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TAPES 2014

Trans-Atlantic Public Economics Seminar

Personal Income Taxation and Household Behavior

June 16 - 18, 2014

Institute for Advanced Studies, Vienna

SCIENTIFIC PROGRAM

MONDAY, June 16, 2014

Session 1: **TAXES AND HOUSEHOLD LABOR SUPPLY RESPONSES**
Chair: Christian Keuschnigg, IHS

1.30 - 2.00	*Registration, Welcoming Remarks*
2.00 - 3.15	**Female Labour Supply, Human Capital, and Welfare Reform** MONICA COSTA DIAS, Institute for Fiscal Studies, Richard Blundell, University College London and Institute for Fiscal Studies, Costas Meghir, Yale University and Jonathan Shaw, Institute for Fiscal Studies Discussants: James Poterba, MIT, Andreas Peichl, ZEW
3.15 - 4.30	**Labor Force Participation Elasticities of Women and Secondary Earners Within Married Couples** SHANNON MOK, Congressional Budget Office, Robert McClelland, Congressional Budget Office, and Kevin Pierce, Internal Revenue Service Discussants: Simon Loretz, IHS, Monica Costa Dias, Institute for Fiscal Studies
4.30 - 4.45	*Coffee / Tea*
4.45 - 6.00	**The Elasticity of Deferred Income with respect to Marginal Income Tax Rates** ASPEN GORRY, Utah State University, Kevin Hassett, American Enterprise Institute, R. Glenn Hubbard, Columbia University, and Aparna Mathur, American Enterprise Institute Discussants: Martin Feldstein, Harvard, Shannon Mok, Congressional Budget Service

TUESDAY, June 17, 2014

Session 2: **TAXES AND OTHER HOUSEHOLD RESPONSES**
Chair: James Poterba, MIT

8.30 - 9.45	**Capital Gains Taxes and Realizations: Evidence from a Long Panel of State-Level Data** JON BAKIJA and William Gentry, Williams College Discussants: Aspen Gorry, Utah State University, Michael Devereux, Oxford
9.45 - 11.00	**How responsive are deductions to tax rate changes?** ANDREAS PEICHL, ZEW, University of Mannheim & IZA, Philipp Dörrenberg, and Sebastian Siegloch, IZA Bonn Discussants: Roger Gordon, UCSD, Jarkko Harju, Government Institute for Economic Research
11.00 - 11.15	*Coffee / Tea*
11.15 - 12.30	**Voluntary Disclosure of Evaded Taxes – Increasing Revenues, or Increasing Incentives to Evade?** DOMINIKA LANGENMAYR, University of Munich Discussants: Joel Slemrod, Michigan, Stephanie Sikes, Wharton
12.30 - 1.45	*Lunch*

Session 3: **RETIREMENT PLAN PROVISIONS AND HOUSEHOLD BEHAVIOR**
Chair: Martin Feldstein, Harvard

1.45 - 3.00	**Does Front-Loading Taxation Increase Savings? Evidence from Roth 401(k) Introductions** BRIGITTE MADRIAN, Harvard, John Beshears, Harvard, James Choi, Yale, and David Laibson, Harvard, Discussants: Amy Finkelstein, MIT, Michelle White, UCSD
3.00 - 3.15	*Coffee / Tea*
3.15 - 4.30	**Do Required Minimum Distributions Matter?The Effect of the 2009 Holiday on Retirement Plan Distributions** JAMES POTERBA, MIT, Jeffrey Brown, Illinois, and David Richardson, TIAA-CREF Institute Discussants: William Gentry, Williams, Brigitte Madrian, Harvard

Dinner Speech
Political Economy of Redistribution and Economic Reforms in Russia
SERGEI GURIEV, New Economic School, Moscow and Sciences Po, Paris

