Questions TA 9 session

Question 1

Consider a policy reform that increases the standard allowance in Universal Credit and increasing the tax burden of the wealthiest consumers to finance the reform. Which of the following statements are true?

Select one or more:

- [ ] a. This type of revenue-neutral redistributive policy creates no consumption effect in the aggregate in a model where the marginal propensity to consume is identical across consumers.
- [ ] b. When we consider a model with liquidity constraints and precautionary savings, where the marginal propensity to consume is heterogeneous across consumers, this reform can decrease aggregate consumption.
- [ ] c. Instead of increasing the tax burden of the wealthiest consumers to finance the reform, policy-makers can issue debt to finance the reform. This debt-finance reform can achieve a larger impact on aggregate consumption than the revenue-neutral redistributive reform in a model with heterogenous marginal propensity of consume.

Question 2

The Ricardian equivalence is that rational agents would not change their consumption decisions unless the timing of taxes affects the lifetime budget constraint. Which of the following assumptions are compatible with the Ricardian equivalence?

Select one or more:

- [ ] a. Consumers are infinitely lived.
- [ ] b. Taxes are not distortionary.
- [ ] c. Consumers are rational.