

Equity and redistribution of income and wealth

A2

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Read first: [Addressing income and wealth inequality](#), [Efficiency and market failure](#)

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What you need to know

This topic has five learning outcomes:

1. **Equity and equality:** equality means equal shares (of income, wealth or opportunity); equity means fairness. Know the difference and why a fair outcome need not be an equal one.
2. **Equity and efficiency:** efficiency is about getting the most out of scarce resources; equity is about who gets the results. Know why an efficient economy can still be unfair, and why policies that make it fairer can cost some efficiency.
3. **Absolute and relative poverty:** absolute poverty is too little income to buy the basic necessities of life; relative poverty is income far below what is normal in that society.
4. **The poverty trap:** why a low-paid worker can gain little, or even lose, from earning more, when income tax rises and means-tested benefits are withdrawn at the same time.
5. **Policies towards equity and equality**, including **negative income tax**, **universal benefits** and **means-tested benefits**, and **universal basic income**: how each works and its strengths and weaknesses.

Exam questions on this topic also ask you to read and explain the **Gini coefficient** and the **Lorenz curve**, to judge whether a policy narrowed the gap. These come from AS topic 3.3 and A Level topic 11.4 (*Characteristics of countries at different levels of development*), not from 8.2 itself, so they are revised briefly here as a tool. Wages, trade unions and the minimum wage in labour markets are topic 8.3; progressive taxes, transfer payments and state provision were introduced in AS topic 3.3.

Understand it

Equality and equity

Equality is a matter of measurement: are the shares the same? It can refer to:

- **equality of outcome:** everyone has the same income or wealth;
- **equality of opportunity:** everyone has the same chance, for example the same access to schooling, jobs and credit, whatever their sex, background or region.

Equity is a judgement of **fairness** or justice. It is **normative**: people disagree about what is fair, so it cannot be measured by one number. Economists separate two ideas:

- **Horizontal equity**: people in the same situation are treated the same. Two workers with the same income pay the same tax.
- **Vertical equity**: people in different situations are treated differently, in a way that reflects the difference. A richer person pays a higher share of income in tax; a household with a disabled member receives extra support.

Equal treatment is not always fair. If every household gets the same \$200 energy rebate, that is **equal**, but a rich household hardly notices it while a poor one can heat its home for a month. Scaling the rebate down as income rises is **unequal** treatment that many would call more **equitable**. Equal outcomes can be unfair too: someone who works twice the hours, or trains for years, may fairly expect to earn more.

Equity and efficiency

Efficiency means making the best use of scarce resources. An economy is **productively efficient** when goods are made at the lowest possible cost (it is on its production possibility curve) and **allocatively efficient** when it makes the mix of goods consumers value most (price equals marginal cost). When both hold, the economy is **Pareto optimal**: nobody can be made better off without someone else being made worse off.

Pareto optimality says nothing about **who** has what. An economy where one family owns almost everything can be Pareto optimal, because taking anything from that family makes it worse off. So efficiency does **not** guarantee equity. There are many efficient outcomes, some fair and some not, and choosing between them is a value judgement.

Redistribution often costs some efficiency (the **equity–efficiency trade-off**):

- higher taxes on income and profit reduce the reward for working, saving, investing and taking risks;
- benefits that are withdrawn as income rises discourage extra work (the poverty trap below);
- collecting taxes and checking claims uses resources (administration costs), and some taxpayers move or avoid tax.

But the two can also go together:

- poor families may not afford education or health care, so talent is wasted; spending that reaches them can raise productivity;
- a dollar is worth more to a poor household than to a rich one (diminishing marginal utility), so moving income from rich to poor can raise total welfare;
- poorer households spend a larger share of each extra dollar (a higher **marginal propensity to consume**), so a transfer from rich to poor raises spending.

So a government chooses how much efficiency to give up for how much more equity. Redistribution is easiest to justify when society values equality highly compared with efficiency.

Absolute and relative poverty

Absolute poverty means income too low to buy the necessities needed to stay alive and healthy: enough food, clean water, shelter, basic clothing. It is measured against a fixed line, for example the World Bank's international poverty line, an income per person per day. In principle the line does not move as the country gets richer.

Relative poverty means income well below the typical income in that society, so that people cannot take part in normal life there. It is measured against a line that moves with the average, usually a fraction of **median** household income (60% is a common choice; some countries use 50%).

The two can move in opposite directions. Suppose median income rises from \$40 000 to \$44 000 and the relative poverty line is 60% of the median, so it rises from \$24 000 to \$26 400. A household whose income rises from \$25 000 to \$26 000 is better off in real terms, yet it moves **into** relative poverty, because its income grew more slowly than the median. Rapid growth can cut absolute poverty while relative poverty rises.

