Perspectives on intergenerational transfers

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The ‘circuit’ of French financial intergenerational transfers
- Upward social transfers to the 60+ \( \approx 20\% \) of GDP
- Downward private wealth transfers \( \approx 10\% \) or more of GDP
- The circuit has doubled in \% of GDP since 1980 due to major historical changes since the end of the 70s  Belgian case similar?
  - Opposite views on such high ‘family returns’ (Kohli vs Esping-Andersen)
Outline

- Aging & other relevant concomitant historical changes (1980->)
- **Generation** effects & issues
  - Conflict, equity or cooperation between generations: an ideological choice
- Social issues
  - Which social model? Sustainability issues. Rise of the risk of longevity
- Wealth issues: ‘patrimonialization’
  - Growing weight of unequally distributed wealth / labor income
- Tax & social reforms
  - Towards intergenerational “solidarity deals”
- Conclusion
- Complements
Aging & other historical changes (1980->)

- Population aging (beyond fertility drop in a number of countries)
  - Rise of life expectancy at old age since the end of the 70s (first in Japan)
- Slowdown of economic growth – against (median) labor income
  - Since thirty ‘jinxed’ years (1978-2007) and the ‘Great Recession’ (2008),
  - After high past growth post WW2: Trente Glorieuses – The Glorious Thirty
- Growing weight of wealth in dev. societies: ‘patrimonialization’
  - After steady decline since 1914: WW1, WW2 & Trente Glorieuses
  - Piketty: ‘Capital is back’ with again increasing wealth inequalities
  - But rise of the Welfare state, now under pressure (pensions & health)
  - & older generations are more numerous and richer than before
    - More on this below
Other historical changes since 1980 (1)

Liberal turn of the 80s, more briefly

- Globalization of more & more financial capital (esp. since 1989)
  - Free movement of capital and commodities => capital tax emigration
  - International competition between social & fiscal norms & systems => danger of a race to the bottom of our ‘social models’
- New technologies (TIC & numerical rev.) & rising agglomeration
  - Information (80s), Internet/networks (90s), portables (00s), big data (10s)
  - Knowledge economy => demand of qualified human capital (women?)
  - Megacities => rise in land & housing rents
- Labor market: end of Fordism compromise => post-Fordism
  - Technological reasons: decline of Taylorism & wage-earner status
    - More autonomy given to the worker but assigned objectives to be fulfilled
  - Political reasons: globalization of financial capital
    - Decline of life employment, more ‘flexible’ human capital => retirement points system?
Other historical changes since 1980 (2)

- Labor market change => pending issue: worker’s protection
  - More old days to secure: social transfers, wealth & savings, or…

- … working longer (beyond negative incentives of pension systems => marginal actuarial fairness); what may allow a points system, but:
  - Real “choice” for whom: good & stable job, good health, sizeable savings? At what conditions (wage, security, working conditions)?
  - Danger of rising social inequalities

- Family changes & women role (rise in education & labor participation)
  - Crucial for the design of pension systems & gender issues
    - More working women helped financing the pension system, but now retired
  - But perhaps less relevant for intergenerational issues on transfers?
    - Most recent reforms aim at giving to new families (recomposed, homosexual…) the same possibilities of wealth transmission as to “traditional” families?
Intergenerational relationships: an ideological choice (1)

- Issue: conflict (‘war’), equity, or cooperation?
- Ideological choice => debates, no possible consensus…
  - … driven by the facts, only by the facts
  - Different values (e.g. efficiency vs equity) & more: different views of the world, Weltanshauunugen, so that…
  - … any intergeneration discourse has an irreducible ideological substrate based upon metaphysical a priori / postulates that “resist” empirical facts
  + social & family relations between generations are **ambivalent**, as gifts for Mauss: *both* relations of sharing / solidarity & of domination / violence

1) **Conflict / war** benefitting older generations (greedy geezers)
- L. Kotlikoff: for decades, too high social transfers from the young to the old who “consume too much, contribute too little”… & also to the dead
- Which is detrimental to savings, productive investment, wages & growth
- Pessimism: ‘cancer’, ‘tumor’, no inter altruism. Why giving to all the old?
  - Singapore ideal (each generation for itself). Selfish old workers leading unions, etc.
2) **Generational equity**: an ill-defined concept (owing to history)?

