

Seminar on Public Finance

Lecture #5: February 13

Institutions, Process, and Public Choice

Public Choice

What is public choice?

- Buchanan: “politics without romance”
- Application of theories and methods of economics to the study of political behavior
- A *positive* theory of politics and policy
 - Descriptive not prescriptive
 - Welfare calculations are *normative*.

What can public choice tell us?

- Actual tax policies \neq optimal tax theory
- Why not?
 - Perhaps politics plays a role?
 - Can models of political behavior help shed light on actual policies we see?

Work Horse Electoral Model: Median Voter Model

- Setup:
 - Voters
 - Care only about policy (not charisma, etc.)
 - Have single-peaked preferences
 - Policy is one-dimensional (e.g., liberal-conservative)
 - Elections
 - Two parties
 - Winner take all (most votes wins)
 - Politicians
 - Care only about winning office
 - Choose position in policy space

Median Voter Model (2)

- Question: Where should the candidates position themselves to win?
 - Imagine two candidates: one on left and other on right
 - Left candidate captures all votes to his left, right candidate captures all votes to his right
 - Voters with preferences between these two are split
 - What if left candidate moves his position to the right?
 - And what about if guy on the right moves to the left?
 - Equilibrium: both choose *same* position, that of median voter.
 - This is the **the Median Voter Theorem** (MVT).
 - Given assumptions above (2 parties, single-peaked prefs, one-dimensional policy space, etc.), the majority selected policy will be that policy most preferred by the median voter.

Median Voter Model (3)

Are the assumptions of the median voter model reasonable?

- Poole and Rosenthal (political scientists) find that 90%+ of congressional voting records can be determined by position along one policy dimension - the liberal-conservative spectrum
 - Very high correlation between pro-life position and support for lower taxes and more gun rights
 - Single biggest predictor of party vote: “do you attend church at least once a week?”

Are the predictions of the MVT accurate?

- Policy convergence? Consider Bush v. Obama
 - Rhetoric very different
 - Policy positions?
 - Gitmo
 - Drone strikes
 - Tax Cuts
 - Affordable Care Act

The MVT and Tax Policy: Meltzer and Richard (1981)

- Model:
 - Individuals have preferences over consumption and leisure
 - There is a distribution of productivity and hence wages/income
 - Individuals choose labor supply, consumption, and vote on linear income tax rate
 - Key is that labor supply is endogenous - so cost to higher taxes because it decreases labor supply
 - Tax receipts refunded, lump sum, to individuals

Meltzer and Richard (2)

- Voting decision
 - Individuals balance how higher taxes increase their lump-sum transfer with how they lower their after-tax earned income
 - Higher taxes have a declining effect on revenue at some point (i.e., there is a Laffer Curve)
 - FOC for choice of tax rates by individual i is:

$$\bar{y} + t \frac{\partial \bar{y}}{\partial t} - y_i = 0,$$

where \bar{y} is mean income, y_i income of individual i , t the tax rate.

Meltzer and Richard (3)

- Voting decision (cont'd)
 - Can show preferences over tax rates is single-peaked \Rightarrow MVT
 \Rightarrow decisive voter is the median
 - $\Rightarrow t = \frac{(y_m - \bar{y})}{\frac{\partial \bar{y}}{\partial t}}$, where denominator < 0
 - That is, tax rate is increasing as median is further below the mean
 - Result: “size of government” (i.e., amount of redistributive taxes) increases with increase in income inequality

Special Interests and Lobbying

- “Concentrated benefits versus diffuse costs”
 - Special interests are well informed, because there is a lot at stake
 - Regular voters are “rationally ignorant”
 - Costs to acquiring info, and benefits of knowing small
 - E.g., consider a \$3 billion tax break divided by 300 million people...
 - And can free ride off info from others (informed voting is a public good)

Special Interests and Lobbying (2)

Where do special interests show their influence?

- General consensus is that special interests influence policy along the margins
 - E.g., with tax policy:
 - Regular voters determine general tax rate and tax base structure
 - Interest groups poke holes in base (e.g., tax expenditures)

Institutions & Process (1): Congressional Budget Committees

- The House and Senate Budget Committees draft budget resolutions that guide the Appropriations committees by setting spending levels.
 - The budget resolution is a concurrent resolution hence it does not go to the president
- The budget resolution may also include reconciliation instructions which may guide tax changes
 - Reconciliation bills can not be filibustered in the Senate hence are popular vehicles for tax changes
 - Both 2001 and 2003 tax cuts were done in this manner which is the reason why these were set to expire at the end of 2010

Institutions & Process (2): Congressional Tax Committees

- The constitution states:
 - “All Bills for raising Revenue shall originate in the House of Representatives; but the Senate may propose or concur with Amendments as on other Bills.”
- Jurisdiction for tax matters is given to the House Ways and Means Committee and the Senate Finance Committee
 - Each committee supplies 5 members (3 from the majority) to the Joint Committee on Taxation (JCT)

