

From person to person: Studies of nongovernmental transfers

The explosive growth of government transfers has been recognized by all—in 1981, public expenditures on income transfers alone are estimated to have reached perhaps \$300 billion, equal to 10 percent of gross national product—but their effects have been disputed by many.

There is, however, another type of transfer; namely, private transfer—the giving of aid and funds by one person (family) directly to another person (family). Private transfer has been the subject of recent work by several Institute affiliates: Martin David and Paul Menchik, who look at the transmission of wealth from parents to children, and Robert Lampman and Timothy Smeeding, who look at transfers from family to family as alternatives to government transfers (see box, p. 10).

From one generation to the next

The David and Menchik research has two components: first, patterns of bequests to children, a subject with important bearing on the transmission of equality or inequality from one generation to another; and second, the effect of parents' social security income both on their own savings and on the amount of money they bequeath at death. The second issue is more complex in terms of statistical analysis, and has been the subject of argument for several years.

Less saved, or more bestowed?

The controversy over the effect of social security on private savings features at least two opposing sides; the findings of David and Menchik substantiate neither. One side contends that public old age insurance reduces savings because it “forces” transfers from the working generation to the retired generation, and workers consequently save less because their social security taxes assure both them and their parents an old-age income. In other words, government transfers replace private savings, which reduces the nation's capital stock, which in turn depresses the country's economic growth rate.

But, contends another side, that argument overlooks other incentives to save: for example, parents may wish to leave their children a compensation for the taxes that the younger generation must pay into the system. Moreover, since social security has apparently reduced the number of retired people who live with their children, those children can now save more because they are relieved of the responsibility to support aged parents.

Empirical studies using aggregate time-series data on consumption expenditures since 1929 have not resolved the argument. A summary of the results of those studies and others, many of them at odds with one another, can be found in the summary review of the literature on transfer programs by Institute affiliates Sheldon Danziger, Robert Haveman, and Robert Plotnick (*Focus*, 5:1, 1981; IRP Reprint no. 429).

In place of aggregate data from time series, David and Menchik focus on a small but reliable set of data; estate values reported in Wisconsin probate records, and earnings information on the same individuals from income tax records and social security earnings records. These figures have the advantage of being administratively determined, avoiding the problem of using self-reported (and usually underreported) dollar information, a problem that characterizes many other microdata sets.

David and Menchik wanted to see whether social security has displaced private savings, and whether receipt of social security income increases bequests. To do so, they focused on the “start-up” generation of social security recipients—the first generation that both paid into and took out of the system. They selected those born in the years 1890–1899, who were likely to have retired in the 1950s and 1960s and to have benefited from the large increases granted by the post-war amendments to the original Social Security Act. The sample was restricted to men, the primary earners among that particular generation. The final sample therefore included 531 Wisconsin men who were born in the decade 1890–1899 and who died in the years 1947–1978.

The two investigators estimated what the distribution of bequests by these men should look like in the *absence* of social security, given their earnings, other wealth, and age at death. They then compared these figures with what they actually observed, in the *presence* of social security. The end result of their series of regressions was that none of the social security variables exerted a statistically significant effect on the level of bequests. They also found that wealth of the men increased, rather than decreased, with age after 65, a result suggesting that people do not deplete their savings in retirement. (A parallel finding, that the elderly do not consume their savings and actually spend less on goods and services than the nonelderly, is featured in another Institute publication by Danziger and colleagues; see box, p. 10.)

David and Menchik's general conclusion is, therefore, that within the cohort they studied, the receipt of social security benefits did not affect bequests: "One cannot distinguish between the bequeathing behavior of beneficiaries of the social insurance system and the behavior of persons who were ineligible. One cannot distinguish a response of those who contributed heavily to their old age benefits from those who did not." And, contrary to a common supposition, when they retired, the men in this sample did not use up their assets.

Who bequeaths what to whom?

