

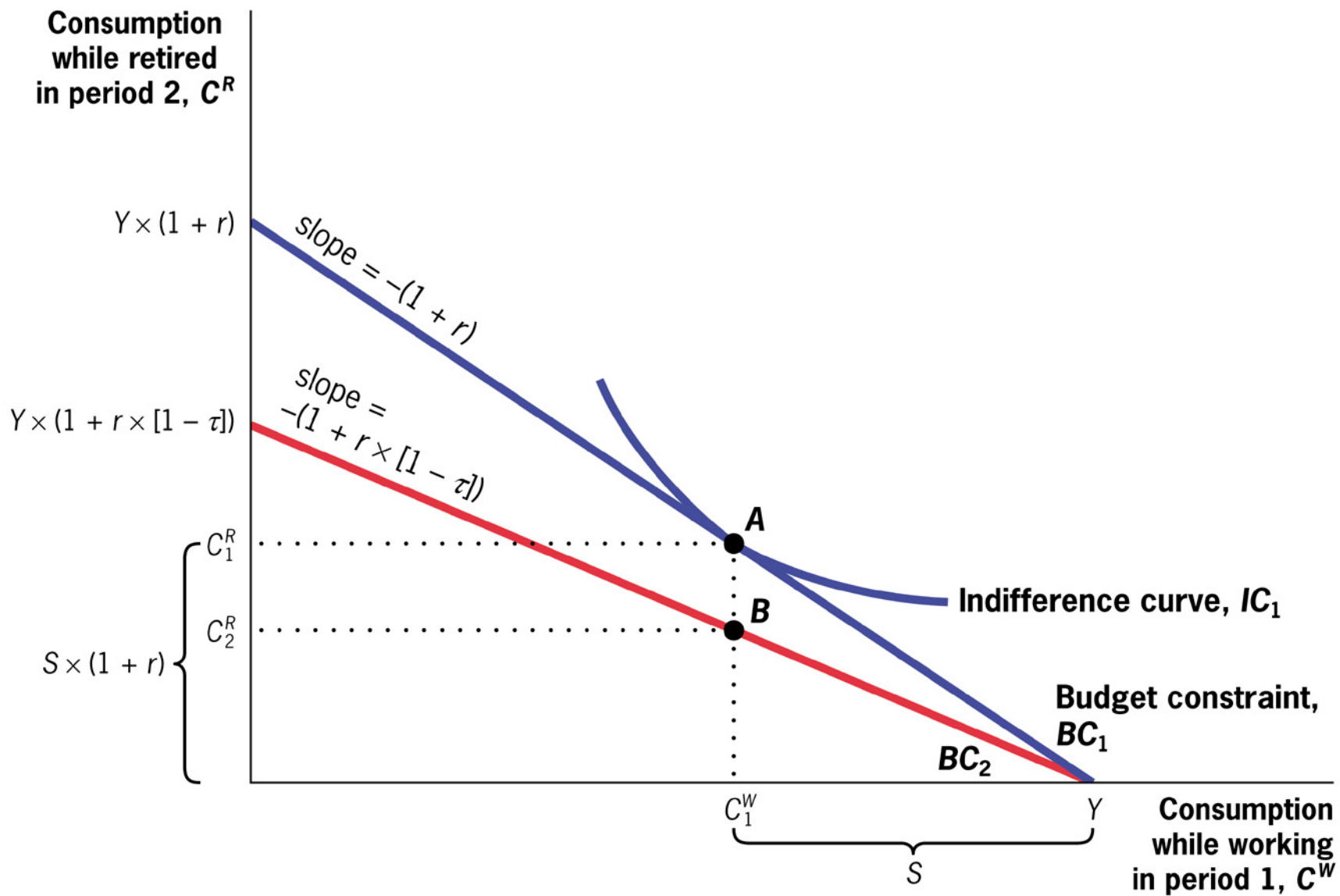
Jonathan Gruber

# **Public Finance and Public Policy**

**First Edition**

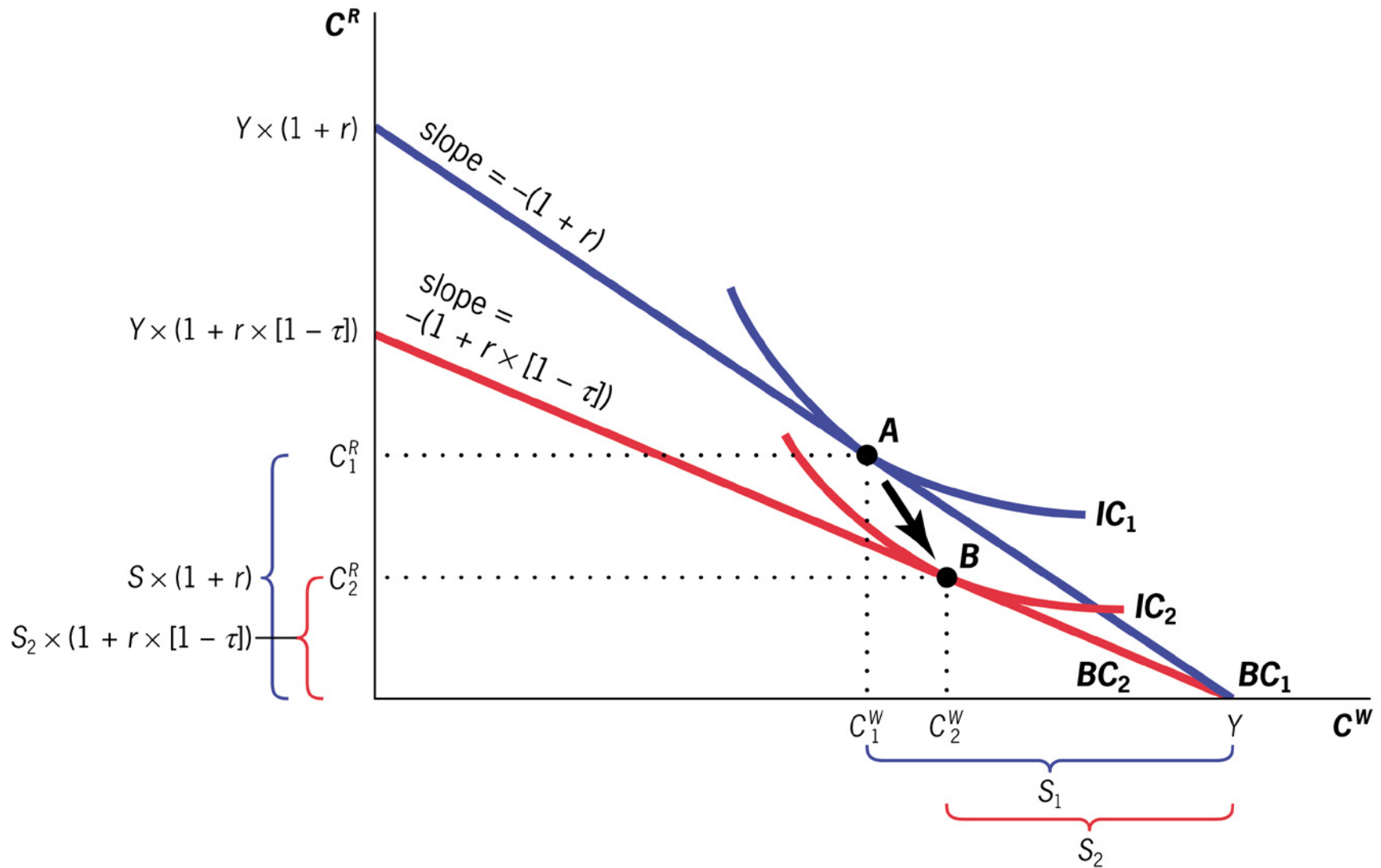
## **Chapter 22:** Taxes on Savings

Copyright © 2005 by Worth Publishers



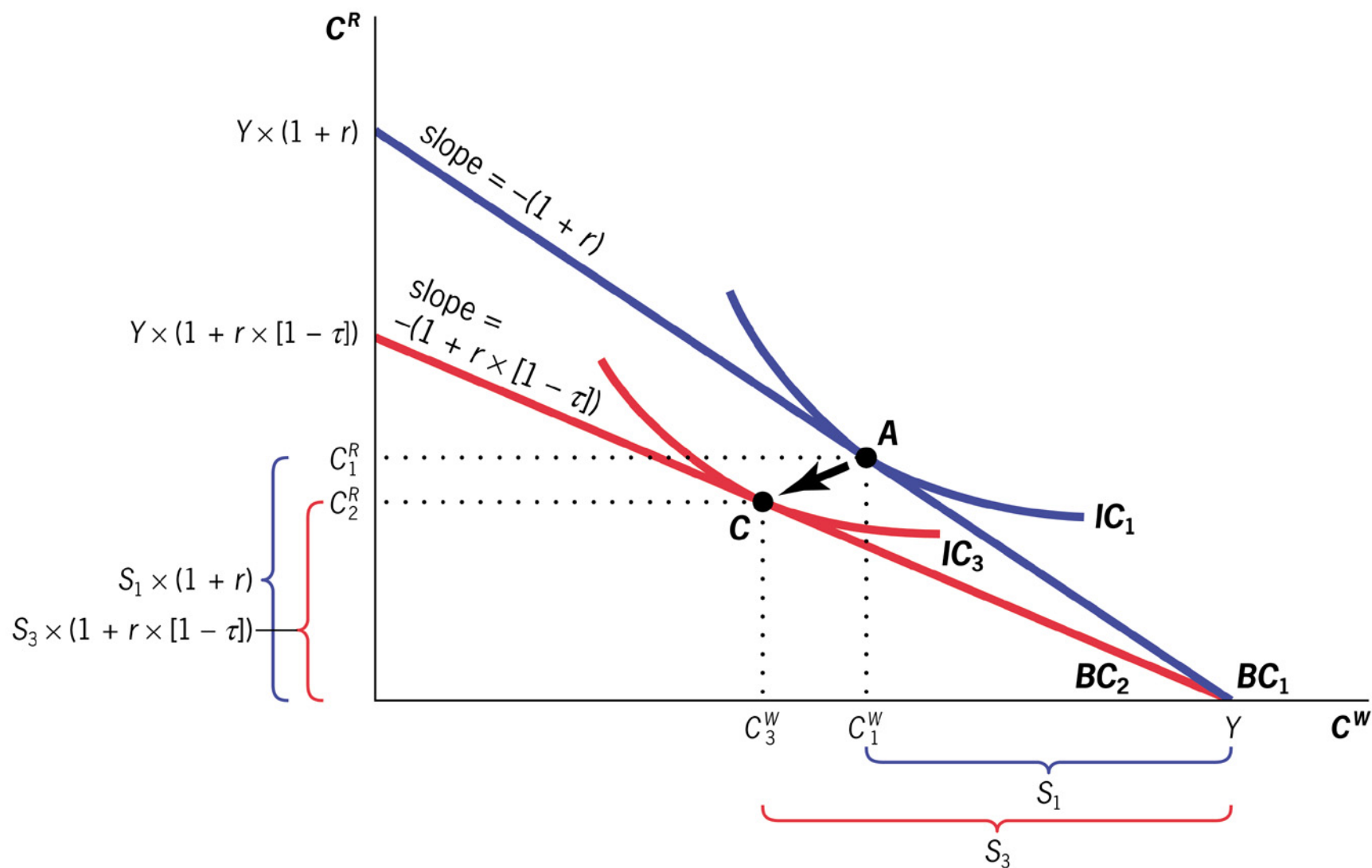
**Figure 22.1** Taxation and the Intertemporal Consumption Decision  
 Gruber: Public Finance and Public Policy, First Edition  
 Copyright © 2005 by Worth Publishers

(a) Substitution effect is larger



**Figure 22.2 (a)** Intertemporal Substitution Versus Income Effect  
 Gruber: Public Finance and Public Policy, First Edition  
 Copyright © 2005 by Worth Publishers

(b) Income effect is larger



**Figure 22.2 (b)** Intertemporal Substitution Versus Income Effect  
 Gruber: Public Finance and Public Policy, First Edition  
 Copyright © 2005 by Worth Publishers

■ TABLE 22-1

**Capital Taxation in an Inflationary Environment**

Case	Inflation	Tax rate on interest	Savings	Nominal rate	Interest earnings	After-tax resources	Price of skittles	Bags of skittles
No inflation	0%	0%	100	10%	\$10	\$110	\$1.00	110
	0%	50%	100	10%	\$10	\$105	\$1.00	105
Inflation	10%	0%	100	10%	\$10	\$110	\$1.10	100
	10%	50%	100	10%	\$10	\$105	\$1.10	95.5
Constant real rate	10%	0%	100	21%	\$21	\$121	\$1.10	110
	10%	50%	100	21%	\$21	\$110.5	\$1.10	100.5

