

Causes, Consequences And Measures To Reduce Inequality Of Income Distribution –Role Of Government To Reduce In Equality.

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ABSTRACT: It is not enough for a country to attempt to increase its national income. It is also necessary to ensure that it is evenly distributed. But inequality of income is an important feature of capitalist economies. The socialist countries like the U.S.S.R. and Communist China have established systems whose aim is to reduce inequalities of incomes. Even they have failed to attain perfect equality. In the capitalist countries, on the other hand, it is generally recognized that inequalities will remain and that cannot be helped. Some economists make even virtue of this necessity and they see lot of good in these inequalities from the point of view of capital formation.

KEYWORDS: Inequality of Income, Progressive Tax, Capital formation, Distribution.

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I. INTRODUCTION:

Income inequality is an extreme concentration of wealth or **income** in the hands of a small percentage of a population. It has been described as the gap between the richest and the rest. Besides others the main cause of inequality is Another **cause of inequality** is inflation. During inflation, few profit earners gain and most wage earners lose. ... Moreover, during inflation, money **income** increases no doubt but real **income** falls. And this leads to a fall in the standard of living of the poor people since their purchasing power falls. Both cash benefits and income tax lead to an overall reduction in income inequality. Although richer households pay more in indirect taxes than poorer ones, they pay less as a proportion of their income. This means that indirect taxes can increase income inequality.

Generally it is believed that income inequality of a country can be reduced by the following ways, such as, Increase the minimum wage., Expand the Earned Income Tax., Build assets for working families, Invest in education, Make the tax code more progressive, End residential segregation.

Increases in the level of income inequality have a negative long-run effect on the level of GDP per capita. ... The estimates from the interaction model thus suggest that in poor countries, increases in income inequality raise GDP per capita while the opposite is the case in high- and middle-income countries. While one school of research shows how income inequality might harm economic growth, empirical studies show that in the United States, a positive linkage between economic growth and income inequality has existed since the 1970s. The aim of this paper is to see how economic growth affects income inequality. Inequality Is the Main Cause of Persistent Poverty. ... Had income growth been equally distributed, which in this analysis means that all families' incomes would have grown at the pace of the average, the poverty rate would have been 5.5 points lower, essentially, 44 percent lower than what it was.

II. CONSEQUENCES OF INEQUALITY:

Inequality of incomes leads to some very serious economic and social consequences:

(a) Class-conflict:

It has created two sections in society—the 'haves' and the 'have-not's'—which are ever on the war path. This has resulted in ever mounting social tensions and political discontent.

(b) Political Domination:

The rich dominate the political machinery, and they use it to promote their own exclusive interests. This results in corruption, graft and social injustice.

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(c) Exploitation:

The rich exploit the poor. The consciousness of this exploitation leads to political awakening and then agitation and even political revolution. Thus inequality of incomes is an important cause of social and political instability.

(d) Creation of Monopolies:

Unequal incomes promote monopolies. These powerful monopolies and industrial combines charge unfair prices from the consumer? And crush the small producers. The bigger fish swallow the small fry.

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(e) Suppression of Talent:

It is said that 'slow rises merit by poverty depressed'. It is not easy for a poor man to make his way in life, however brilliant he may be. It is a great social loss that brainy people without money are unable to make their due contribution to social welfare.

(f) Undemocratic:

Democracy is a farce when there is a wide gulf between the rich and the poor. Political equality is a myth without economic equality.

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(g) Moral Degradation:

The rich are corrupted by vice and the poor demoralized by lack of economic strength. Thus inequalities spoil the rich and degrade the poor. Vice and corruption rule such a world. The poor man finds it almost impossible to regain the virtues of honesty and integrity. Human dignity is lost altogether.

(h) Promotes Capital Formation:

However, there is one good which comes out of these inequalities of incomes and that is that it facilitates savings. If the national income of the country is evenly distributed among all its citizens, it is clear that it will be only thinly spread over the whole population. Everyone will have nothing left for saving. It is only when income is unequally distributed that there are people who are so rich that in their case saving is automatic.

It is only a minority of the people who have the saving habit. To the rest if income comes, it is squandered away. Under a system, where there are large accretions of wealth in certain patches, not only is the capacity for savings greater, but the ability to invest and gain is also greater. There are people who save and turn their saving into capital. Thus inequality of incomes helps capital formation in a country.

Hence, governments have to look to avoid these unwanted situations in the country.

