

Why is Europe more equal than the US?

New evidence on European inequality & prospects for a fiscal union

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- Revisiting standard views about inequality and redistribution in Europe thanks to novel Distributional National Accounts
 - *"Why is Europe More Equal than the US?"*, T. Blanchet, L. Chancel, A. Gethin WID.world Working Paper 2020. (www.wid.world/europe2019)
- Prospects for equitable (and sustainable) growth in the EU in the decades to come
 - *"Treaty for the Democratization of Europe"*, M. Bouju, L. Chancel, S. Henette, T. Piketty, G. Sacriste, A.-L. Delatte, A. Vauchez et al. (www.tdem.eu)

What Do We Know about Inequality in Europe? Not enough

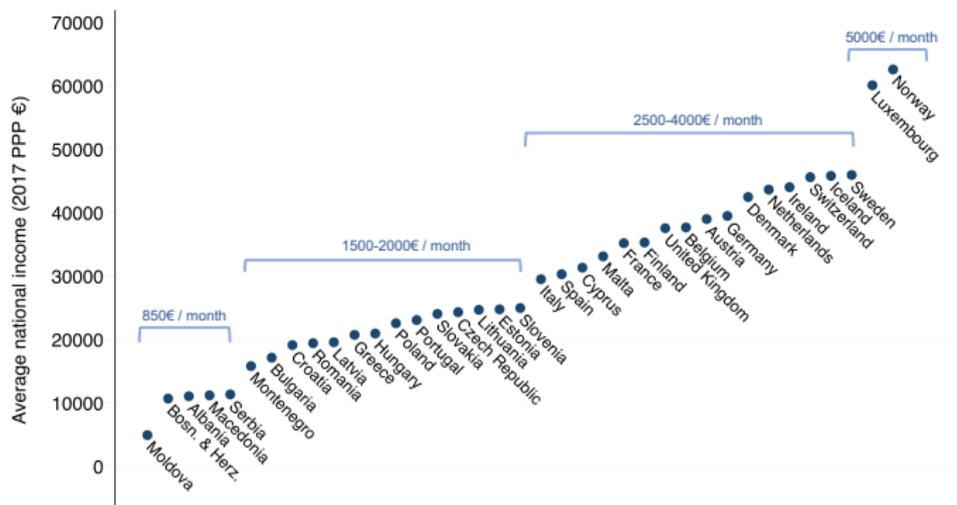
Disparate set of indicators (National accounts, surveys, tax data): hard to compare and tell consistent stories.

⇒ **Previous studies have struggled to answer simple questions:**

- Is European inequality mainly driven by *between* or *within* country inequality?
- How unequal is Europe when Eastern countries are factored in?
- What drives recent EU inequality dynamics: pre or post tax incomes?

Standard view #1: inequality in Europe is primarily about between-country divergences

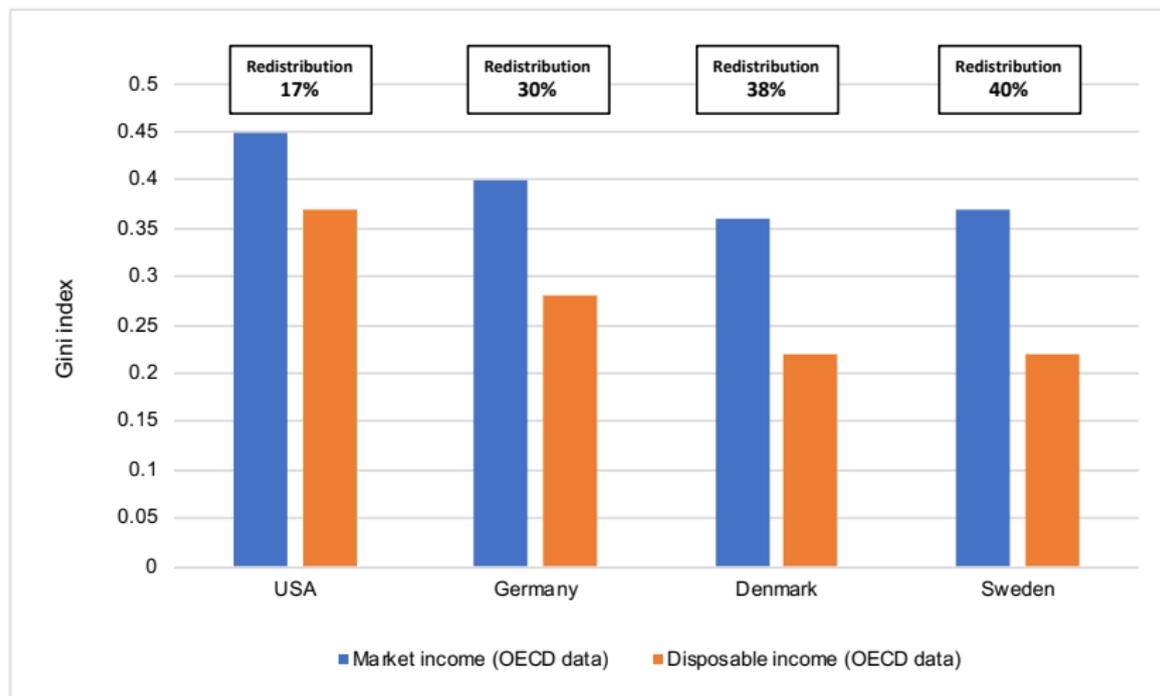
Average national incomes across European countries, 2018