**Table 22.1**

Gruber: Public Finance and Public Policy, First Edition  
Copyright © 2005 by Worth Publishers

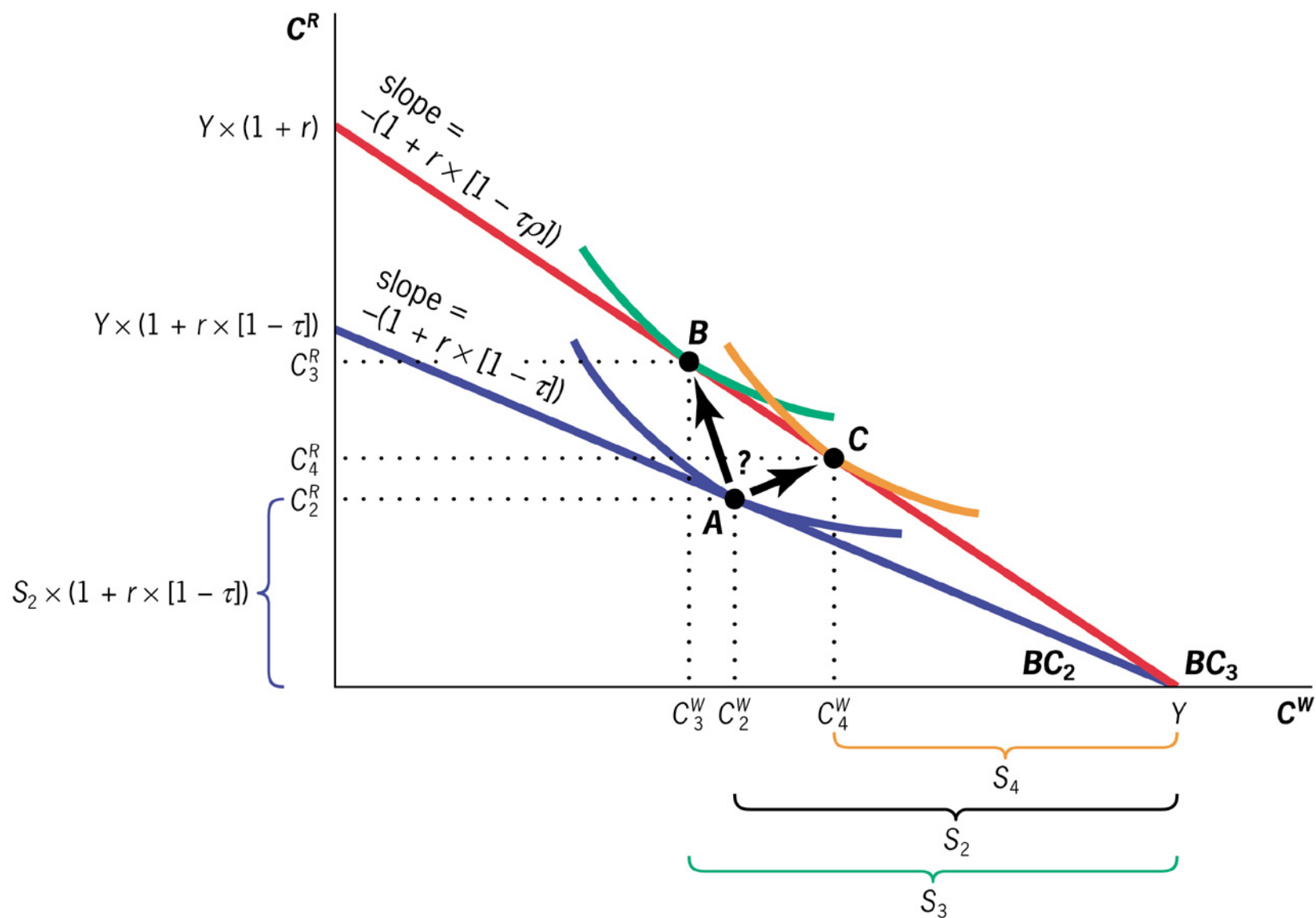
■ TABLE 22-2

**The Tax Advantage of IRA Savings**

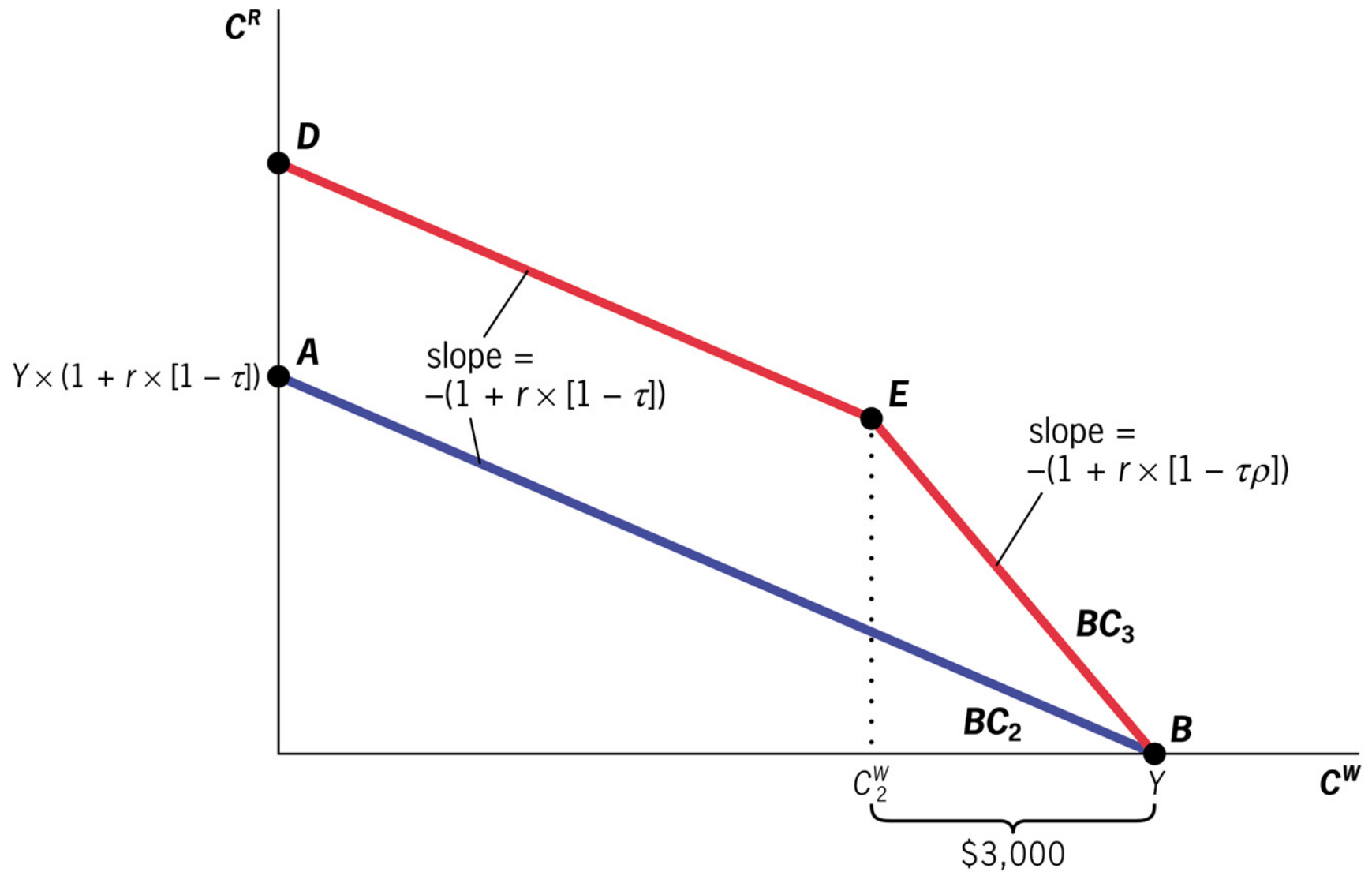
Account type	Earnings	Tax on earnings (tax rate = 25%)	Initial deposit	Interest earned (interest rate = 10%)	Taxes paid upon withdrawal	Total amount withdrawn
Regular	\$100	\$25	\$75	\$7.50	$0.25 \times (\$7.50) = \$1.88$	$\$75 + 7.50 - \$1.88 = \$80.62$
IRA	\$100	0	\$100	\$10	$0.25 \times (\$110) = \$27.50$	$\$100 + 10 - \$27.50 = \$82.50$