III. CAN GOVERNMENT REDUCE INEQUALITY?

Today, economists and political scientists tend to agree that government was a factor in this story, but they have an incomplete picture of precisely how government drove this wedge. Financial deregulation certainly played a central role. So did the decline of private-sector labor unions, which was largely driven by government policies, starting as early as the late 1940s and reaching a moment of maximum impact in the 1980s. After the Great Inflation of the 1970s, the Federal Reserve started placing more emphasis on inflation fighting than on job creation in setting monetary policy. The rise of corporate lobbying during the 1970s and 1980s helped steer government policies toward the interests of the rich. The failure to keep the minimum wage rising in real terms probably exacerbated the problem, too.

Research in economics reacts both to the real world around us and to the new tools available to us. As global inequality increased significantly, new tools of research in neoclassical economics have been developed, mainly the use of models of heterogeneous agents. Economists have begun to analyze the effects of the distribution of income on other macroeconomic variables, like aggregate output and technical change. They have also begun to study what determines the distribution of income and why it differs so much both across countries and over time.

Focusing on the effects of policy on inequality does not mean that we ignore other determinants of inequality, such as the level of development, globalization, and technical change. Nevertheless, our research shows that the effect of public policies is not only statistically significant, but is also quite large. One way to see the effect is to examine the difference between the distribution of economic income, which is determined in the labor market, and disposable income after receiving subsidies and paying direct taxes, mainly income tax. The gap between the two types of income will be due to public policies.

Direct taxes and welfare transfers are actually both the results of public intervention in the economy. As government intervenes more and supplies more public services, it has higher expenditures and needs to raise taxes, including direct taxes. The degree of public intervention also affects subsidies, since welfare benefits are an important channel of intervention in the economy.

In light of these results, we raise a conjecture that inequality of disposable income should decrease if the government increases its intervention in the economy. To test this conjecture, the paper measures public intervention by public expenditures as percent of GDP. Indeed, the analysis shows that the share of public expenditures in GDP has a negative, significant, and large effect on inequality. For a given level of inequality of

market income, a rise of public expenditures by an additional percent of GDP reduces the Gini coefficient of disposable income by 0.35 percentage points. Since the size of public expenditures across the OECD countries varies from 35 to 55 percent of GDP, this variable can therefore explain variability of the Gini coefficient of 7 percentage points across these countries. The Gini of disposable income in the OECD countries varies from 0.25 to 0.4. Hence, changes in public intervention can explain half or even more of these differences. Besides these, following steps can be taken by governments.

Fixing Minimum Wage:

One step that can be taken in the direction of more egalitarian society is to guarantee each citizen a minimum wage consistent with a minimum standard of living. In India in 1948, the Minimum Wages Act was passed in pursuance of which minimum wages are being fixed for agricultural labour and labour in what are called the 'sweated trades'. This is a step which will level up the incomes from below.

Social Security:

Another important measure is the introduction of a comprehensive social security scheme guaranteeing to each individual a minimum standard of economic welfare. The social security scheme that we envisage must include provision of free education, free medical and maternity aid, old-age pension, liberal unemployment benefits, sickness and accident compensation, provident fund and schemes of social insurance, etc. In that manner, substantial benefits can be assured to persons whose incomes are low. Such benefits of course have a money value. This will be another step towards leveling up incomes.

Social services like public parks, libraries, museums, community air-conditioned halls, community radio and TV sets, refrigerators may be provided on a liberal scale, so that the poor are able to enjoy almost all possible amenities available to the rich.

Equality of Opportunity:

The Government may devise and set up some sort of machinery which may provide equal opportunities to all rich and poor in getting employment or getting a start in trade and industry. In other words, something may be done to eliminate the family influence in the matter of choice of a profession. For example, the government may institute a system of liberal stipends and scholarships, so that even the poorest in the land can acquire the highest education and technical skill.

The recruitment to all jobs may be made by an impartial Selection Board or Public Services Commission. Recruitment even in the private sector may be done by employment exchanges or independent selection agencies. In the same manner, to give start in trade and industry, the Government may give financial aid or loans at very reasonable rates repayable in easy installments to all those who wish to enter trade and industry.

In India, several concessions are being offered to scheduled castes and backward classes or persons living in backward areas so that the evils of their backwardness may be minimized. Lot has been done under the 20-Point Economic Programme to help the poor and lift them economically, such as abolition of bonded labour, scaling down or writing off of debts, provision of house sites, etc.

