70th Annual Congress of the International Institute of Public Finance
Redesigning the Welfare State for Aging Societies
August 20th – 23rd, 2014 - Lugano, Switzerland

Conference Agenda
Overview and details of the sessions of this conference. Please select a date or room to show only sessions at that day or location. Please select a single session for detailed view (with abstracts and downloads if available).

Date: Wednesday, 20/Aug/2014
9:00am - 10:00am Opening Ceremony
Aula Magna, Main Building

10:00am - 11:00am
Keynote I: Early Life Conditions and Later Life Outcomes
Session Chair: Mats Dahlberg, Upsala University
Keynote Lecturer: James P. Smith (Rand Corporation, USA)
Aula Magna, Main Building

11:30am - 1:00pm
BusTax 1: Taxing multinational firms
Session Chair: Dhammika Dharmapala, University of Illinois

A 22, Palazzo Rosso

Interest Deductions in a Multijurisdictional World
Dhammika Dharmapala1,2, Mihir Desai1
1University of Illinois, United States of America; 2Harvard University, United States of America
The tax treatment of interest expenses in a multijurisdictional setting raises numerous complexities. This paper catalogs these difficulties and highlights the particular problems associated with efforts to achieve ownership neutrality among multinational corporations (MNCs) when debt financing is involved. We argue that the differential deductibility of debt entailed by various current tax law provisions leads in general to potential distortions in the patterns of asset ownership across MNCs and that various proposed solutions have significant limitations. We suggest several alternative regimes to address both the ownership distortions that we highlight, as well as other well-established problems of income-shifting through debt. These alternative regimes are extensions to a multinationation setting of two general approaches to the neutral treatment of interest expenses - the CBIT and ACC. These regimes – a worldwide debt cap (WDC) and a net financing deduction (NFD) – provide solutions to income-shifting and ownership distortions. However, they have the potential disadvantage of restricting other policy parameters.

International distribution of the corporate tax base: Impact of different apportionment factors under unitary taxation
Simon Long1, Alex Cobham2
1University of Bayreuth, Germany; 2Center for Global Development
Under the current system of separate accounting international profit shifting will result in misalignment of profits and real economic activity. In reaction to increasing fiscal pressure during the current financial crises major tax reforms like unitary taxation with formula apportionment of the profits have been proposed. This paper aims to contribute to understanding of the differences in the international distribution of the corporate tax base between the current system and the leading unitary taxation alternatives, by exploiting a global database of company balance sheets. We find that apportioning profit according to measures of actual economic activity would result in major redistributions of the tax base. First international loss consolidation is likely to reduce the overall tax base in the range of 10 percent in our sample. Further, apportioning according to number of employees will dramatically redistribute to lower income countries while using cost of employees will do the opposite.

Exploiting a Window of Opportunity: Multinationals’ Profit Shifting in the Absence of Restrictions
Carolin Holzmann
FAU Erlangen-Nuremberg, Germany
This paper asks whether and how multinational enterprises’ (MNEs) tax planning responds to changes in the tax law that create new opportunities for profit shifting. We analyze MNE’s internal debt shifting during a window of opportunity. Our empirical identification strategy exploits random variation in the window length that results from the firm-specific introduction mechanism of the anti-shifting legislation. We use data from the Microdatabase Direct Investment which provides detailed information on foreign subsidiaries of German MNEs. Generally, our results show that the window has an impact on both the probability and the volume of internal lending. Even conservative estimates indicate an increase in the probability by 7% and on the volume by 14.4% per 90-day window. Fiscal consequences in terms of tax revenue losses, however, appear to be negligible because the average volume of internal lending is rather small.

11:30am - 1:00pm
Health 1: Long-term care
Session Chair: Theis Theisen, University of Agder

Redesigning the Long-Term Care Financing for Aging Societies
Jaroslav Vostatak
University of Finance and Administration, Czech Republic
We compare the liberal, social-democratic, conservative and neoliberal design of LTC financing, separately mentioning the Austrian and Czech reforms as well. Any LTC model has to take the health care design used into account. England has been trying the combination of a social-democratic health care system with a liberal welfare LTC system, generating many inconveniences due to asset testing and persistence of low universal benefits. The US has been trying the combination of a neoliberal health care system with a not comprehensive LTC system. Sweden has a system of universal health care and LTC insurance services system. Germany relies on a conservative social health and LTC insurance model with neoliberal design additions. The Czech universal LTC benefit and the central subsidizing of LTC institutions require a paradigmatic reform, to arrive at a reasonable social model.

