

4. Public Finance

Mojmír Sabolovic
mojmir.sabolovic@law.muni.cz

Last seminar recap

- **Expenditure is the value of goods and services bought by the State and its articulations**
- **Public expenditure make up charge account of government budget**
- **Can be financed through taxes, public debt, money emission, international aid**

Main roles of Public Expenditures

- **contributes to current effective demand**
- **it expresses a coordinated impulse on the economy, which can be used for stabilization, business cycle inversion, and growth purposes**
- **it increases the public endowment of goods for everybody**
- **it gives rise to positive externalities to economy and society, the more so through its capital component**

Public Expenditures Composition

First, public expenditure can be classified in terms of the kind of goods and services bought, also with very general items:

- 1. capital goods**
- 2. consumption goods**
- 3. personnel expenditure**

Second, public expenditure can be classified according to the official body an organization from which budget it is paid, as for example:

- 1. the central state and its ministries**
- 2. regional and local authorities**
- 3. separate public bodies**
- 4. international organizations**

Pension systems

- **Funded pension system is one wchitch money is collected and invested in a special fund from which payments are made**
- **Unfunded pension system is one in which pension are paid from current revenues**

Taxation

- **Forms income side of state budget**
- **Tax is compulsory payment paid by subjects of the economy, individuals or enterprises, according to legally mandated rules to state treasury. The tax system is differ from country to country, generally they all are similar (mainly for advanced countries).**

History of taxation

- **Ancient Egypt around 3000 BC - 2800 BC in the first dynasty of the Old Kingdom.**
 - **Pharaoh collects the revenues from the people**
- **taxation is also described in the Bible**
 - **it states "But when the crop comes in, give a fifth of it to Pharaoh. The other four-fifths you may keep as seed for the fields and as food for yourselves and your households and your children."**
 - **A share (20%) of the crop was the tax. While not money, the idea is the same.**



- **Quite a few records of the government tax collection in Europe since at least the 17th century are still available today.**
- **But the taxation levels are hard to compare to the size and flow of the economy since production numbers are not as readily available**
- **The taxation as a percentage of production of final goods may have reached 15% - 20% during the 17th century in places like France, the Netherlands, and Scandinavia.**
- **This increase was greatest in England, Peter Mathias and Patrick O'Brien found that the tax burden increased by 85% over this period.**

Tax agencies

- **Tax collection is performed by a government agency such as Revenue Canada, the Internal Revenue Service (IRS) in the United States, or Her Majesty's Revenue and Customs (HMRC) in the UK. When taxes are not fully paid, civil penalties (such as fines or forfeiture) or criminal penalties (such as incarceration) may be imposed on the non-paying entity or individual.**

Income part of state budget

- **The most controversial part concerns income distribution**
- **What is fair is philosophical question**
- **Should the government use**
 - **Progressive tax**
 - **Regressive tax**
 - **Proportional tax**

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- **Should there be exemptions?**
 - **Items of income that are not taxed at all**
 - **Should there be tax loophole?**
 - **Legal but unfair exemption**

Forms of taxation

- **Today, one of the most complicated taxation-systems worldwide is in Germany. Three quarters of the world's taxation-literature refers to the German system.**
- **There are 118 laws, 185 forms, and 96,000 regulations, spending € 3.7 billion to collect the income tax.**
- **Today, governments of advanced economies of EU, North America, and others rely more on direct taxes, while those of developing economies of India, Africa, and others rely more on indirect taxes.**

Tax rates

- Taxes are most often levied as a percentage, called the *tax rate*.
- An important distinction when talking about tax rates is to distinguish between the marginal rate and the effective (average) rate.
- The effective rate is the total tax paid divided by the total amount the tax is paid on, while the marginal rate is the rate paid on the next dollar of income earned.