- **Time**: cross-sectional comparisons (parity between workers & retirees) or longitudinal comparisons (at the same age but different dates)?
- **History**: how to define a *just* reference situation between *distant* cohorts with too different historical experiences? => Solutions:

  - **Restricted generational equity**: each generation for itself
    - Actuarially fair social balance sheets over the life-cycle => just reference situation = market income…
    - **Notional accounts**: pension depends of life expectancy in one’s cohort, hoping that generational equity could be fixed once for all => myth of autopilot steering &… what if health contributions were depending on life expectancy in bad health in one’s cohort?

  - **Approximations** as in E. Fornero: avoid a too large unbalance against young & future generations (*via* a ‘constitution’ protecting the latter)
    - Unbalance, not war. Better incentives, less distortions. Avoid too privileged old
    - Pitfalls: politics (short run & voting generations); economic changes (see above); demographic transition (see above)
Intergenerational relationships: an ideological choice (3)

3) Intergenerational solidarity: mutually advantageous cooperation

- **Longitudinal** chain of *indirect* reciprocities in LT cooperative equilibrium: Rawlsian generations behind the veil of ignorance
  - e.g. pensions: “do for previous generations what you would like – *mutatis mutandis* – next generations to do for you”
  - Appropriate beliefs (Hammond): chain = sovereign common good

- **Social compact** between OLG (Becker-Murphy, 1988; Rangel, 2003)
  - Giving adequate pension & care to the previous generation (indirect reciprocity) and education to the next generation (direct reciprocity) is required to get yourself adequate pension & care

- But also **cross-sectional** present cooperation outside equilibrium
  - Case of population aging & slowdown of growth
  - Rights but also *duties* of the old: callback functions => when needed, efforts must be *shared* between generations
Political economy of generations: a (French) sketch

First baby-boomers BB+, age 20 before 1980 (born 1943-1957)

- Soon all in retirement. According to their selfish interest, should want to:
  - maintain the current (generous) social system for them & the (relative) purchasing power of their pensions: simple & mobilizing claim…
  - with, if needed, a harder social system for the next generations to secure financial sustainability! => retirement: a unique points system welcomed?

- But parental altruism, care for next generations… & also the fear that the young refuse to cooperate: reluctant to reforms = expected loss for them

Younger generations understand population aging but…

- less that life expectancy is supposed to rise for younger cohorts, so that they will have to work longer than their elders for a comparable pension
- or, if not, will receive a lower pension ‘compensated’ (?) by a longer duration of retirement => actuarial fairness is a difficult concept

Pension reform: grandfathering vs intergenerational solidarity

- What happen to already retired & their ‘acquired rights’

French campaign of 2012: 52% of the voters were above age 50
Social issues: towards a unique European model?

- European social model (a European retirement points system?)
  - Socialization of risks: protection // Aversion to inequality: redistribution // Investment in human capital (education / health / training): active social spending
  - But national models = erratic products of ≠ history & politics and…

- … inspired by 3 rival social philosophies (Locke-Rousseau-Hobbes)
  - Free agent: Markets, freedom; individual autonomy & responsibility
  - Equal citizenship: State; equality (ex-post); ‘universal’ citizenship
  - Multi-solidarist: Family-civil solidarities; fraternity; reciprocal links

- Choosing (again) within an ‘ideological triangle’, knowing that…
  - … poles of the triangle (pure philosophy) are forbidden: we would be very unhappy or even, for most of us, unable to live in such societies
  - e.g., favor individual freedom-responsibility, while still giving some weight to equality & solidarity, but always biased compromise (Masson, 2015)
    - See complements
3 competing philosophies of the welfare state (WS)

- **Free agent: minimal WS, priority to the young**
  - Low basic safety net. Defined contribution pension funds with maximum freedom of choice
  - People mainly responsible for their old days through long-term saving

- **Equal citizenship: large WS, individual basis, priority to the young**
  - Notional accounts (or points systems?), high non-contributory base
  - Restricted family care: public pension + direct services to the elderly
    - Wealth as a complement only for the rich

- **Multi-solidarist: large WS, family basis, priority to parents & the old**
  - Defined contribution social insurance: mixed system of redistribution & insurance, focusing on the replacement rate
  - Anti-market views: rely on family & social links (at the state & intermediate levels)
    - Even for well-off people (?)
Different social & intergenerational views