The relationship between costs and quality in nonproft nursing homes
Laura Di Giorgio1, Massimo Filippini2, Giuliano Masiero3
1Institute for Health Metrics and Evaluation, University of Washington, Seattle; 2University of Lugano; 3ETH Zurich, Switzerland
We investigate the relationship between costs and quality in nonprofit nursing homes, which represents a key issue in the present context of cost containment measures. In accordance with the economic theory, we estimate a three-inputs total cost function for nursing home services using data from 45 nursing homes in Southern Switzerland between 2006 and 2010. Quality is measured by means of clinical indicators regarding process and outcomes derived from the Minimum Data Set. We consider both composite and simple quality indicators. Conversely from many previous studies, we use panel data and control for unobserved heterogeneity. This allows to capture nursing homes specific features that may explain differences in structural quality or costs levels. We find evidence that poor levels of quality regarding outcome, as measured by the prevalence of severe pain and weight loss, lead to higher costs. Our results are robust to quality endogeneity concerns.

Does provision of long-term care lead to depreciation of self-care productivity?
Theis Theisen
University of Agder, Norway
We set up a theoretical model for how a long-term care-user responds to rationed long-term care-services. Similarly, we model rationing of service-provision by a public sector agency. The interaction between the agency and care-recipients is modeled as a non-cooperative game. We establish that a Nash-equilibrium exists, and argue that ample provision of care-recipients productivity in self-care. This theoretical result is supported by empirical evidence: The higher per capita income a municipality has, the higher is the share of its population that is low-productive in self-care, controlling for differences in age-structure, death-rates, etc.

Health 2: Health economics
Session Chair: Lars Thiel, Wuppertal University

Price Elasticity of Soft Drink Tax and Obesity in Korea
Eunyoung Lee
Korea Institute of Public Finance, Korea, Republic of (South Korea)
This paper empirically examines the effects of taxing soft drinks on their consumption and obesity in Korea. I estimate price elasticities, using two data sets. Korea had imposed a 10% special consumption tax on soft drinks, but repealed it at the end of 1999. Applying OLS regression models to the Korean National Health and Nutrition Examination Survey—repeated cross section data of 1998 and 2001, I find that the decreased price of soft drinks does increase soda consumption, and the price elasticity is 0.34. Although soda consumption increased with reduced price, obesity prevalence did not change, because soda consumption replaced milk consumption. In addition, using data from a survey, I find that the price elasticity is 0.69 for adults and 1.18 for adolescents. My findings imply that soda tax may be more effective in preventing and controlling adolescents’ obesity. Regarding regressivity, I have contrasting results between these two data sets.

Illness and Health Satisfaction: The Role of Relative Comparisons
Lars Thiel
Wuppertal University, Germany
This paper investigates the role of relative comparisons in health status for individual health satisfaction. Using longitudinal data from a representative German population survey, we estimate the effect of health-related positional concerns, social norms, and comparison processes on individual health satisfaction. We find that women tend to be more satisfied with their health if they belong to a reference group where physical health problems are more prevalent. Furthermore, higher levels of reference-group illness can temporarily alleviate the adverse impact of one’s own illness on health satisfaction. This is also the first study to show the relevance of health-related upward and downward comparisons for health perception in the general population. The results suggest that both being healthier and sicker than the reference standard increases health satisfaction. This finding is consistent with social psychological models, where social comparisons are a viable means to cope with illnesses.

Corruption, Decentralization and Public Expenditure in Economic Community of West African States (ECOWAS)
Adeniyi Jimmy Adefokun
McPherson University, Sieriki Sotayo, Ogun State, Nigeria, Nigeria
This study extends the empirical literature on the effect of corruption and decentralization on public expenditure by using a panel of the 15 countries in ECOWAS for the period of 1996 to 2010. The empirical analysis is based on the level of aggregate public expenditure. However, corruption has a significant negative effect on health expenditure as a percentage of public expenditure. Findings reveal that corruption is felt differently in a non-federal (centralized) country compared to a federal (decentralized) country as regards health expenditure. It is further shown that decentralization lessens the negative effect of corruption on health expenditure. The study also establishes that decentralization has no significant effect on corruption. Finally, it is found that country size (population) has a significant positive relationship with corruption.

Optimal sanctions for refounders: A question of wealth?
Handrik Von Ungern-Sternberg
University of Freiburg, Germany
In a two-period standard law enforcement model individuals stay honest or break the law. It is private information whether they oen deliberately or accidentally. When sanctions are limited by individual wealth constraints the law enforcer chooses an exogenous sanction pattern and the level of monitoring. Should the enforcer implement an increasing, equal or rather decreasing penalty scheme for repeat offenders? Our results are twofold. Wealthy individuals can be deterred from deliberate crimes in both periods and punishment should be equal for every offense or decreasing if a minimum of law enforcement is exogenously given. Poor individuals cannot be fully deterred and escalating penalties are the only way to make criminal careers unattractive.