The same team of researchers studied household bequests to find out what kind of transfers take place between spouses and from parents to children. The subject is important because the transfer of wealth across generations strongly affects the income distribution (degree of inequality) of a nation and because other studies indicate that savings for bequests make up a considerable portion of total savings. Bequeathing also affects inequality to the extent that parents share their wealth equally or unequally among children. Parents may, for example, attenuate inequality by granting a larger share to a child with a lower earnings capacity than others, or may reinforce inequality by granting the largest share to the highest earner, or may be neutral toward inequality among their children by granting equal shares to all. It has been shown that wealth and income inequality are sensitive to this process.

In an earlier study (IRP Reprint no. 403; see box) Menchik found that in a sample of large estates probated in Connecticut, a substantial majority (70 percent) of parents divided their estates equally or nearly so among their children. In another study, in Cleveland (IRP Discussion Paper no. 684-82; see box), David and Menchik found a very large tendency toward equal estate division, larger even than in Menchik's Connecticut study. Hence they found no evidence that parents employ bequests either to attenuate or reinforce inequality *among* siblings.

Having thus documented the tendency toward equality of inheritance within the family, David and Menchik turned to Wisconsin data. They limited the study to once-married couples, to ensure that both parents had the same children, and they looked first at the amount bequeathed by one spouse to another, then at the bequest left by the surviving spouse. Their sample included 377 couples whose estates were probated in Wisconsin. Analysis of those records showed that few predeceasing spouses left a bequest to children, but most surviving spouses then left large bequests to the children. This supports the view that most intergenerational transfers travel in a roundabout fashion, first to spouse and then to children.

The investigators next examined the earnings record of a subsample of couples for whom earnings data for both husband and wife were available. Comparing the earnings record with the bequeathing behavior, they found that little of the interspousal transfer was consumed by those who

were high earners (in the top fifth of the earnings distribution) and, as earnings rose, so did the proportion of bequests to children as compared to bequests to others. Consequently the children of richer parents inherit proportionally more than children of poorer parents, a factor that reinforces the unequalizing effects of the "inheritance" of labor earnings.

The transfer system over time

The Lampman and Smeeding work concerns not just social security transfers, or private savings, or personal bequests, but the whole national transfer system as a method of redistributing income and wealth. They question the method by which the effect of transfers has been measured. Analysts have usually compared the presence of a government transfer with the absence of that transfer—the "zero-transfer counterfactual," comparing a unit's pretransfer income with posttransfer income. For example, they compare the situation of Person A, who is totally disabled and receives a government disability payment of \$100 a month, with his situation if he received no government aid. Lampman and Smeeding point out that before the advent of public disability assistance, Person A may well have been helped by Person B, his relative, perhaps (for hypothesis) to the same extent—a monthly payment of \$100. The emergence of government aid therefore had no effect on Person A, the primary beneficiary, but it helped Person B, the secondary beneficiary, considerably. He no longer pays out \$100 a month, and although he pays a higher income tax to help defray the cost of federal disability insurance, he is better off to the extent that his tax increase is less than his former support of A. "Nongovernment transfers existed before government transfers, and private transfers might have grown more if government transfers had grown less."

How much more and how much less, over the last 30 years? Or 50 years? The authors have amassed the available data, which at best are fragmentary, in an attempt to calculate the extent to which government transfers have replaced the direct giving of cash, food, and housing by one family to another. They explore as well the effect that this replacement may have exerted on the distribution of income, the level of work effort, and the level of personal savings.

In view of the data limitations, Lampman and Smeeding confine themselves to estimating changes in three types of transfers: assistance in cash, and in-kind assistance in the form of food and housing. Excluded are transfers to help people buy education and health care. To calculate the value of cash gifts by one family (defined as the nuclear unit: an individual, or married couple, or parents with children) to persons not in that family, they draw on average estimates compiled by the Bureau of Labor Statistics over the years. Regular cash transfers in the form of "support to others" (alimony and child support, old age support, etc.) are estimated from information available in

other works, including studies by James Morgan et al., F. G. Dickinson, and R. A. Schwartz¹ for certain years before 1970, and the Census Bureau's Current Population Reports for years after that date. In-kind benefits are calculated from firm figures for 1959² and estimations from them for the other years, taking into account the trend away from the extended family and toward smaller but more numerous household units.