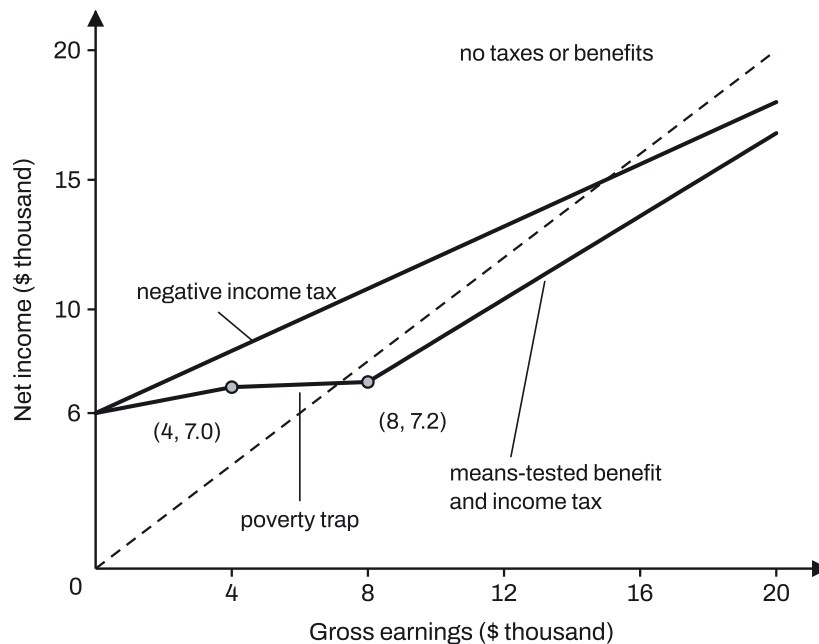
The poverty trap

A **means-tested benefit** is paid only to those whose income (and sometimes savings) is below a limit, and it is reduced as their income rises. That targets help well, but it creates a problem. When a low-paid worker earns an extra dollar:

- income tax (and any social insurance contribution) takes part of it;
- the benefit is cut by part of it as well.

Add the two together and you get the **effective marginal tax rate (EMTR)**: the share of each extra dollar earned that the worker loses. With a 20% income tax and a benefit withdrawn at 75 cents per extra dollar earned, the EMTR is $20\% + 75\% = 95\%$: the worker keeps 5 cents of each extra dollar. If the EMTR is 100% or more, working more makes the worker no better off, or even worse off.

That is the **poverty trap**: low earners have little incentive to work longer hours, take promotion or train for a better job, because almost all the gain is taken away, so they stay poor. (The **unemployment trap** is the related case where out-of-work benefits are close to, or above, what a low-paid job would pay after tax, so there is little gain from taking the job at all.)



In the diagram, a household with no earnings receives a means-tested benefit of \$6000. Income tax at 20% starts above \$4000 of earnings, and the benefit falls by 75 cents for each dollar earned until it runs out at \$8000. Net income at \$4000 of earnings is $4000 + (6000 - 3000) = 7000$. At \$8000 it is $8000 - 800 + 0 = 7200$. Doubling earnings from \$4000 to \$8000 adds only \$200 to net income: the flat stretch of the line is the trap.

The trap gets **worse** when more benefits are means-tested, when benefits are withdrawn faster, or when the tax-free allowance is cut (so tax starts at lower incomes). It **eases** when:

- the **tax-free allowance** (the income on which no income tax is paid) is raised, so low earners pay no tax on the extra income;
- benefits are withdrawn more slowly (a lower **taper rate**), or replaced with benefits that do not depend on income;
- a higher real **minimum wage** makes work pay more than benefits;
- tax and benefits are joined into one system with a single, moderate rate, as a negative income tax does.

Policies towards equity and equality

Universal benefits are paid to everyone in a group whatever their income: a pension for everyone over a certain age, a payment for every child, free school meals for every pupil.

- For: simple and cheap to run; everyone who qualifies receives it, so take-up is high; no stigma; they are not withdrawn as income rises, so they create no poverty trap.
- Against: very expensive, because the rich receive them too; poorly targeted, so each dollar does less to reduce poverty; higher taxes are needed to pay for them.

Means-tested benefits are paid only to those whose income is below a limit: housing support, in-work tax credits, food subsidies for low-income families.

- For: target help at those in need, so they reduce inequality more per dollar spent; cheaper for taxpayers.
- Against: high administration costs (every claim must be checked); some people entitled to them do not claim (stigma, complex forms), so low take-up; withdrawal as income rises causes the **poverty trap**; people just above the limit get nothing.

A **negative income tax (NIT)** joins the tax and benefit systems into one. There is a **threshold** income. Above it, people pay tax on the income above the threshold; below it, they **receive** a payment from the government, a fixed fraction of the shortfall below the threshold.