Institutions & Process (3): Government Tax Entities

- Baseline forecasts
 - CBO and OTA
- Revenue estimates of policy changes
 - JCT and OTA
- Distributional analysis
 - CBO, JCT and OTA
- Economic Analysis of Tax System
 - CBO, Congressional Research Service and OTA
- Legal Analysis of the Tax System
 - JCT and Office of Tax Policy
- Tax Data
 - Statistics of Income at IRS (SOI)

Tax Policy Institutions & Process (4): Annual budget process

- The tax legislative process is typically a part of the annual budget process
- Time line:
 - January 2014: Congressional Budget Office (CBO) issues budget baseline reflecting “current law/services”
 - February 2014: President submits a proposal for the Fiscal Year 2015 budget, typically looks out 10 years (will likely not be until March this year)
 - April 2014: Congress enacts a budget resolution
 - Summer 2014: Congress enacts spending bills and tax bill consistent with the budget resolution
 - July 2014: The administration updates the budget proposal estimates in the “Mid-Session Review” and CBO updates it’s Budget Outlook
 - October 2014: Fiscal Year 2015 begins

Institutions & Process (5): Budget Baselines

- There are two groups that estimate budget and receipt baseline forecasts for a 10 year period
- CBO for the Congress
- The Office and Management and Budget (OMB) for the Administration
 - Agencies submit their own budgets to OMB but OMB has final say
 - Treasury forecasts receipts; by the career staff in the Office of Tax Analysis (OTA)
- Forecasts are released in January/February and during the summer

Institutions & Process (6): Economic Assumptions

- Underlying each forecast is a set of macroeconomic assumptions
- CBO has a panel of outside economists that reviews and comments on the forecast created by CBO staff
- The Administration relies on the “Troika”
 1. The Counsel of Economic Advisors
 2. The Office of Management and Budget
 3. Treasury (via Office of Economic Policy)
- Assumptions are typically similar at least on the surface
 - GDP, income measures, CPI, unemployment rate, and interest rates are publicly reported
 - In practice, detailed National Income and Product Account forecasts are produced and utilized in developing the forecasts of governmental receipts and outlays

Comparison of Economic Projections by CBO, the Administration, and the *Blue Chip* Consensus for Calendar Years 2010 to 2015

	Forecast		Projected Annual Average, 2012-2015
	2010	2011	
Fourth Quarter to Fourth Quarter (Percentage Change)			
Nominal GDP			
CBO	3.8	3.0	5.5
Administration	4.0	5.3	5.7
<i>Blue Chip</i>	4.1	4.6	n.a.
Real GDP			
CBO	2.8	2.0	3.7
Administration	3.1	4.0	4.0
<i>Blue Chip</i>	2.8	3.0	n.a.
GDP Price Index			
CBO	1.0	1.0	1.7
Administration	0.8	1.3	1.7
<i>Blue Chip</i>	1.3	1.5	n.a.
Consumer Price Index ^a			
CBO	0.8	1.2	1.9
Administration	1.0	1.6	2.0
<i>Blue Chip</i>	0.9	1.7	n.a.
Calendar Year Average (Percent)			
Unemployment Rate			
CBO	9.5	9.0	6.3
Administration	9.7	9.0	6.8
<i>Blue Chip</i>	9.6	9.1	n.a.
Three-Month Treasury Bill Rate			
CBO	0.2	0.2	3.3
Administration	0.2	0.7	3.4
<i>Blue Chip</i>	0.2	0.7	n.a.
Ten-Year Treasury Note Rate			
CBO	3.4	3.5	5.0
Administration	3.5	4.0	5.1
<i>Blue Chip</i>	3.4	3.8	n.a.

Summary Measures of Performance for Five-Year Average Projections

(Percentage points)

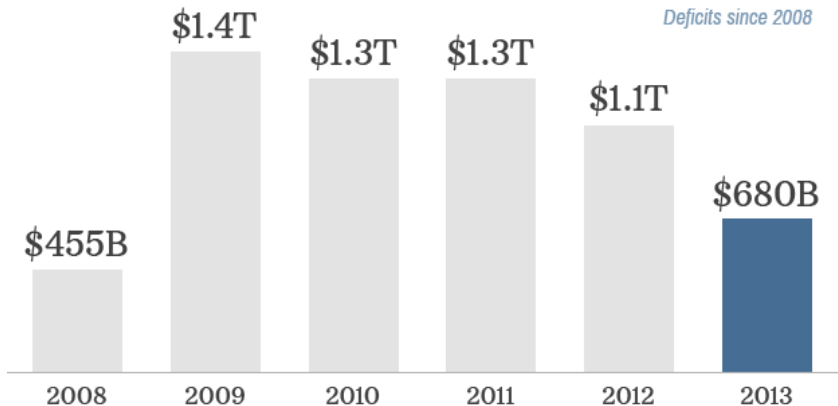
	CBO	<i>Blue Chip</i> ^a	Administration
Growth Rate for Real Output (1979-2005)			
Mean error	-0.1	-0.1	0.1
Mean absolute error	0.7	0.7	0.9
Root-mean-square error	1.0	1.0	1.0
Growth Rate for Nominal Output (1982-2005)			
Mean error	0.3	0.5	0.4
Mean absolute error	0.8	0.8	0.8
Root-mean-square error	1.0	1.0	1.0
Difference Between Inflation in the CPI and in the GDP Price Index (1983-2005)			
Mean error	-0.1	-0.2	-0.3
Mean absolute error	0.4	0.4	0.5
Root-mean-square error	0.4	0.4	0.5
Wage and Salary Disbursements (1980-2005)			
Mean error	0.1	*	0
Mean absolute error	0.9	*	0.9
Mean absolute error	1.1	*	1.2
Root-mean-square error			
Change in Wage and Salary Disbursements as a Share of Output (1980-2005)			
Mean error	0.4	*	0
Mean absolute error	1.6	*	1.5
Root-mean-square error	1.8	*	1.7