Source: Blanchet, Chancel and Gethin (2019)

Standard view #2: Europe more equal thanks to redistribution

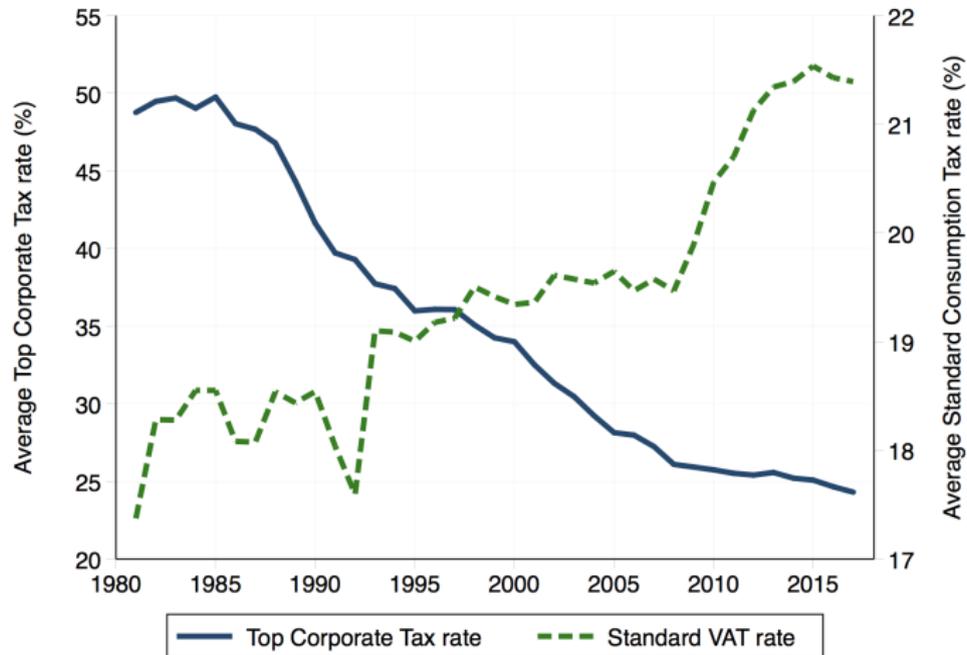
Inequality in Europe and the US according to the OECD



Source: OECD (2011)

Standard view #3: in tax matters, it's unanimity rule or nothing

Average VAT and top corporate income tax in the EU, 1980-2018



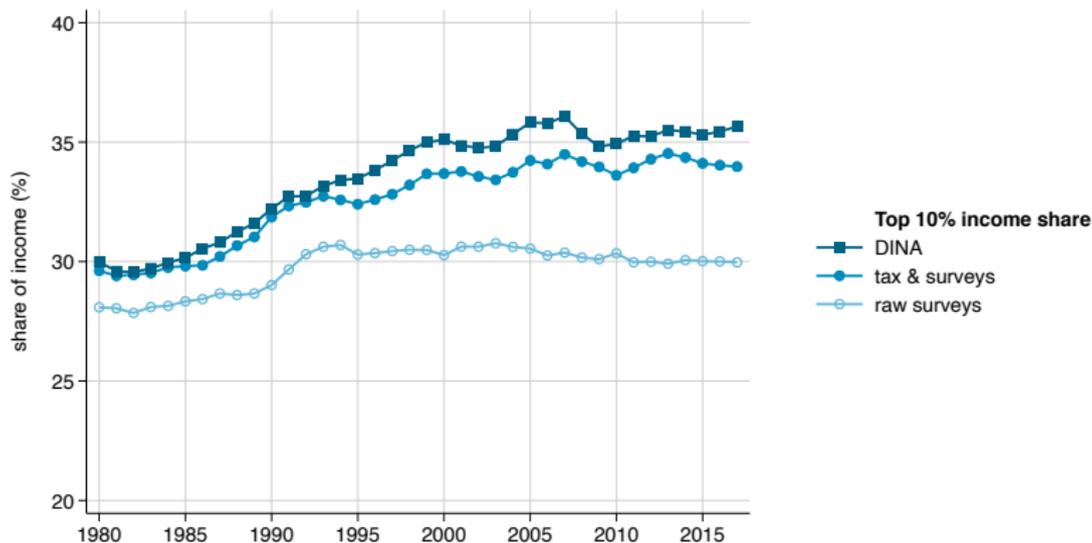
Source: Blanchet, Chancel and Gethin (2019)

