

# **The Marginal Cost of Public Funds and Redistribution under Imperfect Competition\***

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## **Abstract**

This paper explores the marginal cost of public funds (MCPF) and redistribution under imperfect competition. If 100% profit taxation is available to the government, since the MCPF is less than one in the optimal linear wage tax system, the redistribution should be carried to the point where the equity gain by increasing the marginal tax rate is more than efficiency loss. However, for a profit tax rate smaller than 100%, the opposite result is obtained when the marginal propensity to consume is high. This result holds under comprehensive income taxation, where the wage and profit tax rates are the same.

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*Keywords:* Imperfect competition; Marginal cost of public funds; Income redistribution

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