With a threshold of \$15 000 and a rate of 40%:

- a household earning nothing receives $0.4 \times 15\,000 = 6000$, its guaranteed minimum income;
- a household earning \$5000 receives $0.4 \times (15\,000 - 5000) = 4000$, so its net income is \$9000;
- a household earning \$25 000 pays $0.4 \times (25\,000 - 15\,000) = 4000$ in tax, keeping \$21 000.

Every extra dollar earned adds 60 cents to net income at every income level, so there is no poverty trap (the steady line in the diagram above). One system replaces many separate benefits, which saves administration, and nobody has to apply for help, so there is no stigma or low take-up. The drawbacks: a generous guaranteed minimum with a low rate costs a great deal; a rate high enough to pay for it reduces the incentive to work; and payments based on annual income respond slowly when someone's income suddenly falls.

A **universal basic income (UBI)** pays every adult the same regular sum, unconditionally: whether they work or not, whatever their income. It is a universal benefit paid to everyone, usually funded by higher income tax.

- For: no withdrawal as income rises, so no benefit-led poverty trap; very simple; no stigma; protects people in insecure or part-time work; improves **equality**, because the same sum is a bigger share of a poor person's income, and the higher taxes that fund it fall mainly on higher incomes.
- Against: enormously expensive; a guaranteed income lets some people work less, and the higher tax rates that fund it reduce the reward for working, so mark schemes treat a UBI as **reducing the incentive to work**; a flat sum ignores extra needs such as disability or housing costs, so it may be less equitable than targeted help unless kept alongside it.

Other redistribution tools

The rest of the tools from AS topic 3.3 come up in multiple choice here. Their effect on the distribution of income:

Change	Effect on income inequality
More progressive income tax (higher top rate, higher tax-free allowance)	Reduces it
Higher indirect taxes (sales tax, VAT), which are regressive	Widens it
Lower indirect taxes, especially on food and other necessities	Reduces it
More transfer payments or benefits in kind to low-income households	Reduces it

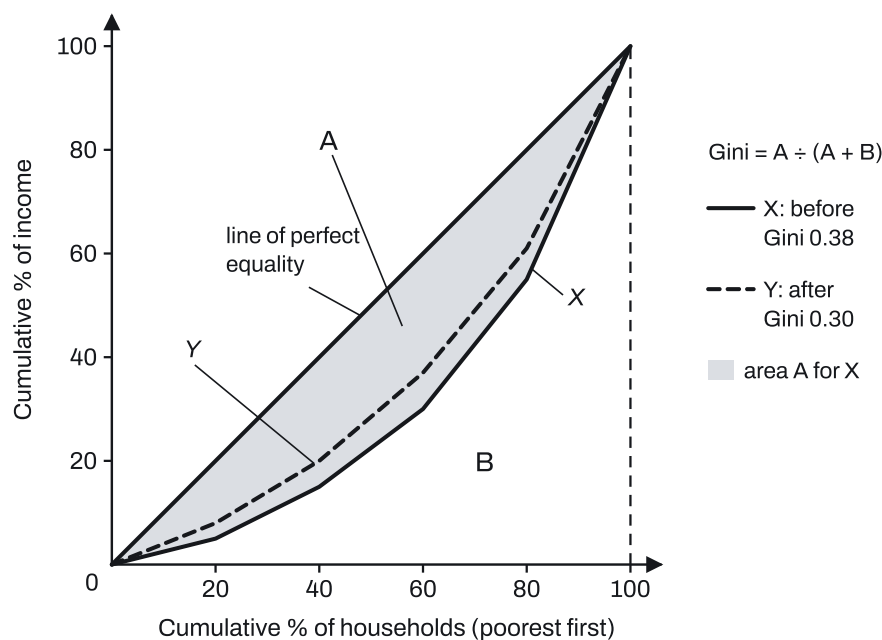
Change	Effect on income inequality
Means-tested benefits cut in real terms	Widens it
Higher real minimum wage, stronger trade unions	Reduces it, quickly, for those in work
More spending on education and training	Reduces it in the long run
Lower corporate tax or top income tax rate	Widens it
More discrimination in pay or hiring	Widens it

A tax is **progressive** if the share of income paid in tax rises as income rises, **regressive** if it falls, and **proportional** if it stays the same. Indirect taxes are regressive because poorer households spend a larger share of their income, so the same tax per item takes a larger share of their income.

Measuring the result: the Lorenz curve and Gini coefficient

(AS topic 3.3 and A Level topic 11.4, used in questions on this topic.)

A **Lorenz curve** plots the cumulative percentage of households, poorest first, on the horizontal axis against the cumulative percentage of income they receive on the vertical axis. If every household had the same income, the poorest 20% would get 20% of income, the poorest 40% would get 40%, and so on: the 45° **line of perfect equality**. A real distribution sags below it. The further it sags, the more unequal the distribution.



