

LOUIS KAPLOW

# The Theory of Taxation and Public Economics



PRINCETON UNIVERSITY PRESS  
PRINCETON AND OXFORD

## *Summary of Contents*



<i>Preface</i>	xvii
1. Introduction	1
PART I: FRAMEWORK	
2. An Integrated View	13
3. The Social Objective	35
PART II: OPTIMAL TAXATION	
4. Optimal Income Taxation	53
5. Elaboration and Extensions	80
6. Income and Commodity Taxation	122
PART III: GOVERNMENT EXPENDITURES	
7. Transfer Payments	151
8. Goods and Services	179
PART IV: ADDITIONAL ASPECTS OF TAXATION	
9. Taxation of Capital	221
10. Taxation of Transfers	249
11. Taxation and Social Security	275
12. Taxation of Families	315

PART V: DISTRIBUTIVE JUSTICE AND  
SOCIAL WELFARE

13. Welfare	347
14. Social Welfare Function	370
15. Other Normative Criteria	391
16. Conclusion	407
<i>References</i>	417
<i>Index</i>	455

## Contents



<i>Preface</i>	xvii
1. Introduction	1
PART I: FRAMEWORK	
2. An Integrated View	13
A. Completeness of Policy Specification	15
B. Comprehensiveness of Instruments Considered	19
C. Comparability of Proposals under Assessment	22
1. The Problem	22
2. Distribution-Neutral Income Tax Adjustments as a Solution	25
3. Applicability	29
3. The Social Objective	35
A. Motivation	35
1. Examples	36
2. Implications	37
B. Exposition	41
1. Social Welfare Functions	41
2. Comments on a Range of Social Welfare Functions	44
3. Relevance of the Choice of a Particular Social Welfare Function	48
PART II: OPTIMAL TAXATION	
4. Optimal Income Taxation	53
A. Statement of the Problem	53
B. Results	57
1. Linear Income Tax	58

2. Two-Bracket Income Tax	63
3. Nonlinear Income Tax	65
a. Analysis	65
b. Qualifications	70
c. Simulations	74
4. Discussion	77
5. Elaboration and Extensions	80
A. Behavioral Response to Labor Income Taxation	80
1. Labor Supply Elasticity	80
2. Taxable Income Elasticity	82
3. Long-Run Elasticity	87
B. Problems of Implementation	90
1. Administration and Enforcement	90
2. Lack of Comprehensive Tax Base	94
C. Income and Ability	96
1. Taxation of Earning Ability	96
2. Income as an Indicator of Ability versus Preferences	103
D. Interdependent Preferences	110
E. Additional Considerations	116
1. Liquidity Constraints	116
2. Uncertain Labor Income	117
3. General Equilibrium Effects	119
4. Nontax Distortions	120
6. Income and Commodity Taxation	122
A. Statement of the Problem	125
B. Optimal Commodity Taxation	127
1. Distribution-Neutral Income Tax Adjustment and Labor Effort	128
2. Elimination of Differential Commodity Taxation	132
3. Other Reforms of Commodity Taxation	133
C. Qualifications	135
1. Externalities	137
2. Preferences Nonseparable in Labor	137
3. Preferences Dependent on Earning Ability	139
4. Preference Heterogeneity	140
5. Administration and Enforcement	142

6. Taxpayer Illusion	143
7. Political Economy	144
D. Ramsey Taxation	145

### PART III: GOVERNMENT EXPENDITURES

7. Transfer Payments	151
A. Integrated View	152
1. Characterization	152
2. Analysis	154
B. Existing System	156
1. Aggregate Marginal Tax Rates	156
2. Application: Earned Income Tax Credit	158
3. Administration, Eligibility, and Measurement of Need	160
C. Categorical Assistance	164
1. Optimal Categorical Assistance	164
2. Application to Existing Programs	167
3. Endogenous Categorization	169
D. Work Inducements	170
1. Rewarding Earnings	170
2. Rewarding Hours	171
3. Other Reasons to Encourage or Discourage Work	173
E. Cash versus In-Kind Transfers	175
8. Goods and Services	179
A. Distribution-Neutral Income Tax Adjustments	182
B. Special Case: Government Provision Perfect Substitute for Consumption	185
C. General Case: Distributive Incidence and Optimal Provision	188
1. Analysis	188
2. Examples	190
3. Comments	192
D. General Case: Distributive Incidence and Optimal Redistribution	197
1. Introduction	197
2. Analysis	198
3. Optimal Income Taxation and Revenue Requirements	200