The authors tabulate this array of figures and conclude, looking at comparisons over the years 1929 to 1979, that since 1950 government transfers measured as a percentage of personal income have increased by 2.5 times (from 4.5 to 11.2 percent of personal income), whereas comparable interfamily transfers declined only slightly, from 6 to 5 percent of personal income. Thus, over the past 30 years there has been a strong growth in government transfer and only a small decline in interfamily transfer. Interfamily transfers in 1935–1936 were twice as great as government transfers (which in those years were mostly veterans' benefits), and up to the mid-1950s remained still larger than government transfers. By 1979, however, the proportions had reversed: government transfer was then twice as great as interfamily transfer.

But what would have happened if there had been *no* increase in government social effort over those years? The authors suggest that because of the forces exerted in that period by increasing urbanization, increased family mobility, higher income, and the breakdown of the extended family into smaller units, private transfers might have grown to a level comparable to the government expenditures quoted at the beginning of this article.

Granting that this supposition of private transfer increase is unprovable, Lampman and Smeeding proceed with the assumption that government transfers are, to some degree at least, conversions of (substitutions for) interfamily transfers.

They next look at the overall effects of such conversion on the distribution of income, the level of work effort, and the extent of private savings—i.e., they compare the effects of government transfer not with the *absence* of such transfer, but with the effects of the private transfer that would have occurred without the government programs. Income distribution, they believe, has not been much affected: everyone's personal taxes have gone up, to help pay for public transfers, but Person B, to return to our illustration, no longer is supporting Person A. The overall effect is to narrow the variation both of benefits and of contributions because more regular government standards have replaced individual variation.

Similarly, conversion from personal to government transfer has probably not involved appreciable change in overall work effort: A's work effort has not changed, for he is still disabled, and B is unlikely to work less. Government transfers may, however, have induced less personal saving

because people are now more confident of being protected from misfortune and supported in retirement. This supposition differs from the findings of David and Menchik, but not to the extent that it might appear: Lampman and Smeeding are looking at a longer time span and a much larger population—the entire United States; and their main point is that they find less decrease in savings than do the estimates based on the zero-transfer counterfactual.

These three Institute studies explore the relationship between government policy and individual behavior. Indications are that whether or not social insurance programs have had a negative effect on the savings of individuals, parents continue to accumulate wealth in order to transfer it to their children. The loss of savings does not appear to be a serious one. Nor have government transfers had a significant effect on work effort or the distribution of income. What transfers may have done is to replace the private contributions that families have made for the well-being of other families. We have only begun to explore the advantages and disadvantages of substituting government programs for private assistance. ■

¹J. N. Morgan, M. David, W. Cohen, and H. Brazer, *Income and Wealth in the United States* (New York: McGraw-Hill, 1962); F. G. Dickinson, *The Changing Position of Philanthropy in the American Economy* (New York: Columbia University Press, 1970); R. A. Schwartz, "Personal Philanthropic Contributions," *Journal of Political Economy*, 78 (1970), 1264-1291.

²Morgan et al., *Income and Wealth*.

Selected papers

Sheldon Danziger, Jacques van der Gaag, Eugene Smolensky, and Michael Taussig. "The Life-Cycle Hypothesis and the Consumption Behavior of the Elderly." IRP Discussion Paper no. 697-82.

Martin David and Paul Menchik. "The Effect of Social Security on Lifetime Wealth Accumulation and Bequests." IRP Discussion Paper no. 671-81.

Martin David and Paul Menchik. "Modeling Household Bequests." IRP Discussion Paper no. 684-82.

Robert J. Lampman and Timothy M. Smeeding. "Interfamily Transfers as Alternatives to Government Transfers to Persons." IRP Discussion Paper no. 689-82.

Paul Menchik. "Primogeniture, Equal Sharing, and the U.S. Distribution of Wealth." IRP Reprint no. 403.