The **Gini coefficient** measures how far the curve sags:

$$Gini = \frac{A}{A + B},$$

where A is the area between the line of equality and the Lorenz curve and B is the area below the curve. It runs from **0** (perfect equality: the curve is the diagonal, so $A = 0$) to **1** (perfect inequality: one household has all the income, so $B = 0$). It is often written as a percentage, 0 to 100.

The diagram is drawn from these shares of income for each fifth of households, poorest first:

	Poorest 20%	2nd	3rd	4th	Richest 20%	Gini
X: before taxes and benefits	5%	10%	15%	25%	45%	0.38
Y: after taxes and benefits	8%	12%	17%	24%	39%	0.30

Redistribution moved income from the top fifth to the bottom three, so the Lorenz curve moved **towards** the diagonal and the Gini coefficient **fell**. A policy that makes the curve sag further away raises the Gini coefficient. The Gini coefficient says nothing about how **rich** a country is, and two different Lorenz curves that cross can have the same Gini coefficient.

Key facts and formulas

There is no formula list in the 9708 exam, so everything here is "Learn it".

Formula	Status
Gini coefficient = $\frac{A}{A+B}$, from 0 (perfect equality) to 1 (perfect inequality); a rise means more inequality	Learn it
Effective marginal tax rate = marginal income tax rate + other deductions rate + benefit withdrawal rate	Learn it
Extra net income kept = extra gross earnings $\times (1 - \text{EMTR})$	Learn it
Negative income tax, income Y below threshold T : payment = $t \times (T - Y)$; above T : tax = $t \times (Y - T)$	Learn it
Disposable income = original (gross) income – direct taxes + cash benefits	Learn it
Final income = disposable income – indirect taxes + benefits in kind (free education, health care)	Learn it
Relative poverty line = chosen fraction (often 60% or 50%) $\times$ median income	Learn it
Progressive tax: share of income paid rises with income; regressive: falls; proportional: constant	Learn it

How to do it

We tagged 51 questions for this topic, from March 2021 to March 2026 (47 different; 4 are repeats across paper variants): 41 Paper 3 multiple choice and 10 Paper 4 data-response and essay questions. 6 Paper 4 questions mix more than one type, so the counts add up to 62.

Question type	Questions
Choose the policy or tax/benefit change that reduces (or widens) income inequality	13
Identify the poverty trap and what causes or eases it	11
Explain the Gini coefficient or Lorenz curve and link a change in it to policy	8
Weigh the strengths and weaknesses of a named redistribution policy	7
Evaluate whether a government policy or action increases equity or equality	7
Distinguish equity from equality	6
Interpret income, tax-and-benefit or inequality data	6
Distinguish absolute poverty from relative poverty	2
Explain the trade-off between equity and efficiency	2

1. Choose the policy or tax/benefit change that reduces (or widens) income inequality (13 questions)

All multiple choice.

1. Decide which way each change moves income: away from the rich (narrows the gap) or away from the poor (widens it). Use the table in "Understand it".
2. In a grid of increase/decrease columns, the answer that narrows the gap is usually: direct (income) tax **up** or more progressive, indirect tax **down**, benefits **up**. Reverse every column to widen it.
3. Check the time scale. "Short run" points to a policy that changes incomes now (a minimum wage, transfers); "long run" points to education and training, which raise the skills and earnings of the poor over years.

Variants:

- **"Least likely to redistribute"**: higher indirect taxes (regressive), or a minimum wage set **below** the market wage, which changes nothing.
- **Causes of rising inequality**: discrimination, a weaker minimum wage or weaker unions, cuts to benefits. Rising labour-market participation and better skills are not causes.
- **Relative poverty rising**: removing a minimum wage pushes the lowest pay further below the median.
- **"A new regressive tax"**: the only certain result is more tax revenue; it does not improve equality.

2. Identify the poverty trap and what causes or eases it (11 questions)

All multiple choice.

1. **Naming it:** a low earner who gains little or loses from earning more, because of income tax **plus** lost means-tested benefits, is in the **poverty trap**. Not the unemployment trap (that is about taking a job at all), not a liquidity trap (monetary policy), not a debt trap.
2. **Cause:** means-tested benefits, withdrawn as income rises. A household simply being below a poverty line, or spending more than it earns, or seeing its pay lag behind inflation, is **not** the trap.
3. **Combinations:** to **reduce** the trap, raise the tax-free allowance and raise the real minimum wage, or means-test a smaller share of benefits. To **worsen** it, cut the allowance and means-test more benefits.

Variant: "where is the trap least likely?" Pick the case that has nothing to do with losing income when earning more, such as unequal pay for the same job (discrimination).