Ad valorem tax

- **An *ad valorem* tax is one where the tax base is the value of a good, service, or property. Sales taxes, tariffs, property taxes, inheritance taxes, and value added taxes are different types of ad valorem tax.**
- **An ad valorem tax is typically imposed at the time of a transaction (sales tax or value added tax (VAT)) but it may be imposed on an annual basis (property tax) or in connection with another significant event (inheritance tax or tariffs).**
- **An alternative to ad valorem taxation is an excise tax, where the tax base is the quantity of something, regardless of its price. For example, in the United Kingdom, a tax is collected on the sale of alcoholic drinks that is calculated by volume and beverage type, rather than the price of the drink.**

Comparison of Taxes paid by a household earning the country's average wage

Country	Single no kids	Married 2 kids	Country	Single no kids	Married 2 kids
Australia	28.3%	16.0%	Republic of Korea	17.3%	16.2%
Austria	47.4%	35.5%	Luxembourg	35.3%	12.2%
Belgium	55.4%	40.3%	Mexico	18.2%	18.2%
Canada	31.6%	21.5%	Netherlands	38.6%	29.1%
Czech Republic	43.8%	27.1%	New Zealand	20.5%	14.5%
Denmark	41.4%	29.6%	Norway	37.3%	29.6%
Finland	44.6%	38.4%	Poland	43.6%	42.1%
France	50.1%	41.7%	Portugal	36.2%	26.6%
Germany	51.8%	35.7%	Slovak Republic	38.3%	23.2%
Greece	38.8%	39.2%	Spain	39.0%	33.4%
Hungary	50.5%	39.9%	Sweden	47.9%	42.4%
Iceland	29.0%	11.0%	Switzerland	29.5%	18.6%
Ireland	25.7%	8.1%	Turkey	42.7%	42.7%
Italy	45.4%	35.2%	United Kingdom	33.5%	27.1%
Japan	27.7%	24.9%	United States	29.1%	11.9%

Source: OECD, 2005 data. ^[12]

Classical supply-side economics

- **Focuses on incentive effects of taxes**
- **It argues that low rates are central to an economy's success**

Principles

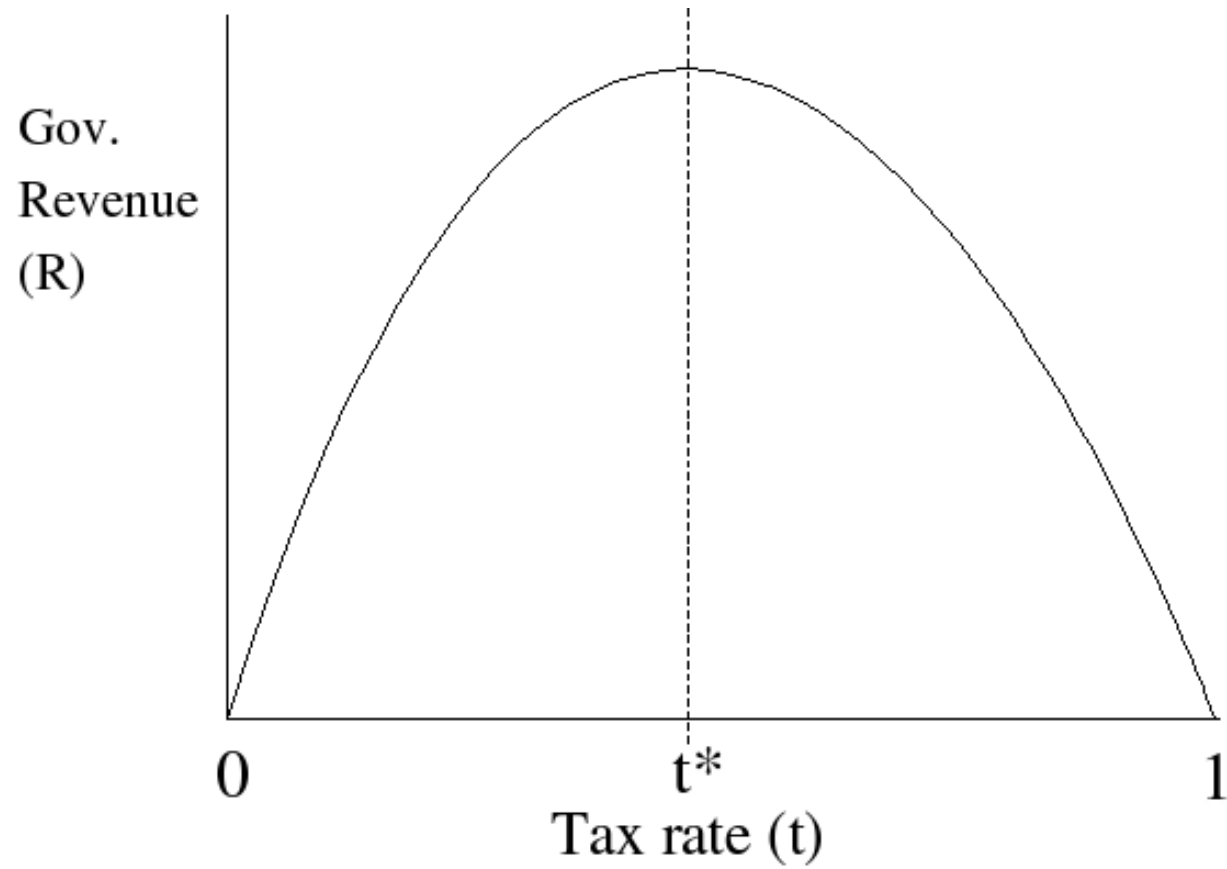
- **Government cuts taxes, people will have greater incentive to work, to save, to invest,**
- **Output will increase, not because of expectations of increased demand, but because of effect of lower tax rates on supply**
- **The aggregate supply curve will shift out**



