Lecture 6. In-class problems

EVENING

10/6/2020

2. Corporate Income Tax

The incidence of the corporate income tax is one of the most heavily debated issues in economics. The United States has just seen substantial corporate tax reform. In the context of this tax reform, corporate tax rates have fallen. Discuss which parties may bear the burden of this tax, and who has therefore benefitted most from its decline.

Don't discuss how the burden of the tax is shared – just identify who could possibly bear the burden of the tax, and who could, therefore, benefit from potential tax changes.

owners of capital -- shareholders
workers.
landowner
upper lvl worker

consumers
government.

Q1. Demand for rutabegas: $Q = 2000 - 100P$

Supply for : $Q = -100 + 200P$

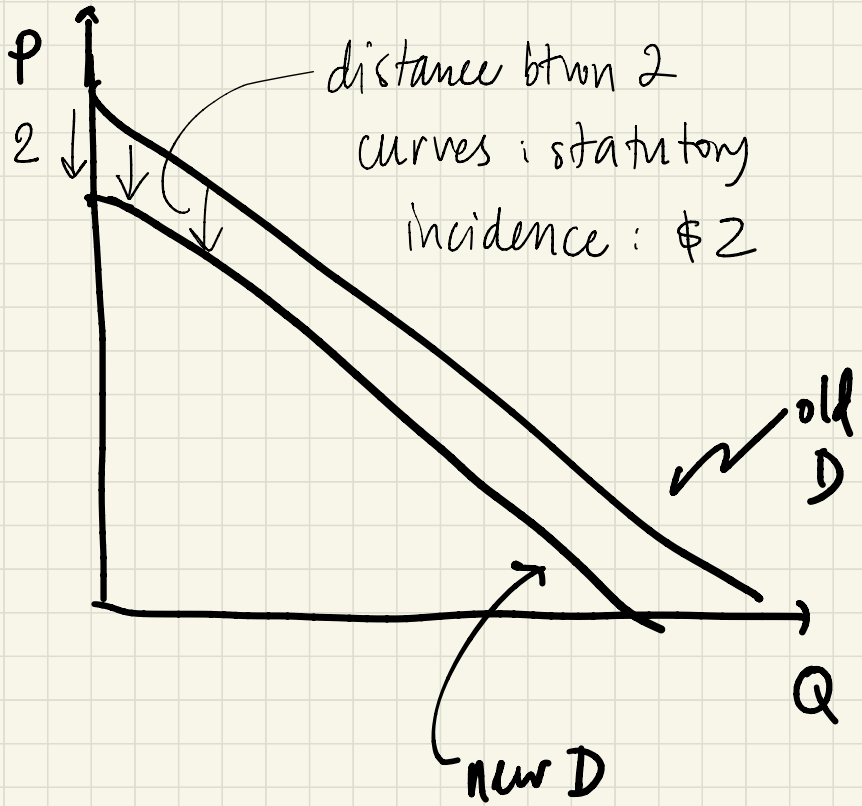
\$2/unit tax on rutabegas. Who bears statutory incidence? Economic incidence?