Distributional National Accounts: distribute macro growth

- **Distributional National Accounts (DINA) seeks to distribute 100% of macroeconomic growth to individuals**
 - Reconciliation of the microeconomic study of inequality (disposable income, poverty...) and macroeconomic issues (public debt, aggregate growth...)
- **Our method combines all available survey, tax and national accounts data in a systematic way**
 - Based on the pioneering work by Kuznets (1953), Atkinson (1978)
 - Improves from top incomes literature thanks to integration of non-taxable incomes: more comparability across countries and over time (Piketty, Saez, Zucman, 2018)
- **International, collaborative, cumulative, open-source project**
 - 100 researchers working on all continents, covering more than 90 countries. All data series & codes available online on *WID.world*.

Income inequality in Europe: mobilizing all data sources

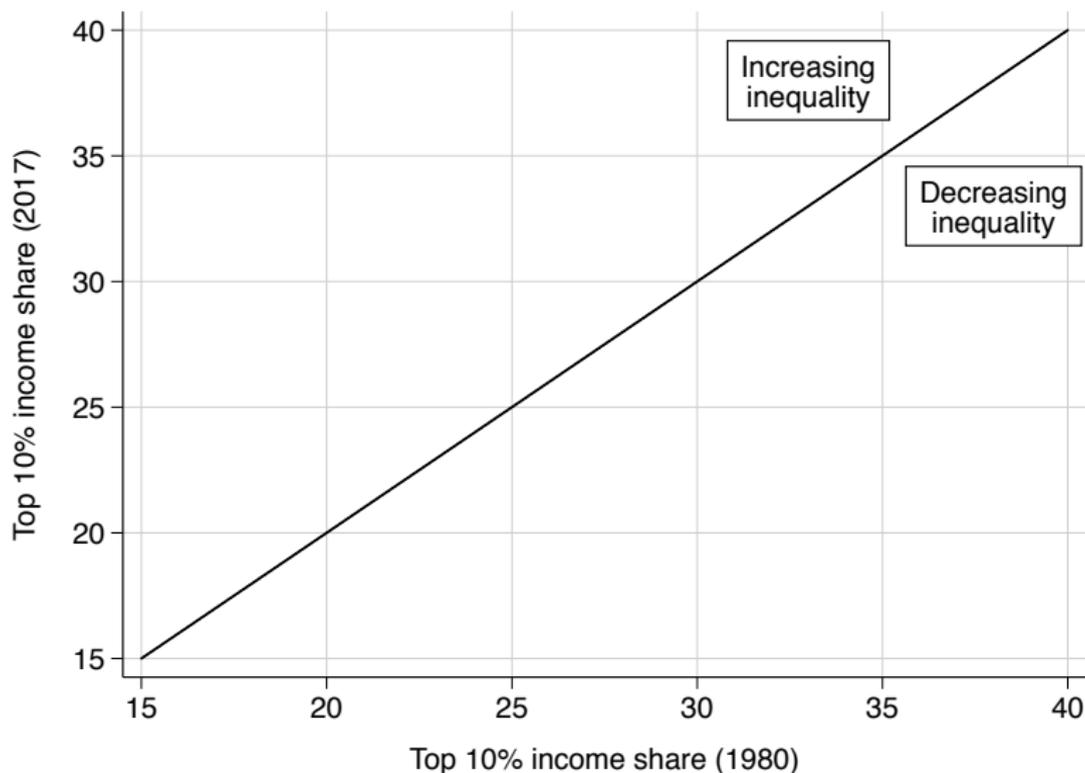
Top 10% income share in Europe:
DINA vs. tax vs. survey data, 1978-2015