- **Failures**

- **Deficit kept mounting up**
- **Supply incentives didn't did not create the needed increase in the growth of potential output**
- **Didn't end the political push for more and more government spending**

Laffer curve



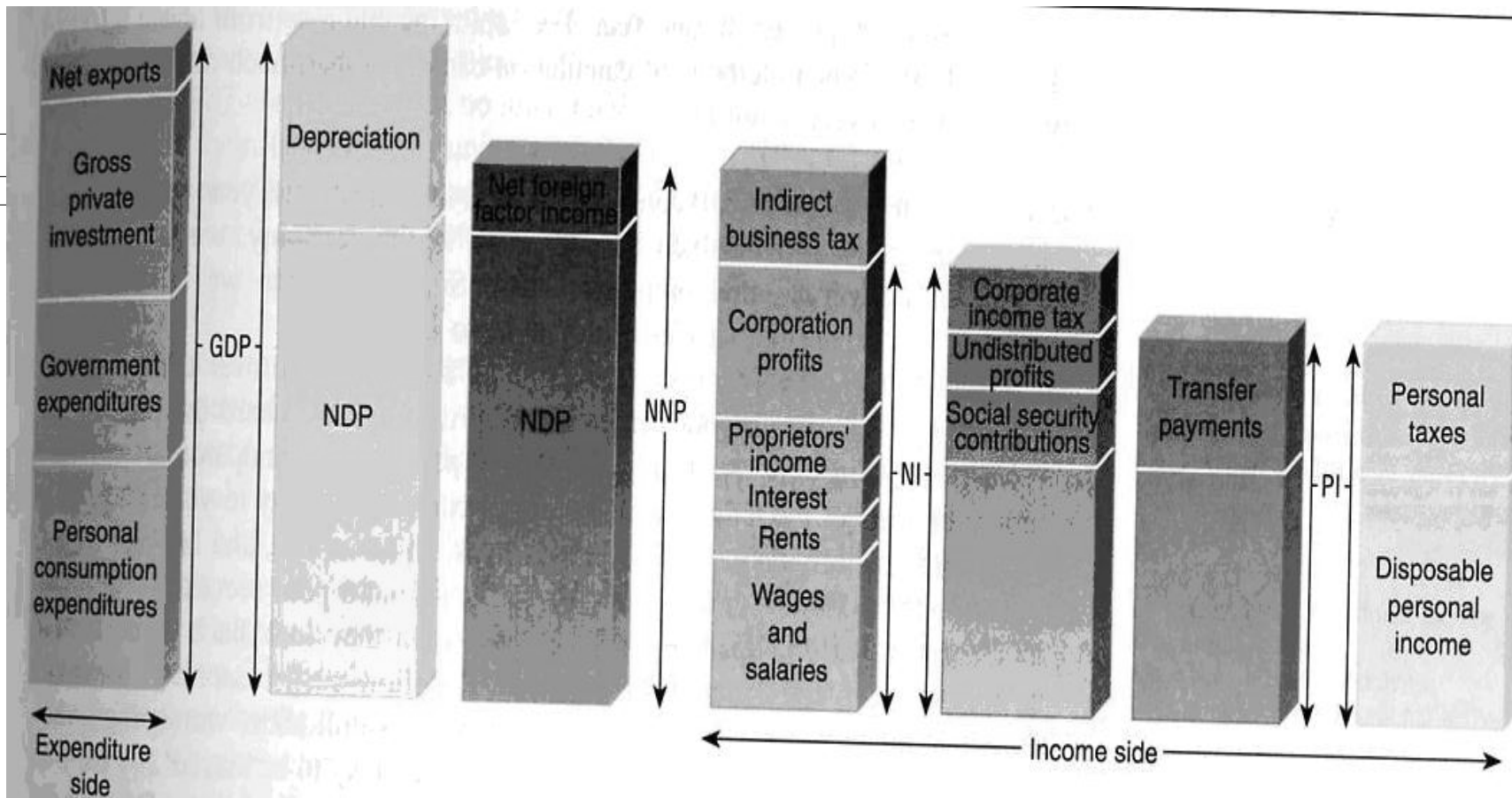
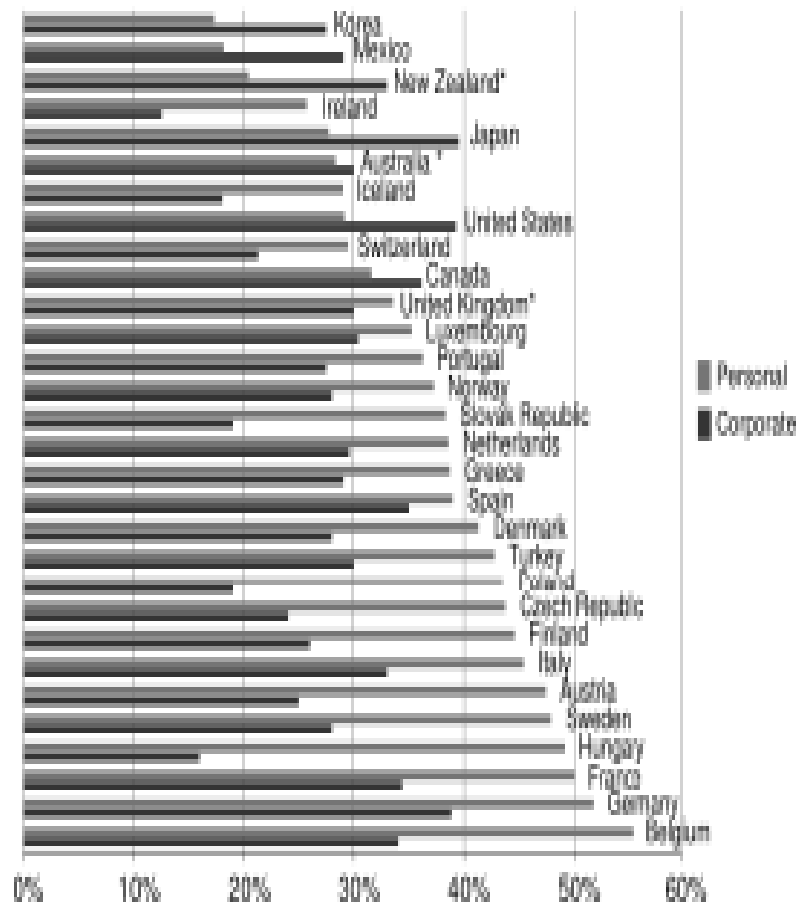


EXHIBIT 12 From GDP to Disposable Personal Income

Here are the steps involved in moving from GDP to disposable personal income.

Income tax rate

Mean Income Tax Rates in the Year 2005
as a Percentage of Income by Country



Tax system of the Czech Republic

The Czech Tax Administration manages these taxes:

- **Direct taxes**

- Legal Entity Income Tax
- Natural Person Income Tax
- Real Estate Tax
- Inheritance tax, Gift tax and Real estate-transfer tax
- Road Tax

- **Indirect taxes**

- Value Added Tax
- Excise duty (Purchase Tax)