Institutions & Process (7): Receipt Baselines

- Given these macroeconomic assumptions economists at CBO and Treasury forecast annual tax receipts
 - Forecasts are by source (wages, capital gains, corporate, excise, etc)
 - Forecasts are annual, currently through 2024
 - All forecasts are point forecasts, no explicit confidence interval
- At the time of forecast e.g. 1/1/2014 the forecasters have:
 - Edited, stratified sample of tax returns for 2011
 - Processing data from 2012
 - Withholding and some estimated payments from 2013

Institutions & Process (8): Budget Deficit (Surplus) Forecasts

- The item given the most attention is the net position of the government given the forecasts of governmental revenues and expenditures
- For FY2013 the deficit was \$0.68 trillion or 4.1% of GDP
 - Revenues were \$2.77 trillion or 16.7% of GDP, which is below the historical average of 18.3%
- Both CBO and OMB project that the budget has a structural deficit

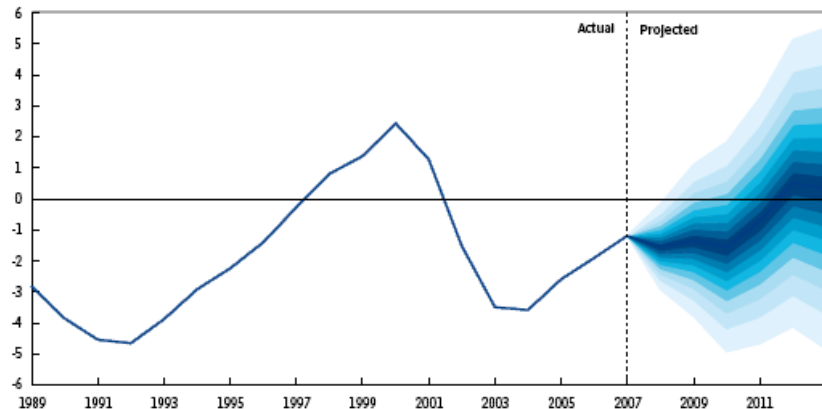


*FISCAL YEARS ENDING SEPT. 30

SOURCE: TREASURY

Uncertainty of CBO's Projections of the Budget Deficit or Surplus Under Current Policies

(Percent)

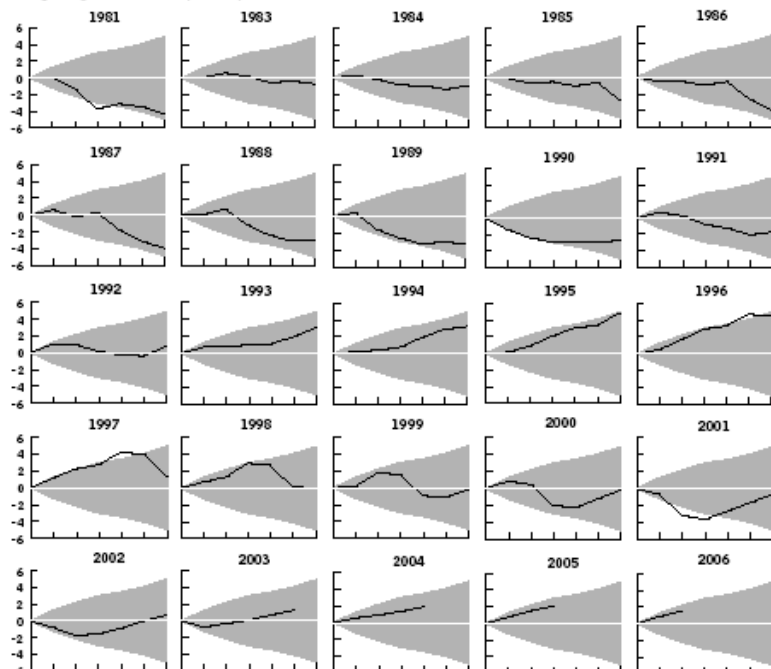


Source: Congressional Budget Office.

