

**Tax Policy**  
Cornell Law School  
Fall 2007

Professor Jon Bakija  
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Class: 4:15-5:55PM Mondays  
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**Overview**

Taxes consume close to one-third of U.S. income, and influence the terms of important life decisions such as how much to work, to how much to save, how much to give to charity, and whether to buy a home. They shape the incentives and strategies of business enterprises, and profoundly affect the economy. And they are the main mechanism through which government affects the distribution of incomes. In this seminar we will consider a selection of issues and debates of current interest in U.S. tax policy. We will investigate critical problems and challenges facing the tax system and explore possibilities for improving its design. Topics to be considered include: views on the appropriate role for government in the economy; evidence on the effects of taxes on work effort and economic activity; questions of fairness and justice in the distribution of incomes and tax burdens; problems with the current income tax and options for fundamental tax reform; the relative merits of consumption taxes versus income taxes; tax evasion, tax avoidance, and tax shelters; problems and potential solutions in the taxation of multinational corporations; and the debate over social security reform.

The course will begin with a brief overview of some basic economic principles useful for analyzing tax policy issues, and will then provide a basic conceptual framework for critically evaluating empirical evidence relevant to tax policy debates. I'll keep it relatively non-technical, and will teach you what you need to know assuming no prior background in economics. Once that's done, for each of the remaining seminar meetings, we will read and discuss a small selection of scholarly writings on particular tax policy issues of interest in the current public debate. Students should come to each class prepared to discuss the readings for that day, as constructive contribution to class discussion will be an important part of the course grade.

## Course materials

The textbook for the course is *Taxing Ourselves: A Citizen's Guide to the Debate over Taxes*, 3rd edition, by Joel Slemrod and Jon Bakija (MIT Press, 2004). This book is available in the campus bookstore, the campus library, or can be purchased online. All other readings will be made available electronically on the course Blackboard web site.

Course requirements	% of final grade
Two short problem sets	5%
Four policy analysis papers, approximately 7 pages double-spaced, due at various points in the semester (see below).	45%
Class participation	20%
Final research paper, approximately 20 pages double spaced, due after classes end (exact date to be announced).	30%

### Problem sets

There will be two short problem sets, each of which gives you a chance to actively think through some of the principles of economic and empirical analysis that we will be covering in the first three classes. The first is due at the beginning of class September 10, and the second is due at the beginning of class September 17.

### Policy analysis papers

For six of our seminar meetings (dates marked with an asterisk on the schedule), there will be a paper of approximately 7 double-spaced pages due at 8:00AM the morning of the seminar meeting. Each student will write four of these papers. **All students must write the first paper (on tax progressivity), and then must write at least one of the next two (on income tax reform and consumption tax reform).** Each paper will construct an argument for or against some policy reform proposition that we will be discussing in class later that day. The purpose of handing the paper in the morning of the class is to get students to think over the issues *before* we discuss them in class, and to help me prepare for the discussion (seeing the papers first will help me anticipate questions and confusions that should be addressed in the discussion). In general, I will have provided a brief introduction to the topic in a previous class to give you some necessary background. Further details on the paper assignments and grading criteria will be distributed shortly.

### Class participation

Students should come to each class having done the readings carefully and should be prepared to contribute constructively to classroom discussion. Each week I will electronically distribute a brief guide to the readings with some questions to help focus your attention and prepare for discussion, and I may periodically suggest areas of the readings to emphasize or to skip. Class participation will count for 20% of your grade, and you can expect that I will sometimes ask questions of specific students rather than relying entirely on volunteers. My purpose is never to embarrass anyone, but rather to encourage broad participation in the discussion and to maintain an incentive to do the reading on time. Both attendance and constructive contributions to discussion will play critical roles in your participation grade.

### Research paper

The final research paper of approximately 20 pages will give you a chance to delve more deeply into a topic addressed in the course. You should meet with me well before the end of the semester to discuss ideas for a research paper and to have your topic approved.

### Submission of assignments

All assignments for the class should be written in a common word processing program that is compatible with Microsoft Word, and should be submitted to me electronically. I will provide technical details on the submission procedure shortly.