Source: Blanchet, Chancel and Gethin, 2020

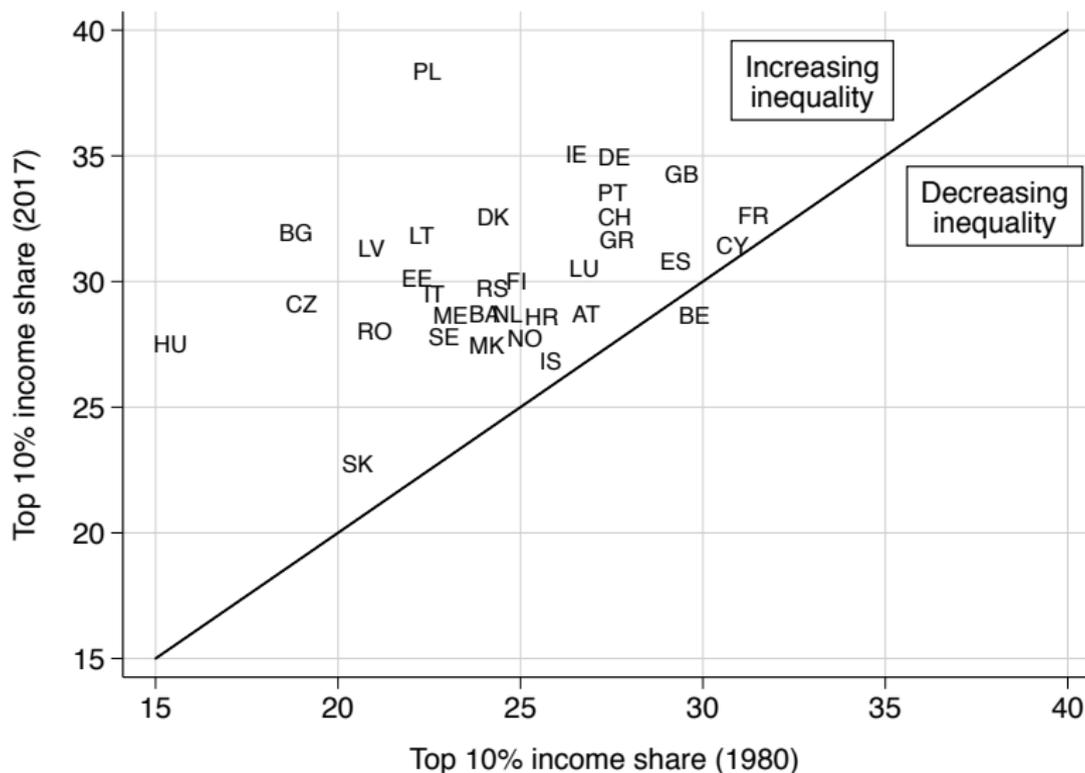
Rise in inequality since the 1980s in most countries

Top 10% shares in Europe, 1980 vs. 2017



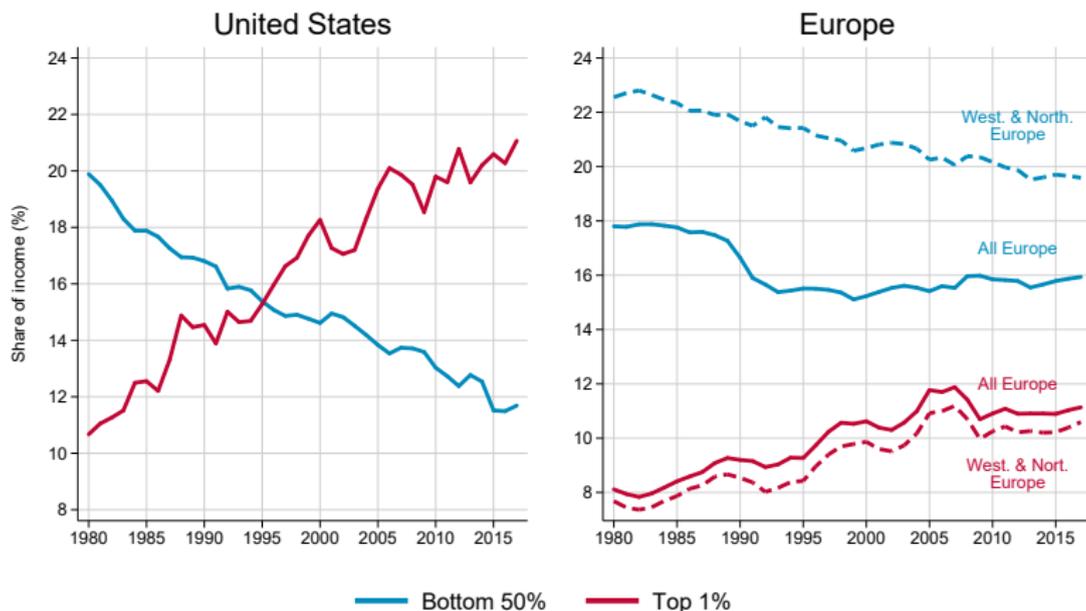
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Top 10% shares in Europe, 1980 vs. 2017