- L. Kotlikoff: more free agent & intergenerational war
- E. Fornero: more equal citizenship & intergenerational equity or at least rebalancing

I will advocate intergenerational ‘solidarity deals’ (see below): more multi-solidarist & intergenerational cooperation

& I will concentrate also on wealth issues & inequalities
  - Wealth inequalities at old age more than about deferred consumption: multi-protection, independence of choices, up to Rawlsian primary goods
  - Wealth used at a social level for contributing more to our Welfare States

Note that wealth is a stock with a long, historical memory
  - Past growth but no more growth => elder generations privileged!
  - See Piketty: capital is back owing to rising $r - g$ ($g$ lower) & wealth concentration rises since the rate of return $r$ rises with the size of wealth
Projections of the French pension system (example)

- For France, OECD-COR projections are rather reassuring...
  - The ratio pensions/GDP would slightly decline in 2035 (under 14%), **but**
  - Macroeconomic scenarios (growth, unemployment) are optimistic
  - The average age at retirement is supposed to increase by 4 years
  - The relative purchasing power of the retirees (ratio of average pension to average wage) would decrease by 20 to 25% at least…

- Radical changes to come… **without any new reforms!**
  - Projections unfavorable to future retirees, with lower replacement rates; & **French exceptions** in Europe would be reduced:
  - High pensions to GDP ratio: 4.7% more than reference group average
    - Germany, Austria, Sweden, Finland, Belgian, Netherland, Denmark, United Kingdom
  - Low average age of actual exit from the labor market (men, 2014, OECD)
    - 59 in France; 60 in Belgian; ≈ 63 in Germany & Netherland; above 65 in Sweden
  - High relative purchasing power of retirees (65+/total, 2014, OECD)
    - 102% in France; 90% in Austria; 87% in Germany; < 80% in Belgian (?) & Denmark
Historical recovery of the risk of longevity: solidarity?

- Up to 1980 or so, the risk of longevity – i.e. to become old & destitute – declined with the rise of the WS for the old
- The rise of life expectancy at old age & the slowdown of economic growth (against wages) makes this risk rise again
  - More old days to secure & the rising risk of long-term care needs…
    - … whose costs follow wages (not inflation), may be very large & are not very well insured, especially in nursing homes
  - Future pensions (& health insurance) are more uncertain due to the problematic financial sustainability of the WS
  - Family care is more problematic owing to the increasing geographic distance from children (& new individualist norms of the latter)
- This can only raise in younger generations (rightly or wrongly) the desire of **homeownership** (making housing prices rise)
  - For long-term precautionary needs: “at least, we have a roof”
Wealth issues: (French) ‘patrimonialization’ since 1980

1. Rising wealth-income ratio to unknown levels since 1914
   - But due in part to (latent) capital gains on housing (complement, graph 1)
   + & rising wealth concentration (top 1%, 0.1%) after… (graph 2)
     - a continuous decline since 1914 – but growth of social security wealth

2. Rising concentration of wealth in the hands of the elderly
   - Relative wealth of the elderly (60+) increases (graph 3)
     - Insee: rate of homeownership, (gross/net) median or mean total or financial wealth…
   - Saving = low risk store of value (kept from age 60 to 90)…
     - 60+ households: cash-liquid savings, life insurance & housing;
       but no more than average direct or indirect stockholding rate
   - … due in part to the rise of the risk of longevity?
     - Seniors’ “unproductive over-accumulation”
       - one becomes rich (most often) when becoming old?
     - France quite representative (in the euro zone) for 1 & 2
       - For 2, see HFCS (Household Finance and Consumption Survey) data 2010 & 2014
Wealth issues: (French) ‘patrimonialization’ since 1980

3. Inheritance is back but received much later, at 60 on average
   ▪ in full property, due to longevity rise + higher rights of surviving spouse
   ▪ Since 1980, annual flow of bequests B has doubled / income (graph 4)…
   ▪ … and has grown 20% / wealth A (graph 5)
      ▪ whereas B/A has decrease in the US over the period from 1989 to 2007 (Wolff-Gittleman, 2011) owing to the very rapid rise in new accumulation

   Changes in B/A are a good indicator of changes in h, the share of ‘inherited wealth’ in total wealth accumulation (Masson, 2015)

4. Children (more) constrained in their wealth projects
   ▪ Such as home purchase, starting up a business, saving for retirement
   ▪ Early *inter-vivos* transfers ease plans to buy housing, start up a business
      ▪ Arrondel-Garbinti-Masson (2014): probability to become self-employed increases by 50% for gift recipients, but does not depend on parental financial help or inheritance

   So, increase circulation of wealth down to younger generations by giving tax advantages to *inter-vivos* family gifts?

