Editorial Introduction

TAPES 1998 Special Issue

The papers in this issue were presented in an earlier form at the Trans-Atlantic Public Economics Seminar (TAPES), sponsored by the National Bureau of Economic Research jointly with the Economic Policy Research Unit at Copenhagen Business School. The conference/seminar was held in Frederiksdal on the outskirts of Copenhagen during May 21–23, 1998, and organized jointly by Sören Bo Nielsen of EPRU and Roger Gordon of the University of Michigan. The papers have gone through the normal refereeing process under the editorial supervision of Sören Bo Nielsen and Roger Gordon.

The objective of the TAPES conference is to provide European and North American public finance economists a chance to exchange ideas on public finance questions of mutual policy interest. The focus of this particular conference was on “Taxes, Social Insurance Policies, and the Labor Market”.

One standard result in the past literature is that the labor supply of prime aged men seems little affected by income tax rates. In “Tax Arbitrage and Labor Supply”, Jonas Agell and Mats Persson argue that one possible explanation for this apparent lack of responsiveness is that individuals use tax arbitrage opportunities to avoid paying higher tax rates. Given these portfolio adjustments, they argue that individuals should all face more or less the same marginal tax rate on earnings, in spite of any progressivity in the tax schedule.

Even though the labor supply of prime aged men seems relatively unresponsive to tax incentives, the same cannot be said for older men. In “Incentive Effects of Social Security on Labor Force Participation: Evidence in Germany and Across Europe”, Axel Börsch-Supan provides evidence that the retirement ages in Europe have been strongly affected by incentives created by existing Social Security systems encouraging early retirement. The resulting earlier retirement ages along with longer life expectancies will impose a heavy financial burden on younger generations.

In “Welfare for the Elderly: The Effects of SSI on Pre-Retirement Labor Supply”, David Neumark and Elizabeth Powers provide evidence that the U.S. SSI Program (a supplement to the Social Security Program providing a floor on benefits to low-income workers) also encourages earlier retirement. In particular, the asset limits for eligibility mean that extra earnings carried over into retirement...
face a very high implicit tax rate, reducing the incentive to work prior to retirement.

Another group whose labor supply seems to be responsive to fiscal incentives is the currently unemployed. Patricia Anderson and Bruce Meyer, in “The Effects of the Unemployment Insurance Payroll Tax on Wages, Employment, Claims and Denials”, study the impact of a change in the UI system in the state of Washington, where experience rating was introduced in 1985 to replace a uniform tax rate on all workers. They provide clear evidence that the higher tax rate on workers in firms with a high turnover rate reduced the overall turnover rate and also the number of unemployed.

David Card and Phillip B. Levine in “Extended Benefits and the Duration of UI Spells: Evidence from the New Jersey Extended Benefit Program”, provide evidence about the effects of UI using a different “natural experiment”. In response to a temporary increase in New Jersey in the number of weeks of benefits available to unemployed individuals, they find that more individuals remained unemployed long enough to take advantage of these extended benefits.

Thomas Lemieux and W. Bentley MacLeod argue, however, that judging the effects of the UI program on behavior may be more complicated than has been appreciated in past papers. In their paper “Supply Side Hysteresis: The Case of the Canadian Unemployment Insurance System”, they start with the puzzle that the number of UI recipients has been increasing in Canada even during a period when benefits have been becoming less generous. They provide evidence suggesting that workers learn about the generosity of benefits only through use. As a result, an earlier increase in the generosity of the UI program continued to lead to an increase in the unemployment rate as individuals gradually learned about it through use, even though benefits by that point were declining in generosity.

Clemens Fuest and Bernd Huber explore another complication in analyzing the effects of taxes on the labor market: unions. In “Why do Governments Subsidise Investment and not Employment?”, they take into account how the wages and employment levels that result from union-management bargaining adjust in response to changes in tax policy. Given these adjustments, they find that investment subsidies may be more cost effective in raising employment than employment subsidies.

Finally, A. Lans Bovenberg, Johan J. Graafland and Ruud A. de Mooij, in their paper “Tax Reform and the Dutch Labor Market: An Applied General Equilibrium Approach”, develop a sophisticated simulation model to provide a broader overview of the effects of tax/transfer programs on the labor market. The model simulations suggest that benefits to workers are effective in fighting economy-wide unemployment, especially if targeted to unskilled workers. However, hours of labor supplied would be reduced. Cutting marginal tax rates raises the quantity and quality of labor supply, but is less effective in reducing unemployment.

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