WEDNESDAY, June 18, 2014

Session 4: **PERSONAL TAXES AND FIRM BEHAVIOR**
Chair: James Poterba, MIT

8.00 - 9.15	**The Elasticity of Taxable Income and Income-Shifting: What is 'Real' and What is Not?** JARKKO HARJU, Government Institute for Economic Research, and Matikka Tuomas, Government Institute for Economic Research Discussants: Doina Radulescu, Zürich, Martin Jacob, Otto Beisheim School of Management
9.15 - 10.30	**Cross-Country Evidence on the Relationship between Capital Gains Taxes, Risk and Expected Returns** STEPHANIE SIKES, Wharton, Luzi Hall, Wharton, and Clare Wang, Kellogg Discussants: Katharina Erhardt, Zürich, Max von Ehrlich, Zürich
10.30 - 10.45	*Coffee/Tea*
10.45 - 12.00	**Do Dividend Taxes Affect Corporate Investment?** MARTIN JACOB, Otto Beisheim School of Management and Annette Alstadsaeter, Oslo Discussant: Christian Keuschnigg, IHS, Alan Auerbach, Berkeley
12.00 - 1.15	**Personal Income Taxes, Corporate Profit Taxes, and the Heterogeneous Tax Sensitivity of Firm-Level Investments** KATHARINA ERHARDT, ETH Zürich, Peter Egger, ETH Zürich, Christian Keuschnigg, IHS Discussants: Dominika Langenmayr, University of Munich, Harry Huizinga, Tilburg University

Female Labour Supply, Human Capital and Welfare Reform
Richard Blundell, Monica Costa Dias, Costas Meghir, and Jonathan M. Shaw
NBER Working Paper No. 19007
May 2013
JEL No. H2,H3,I21,J22,J24,J31

ABSTRACT

We consider the impact of Tax credits and income support programs on female education choice, employment, hours and human capital accumulation over the life-cycle. We thus analyze both the short run incentive effects and the longer run implications of such programs. By allowing for risk aversion and savings we are also able to quantify the insurance value of alternative programs. We find important incentive effects on education choice, and labor supply, with single mothers having the most elastic labor supply. Returns to labour market experience are found to be substantial but only for full-time employment, and especially for women with more than basic formal education. For those with lower education the welfare programs are shown to have substantial insurance value. Based on the model marginal increases to tax credits are preferred to equally costly increases in income support and to tax cuts, except by those in the highest education group.

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Labor Force Participation Elasticities of Women and Secondary Earners within Married Couples

Rob McClelland*
Shannon Mok*
Kevin Pierce**
May 22, 2014

*Congressional Budget Office
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The opinions expressed in this paper are those of the authors alone and do not necessarily reflect the views of the Congressional Budget Office, the Internal Revenue Service, or the U.S. Treasury Department.

Abstract

Labor supply elasticities are often used to evaluate the effect of changes in tax rates on the total hours worked in the economy. Married women have traditionally been assumed to be the so-called "marginal" workers in their households in the sense of having larger labor supply elasticities. However, those elasticities have fallen sharply in recent decades—a decline that has been attributed to greater participation rates and more generally increased career orientation among married women. Indeed, a growing share of wives earn more than their husbands, raising the question as to whether a person's sex or relative earnings is the relevant factor determining the sensitivity of participation to wage and tax rates. In this paper, we use administrative data to examine whether the woman or the lower earning spouse is the marginal worker. We present descriptive evidence on the share of women who are the primary earner and the frequency of transitions into and out of employment by sex and relative earnings. We find that the lower earning spouse, not the woman, is more likely to start and stop working. We then model an individual's work decision using a dynamic probit model to isolate the labor supply response to changes in tax rates. We estimate that the participation elasticity with respect to the net-of-tax rate of the secondary earner—the spouse who typically has lower earnings—is similar to that for women, though both of these overall elasticities are small. Participation elasticities with respect to income for both women and secondary earners are effectively zero. Our estimates are robust to several alternative models, including specifications of secondary earner.

