

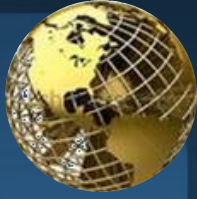
Test Yourself: Income, Transfers and Taxes



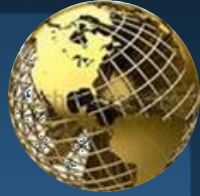
"I wish it need not have happened in my time," said Frodo.

"So do I," said Gandalf, "and so do all who live to see such times. But that is not for them to decide. All we have to decide is what to do with the time that is given us."

JRR Tolkien



What is income?

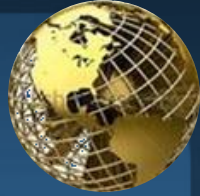


There are several ways to measure income.

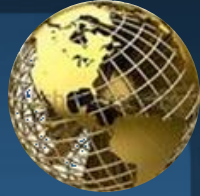
Personal income (PI) is income received by households before payment of personal taxes. Personal income is not a complete measure of income.

In-kind income refers to goods and services received directly, without payment in a market transaction.

Wealth is the market value of assets. Wealth represents a stock of potential purchasing power.

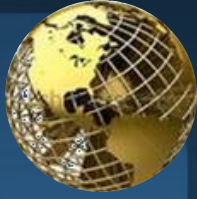


What do we mean by the size
distribution of income?

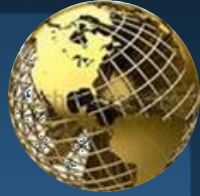


The **size distribution of income** is the way total personal income is divided up among households or income classes.

Income share is the proportion of total income received by a particular group.

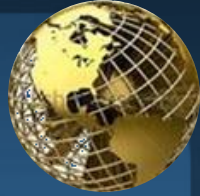


What has led to the concentration of income and wealth in recent decades?

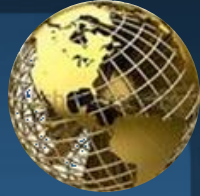


Reasons for the concentration of income and wealth in recent decades include:

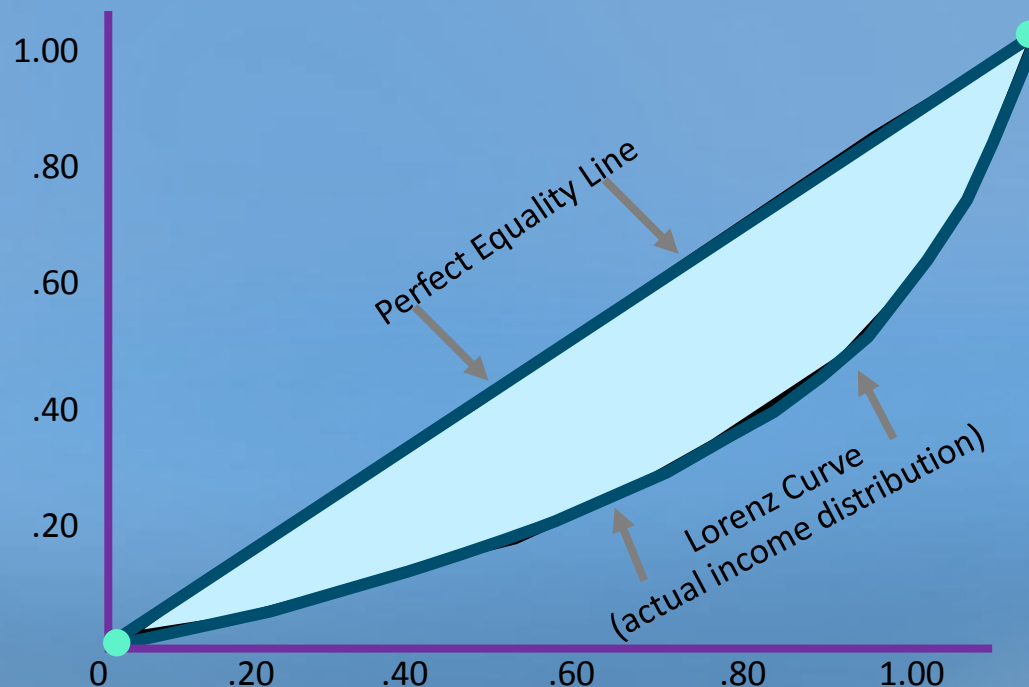
- the trend of making taxes less progressive since the 1970s
- a changing job market that has forced many blue collar workers to compete with cheaper labor abroad
- a lack of saving by the middle class due to stagnant wage growth

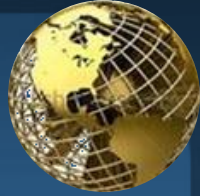


What is a Lorenz Curve?