   ➢ But gifts are a luxury good, *i.e.* highly concentrated among the rich (with the exception of farmers & small self-employed who make small gifts)
A new and unfavorable wealth situation (in France)

- That is quantitatively very important
  - Flow of bequests: 10% of GDP today, 5% in 1980

- A novel situation, esp. if compared to the 1950s-1960s when:
  - Limited weight of inheritance received at an average age of 40 // More limited wealth inequalities // Sizeable economic growth // Limited liquidity constraints against accumulation of the young: home purchase thus required a limited budget with favorable borrowing conditions (inflation)

- Similar current situation elsewhere (at least in the Eurozone)
  - 2010-2014 HFCS: diverse national situations; France by far the nearest to the Eurozone averages (mean-median wealth, inequality, composition)

- Urgent need to remedy an unfavorable wealth situation:
  - Economic growth: mass of inert wealth owned by elderly rentiers
  - Equity = unequal life opportunities between ‘heirs’ and ‘non heirs’, when success or well-being depends more on wealth, less on labor income
  - Intergenerational inequity or unbalance to the detriment of the young
Tax & social reforms: different options

- Redistribution: simply take from the rich (in income or wealth)
  - Ability to pay principle
  - Piketty: progressive taxation both on total income, on total (net) capital stock, & on wealth transfers => rich are heavily targeted!
    - Objections: capital is mobile (emigration tax) & heterogeneous (rate of return, origin…)

- Tax incentives – for ‘good’ choices against ‘bad’ choices
  - Pb: efficient only if strong tax differentials => ‘bad’ choices heavily taxed
  - e.g.: tax more ‘immovable’ housing property & also liquid, risk free saving in order to favor long-term & more risky households’ financial investment
    - A quite popular view today, but raises many problems?

- Reinforce social & family links of intergenerational cooperation
  - Solidarity deals: trading a penalty (e.g. tax hikes) against compensations while reinforcing private / public (intra- &) intergenerational solidarity
    - Issue: is it wise to bet so much on intergenerational solidarity?
Solidarity deal 1
Indexation policies between ages or generations

- Macro level: link public expenses for ‘retirement’ & ‘education’
  - The two types of programs (for the old & the young) should be decided together in the public budget (Rangel, 2003; Boldrin & Montes, 2005)
    - Concerning per capita transfers, but also their total volume (due to population aging): raise the issue of the definition of a retiree & of the normal age of retirement
  - Towards long-term balanced growth benefitting each generation?

- Micro level: solidarity mechanism between old rich & young poor
  - Above a certain floor, high pensions indexed on an indicator of success of unqualified young (indicator to be defined)
  - Not redistribution, but risk sharing…
    - … through a transparent, not manipulable & collective mechanism
  - Old rich directly “interested” in the success of young poor
    - If unskilled youth “successful”, high pensions will be preserved
Solidarity deal 2
(Seniors’) wealth contributing more to the social model

- Issue of financial sustainability & development of our social model (somewhat renovated) – a too labor-financed model
  - In line with a central message of Piketty’s book but different framing
  - Wealth held by the elderly would help the building of a retirement or a social fund
  - Or the 3rd age (after retirement) could contribute to the financing of 4th age needs: long-term care insurance following a ‘Bismarckian’ pattern
  - Contributions based on various incomes but also on the stock of wealth
  - Unproductive overaccumulation of seniors somewhat reduced by the contributions collected, the incentive to gift giving & the reduction of precautionary needs at old age

- Solidarity deal for middle & upper classes:
  - Their retirement life would be a bit more difficult (being more taxed, working longer) but would be secured (with adequate replacement rates)
Solidarity deal 3  The *Taxfinh* program (1)

- *Taxfinh*: two inseparable components  (Arrondel & Masson, 2016)