The Elasticity of Deferred Income With Respect to Marginal Income Tax Rates

Aspen Gorry, Utah State University

Kevin A. Hassett, American Enterprise Institute

R. Glenn Hubbard, Columbia University and the National Bureau of Economic Research

Aparna Mathur, American Enterprise Institute*

This Draft: May 20, 2014

Abstract

A substantial body of theoretical and empirical analysis of time-varying income tax rates focuses on the response of taxable income to changes in the tax rate. Given the increasing use of stock options in executive compensation, we document that income deferral is an important margin of adjustment in response to tax rate changes. The option to defer income changes the welfare effect of taxation as it allows individuals to shift income into the future, reducing their overall tax burden. To account for this option in the empirical analysis, we explore both realization and deferral by estimating the elasticity of deferred income. Our empirical results suggest a large impact of taxes on income timing with magnitude of the elasticity of deferred income that is greater than one.

Keywords: deferred Income, executive compensation, tax policy, elasticity of taxable income.

JEL Codes: G30, H24, H31, J33.

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Capital Gains Taxes and Realizations:
Evidence from a Long Panel of State-Level Data

Jon M. Bakija, Williams College
William M. Gentry, Williams College

June 2014

We estimate how capital gains realizations respond to marginal tax rates on capital gains using a panel of aggregate data for U.S. states for the years 1957 through 2007. In specifications controlling for state fixed effects and year fixed effects, where identification comes from difference-in-differences variation in effective state marginal tax rates, our point estimate of the elasticity of capital gains realizations with respect to the marginal tax rate is -0.66 with a standard error of 0.21. This point estimate suggests a significant and policy-relevant responsiveness of capital gains realizations to incentives, implying that the revenue gain from a capital gains tax increase would be in the ballpark of one-third as large as it would have been in the absence of the behavioral response, and is based on a relatively more convincing identification strategy than has been used in the previous literature. When we remove state and / or year fixed effects, relying on cross-state variation in tax rates and / or federal time-series variation tax rates for identification, our estimates of the elasticity of capital gains to the marginal tax rate are larger in absolute value, but also potentially subject to greater concerns about omitted variable bias.

Contact information: jbakija@williams.edu; wgentry@williams.edu. Thanks to Len Burman, Wojciech Kopczuk, and seminar participants at Williams College for helpful comments. We are grateful to Patrick Aquino, Josephat Koima, Trust Mandevhana, and Tarun Narasimhan for outstanding research assistance. We are also grateful for financial support from the American Council for Capital Formation's Center for Policy Research. Views expressed in the paper are our own and do not necessarily represent the views of our institution or funders.

How responsive are deductions to tax rate changes?*

Philipp Doerrenberg   Andreas Peichl

Sebastian Siegloch

PRELIMINARY WORK IN PROGRESS; COMMENTS WELCOME

May 26, 2014

Abstract

While the large literature on the elasticity of taxable income (ETI) suggests that taxpayers respond to tax rate changes, evidence on the adjustment channels along which these responses occur is relatively scarce. In this paper, we explore whether tax deductions are responsive to tax reforms and hence constitute one of these adjustment channels. We rely on rich German panel data from administrative tax records that include detail information on all income tax relevant parameters including all available tax deductions, and exploit several tax reforms that were implemented in Germany between 2001 and 2008. Our findings suggest an overall ETI of 0.15 for Germany and we provide evidence that this overall response is partly due to deduction adjustments. Our findings can help to design efficient tax systems that close the most responsive deduction possibilities and thus trigger less behavioral adjustments.

JEL Classification: H24, H31

Keywords: elasticity of taxable income, deductions, allowances, tax expenditures, administrative data, Germany

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Voluntary Disclosure of Evaded Taxes – Increasing Revenues, or Increasing Incentives to Evade?

Dominika Langenmayr*
University of Munich

May 21, 2014

Abstract

Many countries apply lower fines to tax evading individuals when they voluntarily disclose the tax evasion they committed. I model such voluntary disclosure mechanisms theoretically and show that while such mechanisms increase the incentive to evade taxes, they nevertheless increase tax revenues net of administrative costs. I then test these theoretical predictions in two separate empirical analyses. First, I confirm that voluntary disclosure mechanisms increase tax evasion, using the introduction of the 2009 offshore voluntary disclosure program in the U.S. for identification. Second, I quantify the additional tax revenues of voluntary disclosures by considering how some state-level governments in Germany bought whistle-blower data from foreign bank employees, thereby increasing the detection probability and the use of voluntary disclosures.