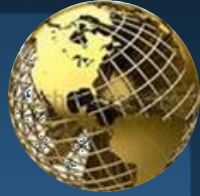


A **Lorenz Curve** is a graph of the actual cumulative distribution of income compared to a perfectly equal cumulative distribution of income (perfect equality line).



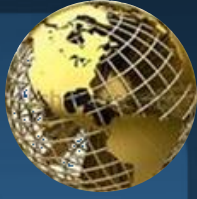


What does the
Lorenz Curve show?

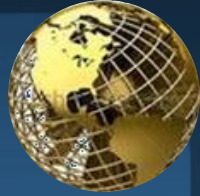


On a Lorenz Curve graph, a straight diagonal line represents perfect equality of wealth distribution. The Lorenz Curve lies beneath it, showing the reality of wealth distribution.

The value of the curve corresponds to a percentile of the population ordered according to wealth. The value of the curve represents that portion of the total value of wealth held. So, the value (0.7, 0.3) means that the bottom 70% of the population owns 30% of the total wealth in that society.



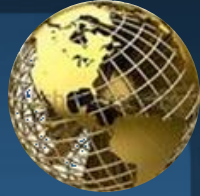
What is poverty?



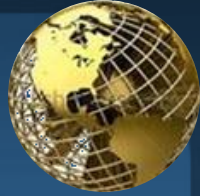
Poverty can be defined in absolute terms or in relative terms.

absolute terms – a dollar figure that represents some level of income per year that is required to purchase some minimum amount of goods and services to meet basic needs

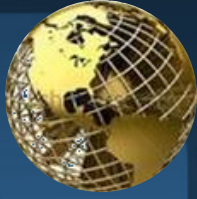
relative terms – a level of income that places a person or family in the lowest, say, 20% of all persons or families receiving income



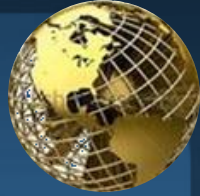
What is the
poverty line?



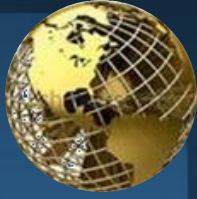
The **poverty line** is the level of income below which a person or family is considered to be poor.



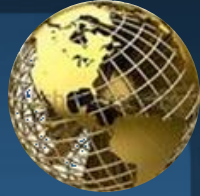
Who is eligible for antipoverty programs?



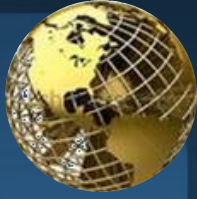
The groups eligible for antipoverty assistance include the disabled, the elderly and poor families with dependent children.



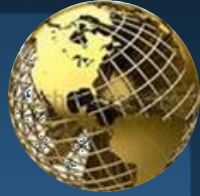
What is a means test?



A **means test** is the requirement that a family's income not exceed a certain level to be eligible for public assistance, e.g. are their economic means sufficient to support them without other assistance.

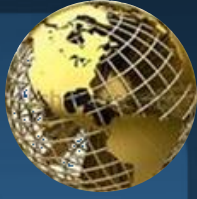


What are some examples of cash transfer programs?

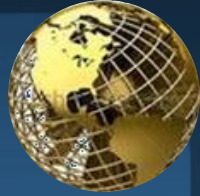


Examples of **cash transfer** programs are:

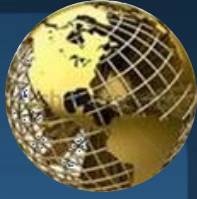
- social security
- unemployment compensation
- temporary assistance to needy families (TANF)
- worker's compensation
- SSI
- Pell grants



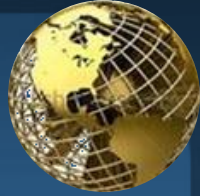
What are
in-kind transfers?



In-kind transfers are government payments in the form of goods and services, rather than cash, including such government programs as food stamps, Medicaid and housing.

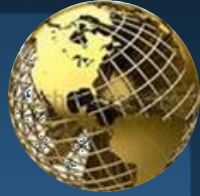


What are some examples of in-kind transfers?

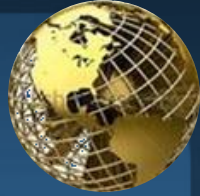


Examples of in-kind transfers are:

- food stamps
- medicare
- medicaid
- housing assistance
- VA medical care

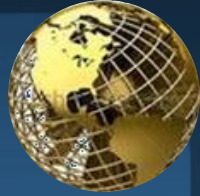


What is a government failure?

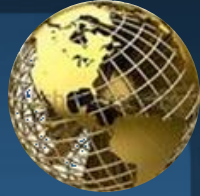


A **government failure** is a government intervention that fails to improve market outcomes.

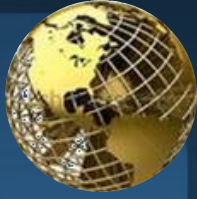
To many people, the apparent ineffectiveness of the transfer system to redistribute income is a mark of government failure.