### Grading policy

I plan to adhere to the law school's 3.35 GPA ceiling. All assignments will be graded on a numerical scale, and letter grades will be assigned to each numeric score at the end of the semester in a way that satisfies the ceiling. I will provide approximate information on mean numeric scores associated with each type of assignment as the semester progresses. Late assignments will be penalized 10% of their numeric grade for each day or part of a day they are late.

### Meeting with me

I am available to meet at my office by appointment, please e-mail me at [jmb569@cornell.edu](mailto:jmb569@cornell.edu) or call my office phone at 255-1698 to arrange an appointment. I will be out of town Oct. 5, Oct. 25-28, Nov. 2-3, and Nov. 15-17.

## Schedule and Reading List

Key:

+ = problem set due at beginning of class

\* = paper due 8AM morning of class

<p>Week 1 August 27</p>	<p><b>Introduction</b></p> <ul style="list-style-type: none"> <li>• <i>Taxing Ourselves</i>, Ch. 1</li> </ul> <p><b>Basic economics of taxation</b></p> <ul style="list-style-type: none"> <li>• <i>Taxing Ourselves</i>, Ch. 3, pp. 72-79 (tax incidence)</li> <li>• <i>Taxing Ourselves</i>, Ch. 4, pp. 121-142 (tax efficiency)</li> <li>• Robert Frank and Ben Bernanke, <i>Principles of Microeconomics</i>, 2nd edition, McGraw-Hill, 2004, pp. 57-67, 71-83, and 182-87 (excerpts on supply &amp; demand, tax incidence, and deadweight loss from taxation)</li> </ul>
<p>Week 2 September 3</p>	<p><b>Economic perspectives on the role of government; or, why have taxes at all?</b></p> <ul style="list-style-type: none"> <li>• Joseph Stiglitz, <i>Economics of the Public Sector</i>, W.W. Norton, 2004, Ch. 4, pp. 76-90 (“Market Failure”)</li> <li>• <i>Taxing Ourselves</i>, Ch. 4, pp. 97-120.</li> </ul> <p><b>Critical evaluation of empirical evidence</b></p> <ul style="list-style-type: none"> <li>• Jonathan Gruber, <i>Public Finance and Public Policy</i>, 1st edition, Worth Publishers, 2005, Ch. 3, pp. 59-85 (“Empirical Tools of Public Finance”).</li> <li>• Nada Eissa and Jeffrey B. Liebman. “Labor Supply Response to the Earned Income Tax Credit.” <i>Quarterly Journal of Economics</i>, v111, n2 (May 1996): [Excerpt]</li> </ul>
<p>Week 3 + September 10</p> <p>Problem set #1 due</p>	<p><b>Critical evaluation of empirical evidence (continued)</b></p> <ul style="list-style-type: none"> <li>• Jonathan Gruber, <i>Public Finance and Public Policy</i>, 1st edition, Worth Publishers, 2005, Ch. 3, pp. 59-85 (“Empirical Tools of Public Finance”).</li> <li>• Martin Feldstein. “The Effect of Marginal Tax Rates on Taxable Income: A Panel Study of the 1986 Tax Reform Act” <i>Journal of Political Economy</i>, June 1995, v. 103, iss. 3, pp. 551-72.</li> <li>• Douglas Clement. “European Vacation.” <i>Federal Reserve Bank of Minneapolis: The Region</i>. December 2003.</li> <li>• Alberto Alesina, Edward Glaeser, and Bruce Sacerdote. “Work and Leisure In The U.S. and Europe: Why So Different?” <i>NBER Macroeconomics Annual</i>, 2005, Vol. 20 Issue 1. [Excerpt]</li> </ul>