Keywords: Tax evasion, voluntary disclosure, self-reporting

JEL Classification: H26, K42, H24

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Does Front-Loading Taxation Increase Savings? Evidence from Roth 401(k) Introductions

John Beshears
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James J. Choi
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May 29, 2014

Abstract: Can governments increase private savings by taxing savings up front instead of in retirement? Roth 401(k) contributions are not tax-deductible in the contribution year, but they are untaxed upon withdrawal in retirement. The more common before-tax 401(k) contribution is tax-deductible in the contribution year, but both principal and earnings are taxed upon withdrawal. Using administrative data from twelve companies that added a Roth option between 2006 and 2010, we find no evidence that total 401(k) contribution rates differ between employees hired before versus after the Roth introduction, which means that the amount of retirement consumption being purchased by 401(k) contributions increases after the Roth introduction. A survey experiment suggests two behavioral factors play a role in the unresponsiveness of contribution rates: (1) employee confusion about or neglect of the tax properties of Roth balances and (2) partition dependence.

Keywords: Roth 401(k), tax salience, partition dependence

We thank Jim Poterba and Scott Weisbenner for helpful comments, andLuca Maini, Brendan Price, Michael Puempel, and Alex Steiny for excellent research assistance. We also thank Warren Cormier and the Boston Research Group for including our questions in their survey. We acknowledge financial support from the National Institute on Aging (grants R01-AG021650 and P01AG005842) and the Social Security Administration (grant FLR09010202-02 through RAND's Financial Literacy Center and grant #5 RRC08098400-04-00 to the National Bureau of Economic Research as part of the SSA Retirement Research Consortium). The opinions and conclusions expressed are solely those of the authors and do not represent the opinions or policy of NIA, SSA, any agency of the Federal Government, or the NBER. The authors have, at various times in the last three years, been compensated to present academic research at events hosted by financial institutions that administer retirement savings plans. See the authors' websites for a complete list of outside activities.

Do Required Minimum Distributions Matter?
The Effect of the 2009 Holiday on Retirement Plan Distributions

Jeffrey Brown
University of Illinois and NBER

James Poterba
MIT and NBER

David Richardson
TIAA-CREF Institute

June 2014

ABSTRACT

This paper investigates how the 2009 one-time suspension of the Required Minimum Distribution (RMD) rules associated with qualified retirement plans affected plan distributions at TIAA-CREF, a large retirement services provider. Using panel data on retirement plan participants at TIAA-CREF, we find that roughly one third of those who were affected by minimum distribution rules discontinued their distributions in 2009. The results also show relatively small differences in the suspension probability between those who had 2008 distributions equal to the RMD amount, who might be classified as facing a binding RMD constraint, and those who were taking distributions in excess of the RMD amount before the distribution holiday. The probability of suspension declines substantially with age and rises modestly with economic resources. We supplement these results based on administrative record data on retirement plan participants with survey evidence on participant attitudes that affected decisions about suspending distributions. Our findings provide potential guidance on the revenue consequences of changing RMD rules, and they also offer insights about the role of various behavioral considerations, such as inertia, in modeling distribution behavior.

Acknowledgements and Disclosures: We are grateful to Ben Bissette for outstanding assistance with data analysis, to the TIAA-CREF Institute (Richardson) and the National Science Foundation (Poterba) for research support, and to Steven Venti and David Wise for helpful discussions. Brown is a trustee of TIAA, and Poterba is a trustee of CREF. TIAA-CREF is a provider of investment and retirement income security products. This paper represents the views of the authors and do not necessarily represent the views of the institutions with which they are affiliated.