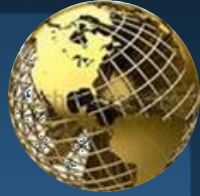
How does discrimination affect wages?



Discrimination in the workplace can lower the equilibrium wage for the group that is being discriminated against.

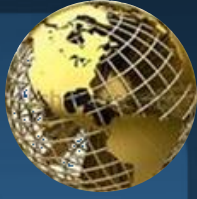


What is
comparable worth?

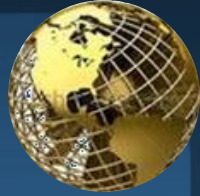


Comparable worth is the principle that employees must be paid the same wage when their jobs, even if different, are similar, e.g. they receive comparable pay for comparable work. The fact that the employees may be of different ethnic groups or different sexes is not relevant to their comparable worth.

(BTW, universities are notorious for paying female professors much lower salaries than male professors of the same rank and teaching the same courses!)

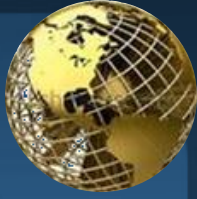


What is the Benefits-Received Principle?

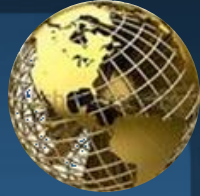


The **Benefits-Received Principle** maintains that whoever benefits from taxes or government assistance should pay in an amount equal to the benefits received.

One example is gasoline (excise) taxes. If you drive a lot you buy a lot of gas, pay a lot of gasoline taxes and therefore help pay for the roads you drive on.

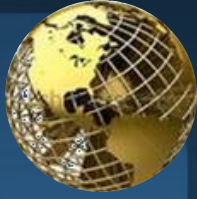


What is the Ability-to-Pay Principle?

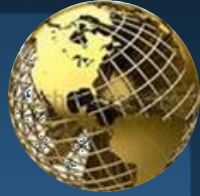


According to the **Ability-to-Pay Principle** whoever is better able to pay taxes should pay.

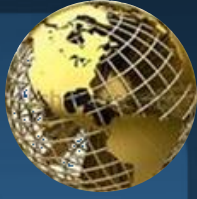
For example, a rich person should pay more taxes than a poor person because the rich are better able to pay taxes.



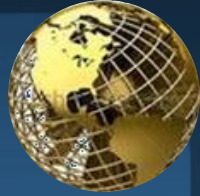
What is a progressive tax?



A **progressive tax** is a tax system in which tax rates rise as incomes rise.

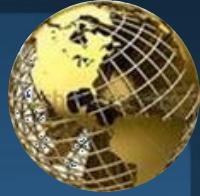


What is the tax elasticity of supply?

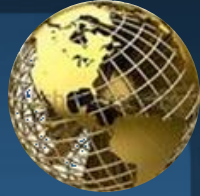


The **tax elasticity of supply** is the percentage change in quantity supplied divided by the percentage change in tax rates.

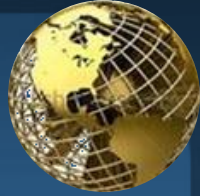
$$\text{tax elasticity of supply} = \frac{\% \text{ change in quantity supplied}}{\% \text{ change in tax rate}}$$



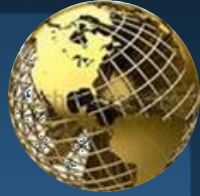
What is the tax base?



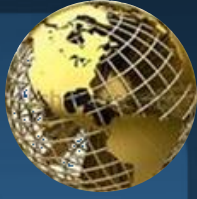
The **tax base** is the amount of income or property directly subject to nominal tax rates.



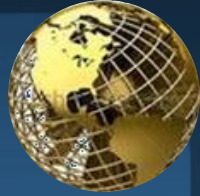
Why is the tax base shrinking?



As deductions, exemptions and credits accumulate, the tax base shrinks.

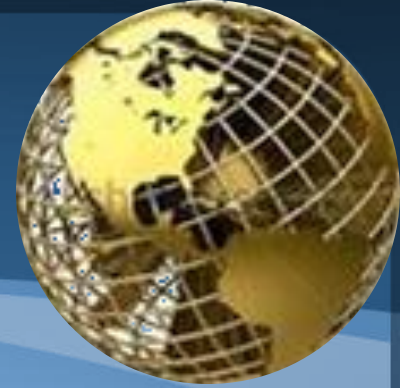


Why are sales taxes and property taxes regressive?



Sales taxes and property taxes are regressive because poor people pay a larger percentage of their income on these taxes than do rich people.

How did you do?! If you didn't do as well as you'd like, review the margin notes and presentations and test yourself again.



"I'M GETTING TIRED OF HUNTING AND GATHERING.
LET'S INVENT TAXES AND GOVERNMENT."

CONTINUED IN
TEST YOURSELF: ANTITRUST AND REGULATION