EU vs. US: diverging pretax inequality trends

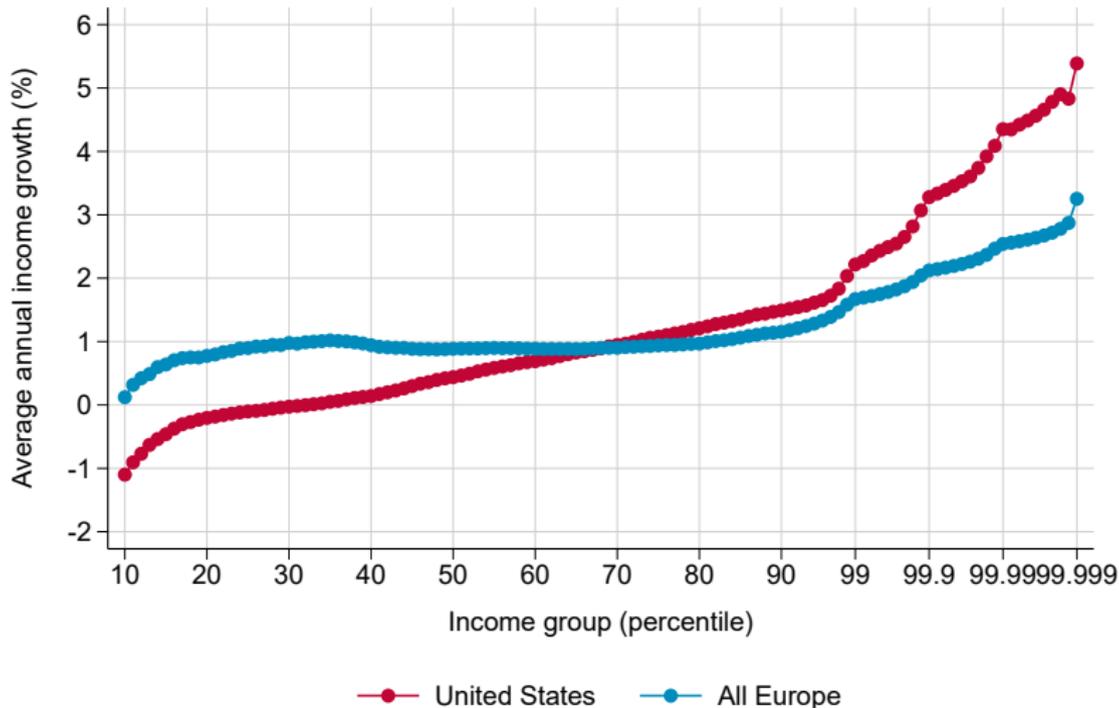
Top 1% and bottom 50% income shares in Europe and the US, 1980-2017



Source: Blanchet, Chancel and Gethin, 2020

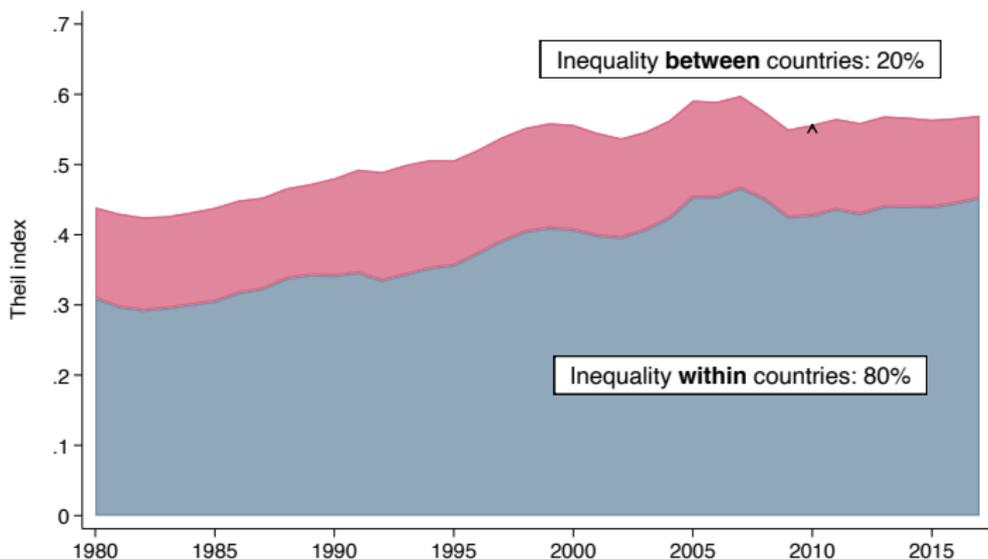
Average annual growth 1980-2017: US 1.4%, EU 1.15%. Europe much more successful at the bottom: 1% vs. 0%.