Pay Me Now or Pay Me Later: Business Permit Applications, Waiting Time, and Bribery of Government Officials in Transition Economies
John Edwin Anderson
University of Nebraska, United States of America
Obtaining permits to operate businesses in transition countries can be a substantial challenge. It is often the case that permits are limited by the government and subject to delays, required bribes, or corruption. The efficiency of the resource allocation mechanism is hindered and overall economic growth can be limited. In this paper I examine the extent to which the inability or difficulty involved in obtaining necessary permits are cited by businesses in transition economies as substantial impediments. Using the 2009 World Bank-EBRD Business Environment and Enterprise Performance Survey (BEEPS) data, 1 empirically model how firm characteristics and country characteristics affect the number of permits required, the time cost involved in obtaining permits, and the frequency with which firms ultimately pay bribes to government officials. Results reveal key factors that affect permits, waiting time, and bribery. Policy recommendations are suggested by the empirical results and are discussed.

Return Migration and Illegal Immigration Control
Alexander Kemnitz1, Karin Mayr2
1TU Dresden, Germany; 2University of Vienna, Austria
This paper investigates the effectiveness of immigration control policies when the duration of stay of illegal immigrants is endogenous because they may return home voluntarily. It shows that return intentions matter, because they policies will typically aect not only the number of immigrants, but also their duration of stay. For example, we find that spending on border enforcement can potentially increase the total amount of illegal labor in the receiving country. Second, in-site inspections reduce illegal labor, unless there is an amnesty: then, they can have the opposite effect. Third, fines on apprehended migrants have only limited effect.

Controlling Illegal Immigration: On the Scope for Cooperation with a Transit Country

Michael Michal1, Slobodan Ojic2
1University of Cyprus, Cyprus; 2Graduate Institute, Geneva
We consider the implications of cooperation with respect to immigration control between a final destination country (D) and its poorer neighbor (T). Assuming that the latter serves as a transit country for undocumented immigrants, a key question is how much aid should D provide to T for the purpose of strengthening its immigration controls. The problem for T is to determine what proportion of aid to use strictly for immigration control rather than trying to meet other border-security objectives. We examine the Nash equilibrium values of the policy instruments of both countries and compare them with those which are optimal when international cooperation is exogenously expanded to maximize joint welfare. We also consider a two-stage game in which D first decides on how much aid to transfer to T, with the latter subsequently choosing how to use it.

Political Economy of Asymmetric Aging, Migration and Fiscal Policy
Mehmet Serkan Tosun1,2,3
1University of Nevada, Reno, United States of America; 2Institute for the Study of Labor (IZA); 3Oxford Institute of Population Ageing
This paper uses an overlapping generations model with international labor mobility and a politically responsive fiscal policy to examine aging in developing and developing regions. Migrant workers change the political structure composed of young and elderly voters in both labor-receiving and labor-sending countries. Numerical simulations show that the developed region benefits more from international labor mobility through the contribution of migrant workers as laborers, savers and voters. The developing region experiences significant growth in all specifications but benefit more under international capital mobility. Restricting political participation of migrant workers in the developed region produces inferior growth results.

An Economic Rationale for Controlled-Foreign-Corporation Rules
Andreas Hauff1, Mohammed Mardan1, Dirk Schindler2
1University of Munich, Germany; 2Norwegian School of Economics
By introducing controlled-firms' foreign direct investment (FDI) across countries and country-pairs. We use data on the universe of German multinational enterprises (MNEs) to empirically explore how marginal investments at one foreign affiliate depend on investments at other affiliates within the same MNE. The empirical approach employs two channels or modes of cross-affiliate interdependence: more geography (capturing horizontal linkages) and output-input relationships within or across industries (which capturing vertical linkages). We find evidence of a significant interdependence of investments within the firm. In the firm-level data at hand, vertical linkages appear to be more important than horizontal ones. Investments at one location tend to stimulate investments at other locations of the same MNE, particularly if input linkages are strong. This relationship seems to be true for output linkages. Beyond vertical linkages, mere geographical nearness matters only to a minor extent.

Measuring the Interdependence of Multinational Firms' Foreign Investments
Simon Bősenberg1, Peter Eggert2, Valeria Merto3, Georg Wamser4
1ETH Zürich; 2ETH Zürich, CEPR, CESifo, GEP, OUGB; 3University of Tübingen, CESifo; 4University of Tübingen, CESifo, NoCeT
Earlier work found evidence of a geographical linkages of aggregate foreign direct investment (FDI) across countries and country-pairs. We use data on the universe of German multinational enterprises (MNEs) to empirically explore how marginal investments at one foreign affiliate depend on investments at other affiliates within the same MNE. The empirical approach employs two channels or modes of cross-affiliate interdependence: more geography (capturing horizontal linkages) and output-input relationships within or across industries (which capturing vertical linkages). We find evidence of a significant interdependence of investments within the firm. In the firm-level data at hand, vertical linkages appear to be more important than horizontal ones. Investments at one location tend to stimulate investments at other locations of the same MNE, particularly if input linkages are strong. This relationship seems to be true for output linkages. Beyond vertical linkages, mere geographical nearness matters only to a minor extent.