Notes: This figure, calculated on the basis of CBO's track record in forecasting, shows the estimated likelihood of alternative projections of the budget deficit or surplus under current policies. The baseline projections described in this chapter fall in the middle of the darkest area of the figure. Under the assumption that tax and spending policies do not change, the probability is 10 percent that actual deficits or surpluses will fall in the darkest area and 90 percent that they will fall within the whole shaded area.

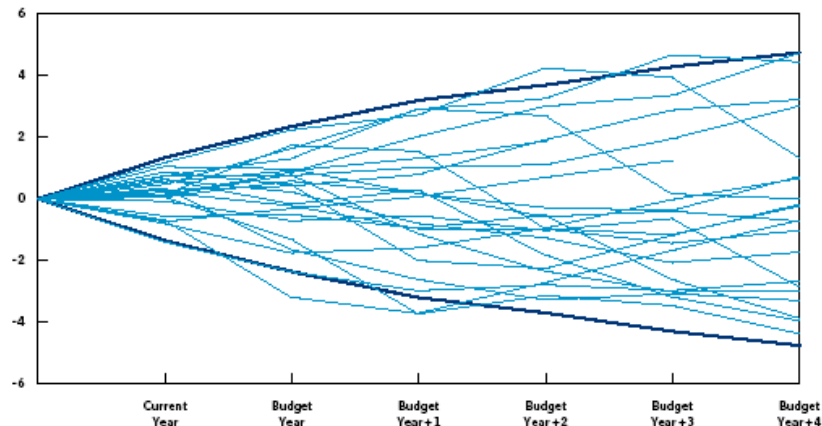
Between 1981 and 2007

(Percentage of gross domestic product)



CBO's Past Deviations in Projecting the Primary Surplus or Deficit, Compared with the Constructed 90 Percent Confidence Ranges

(Percentage of gross domestic product)



Source: Congressional Budget Office.

Notes: Each thin line represents the actual deviations from the set of projections made in a given year. The thick lines represent the 90 percent confidence range constructed from CBO's statistical model for deviations. That range encompasses most of CBO's past record.

The primary budget surplus or deficit is the difference between federal revenues and federal outlays excluding net interest.

Institutions & Process (9): Current Law versus Proposed Law

- CBO forecasts a current law/policy baseline
 - “If Congress maintained status quo what would receipts be”
 - Given current law expiration of certain tax cuts, it can be somewhat unclear what “current policy” is
- OMB issues a proposed policy baseline
 - “What would receipts be if the Presidents policies were enacted”
 - Treasury issues detailed tables on the impacts of proposals on receipts

Institutions & Process (10): Current versus Policy, cont.

- Usually the difference between the baseline concepts is secondary (via the Treasury tables you can convert one to the other)
- With tax reform is it possible that the policy might be expected to have a significant impact on the performance of the economy
- Thus the macroeconomic assumptions might be dependent on policy
 - This may result in significant differences between CBO and Treasury

Institutions & Process (11): PAYGO (pay-as-you-go)

- A class of budgetary restrictions to make/encourage legislators to enact policy in a budget neutral manner.
- The Budget Enforcement Act of 1990 is typically the model and its rules were in effect from FY1991-FY2002
 - If rule violated then an across the board sequester of spending would be applied
 - Expired just before the Bush tax cuts
- Congress currently has legislative rules that attempt to restrict the deficit bill by bill
 - Not viewed as terribly effective
- In February 2010, the Statutory Pay-As-You-Go Act of 2010 was enacted

Institutions & Process (12): PAYGO

Tax changes exempt from PAYGO:

- The following provisions of EGTRRA and JGTRRA:
 - The 10-percent income tax bracket;
 - The child tax credit;
 - Tax benefits for married couples;
 - The adoption tax credit;
 - The dependent care tax credit;
 - The employer-provided child care tax credit;
 - The education tax benefits;
 - The 25-percent and 28-percent tax brackets;
 - For taxpayers with AGI less than \$200,000 (\$250,000 if married):
 - The 33-percent tax bracket
 - The tax rates on capital gains and dividends
 - The phase-out of personal exemptions (PEP) and the limitation on itemized deductions (Pease)
 - The increased limits on small business “expensing”
- AMT “relief” through 2011
- Estate tax through 2011 (using 2009 law)

Institutions & Process (13): Estimates of Tax Changes

Any changes in tax law are estimated by:

1. The Joint Committee on Taxation (JCT)
 - Estimate is relative to the CBO baseline
 - Estimate is released publicly before Committee and floor consideration
2. The Office of Tax Analysis at Treasury
 - Estimate is relative to the OMB current law baseline
 - Estimates are provided within the Administration and are typically are not released until next budget