Find y-intercept of supply curve

$$0 = -100 + 200P$$

$$200P = 100$$

$$P = 100/200 = 1/2$$



consumer bears statutory burden

new demand curve

$P_{post} - P_{pre} + tax$

$P_{post} = P_{pre} - tax.$

$y = mx + b$

↑ b must decline by 2

demand curve $Q = 2000 - 100P$ — old demand

$100P = 2000 - Q$

$\frac{100P}{100} = \frac{2000 - Q}{100}$

$P = 20 - \frac{1}{100}Q$

$y = b + mx$

when $P = 0$, $Q = 2000$

Using $y = mx + b$

new demand c is $P_{new} = 20 - \frac{1}{100}Q - 2$

Using $P_{post} = P_{pre} - 2$

$= 20 - \frac{1}{100}Q - 2$

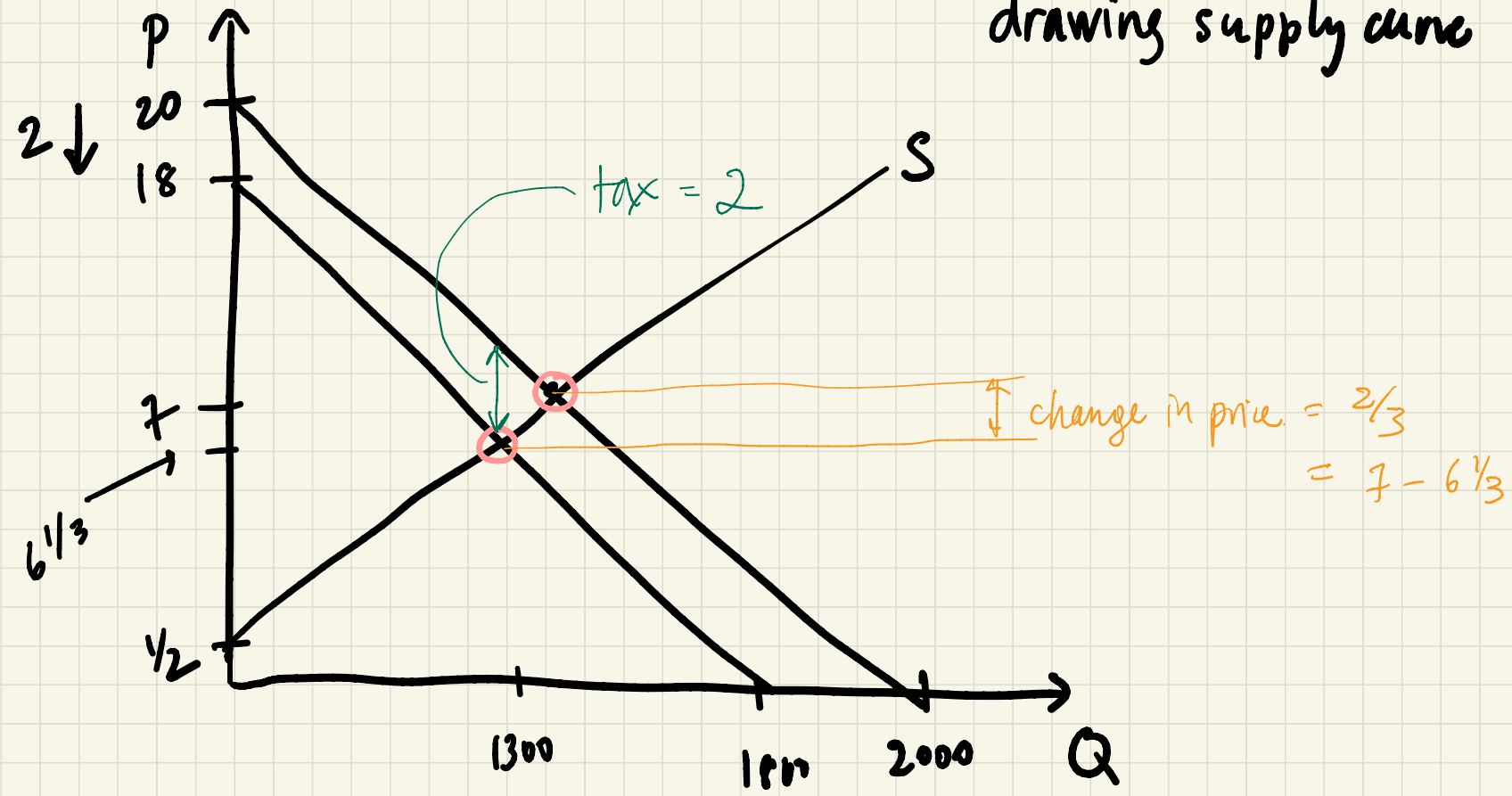
$= 18 - \frac{1}{100}Q$

new demand

when $P = 0$, $\frac{1}{100}Q = 18$

$\Rightarrow Q = 1800$

drawing supply curve



Find orig eqbm price. Set $Q_s = Q_D$

$$2000 - 100P = -100 + 200P$$

$$2100 = 300P$$

$$P = 7$$

Find eqbm Q

$$Q = -100 + 200P$$

$$Q = -100 + 200(7)$$

$$Q = -100 + 1400$$

$$Q = 1300$$

Find new eqbm P & Q after tax

$-100 + 200P = 1800 - 100P$

$300P = 1900$

$P = \frac{1900}{300}$

$P = \frac{19}{3}$

Make new demand in terms of Q

$P = 18 - (1/100)Q$

$[(1/100)Q = 18 - P] 100$