**Table 22.2**

Gruber: Public Finance and Public Policy, First Edition  
Copyright © 2005 by Worth Publishers

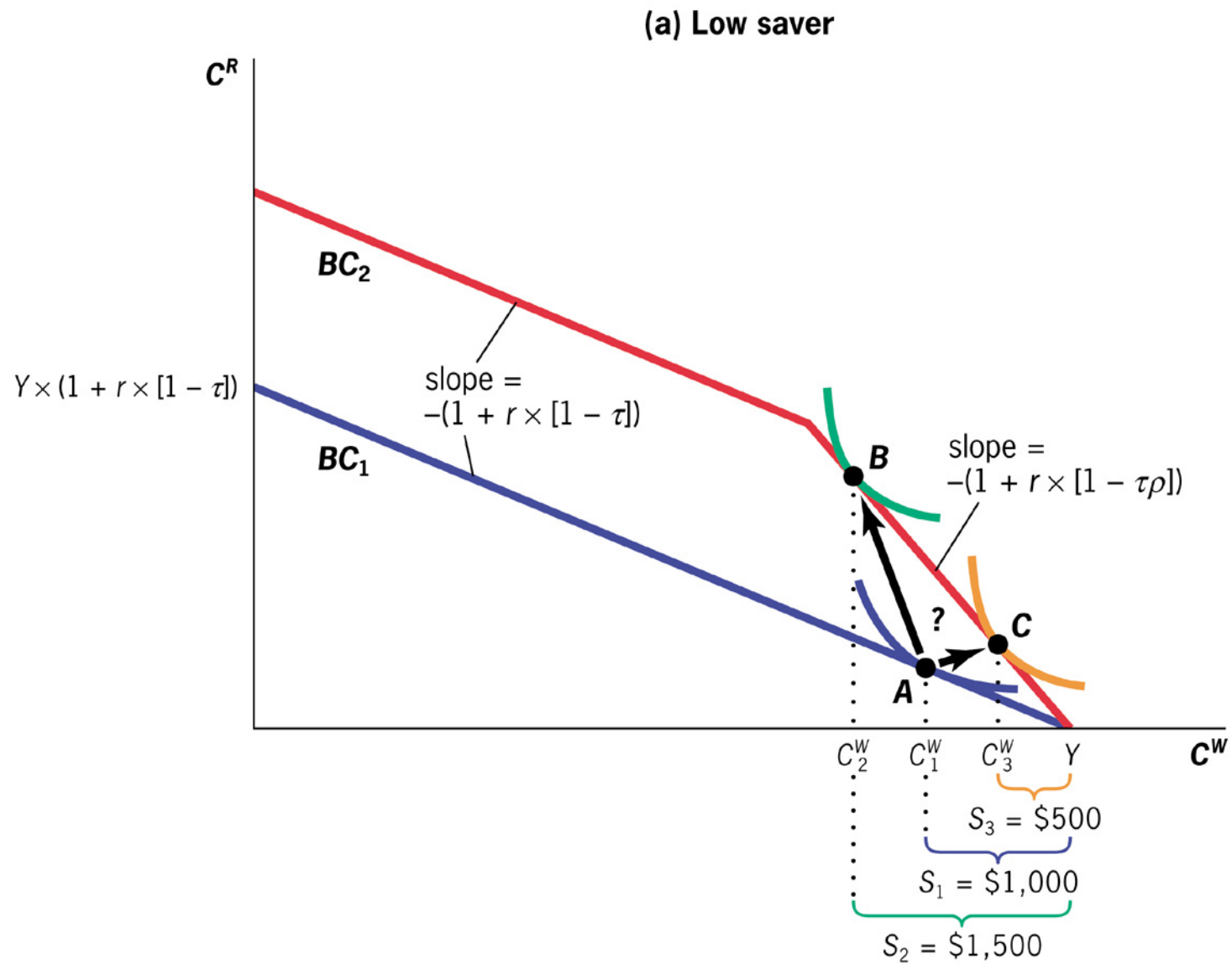


**Figure 22.3** Tax Subsidies and the Intertemporal Consumption Trade-off  
 Gruber: Public Finance and Public Policy, First Edition  
 Copyright © 2005 by Worth Publishers