Institutions & Process (14): Revenue Estimates

- JCT and OTA estimate all types of policies from very narrow to comprehensive changes
- Narrow proposals require rapid research and creative modeling, often few taxpayers impacted
- Broad proposals typically rely on sophisticated simulation models
 - Individual model (ITM) built upon a stratified sample of tax returns supplemented with records for non-filers
 - All fields imputed through the budget window
 - Simulation optimizes taxpayer choices
 - Income responses to rate changes built in

Issues in Revenue Estimating: Meaning of “Static”

- Since the estimates are relative to a set baseline certain things are held constant
 - Nominal GDP, Prices, Income shares
 - There is no macroeconomic feedback effects from tax changes
- But there are individual behavioral changes motivated by the tax change
- Current practice is to include microeconomic behavioral responses but not macroeconomic behavioral responses
- Termed “micro-dynamic” estimation

Issues in Revenue Estimating (2): “Static” vs “Completely Static”

- What would a completely static estimate imply?
 - No matter what the tax rate behavior would not change.
 - If there was a 100% capital gains tax people would still realize capital gains just like there was a 15% rate.
 - Cut the tax rate on dividends and the same amount of dividends are paid.
- Treasury and CBO use the economic literature's findings to estimate individual responses to changes
 - Individual behavior changes but the size of the economy does not.

Issues in Revenue Estimating (3): “Static” vs “Dynamic”

- What is missing due to current practice?
- Supply-side effects
- As we have discussed economists believe that taxes have the ability to alter the incentives to work or to invest
- These in turn can alter productivity and the growth rate of the economy
- By ignoring these effects, policies that improve economic efficiency look more expensive than they should and poorly designed policy looks too cheap

Issues in Revenue Estimating (4): Why are “dynamic” scores hard?

- Usually there is not an econometric literature measuring these types of effects
- Have to rely on theory which in turn is often very sensitive to assumptions
 - Partial equilibrium versus general equilibrium
 - Assumptions about uncertainty and the future

Issues in Revenue Estimating (5): 1997 Symposium Results

- In 1997 the JCT asked a number of different forecasters to estimate the macro effects of tax reform
- Identical policies were used, both an income tax and a consumption tax
- Models differed and the resulting estimates differed dramatically
 - In some cases even the sign of the dynamic effect differed across models

Issues in Revenue Estimating (6): Uncertainty

- If we are going to allow GDP to change we need to think more carefully about how decisions are made and the expectations that influence them
 - What is future fiscal policy? Tax increases, more borrowing, less spending?
 - What is the Fed's response? Do they offset or accommodate the macro effects of policy?
 - Generally what are individuals' expectations regarding the policy and future changes?

Issues in Revenue Estimating (7): Recent Use of “Dynamic” Estimates

- In 2003 the House adopted a rule that requires JCT, upon request, to analyze the macroeconomic effects before consideration. This was done for May 2003 Jobs and Growth bill
- In March 2003 CBO did a macroeconomic analysis of the Administration's budget which included the impact of the dividend exclusion proposal
- Treasury reportedly did a separate dynamic score of the President's proposal but never released it
- Treasury now reports the macro effects of the president's tax proposals but not dynamic revenue estimates

Issues in Revenue Estimating (8): Pros for Dynamic Scoring

- Most complete estimate, uses all information
- Lack of dynamic scoring introduces a systematic bias against certain types of policies
- Lack of dynamic scoring can create some anomalous results
- As technology and economics advance these estimate should become easier and more precise

Issues in Revenue Estimating (9): Cons against Dynamic Scoring

- Much more reliant on assumptions which in turn are more likely to be subject to political pressure
- Cumbersome to integrate with the baseline, need to estimate for all legislation
- Need to account for the expenditure side to be consistent
- Different models give different answers
- Assumptions regarding fiscal and monetary policy very important and difficult to defend

Issues in Revenue Estimating (10): Is there a right answer?

- Probably not, since it depends on what the estimates are being used for:
 - To estimate the deficit
 - To choose between alternative policies
- Transition issues can have big effects
- Currently thinking is ...

Distributional Analysis

- Both Treasury and JCT have built substantial models to measure the distributional effects of tax policy
- Neither has released many distributions over the past few years
- The Urban-Brookings Tax Policy Center has stepped into the void and has done substantial modeling that has gotten reported in the press
- Saez has done work looking at longer trends and what is happening in the extreme tail of the income distribution

Distributional Analysis (2): Issues

- What taxes should be distributed?
 - Income taxes
 - Estate taxes
 - Corporate taxes
- What is the right base/income concept?
 - Cash income
 - Expanded income: AGI plus tax-exempt interest, employer contributions for life and health insurance, employer share of Social Security and Medicare payroll tax, workers' compensation, untaxed Social Security benefits, insurance value of Medicare benefits, alternative minimum tax preference items, and excluded income of U.S. citizens living abroad
 - Family economic income: broad measure that includes imputed rental value of housing and change in value of assets
- How to define the classes?
- What are the implications of income mobility?

