

# Public Economics

## Lec 14: Globalization & Tax Competition

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# AM's reminders

- **Exam**
  - 5 short questions (5/6 lines, 4 points each)
  - 3 longer questions (20 points each)
  - Essay added | exam > 40
  - **Handwriting**
- **Essay discussion**
- **Can do shared presentations**
- **If you have slides, upload them during the breaks**
- **See you tomorrow!**

# Reading list

- **Bergh**
- **Hansson (2007)**
- **Recommended readings:**
  - Genschel & Schwarz (2011)

# Threats to the welfare state

- ① Ageing and demography
- ② Increasing demand for public services
- ③ Globalization
  - Tax competition

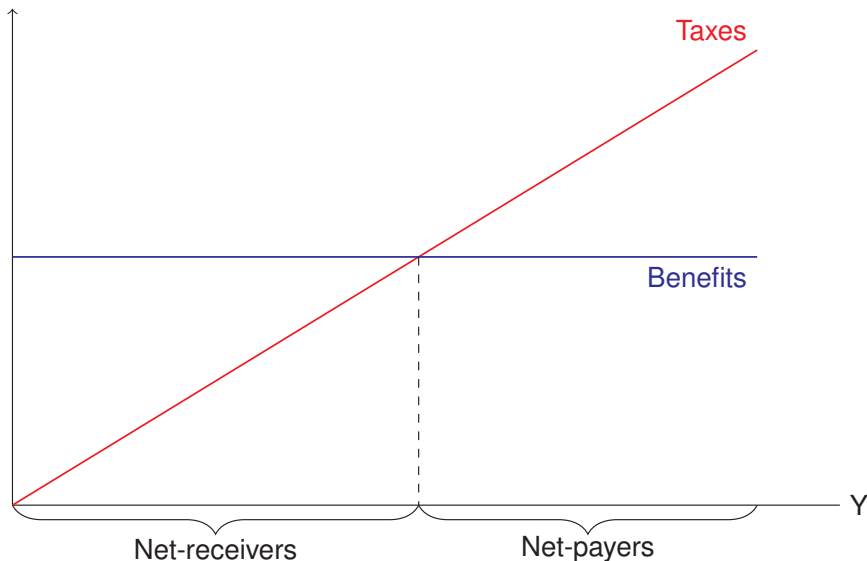
# Increasing demand for public services

- **Wagner's (1835-1917) law**
  - **Voting for ever-increasing social state**
- **Social preferences**
- **Increase in income  $\implies$  increase in welfare**
  - E.g. **Education**: elasticity  $> 1$ : demand for education increases more than proportionally with income
- **Demography**



- **Factor mobility increasing**
  - Cornerstone of EU politics
  - **Efficient:** better reallocation of resources, growth
  - **Great for the market**
- **Tax competition**
  - **Tiebout model**
  - **Competition**  $\implies$  **better use of resources**
  - **Race to the bottom**
    - Outbidding each other for winning net-payers
  - **Analogy with market impossible**
    - **Governments needed to correct for market failures!**

# Welfare state support simplified

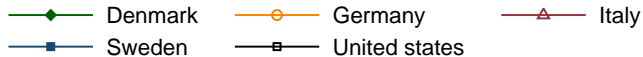
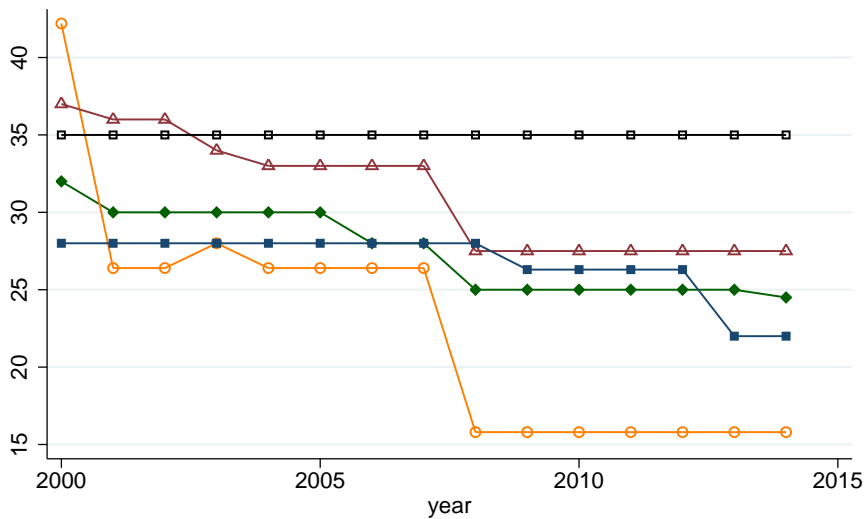


# Tax competition

- **Simple framework, powerful implications**
- **Empirical evidence**
  - Tax revenues have not declined over years (if anything, increased)
  - States continue to expand in size
- **Q:** are all factors equally mobile?
  - **Workers** do not shop for welfare much (see problems with Tiebout model)
  - **Capital**



# Corporate taxation



# Tax avoidance

- **Tax havens**
  - Luxembourg
  - Cayman Island, Bermuda
  - Isle of Man, Guernsey, Jersey
  - City of London (hub)
- **Offshore finance**
- **Problem to finance correction of market failures**
- **Ethically:** taxes where creation of value is (use of infrastructures)
  - **Internet companies?**
- **Push for cooperation across nations**
  - Not so different principle than Piketty's world wealth tax

## ① Restructuring the tax system

- Shifting the tax burden to less mobile factors
- Compensate mobile production factors
  - Expert tax (SE)

## ② Tying benefits to taxation

- E.g. pensions, migration

## ③ Work incentives (demographics)

- Incentive + rules

## Increasing demand for quality public services

**Problem: cost too high / crowd-out**

- ④ **Topping-up**
  - **Public consumption**
  - **Social insurance**
- ⑤ **Vouchers**
- ⑥ **Increasing efficiency: competition + subsidies**
  - **Lecture on privatization**

# The future

- **Can the government have a role in a globalized world?**
  - **It must:** if not for equity, for efficiency
  - **Market failures need to be corrected**
  - **Second best**
- **Resources are scarce (and scarcer)**
  - **Efficiency is a must!**
  - Alternatives **must** be considered
- **The long VS the short run?**
  - **Pol. economics: median voter**
  - **Role of leadership**



*“That’s all Folks!”*

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