The Elasticity of Taxable Income and Income-shifting: What is "Real" and What is Not?*

Harju, Jarkko† and Matikka, Tuomas‡

May 23, 2014

Abstract

Previous literature shows that income taxation significantly affects the behavior of high-income earners and business owners. However, it is still unclear how much of the response is due to changes in effort and other real economic activity, and how much is caused by tax avoidance and tax evasion. This distinction is important because it affects the welfare implications and policy recommendations. In this paper we distinguish between real responses and tax-motivated income-shifting between tax bases. Our empirical example shows that income-shifting accounts for over two thirds of the overall elasticity of taxable dividend income among Finnish business owners. As the shifted income is also taxed, this halves the marginal excess burden compared to the standard model in which the overall elasticity defines the welfare loss. However, in addition to income-shifting, we find that dividend taxation significantly affects the real behavior of the owners.

JEL Classification Codes: H24; H25; H32

Keywords: Elasticity of taxable income, Business owners, Tax avoidance, Income-shifting, Real responses

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Cross-Country Evidence on the Relation between Capital Gains Taxes, Risk, and Expected Returns*

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May 2014

Abstract

This study empirically examines the prediction in Sikes and Verrecchia (2012) that the relation between capital gains tax rates and expected rates of return varies in the cross-section and over time with firm risk and market risk. Specifically, we test whether the general positive relation between expected returns and the capital gains tax rate becomes weaker or even reverses when (i) a firm's systematic risk is high, (ii) the market risk premium is high, or (iii) the risk-free rate is low. Using an international panel from 27 countries over the period 1990 to 2004, we find evidence supporting these predictions. The results are particularly pronounced in countries with substantive changes in tax rates, more trust in government institutions, less integrated and less liquid capital markets, and lower institutional ownership as well as around substantive increases and decreases in the three risk proxies. We corroborate our findings in a single country setting, using the 1978, 1997, and 2003 changes to the capital gains tax rate in the United States as events. Our results underscore the importance of macroeconomic and firm-specific factors in determining the effect of capital gains taxes on expected returns and suggest that tax rate changes can sometimes have opposite valuation implications than what policymakers have in mind.

JEL Classification: G12, G15, G32, H24, K34, M41

Key Words: Tax capitalization, Personal taxes, Market risk, Cost of capital, International economics

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Do Dividend Taxes Affect Corporate Investment?*

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This draft: May 2014

ABSTRACT

We test whether dividend taxes affect corporate investments. We exploit Sweden's 2006 dividend tax cut of 10 percentage points for closely held corporations and 5 percentage points for widely held corporations. Using rich administrative panel data and triple-difference estimators, we find that this dividend tax cut affects allocation of corporate investment. Cash-constrained firms increase investment after the dividend tax cut relative to cash-rich firms. Reallocation is stronger among closely held firms that experience a larger tax cut. This result is explained by higher equity in cash-constrained firms and by higher dividends in cash-rich firms after the tax cut. The heterogeneous investment responses imply that the dividend tax cut raises efficiency by improving allocation of investment.

JEL No.: G30, G31, H25

Keywords: Investment, Dividend Taxation, Private Firms

* We are grateful to Seppo Kari, Jan Södersten, Kelly Wentland, and workshop participants at the Oslo Fiscal Studies 2014 Workshop on Taxing Capital Income, for helpful comments and suggestions.

Personal Income Taxes, Corporate Profit Taxes and the Heterogeneous Tax Sensitivity of Firm-level Investments*

PETER EGGER, KATHARINA ERHARDT & CHRISTIAN KEUSCHNIGG

June 9, 2014

Abstract

Firms are heterogeneous in size, productivity, ownership concentration, governance, financial structure and other dimensions. The paper introduces a stylized theoretical framework to account for such differences and to explain the heterogeneous tax sensitivity of firm-level investments. We econometrically test the theoretical predictions, taking account of selection of firms into different classes. We find important differences in the tax sensitivity of investment of small entrepreneurial and larger managerial firms in different financial regimes that are largely in line with theoretical results.

JEL classification: D22, G32, H25, L21.
Keywords: Corporate tax, personal taxes, firm heterogeneity, access to capital, manager shareholder conflicts.

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