**Table 11.– Distribution of Income and Taxes, and Average Tax Rates
2010**

INCOME CATEGORY (1)	Number of Returns (2) (Thousands)	Share of Returns	Income (Millions of Dollars)	Share of Income	COMBINED INCOME, SOCIAL INSURANCE, AND EXCISE TAXES UNDER PRESENT LAW (3)			INDIVIDUAL INCOME TAXES			EMPLOYMENT TAXES		
					\$ Billions	Percent Share	Average Tax Rate	\$ Billions	Percent Share	Average Tax Rate	\$ Billions	Percent Share	Average Tax Rate
Less than \$10,000.....	28,197	17.7%	130,485	1.3%	6.3	0.3%	4.8%	-13.4	-1.4%	-10.2%	13.2	1.5%	10.1%
\$10,000 to \$20,000.....	23,872	15.0%	363,202	3.7%	3.6	0.2%	1.0%	-33.4	-3.6%	-9.2%	31.5	3.6%	8.7%
\$20,000 to \$30,000.....	18,456	11.6%	466,973	4.8%	34.8	1.8%	7.5%	-20.7	-2.2%	-4.4%	50.4	5.8%	10.8%
\$30,000 to \$40,000.....	15,769	9.9%	562,324	5.7%	69.3	3.7%	12.3%	1.7	0.2%	0.3%	62.1	7.1%	11.0%
\$40,000 to \$50,000.....	12,970	8.1%	593,855	6.1%	86.4	4.6%	14.5%	16.9	1.8%	2.8%	64.1	7.3%	10.8%
\$50,000 to \$75,000.....	23,656	14.8%	1,489,164	15.2%	244.3	12.9%	16.4%	75.8	8.1%	5.1%	156.5	17.9%	10.5%
\$75,000 to \$100,000.....	14,952	9.4%	1,318,004	13.5%	250.6	13.2%	19.0%	97.3	10.4%	7.4%	143.8	16.4%	10.9%
\$100,000 to \$200,000.....	16,748	10.5%	2,281,583	23.3%	532.8	28.2%	23.4%	268.7	28.6%	11.8%	245.4	28.0%	10.8%
\$200,000 to \$500,000.....	3,782	2.4%	1,079,625	11.0%	291.1	15.4%	27.0%	206.4	22.0%	19.1%	77.8	8.9%	7.2%
\$500,000 to \$1,000,000.....	622	0.4%	429,053	4.4%	112.3	5.9%	26.2%	94.8	10.1%	22.1%	16.1	1.8%	3.7%
\$1,000,000 and over.....	336	0.2%	1,068,415	10.9%	260.8	13.8%	24.4%	244.7	26.1%	22.9%	15.3	1.7%	1.4%
Total, All Taxpayers.....	159,359	100.0%	9,782,685	100.0%	1,892.2	100.0%	19.3%	938.9	100.0%	9.6%	876.2	100.0%	9.0%

- (1) The income concept used to place tax returns into income categories is adjusted gross income (AGI) plus: [1] tax-exempt interest, [2] employer contributions for health plans and life insurance, [3] employer share of FICA tax, [4] worker's compensation, [5] nontaxable social security benefits, [6] insurance value of Medicare benefits, [7] alternative minimum tax preference items, and [8] excluded income of U.S. citizens living abroad. Categories are measured at 2009 levels.
- (2) Includes nonfilers, excludes dependent filers and returns with negative income.
- (3) Federal taxes are equal to individual income tax (including the outlay portion of the EIC), employment tax (attributed to employees), and excise taxes (attributed to consumers). Corporate income tax is not included due to uncertainty concerning the incidence of the tax. Individuals who are dependents of other taxpayers and taxpayers with negative income are excluded from the analysis. Does not include indirect effects.
- (4) The average tax rate is equal to Federal taxes described in footnote (3) divided by income described in footnote (2).

Source: Staff of the Joint Committee on Taxation.

**Table 12.—Tax Returns with Income or Social Insurance Taxes
2010**

INCOME CATEGORY (1)	Millions of Returns	Individual Income Taxes	Employment Taxes	Returns with Employment Taxes <u>Greater</u> than Income Taxes	Returns with Employment Taxes <u>Less</u> than Income Taxes	Percentage of Returns with Employment Taxes Greater than Income Taxes
		\$ Billions	\$ Billions	Millions of Returns	Millions of Returns	
Less than \$10,000.....	17.2	-13.4	13.2	17.2	[3]	99.8%
\$10,000 to \$20,000.....	16.1	-33.4	31.5	15.6	0.5	97.1%
\$20,000 to \$30,000.....	15.7	-20.7	50.4	15.1	0.6	96.0%
\$30,000 to \$40,000.....	14.4	1.7	62.1	13.2	1.2	91.5%
\$40,000 to \$50,000.....	12.3	16.9	64.1	10.5	1.8	85.3%
\$50,000 to \$75,000.....	22.5	75.8	156.5	18.3	4.2	81.5%
\$75,000 to \$100,000.....	14.8	97.3	143.8	10.7	4.0	72.7%
\$100,000 to \$200,000.....	16.7	268.7	245.4	8.5	8.1	51.2%
\$200,000 to \$500,000.....	3.8	206.4	77.8	0.1	3.6	3.1%
\$500,000 to \$1,000,000.....	0.6	94.8	16.1	[3]	0.6	2.1%
\$1,000,000 and over.....	0.3	244.7	15.3	[3]	0.3	1.5%
Total, All Taxpayers.....	134.4	938.9	876.2	109.3	25.1	81.3%

