*Opening the fiscal channels on the budget constraint (Income Policies)

CEQ Assessment: Fiscal Incidence Analysis

\[ Y_h = I_h - \sum_i T_i S_{ih} + \sum_j B_j S_{jh} \]

Income after taxes and transfers
Taxes
Transfers
Income before taxes and transfers
Share of tax \( i \) paid by unit \( h \)
Share of transfer \( j \) received by unit \( h \)

Figure 1: Size and composition of government budgets (circa 2010)

Panel a: Composition of Social Spending as a Share of GDP

(rank by social spending/GDP)

Lustig, Nora. 2015b. *Inequality and Fiscal Redistribution in Middle Income Countries: Brazil, Chile, Colombia, Indonesia, Mexico, Peru and South Africa. Evidence from the Commitment to Equity Project (CEQ).*

Brazil spends (and taxes) as a rich country but its impact on inequality is rather small.
Measuring the Social State

Three key indicators of a government’s commitment to reducing inequalities, poverty and social exclusion

- The share of total income devoted to social spending and how it is financed
- How equalizing and pro-poor net spending is
- Who pays for what the government spends

www.commitmenttoequity.org

***COMPLEXITIES: Lambert’s Conundrum

<table>
<thead>
<tr>
<th></th>
<th>ED</th>
<th>C</th>
<th>B</th>
<th>A</th>
<th>Total</th>
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<td>20</td>
<td>30</td>
<td>40</td>
<td>100</td>
</tr>
<tr>
<td>Tax t</td>
<td>6</td>
<td>9</td>
<td>12</td>
<td>15</td>
<td>42</td>
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<tr>
<td>Transfer B</td>
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<td>14</td>
<td>7</td>
<td>0</td>
<td>42</td>
</tr>
<tr>
<td>Net Income N</td>
<td>25</td>
<td>25</td>
<td>25</td>
<td>25</td>
<td>100</td>
</tr>
</tbody>
</table>

Source: Lambert, 2001, Table 11.1, p. 278

- The Redistributive Effect of the tax only in this example is equal to -0.05, highlighting its regressivity
- The Redistributive Effect of the transfer is equal to 0.19
- Yet, the Redistributive Effect of the net fiscal system is 0.25, higher than the effect without the taxes!

Taxes can be unequalizing by themselves but when combined with transfers make the system more equalizing than without the regressive taxes

- The US and the UK had regressive equalizing taxes in the past (O’Higgins & Ruggles, 1981)
- Chile’s 1996 fiscal system had equalizing regressive taxes (Engel et al., 1999)
Analyzing the impact on traditional poverty indicators can be misleading. Fiscal systems can show a reduction in poverty for all possible poverty lines and yet a substantial share of the poor could have been impoverished by the combined effect of taxes and transfers.

Brazil: 36.8% of post-fisc poor are fiscally impoverished.

**CEQ Assessment: Income Concepts**

1. **MARKET INCOME**
2. **PLUS DIRECT TRANSFERS MINUS DIRECT TAXES**
3. **DISPOSABLE INCOME**
4. **PLUS INDIRECT SUBSIDIES MINUS INDIRECT TAXES**
5. **POST-FISCAL or CONSUMABLE INCOME**
6. **PLUS MONETIZED VALUE OF PUBLIC SERVICES: EDUCATION & HEALTH**
7. **FINAL INCOME**
WHAT IS THE IMPACT OF TAXES AND CASH TRANSFERS (SUBSIDIES) IN INEQUALITY?

WHAT IS THE IMPACT OF TAXES AND CASH TRANSFERS (SUBSIDIES) IN INEQUALITY?

Fiscal Redistribution: Brazil, Chile, Colombia, Indonesia, Mexico and South Africa

Gini Coefficient, circa 2010

Source: Lustig (2015a)
B. Final income inequality and market income inequality

Do More Unequal Countries Redistribute More?
Robin Hood is With Us!
His true profession in Brazil is doctor or a teacher

Do More Unequal Countries Redistribute More?

References

- Lustig, Nora. 2015b. Lustig, Nora. 2015b. Inequality and Fiscal Redistribution in Middle Income Countries: Brazil, Chile, Colombia, Indonesia, Mexico, Peru and South Africa. Evidence from the Commitment to Equity Project (CEQ). CEQ Working Paper No. 31, Center for Inter-American Policy and Research and Department of Economics, Tulane University and Inter-American Dialogue.
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