

## 4. Gov't Social Insurance

# Origins of Social Insurance

- German social thinkers in 1870s: Lujo Brentano, Gustav Schmoller, Adolph Wagner. Stressed insurance principles.
- Otto von Bismarck's government: instituted sickness insurance (Krankenversicherung) 1883, accident insurance (Unfallversicherung) 1884, old-age insurance (Invaliden und Altersversicherung), 1889.
- Unemployment insurance, UK, Lloyd George, 1911.

# Gustav Schmoller Reviews 19<sup>th</sup> Century

“The triumph of insurance in every imaginable area was one of the century’s great advances in social progress. It was an entirely logical development that insurance spread from the upper classes to the lower classes, that it had to attempt, as far as possible, to eliminate poverty; and that the older charitable relief funds for the workers were more and more constructed on the sound principle of insurance.”

# Social (Governmental) Insurance

- Progressive Taxes (US 1913)
- Free public education and services
- Social Security: OASDI, Old Age, Survivors and Disability Insurance (US 1935)
- Health Insurance: Medicare, Medicaid (US, both 1965) US is only major developed country without comprehensive health insurance.
- Workers Compensation (US before 1920)

# Failure of First US Income Tax

- After Civil War, compliance declined, estimated that in 1872 only 10% of eligible taxpayers actually paid.
- Failure attributed to “incapacity of the lower officers and dishonesty of the higher ones.” (Harry Smith, *The United States Federal Internal Tax History from 1861 to 1871*, 1914. 94 282-96.
- Tax rescinded 1872

# Withholding of Income Taxes

- Important human engineering element of income tax system
- Endowment effect Thaler
- Fairness issues
- Underground economy flourishes where withholding is impossible.

# Survivors Insurance

- Created in 1939 Amendments to the Social Security Act
- Government life insurance
- For most people, bigger than their life insurance
- Surprising lack of opposition from insurance industry in 1939
- Framing: calling it survivors insurance

# Recap

- Public finance shares many aspects of private finance and insurance.
- Finance is always about incentivization in a risky world, people have purposes and fears, and they choose alternative financing methods to achieve them.
- First principle of this course: you should have purposes beyond making money, beyond abstract finance.