Executive summary

This report on the measurement of inequality and redistribution is the result of the work of some forty experts, brought together at the initiative of INSEE (French National Statistics Institute) on the basis of a mission statement from its Director General, dated 19 March 2019. This group was established in response to two key drivers. On the one hand, the publication, in late 2018, of studies conveying seemingly different messages regarding the comparative extent of redistribution in France and in a number of other developed countries. On the other hand, faced with growing sentiment within society that people are not getting a “fair return on their taxes”, the need to inform the public debate with regard to what taxes are actually used for. Who pays what and how much? Who receives what and in what form?

It is not just monetary transfers that people receive in return for tax and social security deductions, they also receive social transfers in kind such as free access to health and education, and collective expenditure that benefits the whole population: assessing who benefits from redistribution and who finances it requires a broad overview of what is offered in return for the contributions.

In order to examine these issues, the expert group was comprised of members from the following institutions: the relevant INSEE directorates (Director of Economic Studies and Reports and Demographic and Social Statistics Directorate); the main academic teams that had fuelled the debates at the end of 2018 or that make regular contributions to the findings on redistribution; the *World Inequality Lab* (WIL) at the Paris School of Economics; the Institute of Public Policies (IPP); the French Economic Observatory (OFCE); the Laboratory for Interdisciplinary Evaluation of Public Policy (LIEPP) at Sciences-Po; several Ministerial Statistical Offices (DREES, DEPP and SIES); the Directorate-General of the French Treasury; and, on an ad hoc basis, the OECD, where an *Expert group on Distributional National Accounts* (EG DNA) has been working in recent years on the standardisation of national accounts by household category, as regularly published by INSEE.

The report begins with a systematic examination of the factors that may explain why different teams come to different findings: (i) differences in the sources used; (ii) selection of analytical units (individuals *versus* households, with different ways of taking account of economies of scale within those households); (iii) selection of inequality indicators (indices evaluating distribution as a whole, such as the Gini and Atkinson indices, or the use of different types of ratio indicators for the incomes or standards of living of different population categories); (iv) and, last but not least, the question regarding the scope of redistribution.

The comparisons drawn by the working group allow the first two sources of discrepancy to be put into perspective. In the case of identical concepts, the findings are similar regardless of the sources used (i). And the selection of the analytical unit, although not completely without effect, does not explain the discrepancies (ii). On this second point, however, the report highlights the need for a precise rule for the grouping of the elementary units into stable population subgroups. In fact, the indicators make use of average incomes or standards of living for more or less fine bands of the population: inter-deciles, inter-centiles or even finer bands are used to explore the high end of redistribution, subject to the representativeness of the sources at these fine levels. It is essential that the comparisons of distribution before and after transfers are based on a stable classification of the individual units within these various groups.

The question of indicators (iii) then becomes crucial: each indicator represents a specific way of exploring the distribution of incomes and standards of living, each weighting the various bands of this distribution in its own way. The report offers a comparative assessment of the properties of these indicators and argues that every study should make use of at least one global indicator and one ratio indicator, and also that the information needed to calculate the other indicators should be made available.

The final question (iv) concerns the definition of the scope of redistribution. This is the main area in which the various approaches differ from one another. The usual studies looking into redistribution, conducted by DREES or the OFCE and INSEE's annual publications alike, focus on transfers, including direct taxes, social security contributions and cash benefits. The work carried out by the WIL on distributional accounting also adds taxes on production and products to this. The other public transfers are included in principle; however, their effects are neutralised pending future studies, by a normative assumption of proportionality. The OECD (EG DNA) excludes taxes on products and production, but takes account of social security benefits in kind and public services that can be individualised, which INSEE also includes in its analyses but on a more ad-hoc basis. None of these approaches take account of the redistributive aspect of fully collective public expenditure.

This situation poses several overlapping problems. Different definitions inevitably lead to different assessments of the extent of redistribution. The fact that the coverage is only partial leads to "unbalanced" sets of transfers being taken into account, which distorts the analyses, since we are led to consider either services for which there is no mention of how and therefore by whom they are financed, assuming they are financed upstream of the field in question, or deductions that will be described as being "at a loss", since they are used to finance services positioned downstream of the field in question. At the same time, partial coverage lends bias to international comparisons given the highly variable nature of social protection, public policy and the financing thereof from country to country, with proportions of out-of-scope coverage that will vary greatly from one country to the next.

In an ideal world, it would therefore be desirable to adopt a comprehensive overview of redistribution that includes all modes of financing and all types of public benefits or services: this is the only way to take account of the fact that everything provided by the community is financed directly or indirectly by the population and ultimately benefits that population, again either directly or indirectly. Nevertheless, adopting such a broad view then raises questions of imputation as soon as you start examining transfers beyond the traditional scope of directly measurable redistribution.

It involves quantifying all that individuals or households receive for free or are able to buy in the observed state of the world, compared with what they would have been able to or would have needed to buy in a world without government intervention. The performance of an evaluation of this type relies on the imputations that the report is striving to substantiate from an economic point of view. Who ultimately pays the VAT or production taxes? What market income would individuals have if these taxes did not exist and what pricing system would be in place? Which households benefit from retained company earnings? Which key should be used to distribute the benefits of collective public spending to individuals?

The report answers these questions by making some twenty recommendations to practitioners and proposes a structured response in the form of "distributed national accounts" (DNA), the purpose of which is to integrate the international standards for national accounting. Using the rows in the table of integrated economic accounts (TIEA) for national accounting as a starting point, the report builds a table of integrated distributional accounts (TIDA), each row of which breaks down income and transfers by ascending standard of living bands. The standard of living concept used to enable classification into these bands is disposable income per consumption unit. This reference classification is used since it is both the closest to the way that households feel and, being directly observed, is independent of the breakdown and imputation assumptions used for the exercise. The selection of this standard, which forms an essential basis for international comparisons, does not detract from the relevance of work based on other classifications, such as primary income.

The proposed tool can be used in a number of different ways: its intermediate rows, which correspond to the usual scope of redistribution, can be used with the above-mentioned limitations, or it can be considered in its entirety. For the rows most likely to be affected by imputation, for example the distribution of non-individualizable collective expenditure or taxes on products and production, the underlying micro founded data are made available to allow other variants to be explored.

The report concludes by illustrating the approach by applying it to France, using the Tax and Social Incomes survey and INES micro-simulation model imputations for the majority of the rows in the table, with the remaining rows being supplemented by the assumptions detailed in the report, which may, of course, be subject to debate. As it stands, the result shows that, while only 40% of the least privileged households are net beneficiaries of redistribution in the traditional sense that INSEE lends to this term, i.e. monetary, the proportion increases to two-thirds when you look at a broader standard of living.

A comparison with the United States is also proposed based on WIL data. It reveals lower levels of inequality in France than in the United States, both before and after transfers. The findings regarding the intensity of redistribution are linked to the position on the income scale and on whether reasoning takes place on the basis of absolute transfers or as a percentage of income prior to redistribution. However, the discrepancy does not lie in the tax system, but in the benefits system, which, in France, is targeted more towards persons on low incomes in the case of cash benefits, and offers greater amounts for benefits in kind such as education, health or even housing.