1)  Tax more (progressively) family inheritance on death
   - Excluding *inter vivos* transfers & charitable bequests
     => disincentive to *post-mortem* bequests to one’s offspring
   - Progressive tax: top 10-15% families (2/3 total wealth) who can make gifts

2)  Multiply & facilitate ways to sidestep this ‘inheritance surtax’: give, consume or invest wealth sufficiently early before death
   - Give (sufficiently early) to children: “reserve” maintained
   - Charitable gifts / bequests: more freedom to bequeath outside the family
   - Gift of family business: more freedom to bequeath (in or out the family)
   - Run down or consume (net, housing) wealth at retirement
     - New forms of reverse mortgage (only when dependent) & ‘viager’ (buyer = institution)
   - Invest in long-term risky assets: tax exemption if asset kept in the family for a long period (25 years?) by parents or beneficiary children
     - In dedicated funds run by long-term responsible investors
The *Taxfinh* program (2)

- Gradual & **credible** implementation (transition period)
  - At 90 years old, there is no way to adapt to the *Taxfinh* reform
  - But the program will have an **immediate** impact on first Baby-boomers, encouraged to prepare the transfer of their property soon enough

- A win-win program
  - Either, wealthy families react to tax incentives in the desired direction
  - Or, if not, additional tax revenue

- *Taxfinh* far superior to a standard inheritance tax
  - Gives ‘good’ incentives to families in order to sidestep the surtax; ways & incentives that reduce fiscal distortions, including **fiscal emigration**
  - Responds to many objections: e.g. virtue tax or (sudden) death tax
    - Impacts wealth (behavior) quite early before death // gift of family business: less taxed
  - More popular, since **fairer**: the surtax would be only paid by those who “deserve” it – being too short-sighted, or family- or socially-“selfish” =>
The *Taxfinh* program (3)

- But *Taxfinh* first a **remedy to a new wealth situation** generating…
  - lack of growth, unequal life opportunities, intergenerational unbalance
  - If the situation was like that of the 1950s or 1960s, the *Taxfinh* reform would not be that necessary

- Possible earmarking: additional tax revenue to finance either:
  - Long-term care insurance
  - Opportunity-enhancing programs for the young (universal capital at 18)

- Some caveats: resistance to an unpopular tax today
  - “Interfering with *inheritances* is tantamount to interfering with the *family*” but (liberal flavor): wealthy families are free to decide for themselves
  - Only gifts of full property should escape the surtax
  - Horizontal inequity: children from altruistic wealthy families advantaged
  - *Taxfinh* not that hard or radical, see Andrew Carnegie: “A man who dies rich dies disgraced”; in *Taxfinh*, his bequest will just be more taxed
Conclusions

- Population aging intertwined with other major changes (1980->)
  - Puts our social models under pressure (financial sustainability)
  - Has also produced a massive & damaging wealth situation
  - & created a worrying intergenerational imbalance

- To remedy such ill consequences I have proposed various (intergenerational) “solidarity deals”
  - Which suppose a cohesive society, that can count on the contribution of all its members, including the richest ones
  - & is able to carry out credible reforms over the long run
  - These conditions may appear wishful thinking. But otherwise…
  - … threats on our social model, seniors’ unproductive overaccumulation & the return of inheritance, reinforcing inter- & intra-generational inequalities
  - could well become major & durable features of our societies – like a screed of lead over our heads
Tensions between generations (France)

- Separating four historical adult generations
  - **Pre-baby-boom** (typically born before 1940), soon age 75+: dramatic childhood, Algerian war, ‘free lunch’
  - **First baby-boomers (BB+)**, age 20 before 1980 (born 1943-1957, say)
    - “4P”: Peace after 1962, Prosperity (Trente Glorieuses), belief in Progress, Plein emploi (full employment). *Soon all in retirement*
  - **Post BB+** (born 1958-1982 or 1985), working (now insiders)
    - Reconciling work & family life, home mortgage reimbursements
  - **Young generations**, above age 18
    - End of education & training, difficult professional integration

- Tensions: high public & social debts left by older generations
  - BB+ & elders: good wages, low unemployment, limited social contributions & good pensions; easy home purchase with capital gains
  - Younger generations: lower wages, high unemployment, high social contributions & more limited pensions; more costly home purchase
Basic limits of the 3 social philosophies (1)

