The five papers in this issue of Tax Policy and the Economy are all directly related to important issues concerning the U.S. tax system, its transfer system, and their effects on productivity, charitable giving, and the distribution of firm sizes.

In the first paper, Shepard, Baicker, and Skinner note increasing recent interest in expanding Medicare coverage, often through so-called “Medicare for All” plans. Traditional Medicare in the U.S. covers a uniform set of benefits for all enrollees that is much more generous than public plans in nearly all other developed countries, but over time the efficiency costs of this uniform structure has grown substantially. Focusing on the elderly Medicare population, the authors develop an economic framework to assess the potential efficiency and equity gains from reforming Medicare’s current benefit designs. They argue that there is an inherent inefficiency in providing a uniform benefit to all enrollees because those with higher incomes might prefer a more generous insurance plan than those with lower incomes, who might prefer more money income coupled with a less generous plan. Shepard et al. show that three major shifts have increased this cost of uniformity since Medicare began in 1965: rising income inequality, expanding availability of expensive medical technologies, and increasing costs of financing the program. They then study optimal plans, finding that the optimal uniform Medicare benefit would be substantially less generous than the current plan, and that an alternative design with a basic insurance plan that could be supplemented with additional benefits – as seen in many other countries – would generate even higher social welfare benefits. Such a plan may
appear less equitable, but the authors demonstrate that the resulting Medicare savings could be
distributed in a manner that raised social welfare at all income levels.

In the second paper, Beshears, Choi, Iwry, John, Laibson, and Madrian provide a detailed
discussion of the potential of employer-sponsored rainy day savings accounts. Noting that
roughly half of Americans live paycheck to paycheck and that, when financial shocks occur
during their working lives, many of these households tap their retirement savings accounts, the
authors explore the practical considerations and challenges associated with helping households
accumulate liquid savings that can be deployed when urgent pre-retirement needs arise. In
particular, they consider plans that would allow employers to automatically enroll workers into
an employer-sponsored payroll deduction “rainy-day” or “emergency” savings account. They
argue that having separate rainy-day and retirement savings accounts can facilitate greater saving
for short- and long-term purposes by helping to psychologically segregate and catalyze these two
motives to save, and that auto-features and mental accounting can be jointly deployed to reduce
the frequency with which short-term needs crowd out long-run retirement savings. Beshears et
al. describe three specific implementation options: (a) after-tax employee 401(k) accounts; (b)
deemed Roth IRAs under a 401(k) plan; and (c) depository institution accounts. They present
pros and cons of each approach, given the existing regulatory regime, relative to the following
criteria: the ability to automatically enroll employees into the rainy-day account; the targeted size
of the rainy-day account; the investment allocation used for the rainy-day account; the fees and
expenses associated with setting up and administering the rainy-day account; employers’ ability
to match employee contributions to the rainy-day account and the destination of those matching
contributions; the ability of the rainy-day account to provide liquidity when the funds are needed;
the tax treatment of contributions to, earnings in, and withdrawals from the rainy-day account;
the portability of account balances when employees separate from a sponsoring employer; and
compliance and potential interactions with the nondiscrimination rules that apply to tax-qualified
employer-sponsored plans. They conclude that field-testing would provide important new
information on the performance of each of these options and that new legislation would be
needed to address some of the drawbacks with each approach.

Robert J. Barro and Brian Wheaton, in the third paper, return to the issue of the effect of
corporate legal form in the tax system, considering its effect on productivity. The authors note
that there are differences in the tax liability between businesses organized as C-corporations and
those organized as pass-through entities such as S-corporations, limited liability companies
(LLCs), and partnerships. Corporate versus pass-through status trades off benefits (perpetual
identity, limited liability, public trading, earnings retention) against tax wedges, and incentives to
organize in one form or another are affected by a tax wedge. Barro and Wheaton show that
those wedges have changed over time and were affected by the Tax Cut and Jobs Act of 2017
(TCJA), which lowered the tax rate on C-corporations while also liberalizing some rules on
taxation of pass-through entities. They note that changes in the tax wedge may affect not just
the choice of organizational form, but also productivity in the economy. They then go on to
assemble a data set that charts the changes in the tax wedge over time, the share of economic
activity going through C-corporate versus pass-through form, and measures of productivity.
Their results show that the tax wedge has declined, on average, over time, implying that the C-
corporation form has been increasingly favored. In further work using regression analysis, they
find that C-corporate economic shares decline with the wedge and exhibit negative trends that
they relate to legal changes for LLCs. A model which they calibrate to observed total factor
productivity (TFP) and C-corporate shares implies that, for 1958-2013, the declining wedge and
the gap between corporate and pass-through productivity contributed 0.37% per year out of a total TFP growth rate of 1.09%. From 1994 to 2004, when the TFP growth rate was unusually high—2.00% per year—they find the contribution from the falling productivity gap to have also been unusually large—0.77% per year.

In the next paper, Meer and Priday consider the effect of the 2017 TCJA on charitable giving. The authors note that the U.S. tax code subsidizes charitable giving through the itemized deduction, with the justification that charitable organizations may provide valuable societal services while being more responsive than the government. They argue that the degree to which donations are responsive to the tax incentive is a crucial one, especially in light of the changes introduced by the TCJA, especially its reduction in marginal tax rates and substantial increases in the standard deduction. They note that the former directly changes the tax price of charitable giving – that is, the net cost of donating a dollar after accounting for the tax subsidy – while the latter reduces the number of taxpayers who are eligible for that subsidy. Meer and Priday provide estimates of the responsiveness of charitable giving to its tax price using newly-updated data, then apply those estimates to the parameters of the TCJA. Consistent with previous findings, they find that giving is sensitive to its tax treatment, with a 10 percent increase in the tax price of giving expected to reduce giving by about 10.4 percent. They find that the TCJA should be expected to reduce giving by a significant amount for households that stop itemizing as a result of the policy, and that increases in disposable income resulting from the reduction in tax liability offset a small proportion of this projected reduction.

In the final paper, Mulligan provides a new study of the effect of the employer mandate in the 2010 Affordable Care Act (ACA). Mulligan notes that taxes and regulations are known to affect the size distribution of businesses because smaller businesses are less subject to
enforcement. The author argues that large informal sectors are an obvious result in developing
countries but that measurement challenges have hindered quantifying the size distortions’ impact
on developed-country employment and productivity. His analysis uses new and unique data that
are readily linked to a specific regulation: the ACA’s employer mandate, which establishes a
bright-line legal definition of a “large” business at 50 full-time equivalent employees. He reports
on the results of a new survey of 745 small businesses which shows little change in the size
distribution of businesses between 2012 and 2016, except among businesses with 40–74
employees, in a way that is closely related to whether they offer health insurance coverage.
Using measures of both size and voluntary regulatory compliance, he then links these changes to
the Affordable Care Act’s employer mandate. As of 2017, he finds that between 28,000 and
50,000 businesses nationwide appear to be reducing their number of full-time-equivalent
employees to below 50 because of that mandate. This translates to roughly 250,000 positions
eliminated from those businesses. He concludes that the amount and character of distortions
going forward may be different if the mandate proves to be exceptionally difficult to enforce.