3. Explain the Gini coefficient or Lorenz curve and link a change in it to policy (8 questions)

Written (3–5 marks):

1. Define it: a measure of how unequally income (or wealth) is distributed across a population. (1)
2. Give the range and meaning: 0 = perfect equality (1); 1 = perfect inequality (1).
3. If a diagram is asked for, draw the Lorenz curve accurately: both axes labelled as cumulative percentages (households, poorest first; income), the line of perfect equality, the curve below it, and areas *A* and *B* marked (up to 2). Give $Gini = A / (A + B)$ (1).

Multiple choice:

- Gini **rose**: policies that took from the poor or gave to the rich (lower corporate or top income taxes, higher sales taxes, benefits falling in real terms).
- Gini **fell** after a higher tax rate on top earners: the tax system became **more progressive**.
- Policies that would **fail** to lower the Gini: a more regressive income tax. Cutting a sales tax lowers it, because sales taxes are regressive.
- Shifting the Lorenz curve **towards** the diagonal: a higher top tax rate, free education, a higher minimum wage.

4. Weigh the strengths and weaknesses of a named redistribution policy (7 questions)

All multiple choice. Match each policy to its own pros and cons (see "Understand it"):

Policy	Typical strength	Typical weakness
Means-tested benefit	Targets those in need	High administration cost; poverty trap; people just outside the limit (or not working) get nothing

Policy	Typical strength	Typical weakness
Universal benefit	Low administration cost; full take-up	Expensive; poorly targeted
Negative income tax	Joins tax and benefits; no poverty trap; more equitable	Costly if generous; slow to react to sudden income falls
Universal basic income	Improves equality; simple	Reduces the incentive to work; very expensive

Variants:

- A pairing is wrong if the weakness doesn't belong to that policy (for example a universal benefit is not known for reducing labour mobility).
- **Means-testing one group to fund another** (for example older people who now have high incomes, to pay for younger adults): equality **between generations** rises.
- **Transfers from rich to poor**: the poor spend more of each dollar, so the economy's **marginal propensity to consume rises**.
- **Cutting income tax and means-tested benefits together**: the aim is incentives and **economic growth**, not equity.

5. Evaluate whether a government policy or action increases equity or equality (7 questions)

Paper 4 only: data-response parts of 3–8 marks and essays (25-mark questions with 12- and 13-mark parts in 2021–2022; 20 marks from 2023, Table A 14 and Table B 6).

1. **Define** equity (fairness) and equality (equal shares) at the start, and say which one the question asks about.
2. **For each policy, a chain**: what it is → who pays and who receives → how the gap between rich and poor (or the fairness of the outcome) changes. End each chain with an explicit **link to equality or equity**; the June 2024 report said this link was needed for each policy.
3. **The other side**: incentives, cost and opportunity cost, take-up, time lags, who really gains.
4. **Judgement**: does it increase equity, equality, both or neither, and under what conditions?

Two developed policies for a typical 8-mark "use one fiscal and one supply-side policy" part:

- **Fiscal: a more progressive income tax** (example) → higher earners pay a larger share of income, and the revenue can fund benefits or services used mostly by low-income households (development) → disposable incomes move closer together, so the Lorenz curve moves towards the diagonal (link to equality). Limit: high top rates may cause avoidance or emigration of skilled workers, which cuts revenue.
- **Supply-side: free or subsidised education and training** (example) → workers from poor households gain skills and productivity, so they can move into better-paid jobs (development) → their earnings rise towards the average and future inequality falls (link to equality). Limit: it takes years, and only works if the jobs exist.

Variants:

- **A price cut or tax cut on a necessity** (fuel, electricity, food): rich and poor both pay less, so in money terms it is not clear that **equality** improves. But the poor spend a bigger share of income on necessities, so their gain is larger relative to income, which supports **equity**.
- **Equity or equality between producers**: a policy that helps small firms buy inputs cheaply at a large firm's expense may make producers more equal; but a general tax cut can help the largest firm most, so the effect is uncertain. A price change on its own is not "fair" or "unfair" to producers unless it is linked to some idea of fairness.
- **"Fiscal policy alone"** (2021 essay): discuss taxes **and** government spending, then other tools (minimum wage, education, monetary policy) and conclude. In 2021 the top level (9–13 marks) needed a clear discussion of three policies, and 12 or 13 marks also needed a conclusion.
- **"An equitable solution" to a market failure** (March 2026 essay): judge each corrective policy for fairness as well as efficiency; for example an indirect tax on a polluting good is regressive and can cost jobs, while subsidies have to be paid for by taxpayers.

6. Distinguish equity from equality (6 questions)

Usually 2–3 marks, one for each definition plus one for developing either.