<p>Week 4 + September 17</p> <p>Problem set #2 due</p>	<p><b>Taxation and theories of distributive justice</b></p> <ul style="list-style-type: none"> <li>• <i>Taxing Ourselves</i>, Ch. 3, pp. 54-65, 85-95.</li> <li>• Harvey Rosen. "Income Redistribution: Conceptual Issues." from <i>Public Finance</i>, 7<sup>th</sup> edition, McGraw-Hill 2005, pp. 148-156.</li> <li>• Jonathan Gruber, <i>Public Finance and Public Policy</i>, 2<sup>nd</sup> ed., Worth Publishers 2007, pp. 592-600 ("Optimal Income Taxation").</li> <li>• David Weisbach. "Should Legal Rules be used to Redistribute Income?" <i>University of Chicago Law Review</i>. Vol. 70, 2003, pp. 439-453.</li> <li>• Edgar K. Browning. "The Case against Income Redistribution." <i>Public Finance Review</i>, 2002, Vol. 30; pp. 509-530</li> <li>• John E. Roemer. "Equality and Responsibility." <i>Boston Review</i>. April/May 1995.</li> </ul>
<p>Week 5 * September 24</p> <p>Paper #1 due: How progressive should the tax system be?</p>	<p><b>Tax progressivity and income inequality: evidence and implications</b></p> <ul style="list-style-type: none"> <li>• <i>Taxing Ourselves</i>, Ch. 3, pp. 65-72, 79-85</li> <li>• <i>Taxing Ourselves</i>, Ch. 4, pp. 144-152</li> <li>• Robert Frank and Ben Bernanke, <i>Principles of Macroeconomics</i>, 3rd edition, McGraw-Hill, 2007, pp. 222-226 (excerpt on conventional explanations for increasing income inequality).</li> <li>• Emmanuel Saez. "Income and Wealth Concentration in Historical and International Perspective." in Alan J. Auerbach, David Card, and John M. Quigley, eds., <i>Public Policy and the Income Distribution</i>, New York: Russell Sage Foundation, 2006. [Excerpt]</li> <li>• Steven N. Kaplan and Joshua Rauh. "Wall Street and Main Street: What Contributes to the Rise in the Highest Incomes?" NBER Working Paper No. 13270, July 2007.</li> </ul>

<p>Week 6 October 1</p>	<p><b>The design of income taxation in the U.S.</b></p> <ul style="list-style-type: none"> <li>• <i>Taxing Ourselves</i>, Ch. 2</li> <li>• <i>Taxing Ourselves</i>, Ch. 6, pp. 217-231 (“A Clean Tax Base”)</li> <li>• <i>Taxing Ourselves</i>, Ch. 8, pp. 273-294.</li> <li>• Gruber, Ch. 24, pp. 684-686 (“How to Tax International Income?”)</li> <li>• James Hines, “International Taxation for Beginners,” [excerpted from pp. 306-308 of “Lessons from Behavioral Responses to International Taxation,” <i>National Tax Journal</i>, June 1999, v. 52, iss. 2, pp. 305-22.]</li> </ul>
<p>No class October 8 (fall recess)</p>	
<p>Week 7 * October 15</p> <p>Paper #2 due: Critique or defend an income tax reform proposal.</p>	<p><b>Income tax reform</b></p> <ul style="list-style-type: none"> <li>• Report of the President’s Advisory Panel on Federal Tax Reform, 2005. [Excerpts on Income Tax Reform]</li> <li>• Leonard Burman and William Gale. “Tax Reform Proposals: Some Good Ideas, But Show Me the Money.” <i>Economist’s Voice</i>, December 2005, pp. 1-7.</li> <li>• George R. Zodrow and Charles E. McLure, Jr. “Time for US Tax Reform? The Tax Reform Panel’s Recommendations.” <i>Bulletin of the International Bureau for Fiscal Documentation</i>, April 2006, pp. 134-149.</li> <li>• Hubbard, Glenn. “Corporate Tax Integration: A View from the Treasury Department,” <i>Journal of Economic Perspectives</i> 7, Winter 1993, pp. 115-132.</li> </ul>
<p>Week 8 October 22</p>	<p><b>Consumption tax reform: an introduction</b></p> <ul style="list-style-type: none"> <li>• <i>Taxing Ourselves</i>, Ch. 6, pp. 195-217 (“A Consumption Base”)</li> <li>• <i>Taxing Ourselves</i>, Ch. 7</li> </ul>
<p>Week 9 * October 29</p> <p>Paper #3 due: Should we replace the income tax with a consumption tax?</p>	<p><b>Consumption tax reform: debate</b></p> <ul style="list-style-type: none"> <li>• Joseph Bankman and David Weisbach. “The Superiority of an Ideal Consumption Tax over an Ideal Income Tax.” <i>Stanford Law Review</i>, Vol. 58, March 2006, pp. 1413-1456.</li> <li>• Eric Toder and Kim Rueben “Should We Eliminate Taxation of Capital Income?” in Henry J. Aaron, Leonard E. Burman, and C. Eugene Steuerle, eds., <i>Taxing Capital Income</i>. Urban Institute Press, 2007, pp. 245-284.</li> <li>• Report of the President’s Advisory Panel on Federal Tax Reform, 2005. [Excerpts on Consumption Tax Reform]</li> </ul>

