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INTRODUCTION

The NBER Tax Policy and the Economy conference is now in its thirteenth year. The goal of this somewhat unusual conference is to communicate new research findings in the areas of taxation and government spending to interested policymakers in industry and government. The interplay between research and policymaking is evident in the fields of taxation and government expenditure program design. I like to believe that the Tax Policy and the Economy meetings have strengthened this link by providing greater visibility for the central findings of new academic research projects.

There have been many changes in the years since the Tax Policy and the Economy series began. Federal budget deficits have been replaced by surpluses, the top marginal tax rate in the federal income tax has declined and then risen, and social security reform has changed from being the "third rail" of Washington politics to being one of the most-debated policy issues in the nation. These shifts in the focus of policy debate are reflected in the emphasis of the papers that make up this volume. Two of the five papers presented at this year's meeting were concerned with social security. Another focused on the Medicare program. The remaining papers addressed two long-standing tax policy questions, namely the taxation of tobacco products and the economic effects of tax exemption for non-profit organizations. Each paper addresses a concrete question in tax policy or the design of expenditure programs, and presents empirical evidence that is directly relevant to the issue at hand. Taken together, the papers testify to the ongoing intellectual exchange between academic public finance researchers and the policy-making community.

The first paper, by William Evans, Jeanne Ringel, and Diana Stech, considers "Tobacco Taxes and Public Policy to Discourage Smoking." This paper presents new evidence on how excise taxes on tobacco products affect the consumer prices of these products, and thereby addresses the basic question of tax incidence. The empirical results, based on careful analysis of cigarette tax changes in various states, suggests that roughly the full amount of the excise-tax change is passed through to consumers. The authors also use these tax changes to develop new estimates of the price elasticity of demand for cigarettes. The point estimates vary depending upon details of the econometric specification, but the central estimate is approximately −0.40. The paper also explores the external costs of smoking. The authors calculate when a smoker smokes a pack of cigarettes, he or she imposes costs of between 40 and 70 cents on society at large. Estimates like this provide an important input in the design of tobacco tax policy.

James Hines is the author of the second paper, "Non-Profit Business Activity and the Unrelated Business Income Tax." This paper addresses a long-standing topic in income tax policy: what are the consequences of corporate income taxation of the "unrelated business activities" of non-profit organizations? The Unrelated Business Income (UBIT) was introduced in 1950. While 501(c)(3) organizations reported revenue of nearly $425 billion in 1994, their UBIT liability was less than $200 million. This tax was paid by the subset of non-profit organizations that reported positive UBIT, but the aggregate UBIT was actually negative in 1994. (Net UBIT was $−1.1 billion.) Hines uses data from the form 990-T filings of organizations with UBIT to explore the characteristics of organizations that report UBIT. He finds a negative correlation between UBIT and other sources of revenue for non-profit organizations. While larger organizations are more likely to report UBIT, those with more income from contributions or grants are less likely (other things equal) to report UBIT. This finding represents a first step toward analyzing the economic effects of the UBIT, and toward modeling how non-profit organizations respond to this tax.

The third paper, by Julie Lee, Mark McClellan, and Jonathan Skinner, considers "The Distributional Effects of Medicare." The paper uses a new longitudinal data set on Medicare beneficiaries over the 1990–1995 period to analyze the distribution of Medicare outlays by the lifetime income category of the recipients. The results show a sharp increase during the 1990s in the share of Medicare expenditures on behalf of low-income beneficiaries. The authors try to explain this change. It appears that rapid growth in Medicare expenditures for home health care is a crucial factor in the changing distribution of outlays. Home health care spending appears to be concentrated among those with lower lifetime incomes; its growth is also concentrated in several states. The findings in this paper suggest that it is difficult to make sweeping generalizations about the pattern of benefits from Medicare, and that this pattern can change over time. The research does not address the question of how health outcomes are affected by Medicare spending; that is the next step in the authors' proposed research program.