Pretax income growth by income percentile, 1980-2017



Most of European inequality occurs within countries

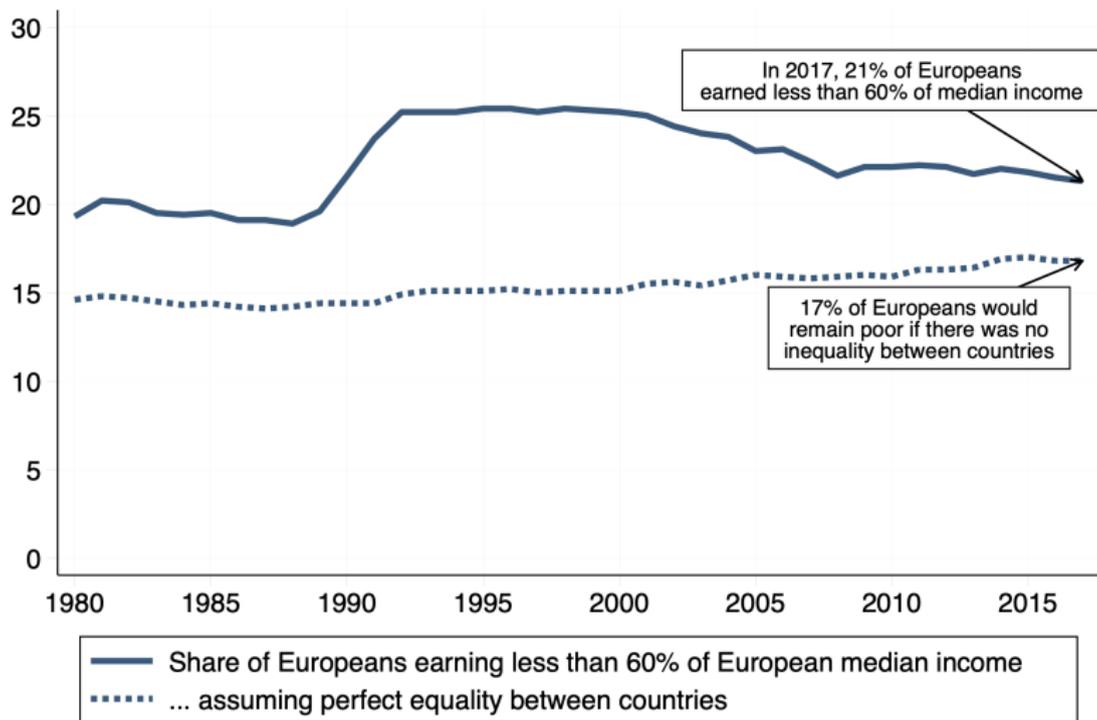
Theil index of inequality in Europe, 1980-2017



Source: Blanchet, Chancel and Gethin, 2020

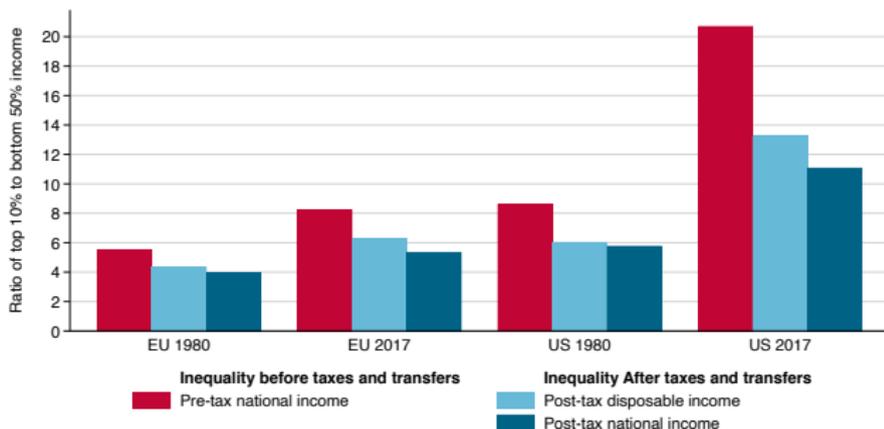
Most of European inequality occurs within countries

Poverty rates in Europe, 1980-2017



” It’s pretax, stupid!”

Inequality and redistribution in Europe and the US:
Ratio of top 10% to bottom 50% average incomes before & after taxes



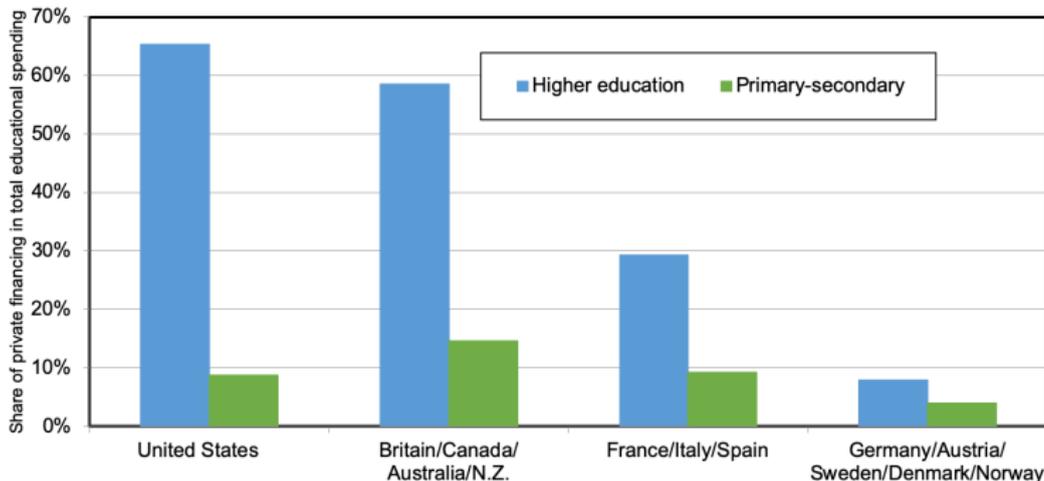
Source: Blanchet, Chancel and Gethin, 2020