Effects of a Sales Tax Increase on Firm Valuation: Free Cash Flow Approach to Individual Firm Data
Keiji Kubota1, Hitoshi Takehara2
1Chuo University, Japan; 2Naseda University, Japan
This paper investigates how firm values change by increased sales tax (and consumption-type VAT) rate and conduct analyses by applying plausible input values of tax rates including the corporate tax rate. Our computation is based on the residual income valuation model in accounting research, starting from the discounted free cash flow (DCF) model applied at the individual firm level. We interpolate future cash flow stream of firms from pro forma financial statements and find that an increase in the Internet penetration rate induces municipalities on the low-tax side of state borders to lower their local tax rates by more than municipalities on the high-tax side; this result is consistent with towns on the high-side having less brick-and-mortar stores and more consumers with easy non-Internet means of tax avoidance.

Tax Interdependence in the U.S. States
Claudio A. Agostini
University Adolfo Ibañez, Chile
State governments finance their expenditures with multiple tax instruments, so when collections from one source decline, they are typically compensated by greater revenues from other sources. This paper addresses the important question of the extent to which personal and corporate income taxes are used to compensate for sales tax fluctuations within the U.S. states. The results show that a one percent decrease in the sales tax revenue per capita is associated with a 3 percent or a 0.9 percent increase in the corporate and personal income tax revenue per capita respectively. On average then, an exogenous reduction of $4.5 in the sales tax revenue per capita is compensated, ceteris paribus, with an increase of either $3.4 in the collections per capita from corporate taxes or $3.6 in the ones from personal income taxes.

Tax Planning of Married Couples in East and West Germany: Are there Differences?
Katharina Erbe
University Erlangen-Nuremberg, Germany
This study evaluates the tax planning behavior of East and West German married couples with regard to the allocation of tax schedules between the spouses. The paper focuses on the choice of “tax classes” (Steuerklassen), which can differ between spouses in the German tax law, depending on the decision of the partners. The analysis utilizes administrative data from the German income tax statistics for the year 2004. The results of an alternative specific conditional logit estimation indicate that West German couples are more likely to choose different tax schedules for the spouses than East Germans, and West Germans are more likely to allocate the advantageous tax schedule to the husband instead of the wife. These findings may be explained by differences in socialization of people due to different political regimes in Germany before 1990.

Household bargaining and the design of couples' income taxation
Helmut Cremer1, Jean-Marie Lozachmeur1, Dario Maldonado2, Kerstin Roeder3
1Toulouse School of Economics, France; 2Universidad del Rosario, Bogota, Colombia; 3LMU, Germany
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The paper studies the design of couples’ income taxation when decisions within the couple are made according to some bargaining scheme. Specifically, the couple maximizes a weighted sum of the spouses’ utilities. In the first part of the paper, the spouses’ bargaining weights (specific to each couple) are exogenously given. In the second part, these bargaining weights are endogenous, and depend on the spouses’ respective contributions to total family income. The social welfare function is utilitarian. We show that the expression for a spouses’ marginal income tax rate includes a "Pigouvian" (paternalistic) and an incentive term. With exogenous weights the Pigouvian term favors a marginal subsidy (tax) for the high-wage (low-wage) spouse, whose labor supply otherwise tends to be too low (high). In some cases both terms have the same sign and imply a positive marginal tax for the low-wage spouse and a negative one for the high-wage spouse.

Tax Treatment of Bequests when Donor Benefits do not Count

Robin Broadway1, Katherine Cuff2
1Queen's University, Canada; 2McMaster University, Canada

In this paper, we study the consequences for bequest taxation of giving less than full social weight to the benefit to donors. We analyze a simple model of parents and children with different skills where parents differ in their preferences for bequests. The government implements nonlinear income taxes on both parents and children as well as a linear inheritance tax, and gives differential linear bequest tax credits to donors based on income. The nonlinear income taxes take standard forms. The inheritance tax and bequest tax credits are of indeterminate absolute level and together determine the effective price of net bequests. This effective price plays both an externality-correcting and redistributive role. The optimal effective price will depend on the social weight given to donor benefits and the share of donors of a given skill type.

MARKET ENTRY, CORRUPTION AND TAX EVASION

André Seidl1, Thum Marcel
TU-Dresden, Germany

Corruption and tax evasion are often mentioned as impediments to growth. In the economic literature, both phenomena are mostly treated separately. In this paper, we will argue that corruption and tax evasion have to be considered simultaneously. Bribery officials is illegal; therefore, bribes are usually paid from hidden accounts. Hence, financing bribes almost always goes along with tax evasion. We extend the literature on corruption by modeling the financing side of corruption. It turns out that fighting tax evasion can result in some unexpected side effects, if corrupt officials control the market entry of firms. There is a U-shaped relationship between the costs of tax evasion and the market entry of firms. Furthermore, a revenue maximizing government may not have an incentive to monitor the tax statement of firms too closely. Increasing the costs of tax evasion can decrease total tax revenues.