E. Measurement of Distributive Incidence	202
F. Benefit Taxation	209
G. Extension: Government Regulation	211

## PART IV: ADDITIONAL ASPECTS OF TAXATION

9. Taxation of Capital	221
A. Analysis	222
1. Taxation of Capital as Differential Commodity Taxation	222
2. Qualifications	225
B. Applications	230
1. Income versus Consumption Taxation	230
2. Wealth Taxation	235
3. Corporate Income Taxation	236
C. Extensions	239
1. Uncertain Capital Income	239
2. Capital Levies and Transitions	242
3. Human Capital	245
10. Taxation of Transfers	249
A. Analysis	251
1. Taxation of Transfers as Differential Commodity Taxation	251
2. Externalities Due to Transfers	253
a. Externality on donees	253
b. Externality involving tax revenue	254
3. Transfers' Effects on the Marginal Social Value of Redistribution	256
B. Transfer Motives	258
1. Altruism	260
2. Utility from Giving Per Se	261
3. Exchange	263
4. Accidental Bequests	264
C. Additional Considerations	266
1. Other Aspects of Distribution	266

2. Human Capital	269
3. Charitable Giving	270
11. Taxation and Social Security	275
A. Redistribution	276
1. Labor Income Tax Comparison	276
2. Lifetime Income	278
3. Intergenerational Redistribution	285
4. Redistribution across Family Types	289
B. Forced Savings	290
1. Myopia	291
a. Myopic labor supply	295
b. Nonmyopic labor supply	298
2. Samaritan's Dilemma	301
3. Liquidity Constraints	306
4. Heterogeneity	309
5. Relationship to Redistribution	310
C. Insurance	312
12. Taxation of Families	315
A. Distribution	317
1. Unequal Sharing	320
2. Economies of Scale	323
3. Intrafamily Transfer Motives	325
a. Altruism	326
b. Utility from sharing per se	327
c. Exchange	329
4. Children	329
5. Distributive Shares as a Function of Income	332
B. Incentives	333
1. Labor Effort	333
a. One-worker families	333
b. Two-worker families	337
2. Endogenous Family Structure	341
a. Marriage	341
b. Procreation	343



## PART V: DISTRIBUTIVE JUSTICE AND SOCIAL WELFARE

13. Welfare	347
A. Welfarism	348
1. Definition	348
2. Basis for Welfarism	349
3. Perspectives on Welfarism	351
a. Two-level moral theory	352
b. Moral intuitions	354
c. Relevance of nonwelfarist principles under welfarism	357
B. Well-Being	359
1. Definition	359
2. Limited Information and Other Decision-Making Infirmities	360
3. Other-Regarding Preferences	362
4. Capabilities, Primary Goods, and Well-Being	367
14. Social Welfare Function	370
A. Aggregation	370
1. Frameworks	370
a. Original position	370
b. Social rationality	373
2. Concerns	375
a. Interpersonal comparisons of utility	375
b. Weight on equality	377
B. Membership in Society	378
1. National Boundaries	378
2. Future Generations	382
3. Population Size	387
15. Other Normative Criteria	391
A. Inequality, Poverty, Progressivity, Redistribution	392
B. Horizontal Equity	396
C. Sacrifice Theories	401

---

D. Benefit Principle	403
E. Ability to Pay	404
F. Definitions as Norms	405
 16. Conclusion	 407
 <i>References</i>	 417
 <i>Index</i>	 455