EU's slower rise of pretax inequality: trade & technology?

- **Lesser exposure to trade?** Share of imports from low-income countries rose slightly more in Europe than in the US (World Bank, 2019)
- **Lesser exposure to new technologies?** No evidence for higher robot penetration in the US (Acemoglu and Restrepo, 2017)

EU's slower rise of pretax inequality: access to universal public services

Share of private spending in higher education

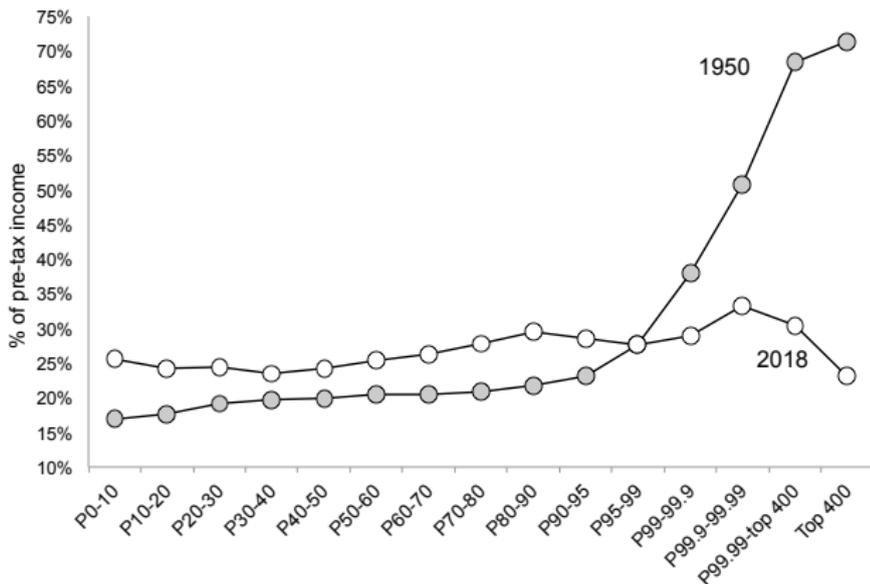


Interpretation. In the U.S., private financing make 65% of total financing (private and public) of higher education, and 9% of total financing of primary and secondary education. The share of private financing in higher education varies substantially across countries, with an anglo-american model, a south-european model and a north-european model. The share of private financing is everywhere relatively small regarding primary and secondary education (2014-2016 figures). **Sources and series:** see piketty.pse.ens.fr/ideology

Source: Piketty, 2019

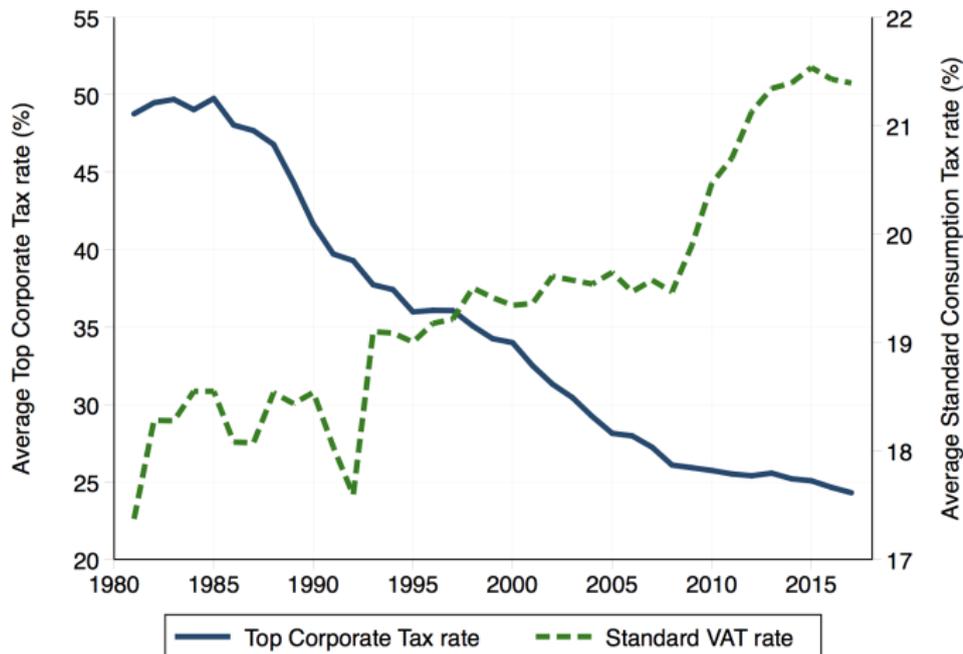
Today's taxes impact tomorrow's pretax income concentration