Government Consumption and the Allocation of Informal and Formal Work Time

Marcelo Arbex1, Isabela Furtado2, Enlinson Mattos3
1University of Windsor; 2Fundação Getulio Vargas, Brazil; 3Fundação Getulio Vargas, Brazil

We explicitly model how households spend their time in the formal and informal sectors and evaluate how publicly provided goods with and without market substitutes affect time allocation. We sort goods into two groups according to whether or not the good has close substitutes being provided by the government. We present empirical tests for this model using Brazilian data (PNAD -National Household Sample Survey) 2008 and 2009. Our results suggest that consumption of goods that present private sector substitutes affect negatively formal labor hours of working. On the other hand, larger consumptions of publicly provided goods without substitutes are associated with an increase in formal labor market hours. This could suggest that individuals might value more exclusive government activities (and are willing to pay taxes for that).

Industrial foundations in the tax system

Søren Bo Nielsen
Copenhagen Business School, Denmark

This paper attempts to place industrial foundations (IFs; similar to trusts) in the tax system. Basic desires as to the structure and logic in the tax system imply clear consequences for the taxation of different types of income. However, the premise “people pay taxes” does not fit industrial foundations. What should we do? The paper explores the implications of treating IFs as if they were individuals. It shows that the optimal effective price will depend on the social weight given to donor benefits and the share of donors of a given skill type. The optimal effective price will determine the effective price of net bequests. This effective price plays both an externality-correcting and redistributive role. The optimal effective price will depend on the social weight given to donor benefits and the share of donors of a given skill type.

Taxes and Mistakes: What’s in a Sufficient Statistic?

Daniel Rock
University of Michigan, United States of America

What determines the efficiency cost of taxation in the presence of optimization errors? Employing recent results quantifying efficiency cost when consumers are subject to biases, this paper shows how budget adjustment rules, biasing, and the source of bias affect efficiency cost. Budget adjustment rules govern how taxpayers meet their budget constraint in spite of misperceptions. Complete consideration of budget adjustment rules shows why simply detecting misperception of taxes is insufficient for welfare. An application to “ironing” — the confusion of average and marginal tax rates — leads to a clarification of prior welfare analysis of ironing. Finally, if consumers “debias” at sufficiently high stakes, policymakers’ attempts to exploit biases to reduce inefficiency — like switching from high- to low-salience taxes — can actually increase inefficiency. Any cognitive costs of debiasing exacerbate this “curse of debiasing.”
Optimal Inefficient Production
Bas Jacobs
Erasmus University Rotterdam, Netherlands

This paper develops a model of optimal non-linear income and commodity taxation to analyze the desirability of aggregate production efficiency. In contrast to Diamond and Mitriss (1971) individuals are assumed to have different production technologies to transform inputs into outputs. It is then demonstrated that the production efficiency theorem breaks down. Output that is produced in sectors in which high- (low-) ability agents have a comparative advantage should be taxed at higher (lower) rates. In addition, output that is produced in sectors where labor demand is more elastic should be taxed relatively less. The Atkinson-Stiglitz theorem also breaks down as optimal commodity taxation is not uniform even if all individuals have identical preferences that are weakly separable. Policy implications of the breakdowns of the Diamond-Mitriss and Atkinson-Stiglitz theorems for capital taxation, taxation of intermediate goods, trade policy, non-uniform sectoral taxation, public production and social cost-benefit analysis are discussed.

The world is flat: Existing tax benefit systems approximate a linear one
Andreas Peichl
University of Mannheim, Germany

Tax benefit systems around the world have evolved to quite complex entities resulting in recurring calls for simplification — including Flat Tax proposals. In this paper, I reveal a statistical regularity that has not been documented before: when taking into account all different taxes and benefits, the relationship between net tax payments and gross income is approximately linear in many countries. My empirical analysis is based on micro data for 26 European countries and the US. I show that a linear tax system explains roughly on average 94% of the variation in taxes. Besides income, non-income characteristics are much more important than non-linearities in income. This has important implications for optimal taxation both in terms of the use of tagging as well as the accordance with the equal-sacrifice principle.

Why is the Long-run Capital Tax Zero? Reinterpreting the Chamley-Judd Result
Bas Jacobs1,2,3, Alessandra Victoria Rusu1
1Erasmus University Rotterdam, 2Tinbergen Institute, 3Netspar

Why is the optimal capital tax zero in the long run? This paper demonstrates that two standard intuitions do not apply. First, it is shown that the optimal capital income tax is zero both in partial and general equilibrium. Consequently, the intuition why the long-run capital tax is zero is neither because the entire capital tax burden is shifted to labor nor because of infinite tax distortions in finite time. Instead, this paper demonstrates that the steady state assumption forces all consumption demands to become linear in labor earnings. Hence, consumption Engel curves become linear in income in the steady state, irrespective of the utility function adopted. Complete standard optimal commodity-tax intuitions therefore explain why the optimal capital tax is zero.

