INTRODUCTION

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Just after the passage of the Tax Reform Act of 1986, the NBER inaugurated an annual conference designed to facilitate an exchange of ideas between public finance scholars and those in industry and government who are directly involved in the tax policy-making process. The Tax Policy and the Economy conference, which celebrates its tenth anniversary this year, is devoted to the presentation of new research findings of relevance for tax policy analysts.

Fundamental changes in federal tax and expenditure policies appear more likely today than at any point in the last 10 years. Discussions of drastically changing or even eliminating the federal income tax, and of far-reaching changes in major federal entitlement programs, have moved from the fringes to the center of the national policy agenda. The outcomes of these current debates are uncertain, but it is clear that this is a critical moment for research input to the policy-design process. The five papers in this volume represent a cross section of some of the best applied research that bears on current deliberations about tax and expenditure policy. Each paper provides new data and new insights on an important policy issue.

The first paper, “Privatization of Social Security: How It Works and Why It Matters,” by Laurence J. Kotlikoff, is directed at a broad class of proposals for social security reform. Kotlikoff first describes the key elements of any proposal that would replace the current pay-as-you-go social security system with a system of mandatory private retirement savings accounts. He then uses a dynamic general equilibrium model, with parameter values chosen for rough consistency with the current U.S. economy, to evaluate the economic consequences of privatization.
The paper considers the short-term and long-term effects of privatization on capital accumulation, on the level of aggregate output, and on the relative well-being of individuals in different generations. The results show that privatization can generate long-run increases in output and per capita income, but that individuals who are alive at the time of the privatization may be worse off as a result of these reforms. The paper also succeeds in identifying a number of research issues where further work is needed both in designing privatization proposals and in evaluating their effects.

Don Fullerton's paper, "Why Have Separate Environmental Taxes?," compares the structure of current U.S. environmental excise taxes with the types of taxes that optimal tax design principles would dictate. Fullerton concludes that existing taxes, which are typically levied at low rates relative to the value of the taxed products, impose high administrative costs relative to the revenue they collect. He also observes that these taxes are not levied on the basis of any objective measure of the environmental damage. Thus, the current tax structure bears little resemblance to the optimal tax structure that would result from including an explicit consideration of environmental damage in a standard tax design framework.

The third paper, by Robert E. Hall, provides a comprehensive summary entitled "The Effects of Tax Reform on Prices and Asset Values." This paper considers a range of consumption tax alternatives to the current personal income tax, including value-added taxes, retail sales taxes, a progressive consumed income tax, and the Hall-Rabushka flat tax proposal. Hall considers how each of these proposals would affect the price level, the real wages earned by workers and paid by firms, the market value of existing assets, and the saving and investment incentives facing households and firms. The paper clarifies much of the previous discussion on each of these topics and highlights the behavioral parameters that are the central determinants of the effects of fundamental tax reform. It also emphasizes differences between the alternative methods of implementing a consumption tax, particularly in the adjustments to nominal wages and nominal prices that would be required to restore equilibrium after tax reform.

Martin Feldstein and Daniel Feenberg's paper, "The Effect of Increased Tax Rates on Taxable Income and Economic Efficiency: A Preliminary Analysis of the 1993 Tax Rate Increases," presents a preliminary analysis of the revenue consequences of the 1993 increase in marginal tax rates on high-income households. This tax increase raised the top marginal income tax rate from 31% to 39.6% for households with taxable incomes in excess of $250,000 and from 31% to 36% for those with incomes between $140,000 ($115,000 for single filers) and $250,000. Feldstein and Feenberg
compare preliminary information from Internal Revenue Service data on 1993 taxable income reported by taxpayers in different taxable income classes with comparable data from 1992. They conclude that 1993 taxable income for the highest income groups was substantially less than one would have expected on the basis of this group’s 1992 taxable income and the overall rate of economic expansion between 1992 and 1993. While definitive measurement of the revenue effects of the 1993 tax bill requires panel data on the taxable income of the same individual in several different years, the Feldstein–Feenberg results suggest that the 1993 tax reform may have raised less revenue than at least some analysts expected it to. If the revenue gain from the 1993 act was small, then its efficiency cost is likely to have been high because the act substantially raised marginal tax rates for high-income households.

The last paper, Nada Eissa’s study, “Tax Reforms and Labor Supply,” describes the evidence on how taxation affects labor supply that has emerged from recent studies of U.S. income tax reforms. The paper begins by describing the author’s previous work on taxation and labor supply. This includes work on how the Economic Recovery Tax Act of 1981 and the Tax Reform Act of 1986 (TRA) affected the labor supply of married women and on how revision of the Earned Income Tax Credit (EITC) rules in the early 1990s affected labor supply. The evidence for both the TRA and the EITC suggests a substantial labor force participation and hours-of-work response by women whose after-tax wage rates increase as a result of tax policy. Eissa’s paper complements this summary of previous work by presenting new evidence on the effect of the 1981 and 1986 tax reforms on men’s labor supply. The evidence suggests relatively small tax effects, if any, on men.

The papers in this volume contribute to a continuing and improving interaction between academics and policymakers concerned with tax policy. In some cases they reflect suggestions of previous Tax Policy and the Economy conference participants with respect to topic choice. In others they represent an attempt to bring current research, and the scholars who are conducting it, into close proximity with the policymaking community. The number of participants in the Washington meeting at which these papers were presented exceeded that at any previous Tax Policy and the Economy meeting. This provides at least some testimony to the value that industry and government tax policy experts place on the dialogue that this conference permits.
Many individuals played a key role in planning and organizing this tenth annual NBER meeting on Tax Policy and the Economy. Martin Feldstein, President of the NBER, was a key proponent of these meetings at their beginning, and he has been an active supporter of this annual conference throughout the last decade. Deborah Mankiw, the NBER's Director of Corporate and Foundation Relations, and Liz Cary helped throughout the conference planning process. The NBER Conference Department, particularly Conference Director Kirsten Foss Davis and Lauren Lariviere, managed the daunting task of ensuring that the papers were prepared and distributed in a timely fashion and handled the complex logistics for a large but very efficient conference in Washington, D.C. Deborah Kiernan shepherded the manuscripts through the prepublishation process with her usual speed and attention to detail.

I am also grateful to Deputy Treasury Secretary Lawrence Summers, who spoke at the conference luncheon and reflected on developments in U.S. tax policy in the 10 years since he organized the first Tax Policy and the Economy meeting.

Finally, I wish to thank each of the authors whose papers are included in this volume for striving to communicate their important research findings to a largely nonacademic audience. I appreciate their efforts and willingness to participate in this very important opportunity for interchange between academics and policymakers.