(1) The income concept used to place tax returns into income categories is adjusted gross income (AGI) plus: [1] tax-exempt interest,

[2] employer contributions for health plans and life insurance, [3] employer share of FICA tax, [4] worker's compensation,

[5] nontaxable social security benefits, [6] insurance value of Medicare benefits, [7] alternative minimum tax preference items, and

[8] excluded income of U.S. citizens living abroad. Categories are measured at 2009 levels.

(2) Includes nonfilers, excludes dependent filers and returns with negative income.

(3) Less than 50,000.

Source: Staff of the Joint Committee on Taxation.

**Table 13.— Marginal Tax Rates On Labor Income and Long Term Capital Gain, by Income Category
2010**

INCOME CATEGORY (1)	Labor Income			Long-Term Capital Gains Income
	Average Marginal Income Tax Rate (2)	Average Marginal Employment Tax Rate (2)	Average Combine Marginal Income and Employment Tax Rate	Average Marginal Tax Rate
Less than \$10,000.....	-10.0%	14.2%	4.2%	0.0%
\$10,000 to \$20,000.....	0.5%	14.2%	14.7%	0.2%
\$20,000 to \$30,000.....	12.9%	14.2%	27.1%	0.5%
\$30,000 to \$40,000.....	15.9%	14.2%	30.1%	0.8%
\$40,000 to \$50,000.....	16.3%	14.2%	30.5%	2.1%
\$50,000 to \$75,000.....	17.2%	14.2%	31.4%	6.1%
\$75,000 to \$100,000.....	20.6%	14.2%	34.7%	7.8%
\$100,000 to \$200,000.....	26.4%	12.1%	38.5%	15.5%
\$200,000 to \$500,000.....	31.5%	8.0%	39.4%	17.8%
\$500,000 to \$1,000,000.....	29.1%	6.6%	35.7%	15.0%
\$1,000,000 and over.....	31.4%	6.6%	37.9%	14.8%
Total, All Taxpayers.....	14.4%	13.6%	28.0%	14.7%

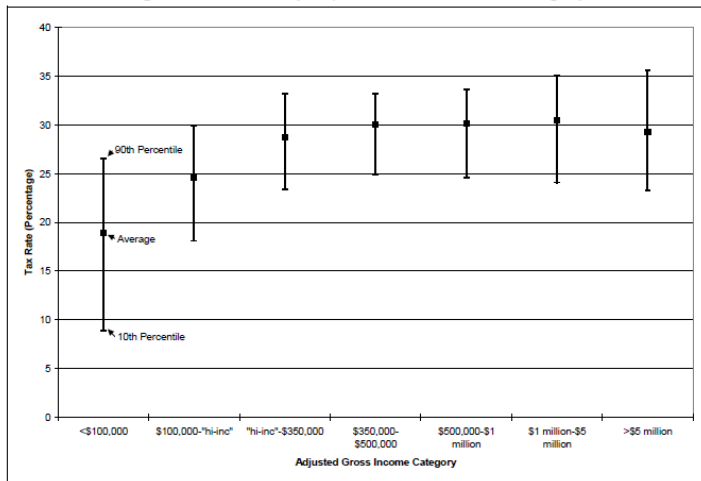
(1) The income concept used to place tax returns into income categories is adjusted gross income (AGI) plus: [1] tax-exempt interest, [2] employer contributions for health plans and life insurance, [3] employer share of FICA tax, [4] worker's compensation, [5] nontaxable social security benefits, [6] insurance value of Medicare benefits, [7] alternative minimum tax preference items, and [8] excluded income of U.S. citizens living abroad. Categories are measured at 2009 levels.

(2) For individual income and employment taxes, the average marginal tax rate is equal to the change in taxes from an additional \$100 of wages to each spouse with positive wages. For long-term capital gain, the average marginal tax rate equals the change in taxes from an additional 1% increase in long-term capital gains to each taxpayer with positive long-term capital gains.

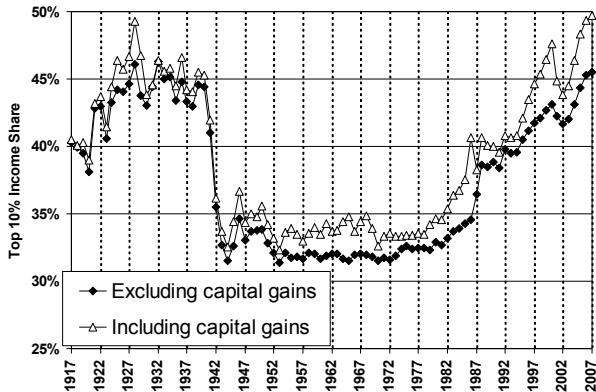
Source: Staff of the Joint Committee on Taxation.

