Taxes, Transfers, and Government Insurance

Applied Microeconomics

Hans-Martin von Gaudecker & Florian Zimmermann

Taxation – what for?

1. Resources for provision of public services / public goods
2. Redistribution
3. Insurance

Consumption insurance

- Main prediction of dynamic models of individual behaviour: Marginal utility of consumption constant over time
- Subsumes all thoughts about taxation, especially 2. and 3.
- Redistribution is insurance under veil of ignorance
- Savings: self-insurance against future income changes

Crucial features of models

- Income processes, transitory vs. permanent shocks
- Effort vs. luck, observability
- Determinants of wages
- Family formation, household economies of scale

Classification: 3 pillars

- Taxes
- Targeted transfers
- Insurance

Taxes

- Income
- Expenditures (VAT)
- Wealth / substance

Transfers

- Means-tested
- Child benefits

Insurance

- Pension (forced savings / longevity)
- Unemployment
- Disability
- Health / long-term care expenditures