Steeply-graded Income Tax:

Mere leveling up will not bridge the gulf between the rich and the poor. It will also be necessary to raze to the ground the high mountains of privilege. For this purpose all possible fiscal devices should be adopted. One such device is the steeply progressive taxes on incomes. This will prevent, to some extent, a rich man from getting richer still. Other direct taxes like the super tax, excess profits tax, and capital gains tax and limitation of dividends, etc., may also be imposed.

High Taxes on Luxuries:

All conspicuous consumption by the rich may be ruthlessly crushed by means of heavy taxation of the consumption of luxuries by them. This will take away from the rich the power to display their wealth. This will also take away the incentive to amassing wealth for exclusive private enjoyment. Expenditure tax in India sought the same objective. (This tax has, however, been abolished.)

Steep Succession Taxes and Estate Duty and Wealth tax:

Lest inequities should be perpetuated from generation to generation, steeply-graded estate duty and/or wealth tax may be imposed. In 1964-65 and again in 1966-6, rate of estate duty were made steeper in India. They went up to 40%, which is almost expropriator. (However in the Finance Act of 1985 the Estate duty was abolished and wealth tax rates were also reduced.)

Ceilings on Agricultural Holdings and Urban Property:

With a view the reducing inequalities between the big and small farmers, ceilings on agricultural land holdings can be imposed. This has been done in India and recently the ceilings have been to lowered to 10-18 standard acres. The main purpose of land ceilings is to bring about a wider and equal ownership and use of land. As a counterpart, a ceiling on urban property can be imposed so that inequalities in urban areas can also be toned down. More radical socioeconomic reforms seem to be in the offing in India. These are some of the measures that can be adopted to reduce inequalities. But inequalities can be reduced, they cannot be eliminated altogether. In fact, absolute equality is unattainable.

Governments can intervene to promote equity, and reduce inequality and poverty, through the tax and benefits system. This means employing a progressive tax and benefits system which takes proportionately more tax from those on higher levels of income, and redistributes welfare benefits to those on lower incomes. Following steps can be taken for this direction.

1. Research shows that higher wages for the lowest-paid workers has the potential to help nearly 4.6 million people out of poverty and add approximately \$2 billion to the nation's overall real income. Additionally, increasing the minimum wage does not hurt employment nor does it retard economic growth.
2. In recent years, the EITC has been shown to have a positive impact on families, lifting roughly 4.7 million children above the poverty line on an annual basis. Increases in the EITC can pull more children out of poverty while providing more economic support for the working poor, especially single parents entering the workforce.
3. Policies that encourage higher savings rates and lower the cost of building assets for working and middle class households can provide better economic security for struggling families. New programs that automatically enroll workers in retirement plans and provide a savings credit or a federal match for retirement savings accounts could help lower-income households build wealth. Access to fair, low-cost financial services and home ownership are also important pathways to wealth.
4. Differences in early education and school quality are the most important components contributing to persistent inequality across generations. Investments in education, beginning in early childhood with programs like Head Start and Universal Pre-K, can increase economic mobility, contribute to increased productivity and decrease inequality.

5. Make the tax code more progressive.

It is a great irony that tax rates for those at the top have been declining even as their share of income and wealth has increased dramatically. The data show we have created bad tax policy by giving capital gains -- profits from the sale of property or investments -- special privileges in our country's tax code; privileges that give investment income more value than actual work. Capital gains tax rates must be adjusted so that they are in line with income tax rates. Savings incentives structured as refundable tax credits, which treat every dollar saved equally, can provide equal benefits for lower-income families.

6. End residential segregation.

Higher levels of racial residential segregation within a metropolitan region are strongly correlated with significantly reduced levels of intergenerational upward mobility for all residents of that area. Segregation by income, particularly the isolation of low-income households, also correlates with significantly reduced levels of upward mobility. Eliminating residential segregation by income and race can boost economic mobility for all. Each of these policies, if carefully implemented, has the potential to lift working families out of poverty, support greater economic mobility and/or reduce the growth of inequality. All of these policies could be enacted at the local, state and federal levels if there is political will. While there is still some disagreements of the best way to reduce inequality, there is a growing consensus that inequality should be reduce. Recently the IMF joined this consensus in finding that inequality reduces overall economy growth as well as challenges basic democratic principle and fairness. But getting policymakers to prioritize these policies will depend on the actions of advocates, voters and other supporters with a vision for a fair and inclusive society so strong that they overwhelm powerful forces that seek to maintain the status quo.

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