From CRS Report R42043 on the Buffet Rule

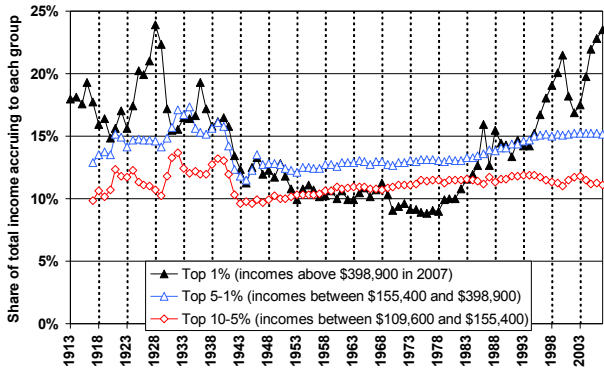
Figure 2. Tax Rates by Adjusted Gross Income Category



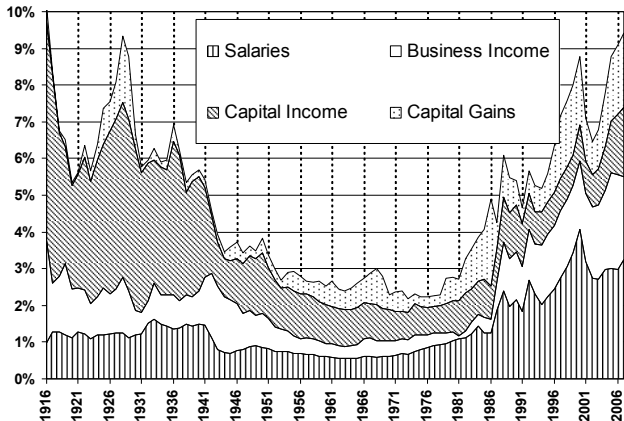
Piketty & Saez: The Top Decile Income Share



Piketty & Saez: Income Shares within the Top Decile



Piketty & Saez: Top 0.1% Income Share & Composition 1916-2007



Institutions & Process (15): Tax Reform of 1986

- In the 1984 State of the Union address President Reagan calls for a Treasury study of tax reform
 - Viewed as a means to defuse the simmering tax issue for a while since the report was requested “by December 1984”
- Treasury report was issued in November of 1984
 - While Reagan explicitly called for broadening the base and lower rates, the report was probably more radical than intended or desired
 - Included a significant increase in corporate revenue but the plan as a whole was revenue neutral
- In May of 1985 the administration put forward a proposal
- Final passage was in the fall of 1986

Institutions & Process (16): 2005 Tax Reform Panel

- In 2005, in an attempt to generate momentum for tax reform President Bush appointed a bipartisan panel to develop tax reform alternatives
- The Executive Order stated:
 - The purpose of the Advisory Panel shall be to submit to the Secretary of the Treasury a report with revenue neutral policy options for reforming the Federal Internal Revenue Code. These options should:
 1. simplify Federal tax laws to reduce the costs and administrative burdens of compliance with such laws;
 2. share the burdens and benefits of the Federal tax structure in an appropriately progressive manner while recognizing the importance of homeownership and charity in American society; and
 3. promote long-run economic growth and job creation, and better encourage work effort, saving, and investment, so as to strengthen the competitiveness of the United States in the global marketplace.
 - At least one option submitted by the Advisory Panel should use the Federal income tax as the base for its recommended reforms.

Institutions & Process (17): 2009 PERAB Tax Sub-Committee

- In February the Administration set up the Presidential Economic Recovery Advisory Board (PERAB)
 - Chaired by Paul Volker
 - Austan Goolsbee is staff director and chief economist (as well as a member of CEA)
- Was tasked with providing recommendations on:
 - Tax code simplification
 - Enforcement
 - Corporate tax reform
- The report of this sub-committee was issued in August 2009. It was a relatively high level discussion of options.

Institutions & Process (18): 2010 Fiscal Commission

- In February, by executive order the President created and set up the National Commission of Fiscal Responsibility and Reform Chaired by former Sen. Alan Simpson and Erskine Bowles
- 18 members: 6 appointed by the President, 6 Senators (3 from each party) and 6 Members of the House (3 from each party)
- The Commission was charged with identifying policies to improve the fiscal situation in the medium term and to achieve fiscal sustainability over the long run.
- Specifically, the Commission shall propose recommendations designed to balance the budget, excluding interest payments on the debt, by 2015.
- Did not get the necessary 14 votes to issue a recommendation. Co-chairs issued a report which included a “Illustrative Plan” for a reformed tax system.