Pokladní plnění státního rozpočtu České republiky 2006 - Příjmy

		v mil. Kč		
		Schválený rozpočet 2006	Skutečnost k 30.9.2006	Plnění v %
	PŘÍJMY CELKEM (A+B)	889 392	673 501	75,7
	z toho:			
A.	DAŇOVÉ PŘÍJMY CELKEM	809 571	588 087	72,6
1.	<i>Daň z příjmů, zisku a kapitálových výnosů</i>	180 300	139 224	77,2
1.1.	Daň z příjmů právnických osob	88 000	73 266	83,3
1.2.	Daň z příjmů fyzických osob	92 300	65 958	71,5
1.2.1.	Daň z příjmů fyz.osob ze závislé činnosti	73 000	55 236	75,7
1.2.2.	Daň z příjmů fyz.osob z kapitálových výnosů	4 600	3 822	83,1
1.2.3.	Daň z příjmů fyz.osob ze samostatné výdělečné činnosti	14 700	6 900	46,9
2.	<i>Daně ze zboží a služb v tuzemsku</i>	275 600	194 006	70,4
2.1.	Daň z přidané hodnoty	156 700	108 293	69,1
2.2.	Zvláštní daně a poplatky ze zboží a služeb v tuzemsku (spotřební daně)	118 900	85 713	72,1
3.	<i>Daně a poplatky z vybraných činností</i>	4 100	2 931	71,5
3.1.	Správní poplatky	4 100	2 931	71,5
4.	<i>Daně a cla za zboží a služby ze zahraničí</i>	1 200	863	71,9
4.1.	Daně a cla za zboží a služby ze zahraničí	1 200	863	71,9
5.	<i>Majetkové daně</i>	10 300	6 069	58,9
5.1.	Daně z majetkových a kapitálových převodů	10 300	6 069	58,9
6.	<i>Pojistné na SZ, příspěvek na státní pol. zaměstnanosti</i>	336 321	243 987	72,5
6.1.	Pojistné na důchodové pojištění	279 078	200 930	72,0
7.	<i>Ostatní daňové příjmy</i>	1 750	1 007	57,5

Assignment requirements

- **Government deficit**
- **Government debt**
- **GDP**
- **Inflation**
- **Exports and Imports of goods and services**
- Unemployment
- Cost of living

Unemployment

- **Unemployment is the condition of not having a job, often referred to as being "out of work", or unemployed.**
- **In economics, unemployment refers to the condition and extent of joblessness within an economy, and is measured in terms of the unemployment rate, which is the number of unemployed workers divided by the total civilian labor force.**
- **The history of unemployment is the history of industrialization. It was not considered an issue in rural areas, despite the "disguised unemployment" of rural laborers having little to do, especially in conditions of overpopulation.**

Types of unemployment

- **Frictional**
When moving from one job to another, the unemployment temporarily experienced when looking for a new job.
- **Structural**
Caused by a mismatch between the location of jobs and the location of job-seekers. "Location" may be geographical, or in terms of skills.
- **Cyclical (Demand deficient unemployment) unemployment**
When there is not enough aggregate demand for the labor. Caused by a business cycle recession.
- **Technological**
Caused by the replacement of workers by machines or other advanced technology (such as artificial intelligence technology).




- **Classical (real-wage)**

When real wage for a job are set above the market-clearing level, commonly government (as with the minimum wage) or unions, although some (such as Murray Rothbard, *America's Great Depression* p. 45) suggest that even social taboos can prevent wages from falling to the market clearing level.

- **Marxian**

When unemployment is needed to motivate workers to work hard and to keep wages down.

- **Seasonal**

When an occupation is not in demand at certain seasons. For example, construction workers in winter, ski teachers in summer.

The unemployment rate

The unemployment rate is:

$$\text{Unemployment Rate} = \frac{\text{Unemployed Workers}}{\text{Total Labor Force}} * 100\%$$

Cost of living

- ***Cost of Living Index* measures relative price levels for consumer goods and services in participating areas. The average for all participating places in each quarter equals 100, and each participant's index is read as a percentage of the average for all participating places.**
- **The cost-of-living index is so constructed to estimate the percentage by which money income would have to rise to allow a household to buy the same bundle of goods as in the base year. Thus, if money income is \$10,000 in the base year, to maintain purchasing power that money income would have to rise to \$11,000 for another year with an index value of 110.**

Task for the next seminar?

- **Question about assignment...**

References

- **COLLANDER, D.C. Macroeconomics. Praha: LEDA, 2001.**
- http://en.wikipedia.org/w/index.php?title=International_trade&oldid=117267698 (lastvisited Mar. 26, 2007).

[1] Unemployment,
<http://en.wikipedia.org/w/index.php?title=Unemployment&oldid=117588170> (last visited Mar. 26, 2007).