Reflections

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Requested purpose for this presentation

- Reflect on the academic contributions of the various papers at the conference
- Discuss key challenges faced in pursuing the policy implications of these contributions
- Given the far greater policy experience of the other three panelists, I'll focus on the academic contributions of these papers

Common element of many of the papers: optimal taxation

- Even with work by Saez and others, public finance research in the U.S. is largely empirical, and increasingly so as well in Europe.
- Refreshing to see continuing work on optimal taxation, with some papers extending past results and others exploring new questions.

Scheuer and Werning

- Helpful integration of two classic papers: Diamond and Mirrlees (1971) with Mirrlees (1971)
- Results aren't as "user friendly" as say the Diamond and Saez updates of Mirrlees, but valuable to be able to draw on the parallel insights in Diamond-Mirrlees.
- Here, I particularly like the extension analyzing an annual income tax in a lifecycle context.
  - Lifetime perspective on an individual's marginal utility of Y (subject to liquidity constraints)
  - Mutes excess burden, since changes in the timing of income generates an excess burden of $\Delta Y(\tau_t - \tau_{t-1})$

Heathcote, Storesletten, and Violante

- Helps resolve a puzzle why we don't see age-dependent taxes
  - This is a puzzle since labor supply elasticities seem to differ a lot by age.
  - Conesa and Krueger (2006) recommend taxing capital as second best way of taxing the young more heavily
- HSV's finding that little is gained through age-dependent taxes helps explain current law, and could reopen this past discussion on the case for taxes on capital income

Laroque and Pavoni

- Taxation of married couples another relatively neglected issue
  - Here, the tax law differs across countries, with joint taxation in the U.S. and largely separate taxation in Europe. Why?
- To what degree should policy deviate from separate taxation of each spouse?
  - The focus in this paper is the equity weights on one-earner vs. two-earner households
  - A conventional assumption is that welfare weights depend on each individual's likely earnings ability, ***given observables.***
  - With assortative mating, the "earnings ability" of the spouses are correlated. Actual earnings of one spouse can then be informative of the earnings ability of the other spouse.
  - Do (did) relative labor supplies of spouses differ more in the U.S. than in Europe??

Griffith, O'Connell, and Smith

- Careful attempt to think through how best to use the tax law to internalize spillovers from binge drinking.
- Tax law may not be the natural focus, though, to discourage binge drinking
  - When someone has already "had a few", they are likely oblivious to the price, even assuming they know it.
- Ideas in Bernheim and Rangel (2004) would be a useful addition to the discussion.
  - They hypothesize that behavior in "hot" and "cold" states can be very different. Can policy shift decision-making to a "cold" state, e.g. require that an evening's order be placed when first arrive at a bar, when most price elastic?

Bhandari, Evans, Golosov, Sargent

- Application of the optimal tax literature to macro policy-making
  - Formalize Musgrave's stabilization role for tax policy
  - In traditional macro approach, the economy is treated as a representative individual.
  - But income shocks during a recession are very heterogeneous, leading to potentially sharp falls in consumption for a few, but little change for most households
    - Benefits of overall stabilization now much larger
    - But valuable to target policies on the subset of people suffering the sharp falls in consumption, implying a different policy mix.
  - To my mind, this is an exciting area for new research,

Giupponi and Landais

- That income shocks are very heterogeneous could in part be due to policy distortions, e.g. subsidies to layoffs from UI programs.
- Short-term work programs (SWP) a useful new focus for applied research, as a supplement to UI programs
- How should these two programs be coordinated?
  - Without full experience rating, UI induces too many layoffs. (Compensate with administrative restrictions on layoffs.)
  - With experience rating, firms have an incentive to shut down, to avoid future liabilities for current layoffs.
  - To what degree are SWP less subject to these distortions, enabling an easing of administrative restrictions on layoffs

Smith, Yagan, Zidar, Zwick

- Distinguishing between capital and labor income requires care, a point that very much merits emphasis
  - Easy for managers to reclassify a return to labor as capital gains or dividends on corporate equity for tax purposes. (Used by Simon to justify a Comprehensive Income Tax.)
- To what degree is reported business income reclassified labor income??

Smith, Yagan, Zidar, and Zwick

- One traditional approach (used in dual income taxes):
  - Investments assumed to earn a market return. Labor income then equals $\Pi - rK$. (What is the right r??)
- Two new tests in this paper for the degree to which growing profits in fact represent growing labor income:
  - Profits grow due to higher profit *rate* rather than expansion in size of firm?
  - Drop in profits following death of an entrepreneur
  - Regardless, income on an entrepreneur's shares can still largely represent a return to his past entrepreneurial effort, so largely represent labor income.
- Third test: Measure above-normal returns on equity held by insiders in a firm?

Akcigit, Grigsby Nicholas, and Stantcheva

- That taxes discourage any given economic activity (R&D in this paper) seems entirely conventional.
- But I find their results puzzling for a variety of reasons.

Akcigit, Grigsby Nicholas, and Stantcheva

- One key complication is that, with R&D, income can easily (and often does) accrues in a different location than R&D expenses.
- In theory, want expenses in a high-tax jurisdiction and income in a low-tax jurisdiction
- If tax rates equal, they are neutral given that R&D can be expensed
- But taxes *encourage* R&D to the extent that these two tax rates differ, leading to more R&D in high-tax states.

Akcigit, Grigsby Nicholas, and Stantcheva

- Net payoff equals: $(1-x)P-(1-t_s)R\&D$, where x is
  - g if inventor sells the firm, once patent acquired.
  - ~ 0 if inventor shifts patent to a subsidiary in a tax haven.
  - t_j if inventor relocates to state j once production begins.
- Here, innovation encouraged to extent $t_s > x$, so should be higher in high-tax states.
- May still expect high-income individuals to avoid high-tax states. Perhaps relocation easier for those working in R&D, e.g. Bell Labs located in Murray Hill.

Akcigit, Grigsby Nicholas, and Stantcheva

- Incentive to locate patent in a tax haven, and then set royalties to shift all firm profits to this tax haven.
- Producing firm then gains from locating in a high-tax jurisdiction.
  - But externalities likely come from production rather than location of patent.
- Another complication is effects of taxes on liquidity constraints and risk-bearing costs, issues mainly for start-ups.

Remaining papers

- Sorry for neglecting some of the papers
- I wasn’t able to find these on the web prior to the conference, and didn’t want to put down reactions now while very jet lagged!