

# Contents

Foreword ix

## **Introduction 1**

Some History 2

Current Tax Systems 5

Overview of the Book 8

References 11

## **I The Effects of Taxation 13**

### **1 Distortions and Welfare Losses 15**

1.1 The Effects of Taxation 17

1.1.1 Labor Supply 18

1.1.2 The Effects of Taxation on Savings 25

1.1.3 Taxation and Risk-Taking 30

1.2 Welfare Losses 33

### **2 Tax Incidence 41**

2.1 Partial Equilibrium 43

2.1.1 The Effect of Payroll Taxes 43

2.1.2 The General Analysis of Partial Equilibrium 45

2.2 General Equilibrium 49

2.2.1 The No-Taxation Economy 50

2.2.2 Introducing Taxes 51

2.2.3 General Remarks 53

2.2.4 Infinitesimal Analysis 54

2.2.5 Final Remarks 60

<b>II</b>	<b>Optimal Taxation</b>	<b>63</b>
<b>3</b>	<b>Indirect Taxation</b>	<b>67</b>
3.1	Ramsey's Formula	67
3.1.1	An Informal Approach	67
3.1.2	The General Model	68
3.1.3	Some Special Cases	73
3.2	Productive Efficiency	77
<b>4</b>	<b>Direct Taxation</b>	<b>83</b>
4.1	The Emergence of the Model	83
4.2	Mirrlees's Model	87
4.2.1	The Two-Type Case	88
4.2.2	The Rawlsian Case	94
4.2.3	The General Approach	97
4.2.4	The Quasi-linear Case	101
4.3	Generalizations	107
4.3.1	Heterogeneous Preferences and the Extensive Margin	108
4.3.2	Endogenous Wage Rates	111
4.3.3	The Income Tax as an Insurance Device	114
4.4	Simulations	115
<b>5</b>	<b>Mixed Taxation</b>	<b>123</b>
5.1	The Negative Income Tax	124
5.2	Is Indirect Taxation Useful?	125
5.3	Criticisms	129
<b>6</b>	<b>Risk and Time</b>	<b>133</b>
6.1	Taxing Savings in a Riskless Economy	135
6.2	A Stochastic Economy	137
6.3	The Inverse Euler Condition	139
6.4	Discouraging Savings	142
6.5	Optimal Taxes	144
6.5.1	Zero Aggregate Wealth Taxes	146
6.5.2	Introducing Productive Capital	147
6.5.3	Illustrations	149
<b>7</b>	<b>Corrective Taxes</b>	<b>153</b>
7.1	Pigovian Taxation in Partial Equilibrium	154

7.2	Optimal Green Taxes	156
7.2.1	The First-Best	157
7.2.2	The Second-Best	159
7.3	Is There a Double Dividend?	161
<b>8</b>	<b>Criticisms of Optimal Taxation</b>	<b>165</b>
8.1	Representing Social Preferences	165
8.1.1	Tax Reforms	166
8.1.2	Horizontal Equity	169
8.2	Putting Tax Theory to Work	172
8.2.1	Taxing Households	174
8.2.2	Behavioral Economics and Taxation	176
<b>III</b>	<b>Some Current Debates</b>	<b>179</b>
<b>9</b>	<b>Low-Income Support</b>	<b>181</b>
9.1	Measuring Poverty	182
9.2	The Main Benefits	183
9.2.1	Guaranteed Minimum Income	185
9.2.2	The Negative Income Tax	185
9.2.3	Low-Wage Subsidies	186
9.2.4	The Minimum Wage	187
9.3	The Lessons from Theory	188
9.3.1	The Negative Income Tax	188
9.3.2	Low-wage Subsidies	194
9.3.3	The Guaranteed Minimum Income	194
9.3.4	The Minimum Wage	195
9.4	Empirical Evaluations	197
9.5	Recent Reforms	199
<b>10</b>	<b>Taxation and Global Warming</b>	<b>203</b>
10.1	The Optimal Price of Carbon	205
10.1.1	The Social Discount Rate	205
10.1.2	Catastrophic Change	210
10.1.3	Discounting Environmental Changes	211
10.2	International Issues	213
10.3	The Dynamics of Carbon Taxation	215

<b>IV</b>	<b>Appendixes</b>	<b>219</b>
<b>A</b>	<b>Some Basic Microeconomics</b>	<b>221</b>
A.1	Consumer Theory	221
A.1.1	Hicksian and Marshallian Demands	221
A.1.2	The Slutsky Equations	223
A.1.3	Interpretation	224
A.2	Producer Theory	224
A.2.1	The Producer's Problem	225
A.2.2	Factor Demands	225
A.2.3	The Special Case of Constant Returns	227
<b>B</b>	<b>Optimal Control</b>	<b>229</b>
	Index	233