11:30am - 1:00pm Welfare 1: Pensions
Session Chair: T. Scott Findley, Utah State University

Have the elderly in England saved optimally for retirement?
Rowena Crawford1, Cormac O'Dea2
1Institute for Fiscal Studies, 2Institute for Fiscal Studies, University College London

Using a model where households can save in either a safe asset or in an illiquid, tax-advantaged pension, we assess the extent to which those who recently reached the state pension age in the UK have saved optimally for retirement. The policy environment specified closely matches that prevailing in the UK. Using the model and administrative data linked with survey data from the English Longitudinal Study of Ageing, an optimal level of wealth is calculated for each household. This is compared to the levels of wealth observed in the data. Our results show that, for those born in the 1940s, the vast majority of households have wealth far greater than necessary to maintain their living standards into and through retirement.

Time-Inconsistent Preferences and the Mandatory Saving Role of Social Security
T. Scott Findley, Frank N. Cailingo
Utah State University, United States of America

We investigate the mandatory saving role of social security as a potential remedy to time-inconsistent saving behavior. Our model incorporates a generalized credit market that rests the extremes of missing credit markets and perfect credit markets, and it also includes the broad spectrum of possibilities in between. We prove that a fully-funded social security arrangement is irrelevant only at the knife edge of perfect credit markets. In other words, if there is a market imperfection of any degree then social security can improve the welfare of individual with time-inconsistent preferences. We conclude that non-standard preferences provide a more compelling justification for the mandatory saving role of social security than previously supposed.

11:30am - 1:00pm Welfare 2: Housing
Session Chair: Daniel Da Mata, IPEA

Is Social Housing Affordable?
Essi Helena Eerola1,2, Tuukka Saarimaa1
1Norwegian School of Economics, 2Université de Liège, CORE, TSE

Supply subsidies to owners of rental housing construction are often aimed at guaranteeing affordable housing for low-income households. This paper studies how the joint interaction of the family, the market and the state influences capital accumulation in a society in which children assistance to dependent parents is triggered by a family norm. We find that, with a family norm in place, the dynamics of capital accumulation differ from the ones of a standard Diamond (1965) model. For instance, if the family help is sizably more productive than the other LTC financing sources, a pay-as-you-go social insurance might foster capital accumulation.

The Effects of Fiscal Equalization on Housing Markets: Evidence from Brazil
Daniel Da Mata
IPEA, Brazil

This paper seeks to understand how local government policies on housing stimulus and city growth are affected by intergovernmental transfers. Cities that receive a smaller amount of fiscal transfers may have more incentives to stimulate housing growth to increase their local revenue and, as a result, they end up attracting more people and having a faster-growing housing sector. By contrast, the lack of fiscal windfalls may also generate lower provision of local public goods and generate emigration of current residents and a stagnated housing market. Quasi-
Experimental evidence from the distribution of intergovernmental transfers to Brazilian municipalities shows that locations less dependent on federal grants have a faster-growing housing sector and they end up attracting more migrants.

**Session Chair:** Daniel Harenberg, ETH Zurich

**Session:** Pay-As-You-Go Pension Systems

**Paper:** Increasing Life Expectancy and Pay-As-You-Go Pension Systems

**Authors:** Markus Knell (Oesterreichische Nationalbank, Austria)

In this paper, I study how PAYG pension systems of the notional defined contribution type can be designed such that they remain financially stable in the presence of increasing life expectancy. For this to happen, two crucial parameters must be set in an appropriate way. First, the remaining life expectancy has to be based on a cross-section measure and, second, the notional interest rate has to allow for a correction for labor force increases that are only due to rises in the retirement age which are necessary to "neutralize" the increase in life expectancy. It is shown that the self-stabilization is effective for various patterns of retirement behavior including a linearly rising, a constant, an optimally chosen and a stochastic retirement age.

**Title:** Transfer paradox under a pay-as-you-go pension system

**Authors:** Akiko Kaneko, Kojun Hamada, Mitsuyoshi Yanagihara

This paper examines how the international transfer affects the welfare levels both of the donor with a higher marginal propensity to save and the recipient with a lower marginal propensity to save, both of which take a pay-as-you-go pension system in one-sector overlapping generations model

We show that the pay-as-you-go pension magnifies the welfare effect by the transfer: It fosters the deterioration of the donor and the recipliant by the transfer when the world economy is dynamically efficient. This is because a pay-as-you-go pension hampers capital accumulation.