Total taxes per income group in the US, 1950 vs. 2018



Source: Saez and Zucman, 2019

The lack of a Fiscal Union limits EU Member States' ability to implement progressive taxation



Source: Blanchet, Chancel and Gethin, 2020

Issues with the establishment of common minimum tax rates

- The implementation of common minimum tax rates on top income, wealth (or carbon emissions) requires EU Council unanimity
- Since Amsterdam (1997) and Nice (2001), enhanced cooperation is possible in tax and other matters
 - It requires a minimum of 9 Member States + EU Council qualified majority (i.e. 55% of votes at the Council, from countries representing 65% of EU population)
 - Without EU Commission prior approval, qualified majority threshold brought to 72% votes from countries represented 65% EU population
 - 4 Member States representing 35% EU population can block the move
- Qualified majority is an option, but an extremely constraining one

No common taxes but economic government

- Through a series of treaties (Treaty on Stability, Coordination and Governance and Treaty establishing the European Stability Mechanism), and legislative packages (the Six-Pack and Two-Pack, European Semester), European economic govt. was implemented in 2010s (cf. Eurogroup).
- It possesses instruments (of surveillance, control and conditionality) to reshape the fiscal social pacts of the EU Member States.
- European and National Parliaments largely excluded from this economic govt. Representative democracy values of the EU (cf. TEU art. 2 & 13) seriously eroded.

Treaty for the Democratization of Europe: parliament to establish new EU taxes

- Idea: bypass EU unanimity rules and rely on parliaments to deal with tax matters
- Treaty establishes a European Assembly, composed of national and EU MPs, with power over new corporate, income, wealth (and carbon) minimum top marginal tax rates.
- Enters into force as soon as any two countries are willing to sign it.
- Half of taxes collected are directly redistributed to participating countries, other half used to fund joint projects (e.g. higher education, climate change, migration).

Treaty for the Democratization of Europe: tax revenues

- Minimum **corporate tax** rate set to 37% (15% above actual 22% average in the EU, back to early 1990s period): tax revenue = 1.5% GDP
- Additional top marginal **income tax** rate set to 10% above EUR 100k and 20% above EUR 200k (implying an average 50% rate above 100k on average and 60% above 200k on average): tax revenue = 1% GDP
- Introduction of a top marginal **wealth tax** rate of 1% above EUR 1 million and 2% above EUR 5 million: tax revenue = 1.1% GDP
- Introduction of minimum **carbon tax** rate of EUR 30 per ton (with rapid increase reaching EUR 100) = 0.4% GDP

- Overall, 4% of GDP of participating countries is levied
- 2% given back to these countries, 2% invested in common projects (innovation, climate change, migration)

What about tax dumping?

- **Corporate taxes:** nothing prevents countries from implementing formulary apportionment (i.e. Amazon, Chanel or Mercedes' taxable profits in Italy computed on the basis of global share of sales made in Italy).
 - Tax sovereignty becomes an asset rather than a brake issue
 - Potential European Court of Justice challenge over "hidden import tariff" but key difference since the measures disappears as soon as companies' home countries increase corporate tax rates
 - If forbidden by ECJ on these grounds: serious arguments for progressive parties to adopt "exit" positions.

What about tax dumping?

- **Income and wealth taxes:** countries can introduce or increase exit taxes, i.e. taxes to be paid in the case of international change of fiscal address. In practice, tax mobility due to changes in top wealth taxes are found to be low (French wealth tax based multiplied by x4 between 1989 and 2017).
- **Carbon taxes:** EU ETS sectors: carbon floor mechanism implemented by the UK before Brexit, compatible with EU legislation. No evidence of important carbon leakage.

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Concluding remarks

- Despite persistent average income gaps, European inequality mostly occurs within countries
- Inequality on the rise in Europe since the 1980s (top 0.1% avg. growth: 2.5-3%, bottom 50%: 1%)
- Europe's relative resistance is mostly about pretax incomes
- "Predistribution" driven by market regulations access to public services, but also progressive taxation
- Common market without tax union fuels tax competition and limits MS ability to invest in public services tax mobile taxpayers
- Proposal: parliamentary assembly to implement minimum progressive tax rates. Franco-German assembly established in 2019 as a precursor?