- Pure forms of each philosophy are inacceptable

- Free agent: everyone is the CEO of his own economic life…
  - Rational & autonomous (an island of sovereignty): an impossible “ideal”
    - A Welfare State would then not be needed
    - If one not able (or fond) of becoming the CEO… social exclusion?
  - Mobile & adaptable, no emotions, just forward-looking, no roots
  - Moral & responsible: danger of plutocracy or pleonexia

- Equal citizenship: everyone is a (full) “citizen”, but what else?
  - National solidarity between isolated individuals is insufficient
    - Too expensive & inefficient: introduce local, social, family & other links
  - Every one is a citizen, but with no other distinction, social status or links
  - Utopia of an homogeneous – consensual – society (soft collectivization?)
Multi-solidarity: everyone is dependent on others

- Favors irresponsibility, moral hazard, laxness:
  - We are in the same boat, pursue a collective goal, but this dependence…
  - undermines the effectiveness of individual incentive mechanisms
- Multiple solidarity circles: overall consistency & articulation?
  - How to preserve the general interest (parochial effect)?
- Solidarities should be freely chosen & open => danger of “social relations” seeking, corporatism, communitarianism, string-pulling, etc.

Vicinity of poles of the ideological triangle is forbidden, but a complete, balanced compromise also
1. Net private wealth / national income ratios
Europe vs USA: 1900-2010 (Piketty, 2013)
2. Wealth inequality in Europe and the US 1810-2010 (Piketty, 2013)

Graphique 3a : L'inégalité patrimoniale: Europe et Etats-Unis 1810-2010

Lecture: jusqu'au milieu du 20e siècle, les inégalités patrimoniales étaient plus fortes en Europe qu'aux Etats-Unis.

Sources: Piketty (2013)
3. Median *relative* gross wealth by age

Source: Insee
4. Ratio of annual bequest flow to national income
Europe 1900-2010 (Piketty, 2013)

Graphique 4b. Le flux successoral en Europe 1900-2010


Sources: Piketty (2013)
5. Annual bequest flow / aggregate private wealth
France 1820-2008 (Piketty, 2013)

Graphique 4c. Flux successoral en France 1820-2010

Lecture: le flux de successions et donations représente chaque année 2,5% du patrimoine privé total en 2000-2010. Sources: Piketty (2013)
Unpopular taxation of wealth transfers (WT)
Coalition of the rich with (upper) middle classes having strong family values

- Over the last 40 years, **specific** growing aversion to the WT tax:
  - Declining revenue of WT tax (as a % of total tax receipts or GDP) 0
  - Many countries have suppressed WT tax since 1972 (Canada), esp. in the 2000s: Sweden, Austria, Portugal, Italy
  - **Not** the same decline for lifetime wealth or capital taxation
    - Ratios are higher in 2007 than in 1995 (even in the US!), owing to rising tax base

➢ Why has the lobbying of the rich been **so** successful for WT tax?
  - Wealth is more a sign of ‘success’, no matter its origin (Beckert, 2012)
  - Rising family values: family = more & more a safe haven against...
    - … declining economic growth, waning trust in the Welfare State & vagaries of globalized markets + aversion to taxation of family home (& business)
  - International competition, fear of tax emigration (Sweden)?

- 2 other basic puzzles
  - Why is the tax also unpopular among people expecting to leave few bequests?
  - Why do richer people do not use more *inter vivos* giving to reduce the WT tax?
Wealth transfers tax: wrong options

As remedies to an inefficient & unequitable wealth situation

- **Reduce the tax on family gifts is not the solution**
  - Good for growth & wealth mobility (positive responses to tax advantages of gifts relative to post-mortem transfers)
  - Gifts are more often motivated by altruism
  - But deadweight effects (Sarkozy reform in 2007); anti-redistributive (gift = luxury good); reduced tax revenue

- **An across-the-board increase in the WT tax is not the solution**
  - Good for more equal life chances only. Inefficient, especially when gifts are further penalized (Hollande reform in 2012)
  - Too unpopular and too contrary to family values: virtue tax; (sudden) death tax; tax on family homes & business.
  - Disincentives effects
  - & comes too late for highly uncertain rates of return to wealth over the long run