The last two papers explore related issues concerning the distributional effects of the current social security system and potential changes in this system. The fourth paper, "Social Security's Treatment of Postwar Americans," was prepared by a group of six collaborators: Steven Caldwell, Melissa Favreault, Alla Gantman, Jagadeesh Gokhale, Thomas Johnson, and Laurence Kotlikoff. This paper uses a detailed social security benefit calculator, along with a complex demographic simulation model (CORSIM), to consider the net lifetime transfers that social security provides to different cohorts and different income groups. Net lifetime transfers are defined as the present discounted value of lifetime benefits minus the present discounted value of lifetime payroll taxes. The CORSIM model is used to impute marriage and divorce rates, death rates, and fertility rates (which can matter for survivor's benefits) to individuals in different lifetime income groups.

The results suggest that the effects of a progressive benefit structure dominate the regressive payroll tax structure in determining the net distribution of social security benefits. The present value of social security benefits, net of taxes, is generally larger for low-income workers than for those with higher incomes. It is generally higher for men than for women. The paper also shows that there has been a dramatic increase in the net present value of taxes, or alternatively, a decline in the internal rate of return on social security contributions less benefits, over the postwar period. The paper notes the importance of prospective changes in the social security system in determining the net tax burden of currently-young generations, and suggests that current official projections of Social Security Trust Fund deficits may understate the actual severity of future shortfalls.

The last paper, "Distributional Impacts of Proposed Changes to the Social Security System," was written by Julia Coronado, Don Fullerton, and Thomas Glass. These authors consider the impacts of various policy changes on the net lifetime benefits associated with the social security system. They use a somewhat different procedure than the previous authors to estimate the lifetime income profiles of various households, but they perform a similar exercise in computing the present value of lifetime benefits net of lifetime taxes. They also allow mortality rates of potential beneficiaries to vary as a function of their lifetime income. There is substantial empirical evidence that mortality rates are higher for individuals in low-income households than for their higher-income counterparts. This mortality effect blunts the net progressivity of the benefits paid by the social security system, since even though benefits in each year are progressive across income groups, those in the highest income groups are more likely to receive benefits for many years.

The authors demonstrate that the current social security system exhibits only a limited degree of progressivity, and they then consider how various changes to the existing social security benefit rules would affect progressivity. They consider changes in the calculation of the primary insurance amount, such as eliminating the dropping of low-earning years in the current law, changes in the social security retirement age, and changes in actual benefit levels. They explore how these reforms would influence the net progressivity of lifetime social security benefits net of taxes, and they indicate what parameters would most directly affect the distributional pattern associated with such changes.

The papers in this volume illustrate the type of policy-relevant research that is carried out by the affiliates of the NBER Public Economics Program. The paper on tobacco taxes presents new regression estimates that provide key behavioral response parameters that affect policy design. The papers on UBIT and Medicare report summary tabulations from large data sets: the IRS Form 990 filings in the first case, and Medicare beneficiary records in the second. These tabulations provide important background information for policy analysis and for further research. Finally, the papers on social security develop complex simulation models that can be used to evaluate a wide range of different policy reforms. I hope that each of these papers will provide useful input to various participants' policy processes who are concerned with tax and expenditure program design.

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In planning and organizing the thirteenth Tax Policy and the Economy meeting, I have incurred debts to many individuals. Martin Feldstein, president of the NBER, has been an active supporter of this conference since its beginning more than a decade ago. Liz Cary, the coordinator of corporate and foundation relations at the NBER, has been very helpful in communicating information about the conference to interested potential participants. This marks Liz's last year at NBER, and her assistance with this conference will be missed. The NBER Conference Department, particularly conference director Kirsten Foss Davis and Rob Shannon, organized the conference logistics with their usual efficiency and extraordinary good cheer. Helena Fitz-Patrick oversaw the publication process with good cheer and outstanding attention to detail.

I am also grateful to Jeffrey Frankel, an NBER Research Associate currently on leave as a member of the President's Council of Economic Advisers, who delivered the luncheon address at the conference. His talk provided many important insights into the public economics problems that arise in global environmental policy, with particular reference to tradable permits for carbon dioxide emissions.

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