**Session:** Capital gains taxation

**Paper:** Social Security and the Interactions Between Aggregate and Idiosyncratic Risk

**Authors:** Daniel Harenberg, Alexander Ludwig

We ask whether a PAYG-financed social security system is welfare improving in an economy with idiosyncratic and aggregate risk. We argue that interactions between the two risks are important for this question. One is a direct interaction in the form of a countercyclical variance of idiosyncratic income risk. The other indirectly emerges over a household's life-cycle because retirement savings contain the history of idiosyncratic and aggregate shocks. In our quantitative analysis, we find that introducing social security with a contribution rate of two percent leads to welfare gains of 2.2% of lifetime consumption in expectation, despite substantial crowding out of capital. This welfare gain stands in contrast to the welfare losses documented in the previous literature, which studies one risk in isolation. We show that jointly modeling both risks is crucial: 60% of the welfare benefits from insurance result from the interactions of risks.

**Paper:** Capital Gains Taxation and the Cost of Capital: Evidence from Unanticipated Cross-Border Transfers of Tax Bases

**Authors:** Nacho Lopez, Jeffrey Hoopes

We show that capital gain tax, land value tax, counterspeculation option and limited period of land usage prevent the occurrence of land bubble. We show that capital gain tax, land value tax, counterspeculation option and limited period of land usage prevent the occurrence of land bubble. Cross-country differences in capital gains tax rates enable us to estimate the discount in target valuation on account of future capital gains. The estimation suggests that a one percentage point increase in the capital gains tax rate reduces the value of equity by 0.225. The implied average effective tax rate on capital gains is 7% and it raises the cost of capital by 5.3% of its no-tax level. This indicates that capital gains taxation is a significant cost to firms when issuing new equity.

**Paper:** Taxpayer Search for Information: Implications for Rational Attention

**Authors:** Jeffrey Hoopes, Daniel Reck, Joel Sternrood

We examine data on capital-gains-tax-related information search to determine when and how taxpayers acquire information. We find seasonal differences in information search driven by tax salience. We find that interactions between the two risks are important for this question. One is a direct interaction in the form of a countercyclical variance of idiosyncratic income risk. The other indirectly emerges over a household's life-cycle because retirement savings contain the history of idiosyncratic and aggregate shocks. In our quantitative analysis, we find that introducing social security with a contribution rate of two percent leads to welfare gains of 2.2% of lifetime consumption in expectation, despite substantial crowding out of capital. This welfare gain stands in contrast to the welfare losses documented in the previous literature, which studies one risk in isolation. We show that jointly modeling both risks is crucial: 60% of the welfare benefits from insurance result from the interactions of risks.

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welfare. Even if child allowances increase fertility, pension benefits do not always increase. Moreover, child allowances can not increase social welfare if the future generation’s utility is greatly discounted.

The difficult case of persuading women: experimental evidence from childcare
Vincenzo Galasso1, Paola Profeta2, Chiara Pronzato3, Francesco Billari4
1Boconi University, Italy; 2Boconi University, Italy; 3University of Torino; 4Oxford University
We use a randomized survey experiment to expose a sample of Italian women to an informational treatment on the positive consequences of formal childcare on children’s future educational attainments. We find treated women to increase their intention to use formal childcare and to reduce their intended use of grandparents. Perhaps surprisingly, we also find treated women to reduce their intended labor supply. These results hold for heterogeneous effects: low-educated women intend to reduce labor supply (and take more child care upon themselves), high-educated women intend to keep their role on the labor market. These findings are consistent with women responding to monetary incentive and having different preferences (or stereotypes) regarding maternal care.

Understanding the Gender Gap in Post-Secondary Schooling Participation: The Divergence between Girls and Boys Before and During High School
A. Abigail Payne
McMaster University, Canada
Only three decades ago women were substantially under-represented post-secondary institutions. Today the gender gap is reversed. Existing studies have argued that this gap can be traced to a growing disparity in high school academic performance of girls and boys. Since end-of-high school grades play such a large role in moderating entry to PSE, even a modest gender gap can lead to big differences in post secondary opportunities available to females versus male students. We analyze the evolution of the gender gap, using a large administrative data set on two cohorts of students who attended publicly funded high schools in Canada. We analyze the gender gap at each of three key stages through high school: (1) the first year of high school; (2) the last year of high school; and (3) entry to college and university. We show how the gaps at earlier stages contribute to the final gender gap in post-secondary participation.

The influence of ethnicity and culture on the valuation of environmental improvements - Results from a CVM study in Southwest China
Michael Althheim1, Tobias Bürger2, Oliver Friel3
1University of Hohenheim, Germany; 2Plymouth Marine Laboratory, England; 3University of Klaster – Landau
The provision of environmental goods by government creates social benefits which might vary between citizen groups with different cultural and ethnic backgrounds. These differences as well as the overall extent of benefits is analysed before the implementation of public projects in order to consider not only the efficiency aspects of such a project but also its distributional effects. In Southwest China we are facing a rapid deforestation for the development of rubber cultivation and at the same time find an ethnically highly diverse population. This Contingent Valuation study tries to assess the short-term and long-term benefits accruing from a public reforestation programme in Xishuangbanna and their distribution among different ethnic groups living in that region. The results show that different ethnic groups value short-term and future benefits of reforestation differently and that these differences can be explained by the different cultural and historical backgrounds of these ethnic groups.