1. **Equality**: equal distribution of income, wealth or opportunity; can be measured. (1) Develop: equal treatment, or the same outcome for everyone. (1)
2. **Equity**: fairness or justice in how resources are shared; a value judgement. (1) Develop: horizontal and vertical equity, or a fair outcome may be unequal. (1)
3. If the article gives a context, apply it: who is treated fairly or unfairly?

Multiple-choice variant: an action that gives everyone the **same** thing (the same subsidy, the same payment) shows **equality**; an action that gives more to those in greater need, or charges more to those with more, shows **equity**.

7. Interpret income, tax-and-benefit or inequality data (6 questions)

1. **Calculations**: disposable income = gross – direct taxes + cash benefits. Indirect taxes are paid **out of** disposable income, so they come off only when you go on to final income.
2. **Before and after tables or bar charts**: first, for each group, compare original income with final income to see who **gains** (final above original) and who **loses** (final below original); an option such as "every group is better off except the highest earners" is tested this way. Then compare the gap (or the ratio) between rich and poor at each stage: if it narrows but does not close, inequality was **reduced, not removed**. Don't conclude that the system "favours" the rich just because they still end with more: what matters is the direction each group moved.
3. **Claim tests** ("does the table support the view that...?"): quote figures, look for countries that break the pattern, say that a link is not a cause, and point out what the data cannot show (for example a table of absolute poverty says nothing about relative poverty). The June 2024 mark scheme gave up to 2 marks for using the data.

4. **World or average figures versus single countries:** global inequality can fall while inequality inside some countries rises; both can be true.

8. Distinguish absolute poverty from relative poverty (2 questions)

3 marks:

1. Absolute poverty: not enough income to buy the necessities to sustain life (1), often measured by a poverty line of income per person per day, such as the World Bank's (1).
2. Relative poverty: income low compared with others in the same society, often below a set share of median income (1).

9. Explain the trade-off between equity and efficiency (2 questions)

1. Define productive efficiency, allocative efficiency and Pareto optimality.
2. Explain that Pareto optimality is about **resources**, not **fairness**: an efficient allocation can be very unequal, and redistribution is a value judgement.
3. Show the trade-off (taxes and benefit withdrawal blunt incentives, administration costs) **and** its limits (education spending raises productivity; diminishing marginal utility).
4. Conclude: efficiency does not by itself create equity. The November 2022 report said only the better candidates fully separated the two, and that was needed for the top level.

Multiple-choice variant: redistribution is most appropriate when **equality is valued more highly than efficiency**.

Worked examples

Example 1

A low-paid worker receives a pay rise of \$50 a week. On each extra dollar she pays income tax at 20% and a social insurance contribution of 10%, and her housing benefit is reduced by 55 cents.

How much better off is she each week?

A \$7.50 B \$15.00 C \$35.00 D \$42.50 [1]

EMTR = 20% + 10% + 55% = 85%, so she keeps $50 \times 0.15 = 7.50$, so **A** (1). C ignores the lost benefit (50×0.70), B is the tax and contribution alone, and D is what she loses. This is a poverty trap: she keeps less than a sixth of her rise.

Example 2

The table shows a year's income and payments for three households in a country, in dollars.

	Household L	Household M	Household H
Original income	10 000	40 000	100 000
Direct taxes paid	500	7 200	31 000
Cash benefits received	6 000	1 000	0
Indirect taxes paid	2 900	5 100	8 300
Benefits in kind received	5 000	4 000	2 500

(a) Calculate the disposable income of each household. [2]

(b) Using the data, explain whether direct taxes and indirect taxes are progressive or regressive. [3]

(c) Compare the ratio of H's income to L's income before and after all taxes and benefits, and comment. [2]

(a) Disposable income = original – direct taxes + cash benefits (1): L \$15 500, M \$33 800, H \$69 000 (1).

(b) Direct taxes take 5% of L's original income, 18% of M's and 31% of H's: the share rises with income, so they are **progressive** (1). Indirect taxes take $2900/15\,500 = 18.7\%$ of L's disposable income, 15.1% of M's and 12.0% of H's (1): the share falls as income rises, so they are **regressive** (1).

(c) Final incomes are L \$17 600, M \$32 700, H \$63 200. H's income is 10 times L's before taxes and benefits, and $63\,200/17\,600 = 3.6$ times after (1). The system greatly reduces inequality, but does not remove it (1).

Example 3

Extract: The country of Kestria pays a means-tested housing allowance to about 15% of households. The government proposes to replace it with a universal basic income (UBI) of \$250 a month for every adult, paid for by raising the basic rate of income tax from 20% to 27%.

