access to early mandatory education, affordable childcare, and more beneficial national service, more individuals will have the opportunity to gain from these favors. Moreover, more student-friendly approaches can be taken by the governments to ensure all students can pay their tuition and don't pay fees during enrollment.

The identification of systemic barriers that minorities and immigrants have to confront based on their race, ethnicity, and immigration status is also important. Countries should look for methods such as new fast citizenship programs and prep courses available to all students, in order to tear down these barriers.

Furthermore, keep in mind that media reports illegal actions of big companies such as revealing that many multinational companies refrain from paying billions of dollars in the countries where they perform business and money transactions. Therefore, the presence of civil society organizations, NGOs, and investigative journalism is quite important in making sure these concerns and unacceptable behaviors are heard by everyone, and so that new solution alternatives can be promoted. The cooperation of governments plus transparency in the way information is reported are also key steps in moving further toward equality.

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