$Q = 1800 - 100P$

Economic incidence of tax

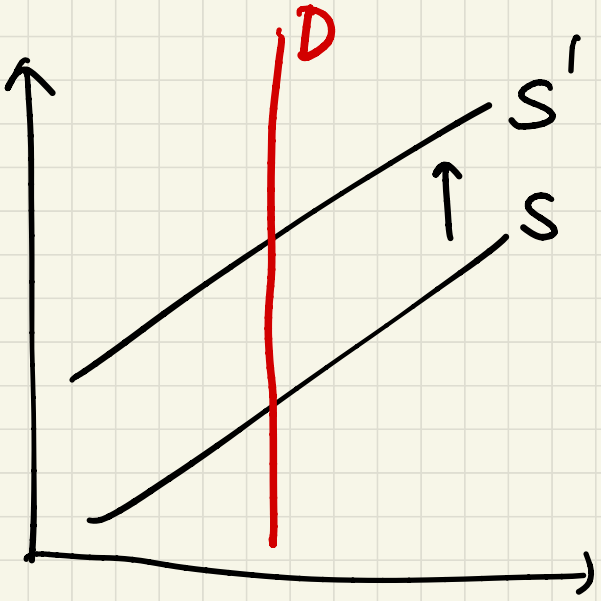
consumers : $2-(7-6\frac{1}{3})$

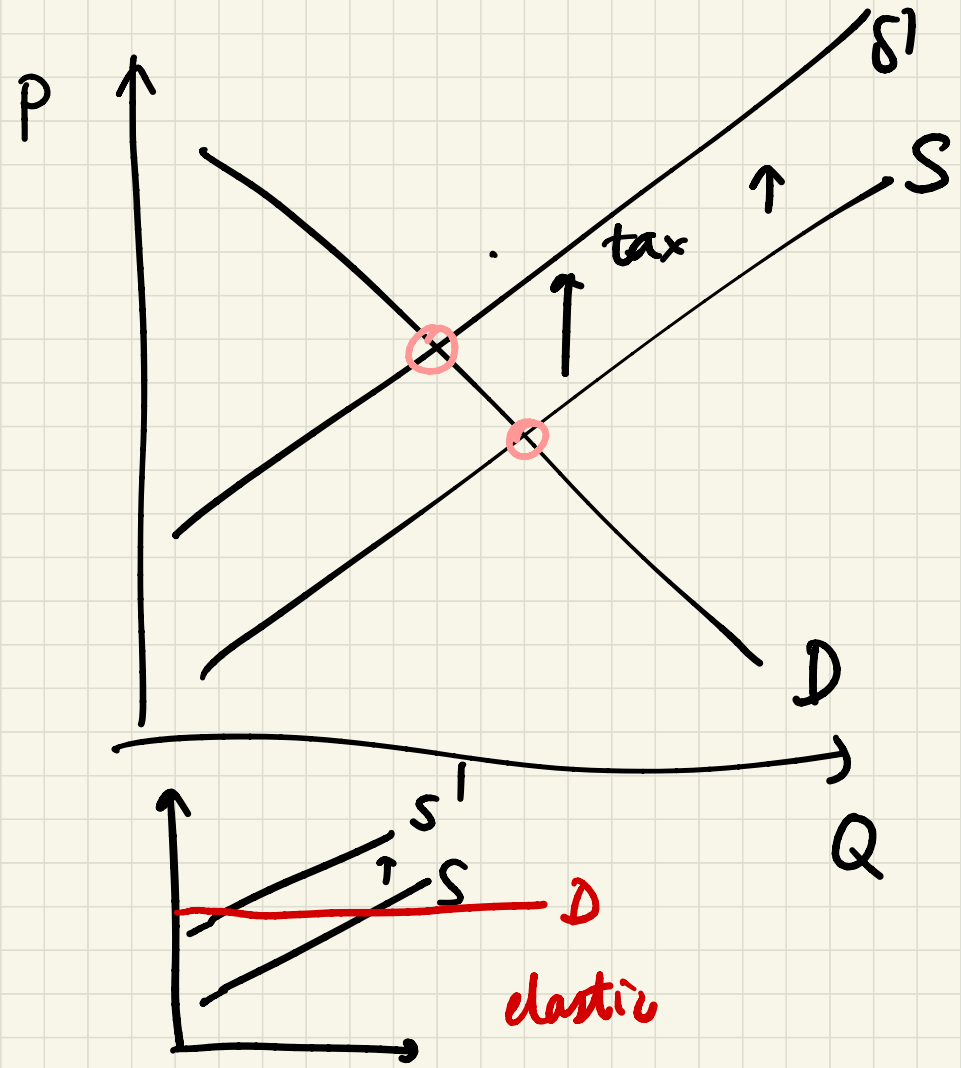
producers : $7-6\frac{1}{3}$

total tax burden = tax = PB + CB

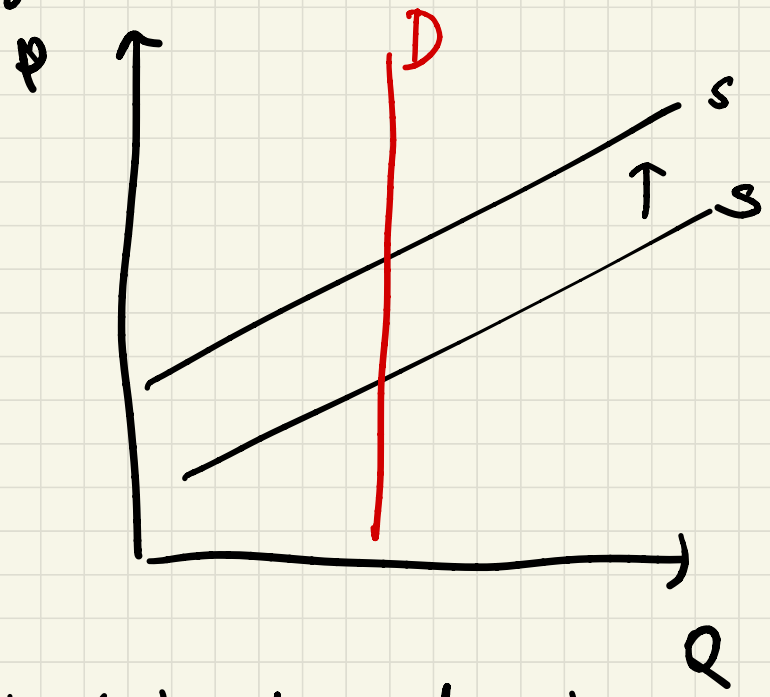
$$2 = (2/3) + (2 - 2/3) = 2$$

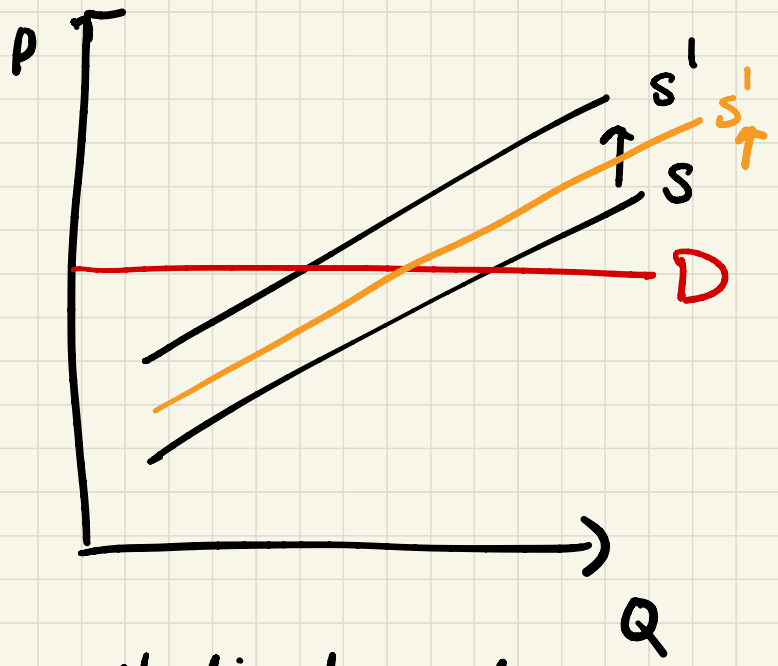
basic set-up





high end rest.





inelastic demand rest.

BETTER OFF

popeye's during chicken sandwich.

elastic demand rest.

WORSE OFF

other fast-food, rest. where consume more price sensitive