<p>Week 10 * November 5</p> <p>Paper #4 due: Policy responses to tax shelters.</p>	<p><b>Complexity, evasion, avoidance, and tax shelters</b></p> <ul style="list-style-type: none"> <li>• <i>Taxing Ourselves</i>, Ch. 5</li> <li>• <i>Taxing Ourselves</i>, pp. 278-283.</li> <li>• Daniel N. Shaviro, <i>Corporate Tax Shelters in a Global Economy: Why they are a Problem and What We Can Do about It</i>. American Enterprise Institute, November 2004, [Excerpt, pp. 1 – 25].</li> <li>• David Weisbach, “Ten Truths About Tax Shelters,” 55 Tax L. Rev. 215-253 (2002)</li> <li>• Joseph Bankman and Michael L. Schler. “Tax Planning Under the Flat Tax.” in Henry J. Aaron, Leonard E. Burman, and C. Eugene Steuerle, eds., <i>Taxing Capital Income</i>. Urban Institute Press, 2007, pp. 245-284.</li> </ul>
<p>Week 11 * November 12</p> <p>Paper #5 due: Policy responses to problems in international taxation.</p>	<p><b>International aspects of taxation</b></p> <ul style="list-style-type: none"> <li>• Harry Grubert and Rosanne Altshuler. “Corporate Taxes in the World Economy: Reforming the Taxation of Cross-Border Income.” Working paper, 2006.</li> <li>• Reuven Avi Yonah &amp; Kimberly Clausing. “A Proposal to Adopt Formulary Apportionment for Corporate Income Taxation.” Working paper, 2007.</li> <li>• Zodrow, George. “Capital Mobility and Source-Based Taxation of Capital Income in Small Open Economies,” <i>International Tax and Public Finance</i>, Vol. 13, 2006, pp. 269–294.</li> </ul>

<p>Week 12 November 19</p> <p>3-page research paper proposal due at beginning of class.</p>	<p><b>Social Security I</b></p> <ul style="list-style-type: none"> <li>• “Social Security,” excerpted from Jonathan Gruber, <i>Public Finance and Public Policy</i>, New York: Worth Publishers 2005, pp. 1-13.</li> <li>• “National Saving and Social Security Reform” by Andrew Eschtruth and Robert Triest, <i>Just the Facts on Retirement Issues</i>, Boston College Center for Retirement Research, April 2005.</li> <li>• Robert Frank and Ben Bernanke, <i>Principles of Macroeconomics</i>, 3rd edition, pp. 299-306 (introduction to finance).</li> <li>• Robert Frank and Ben Bernanke, <i>Principles of Microeconomics</i>, 2nd ed., New York: McGraw-Hill, 2004, pp. 210-213. (“The Invisible Hand in the Stock Market.”)</li> <li>• “Would a Privatized Social Security System Really Pay a Higher Rate of Return?” by John Geanakoplos, Olivia Mitchell, and Stephen P. Zeldes, in <i>Framing the Social Security Debate: Values, Politics, and Economics</i>. Washington: Brookings Institution Press. 1998. (pp. 137-157).</li> </ul>
<p>Week 13 * November 26</p> <p>Paper #6 due: How should we reform Social Security?</p>	<p><b>Social Security II</b></p> <ul style="list-style-type: none"> <li>• John F Cogan and Olivia S Mitchell. “Perspectives from the President’s Commission on Social Security Reform” <i>Journal of Economic Perspectives</i>, v17, n2 (Spring 2003): 149-72.</li> <li>• Peter A. Diamond and Peter R. Orszag. “Saving Social Security” <i>Journal of Economic Perspectives</i>, v19, n2 (Spring 2005): 11-32.</li> </ul>