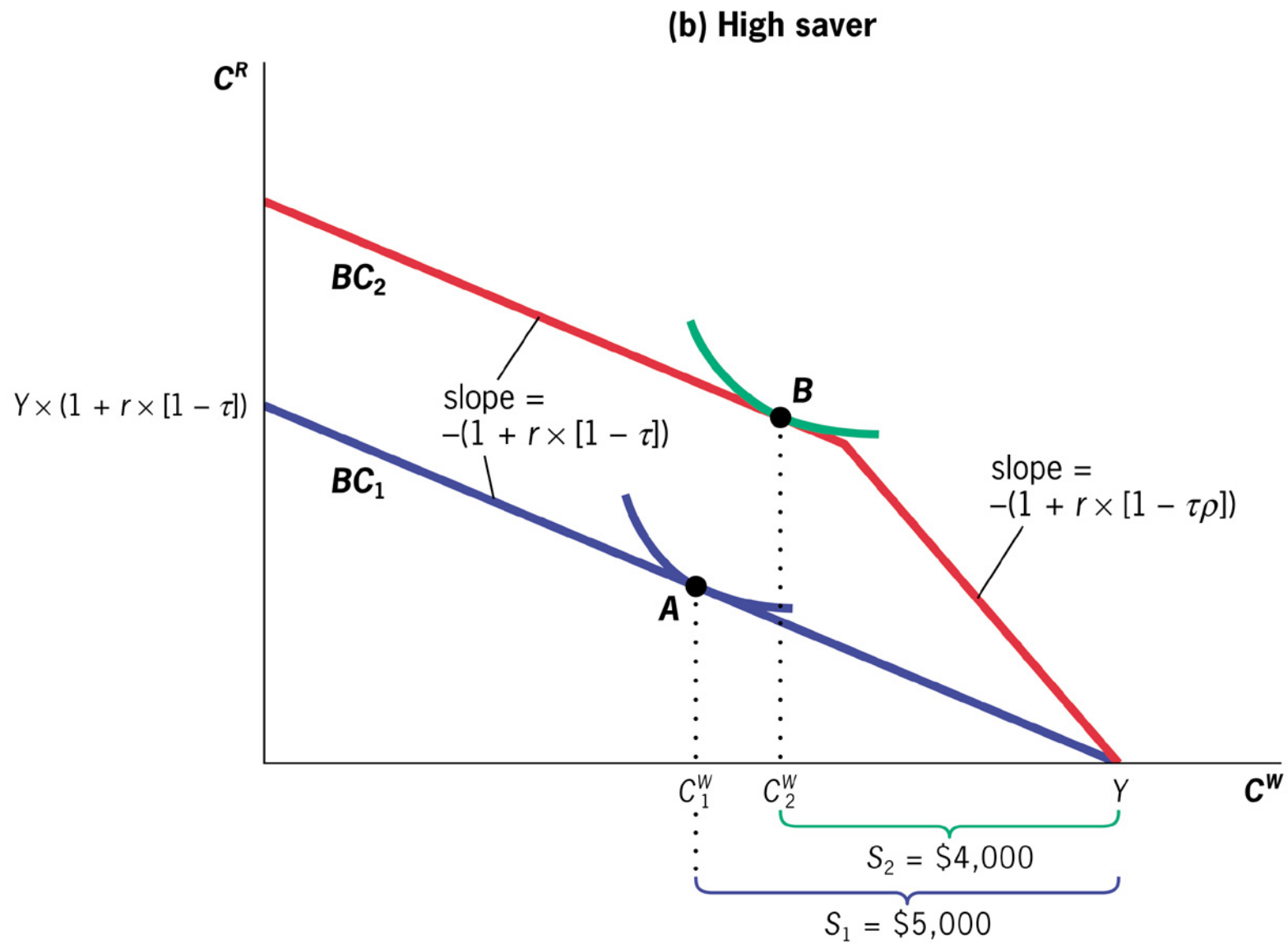


**Figure 22.4** IRAs and the Intertemporal Consumption Decision  
 Gruber: Public Finance and Public Policy, First Edition  
 Copyright © 2005 by Worth Publishers





**Figure 22.5 (a)** Low Savers Versus High Savers  
 Gruber: Public Finance and Public Policy, First Edition  
 Copyright © 2005 by Worth Publishers



**Figure 22.5 (b)** Low Savers Versus High Savers  
Gruber: Public Finance and Public Policy, First Edition  
Copyright © 2005 by Worth Publishers