

Chapter 20

1. Use Table 20.2 from Chapter 20 in your text to answer this question.
 - a. In the most recent year available, what percentage of income did the bottom fifth of the income distribution receive? What percent of income did the top fifth of the distribution receive? Roughly, what is the relationship between what the bottom fifth received and what the top fifth received?
 - b. What is the range of the percentage of income received by the bottom fifth of the income distribution over the last 33 years? What is the range for the top fifth? Describe the trend for each group over the last 33 years.
 - c. Describe three reasons why the measure of income distribution used in Table 20.2 in Chapter 20 may not truly measure someone's ability to maintain a certain standard of living. As a result, are the standard measures of income distribution likely to exaggerate or understate the true distribution of the standard of living? Explain.
 - d. What is permanent income? Why might we wish to use permanent income when measuring the distribution of income? If we used permanent income instead of current annual income when measuring the distribution of income, would this tend to exaggerate or understate the true distribution of the standard of living? Explain. (Hint: If you are a full-time student, can you borrow as much as you want in order to perfectly smooth out your lifetime consumption?)
2. Susan earns five times as much as Joe.
 - a. What would the political philosophy of utilitarianism, liberalism, and libertarianism likely suggest should be done in this situation? Explain.
 - b. Compare the degree of redistribution each suggests.
3. Suppose the government has to choose between two anti-poverty programs. Each program guarantees that every family has at least €15,000 of income. One scheme establishes a negative income tax where: $\text{Taxes} = (0.50 \text{ of income}) - €15,000$. The other scheme is for the government to guarantee every family at least €15,000 to spend and if a family falls short, the government will simply make up the difference.

- a. Using the negative income tax scheme described above, fill out the following table.

Earned Income	Taxes Paid	After-tax Income
€0	_____	_____
5,000	_____	_____
10,000	_____	_____
20,000	_____	_____
30,000	_____	_____
40,000	_____	_____

- b. What is the value of income for which this family neither receives a subsidy nor pays any tax? (That is, how high does income have to be for the family to stop receiving a subsidy?)
- c. Under the second scheme where the government simply guarantees at least €15,000 to every family, what is the level of income at which a family stops receiving a subsidy? Explain.
- d. Which plan is likely to be more expensive to the government? Explain
- e. Suppose a poor family that only earns €5,000 per year decides to plant a garden and sell the produce in a "farmer's market" in the city. Suppose the family earns an additional €5,000 selling the produce. What is the family's final income under each scheme? What is the effective tax rate on the €5,000 earned by family under each scheme? Which scheme promotes a work ethic among the poor and which one discourages work? Explain.