(a) Distinguish between equity and equality. [3]

(b) Consider whether the proposal would make the distribution of income more equitable. [8]

(a) Equality means an equal distribution of income or wealth, or the same treatment for everyone (1). Equity means fairness or justice in how income is shared (1); it is a value judgement, so a fair outcome may be unequal, for example taxing those with more at a higher rate (1).

(b) *Model answer:*

- A UBI is the same sum for every adult, so it is a larger share of a poor adult's income than a rich one's, and it is funded by a higher income tax paid mostly by those who earn more: incomes move closer together (more equal). (1) This is vertical equity: those with higher incomes contribute more, and those with less gain a larger share of their income, which most people would judge fairer. (1)
- The housing allowance is withdrawn as income rises, so it causes a poverty trap; the UBI is never withdrawn, so low earners keep more of each extra dollar, which many would see as fairer. (1)

- Every adult receives it, with no forms and no stigma, so poor households who failed to claim the old allowance now get help. (1)
- **On the other hand**, the UBI goes to the 85% of households who did not need help, so much of the money does nothing for poverty. (1)
- \$250 is the same for a household with high rents as for one with low rents. Households who received a larger housing allowance than the UBI may end up worse off, which is not equitable. (1)
- A tax rise from 20% to 27% applies to low earners above the tax-free allowance as well, and it reduces the reward for work. (1)
- **Conclusion**: the UBI is more equal and removes the poverty trap, but it is less well targeted; it is more equitable only if \$250 at least matches what the poorest received before, or if extra support for housing costs is kept. (1)

Four marks on the "more equitable" side, three on the other and one for the justified conclusion make 8. A mark scheme of this kind allows at most 5 for one side, so a one-sided answer stops at 5.

Example 4

Assess whether a negative income tax would be a better way to reduce poverty than means-tested benefits. [20]

Model answer (paragraph plan):

1. **Definitions.** Absolute poverty (income too low for necessities) and relative poverty (income well below the median). Means-tested benefits: paid only below an income limit and withdrawn as income rises. Negative income tax: one system with a threshold; people below it receive a share of the shortfall, people above it pay tax. (AO1)
2. **How means-tested benefits reduce poverty.** Money goes only to low-income households, so each dollar of public spending raises the poorest incomes most; it can be aimed at particular needs such as housing or children. (AO2)
3. **Their weaknesses, as a chain.** Withdrawal plus income tax gives an EMTR that can exceed 90%, so low earners have little reason to work more, train or seek promotion: they stay in poverty (the poverty trap: the flat stretch of the means-tested line in the poverty-trap diagram). Checking claims is costly, and stigma or complex forms mean some entitled households never claim, so the poorest may get nothing. (AO2)
4. **How a negative income tax works.** It guarantees a minimum income (threshold $\times$ rate) to everyone, automatically, through the tax system. Each extra dollar earned adds the same share (one minus the rate) to net income at every level, so the poverty trap disappears and work always pays. Take-up is complete and administration is simpler. (AO2: *developed chain using the poverty-trap diagram.*)
5. **Evaluating the NIT.** A guaranteed minimum high enough to lift people out of absolute poverty, with a low rate, is very costly; a higher rate pays for it but cuts work incentives for everyone in the middle. A single payment cannot reflect different needs (disability, housing costs) as targeted benefits can. Payments based on annual income are slow to respond when someone loses a job. (AO3)

6. **Evaluating means-tested benefits.** Their poverty trap can be eased without scrapping them: a lower taper rate, a higher tax-free allowance, a higher minimum wage. Targeting keeps the cost down, which matters for a government with a large budget deficit. (AO3)
7. **Conclusion.** A negative income tax is better at reducing **relative** poverty among low earners in the long run, because it removes the trap and reaches everyone. Means-tested benefits may still be better at relieving **absolute** poverty quickly, and for groups with special needs, where targeting matters most. The best answer depends on what the government can afford: a NIT funded at a moderate rate, with a few targeted benefits kept for special needs, gets most of the gain. (AO3: *justified judgement on "better"*)

Table A Level 3 (14): accurate definitions, a diagram used in the argument and developed chains for both policies. Table B Level 2 (6): each policy is evaluated on both sides and the conclusion says which is better under what conditions. **20/20**.

Common mistakes

- **Writing "equal" for equity.** The March 2021 report said many candidates explained equality well but did not explain the **fairness** in equity, repeating "equal distribution" instead. The June 2024 report again found candidates confusing equality with equity.
- **Reversing 0 and 1 on the Gini coefficient.** In June 2024 a number of candidates confused what 0 and 1 represent. 0 is perfect equality; a **rise** means **more** inequality.
- **Not knowing what the poverty trap is.** In June 2024 more than a fifth of candidates chose each of the three wrong answers to a question on its cause. It is about **losing benefits (and paying tax) as income rises**, not about being below a poverty line or overspending.
- **Taking indirect taxes off when finding disposable income.** In March 2023 only 40% of candidates got a disposable income calculation right; 35% chose the answer reached by subtracting sales tax as well as income tax and ignoring the cash benefits. Disposable income is gross income minus direct taxes plus cash benefits.
- **Agreeing with a claim the data don't support.** In June 2024 many said a table showed that greater inequality was linked to poor female literacy and more poverty, when it showed no such link and nothing about relative poverty. Test the claim against every row.
- **Leaving out the link to equality.** In June 2024 a policy example with development still needed an explicit link to a more equal distribution of income.
- **Merging equity with efficiency.** In November 2022 marks were lost because answers did not fully separate the two; the top level needed it.
- **Ignoring the word "equitable".** In March 2026 many answers on an equitable solution to market failure discussed only efficiency, and so could not reach a relevant conclusion.

How to get the marks

- **Multiple choice:** decide first who gains and who loses. Indirect taxes are regressive; a higher tax-free allowance and less means-testing ease the poverty trap; a Gini **fall** means more equality.

- **Definitions** earn the first marks in almost every written part: equity (fairness, a value judgement), equality (equal shares), absolute and relative poverty, the poverty trap (tax plus benefit withdrawal), the Gini coefficient (0 to 1).
- **"Distinguish"** needs both terms defined and the difference made clear. One sentence each is not enough for 3 marks: develop one of them.
- **"Explain, with the help of a diagram"**: the Lorenz curve must have both axes labelled as cumulative percentages, the line of perfect equality, and the areas you use in the Gini formula.
- **Data parts**: quote figures, compare, and say what the data **cannot** show. Use only the information given when the question says "from the evidence" or "with reference to the article".
- **8-mark "consider" and "assess" parts** are point-marked: each relevant point and each development earns a mark, but schemes often cap one side (for example "up to 5 for one side"), so a one-sided answer cannot reach 8. Finish with a short judgement.
- **Essays** (Table A 14, Table B 6 since 2023; levels for 12- and 13-mark parts in 2021–2022): developed chains of reasoning, both sides, and a conclusion that answers the exact wording ("better", "alone", "to what extent"). In 2021 the top level for "fiscal policy alone" needed three policies, with a conclusion for 12 or 13 marks.
- **Answer the word asked**: equity is not equality; absolute poverty is not relative poverty; "short run" and "long run" point to different policies.

Quick check

1. Which policy is an example of vertical equity? **A** every pensioner receives the same state pension **B** an income tax whose rate rises as income rises **C** all passengers pay the same bus fare **D** a tax of 15% on all incomes
2. In a country the relative poverty line is 50% of median household income. Median income rises from \$30 000 to \$34 000. A household's income is \$14 000 in the first year. By what percentage must its income rise for it to reach the relative poverty line in the second year?
3. Under a negative income tax the threshold is \$18 000 and the rate is 30%. Find the net income of a household that earns \$6000, and how much of an extra \$1000 of earnings it keeps.
4. On a Lorenz diagram, the area between the line of perfect equality and the Lorenz curve is 0.14, and the whole triangle under the line of equality is 0.5. Find the Gini coefficient. After new policies the area falls to 0.11. Find the new Gini coefficient and say what has happened to inequality.
5. Explain how raising the income tax-free allowance could reduce the poverty trap, and give one limitation of the policy. **[4]**

Answers

1. **B.** It treats people with higher incomes differently, taking a larger share from them. A, C and D treat everyone the same (equality of treatment, or horizontal equity). (1)
2. The new line is $0.5 \times 34\,000 = 17\,000$. The household needs $17\,000/14\,000 = 1.214$, a rise of 21.4%.
3. It receives $0.3 \times (18\,000 - 6000) = 3600$, so its net income is \$9600. An extra \$1000 cuts the payment by \$300, so it keeps \$700.
4. $\text{Gini} = 0.14/0.5 = 0.28$. Afterwards, $0.11/0.5 = 0.22$. The curve has moved towards the line of equality, so inequality has fallen.
5. Low earners would pay no income tax on more of their income (1), so the effective marginal tax rate on extra earnings falls and they keep more of each extra dollar (1), which increases the incentive to work longer or seek promotion (1). Limitation: it does nothing for people whose income is already below the allowance, and it also cuts tax for higher earners, so it is costly (1).

Past questions to try

- [9708/31/O/N/23 Q15](#): matching a redistribution policy to its advantage and disadvantage.
- [9708/32/F/M/23 Q16](#): calculating disposable income for a group of earners.
- [9708/32/F/M/21 Q20](#): which policies shift a Lorenz curve towards equality.
- [9708/43/O/N/22 Q2](#): a 13-mark essay on whether Pareto optimality creates a more equitable society.