Investment and Adaptation as Commitment Devices in Climate Politics
Clemens Heuson2, Wolfgang Peters1, Reimund Schwarze2, Anna-Katharina Topo3
1European University Viadrina Frankfurt (Oder), Germany; 2Helmholtz Centre for Environmental Research Leipzig, Germany
The strategic roles of adaptation and technological investment in international climate politics have been analyzed within various approaches. What makes this paper unique is that we investigate the combined impact of adaptation and investment on global mitigation where countries either decide on mitigation before or after adaptation. Considering a purely non-cooperative, game-theoretic framework, we find that by investment countries commit to lower national contributions to the global public good of mitigation. Moreover, the sequencing of adaptation before mitigation reinforces this strategic effect of technological investment. A subgame-perfect equilibrium yields a globally lower level of mitigation, and higher global costs of climate change when adaptation is decided before mitigation. Besides this theoretical contribution, the paper proposes some strategies to combat the unfortunate ‘rush to adaptation’ which can be currently observed in climate politics.

Actions and intentions to pay for environmental mitigation: Climate change concerns and the role of economic crisis
Christian Dienes
University of Wuppertal, Germany
We empirically investigate the association between climate change concern and individual’s taken actions and intention to pay for climate change mitigation. However, results also unveil that a moderating effect of economic forces can only be found with high educated individuals. 

Centralized and Decentralized Environmental Policies, Capital Mobility and Public Pollution Abatement
Nikos Tsakiris1, Panos Hatzipanayotou2, Michael Micale2
1University of Ioannina; 2Athens University of Economics and Business; 3University of Cyprus
We build a two regions general equilibrium model with cross-border pollution and either international or inter-regional capital mobility. To control pollution each region uses public pollution abatement and issues either intra-regionally or inter-regionally tradable emission permits. We analyze the non-cooperative (decentralized) and cooperative (centralized) equilibrium level of emission permits, and we examine when and how cross-border pollution and the type of capital mobility affect these equilibrium policies. We provide the welfare ranking of the various cases and we investigate under what conditions the decentralized and centralized equilibrium policies lead to the same result and are equally efficient.

About spatial interaction via public debt. This paper estimates the spatial interdependence in tax and spending competition by ‘competing’ on debt. While the existing spatial econometric literature focuses on tax and spending competition, very little is known about spatial interaction via public debt. This paper estimates the spatial interdependence of public debt among German municipalities using a panel on municipalities in the two largest German states from 1999 to 2006. We find significant and robust interaction across debt of neighboring municipalities, which we compare to spatial tax and spending interactions. The results indicate that a municipality increases its per capita debt by 16-33 Euro as a reaction to an increase of 100 Euro in neighboring municipalities.

Trust in Government and Fiscal Adjustments
Dirk Bursian, Alfons J. Weichenrieder, Jochen Zimmer
Goethe University Frankfurt, Germany
The paper looks at the determinants of fiscal adjustments as reflected in the primary surplus of countries. Our conjecture is that governments will usually find it more attractive to pursue fiscal adjustments in a situation of relatively high growth, but they also consider the impact of cutbacks in government behavior the expectation is that mainly high trust governments will be in a position to defer consolidation to years with higher growth. Overall, our analysis of a panel of European countries provides support for this expectation. The difference in fiscal policies depending
on government trust levels may help explaining why better governed countries have been found to have less severe business cycles. It suggests that trust and credibility play an important role not only in monetary policy, but also in fiscal policy.

The Track Record of Fiscal Forecasting in the EU
Antonio Afonso
ISEG, Portugal
We study the deviations between the budget balance ratio forecasts and the outcomes in the European Commission vintage forecasts for the period 1969-2011 and in the Portuguese official forecasts for the period 1977-2011. The European panel reveals significance (absence of significance) of investment (unemployment) deviations for the budget-to-GDP ratio. Countries with better fiscal rules present more favourable deviations. For Portugal, there is evidence of unfavourable errors about the budget balance in nominal currency in most years, which has been offset (totally or partially) by a favourable nominal GDP effect deviation.

Austrian Public Debt Growth: A Public Choice Perspective
Rainhard Neck1, Gottfried Haberl2, Andrea Klinglmair3
1Alpen-Adria-Universität Klagenfurt, Austria; 2Danube University Krems; 3Institute for Advanced Studies
Sustainability of public deficit and debt in the long run has received much attention in the international political agenda. This paper analyses whether Austrian fiscal policies have been sustainable during the last five decades. Tests indicate that Austrian fiscal policies were sustainable from 1960 to 1974, while from 1975 on public debt grew much more rapidly. Starting in 1975, the rate of unemployment played a significant role in the sense of a counter-cyclical orientation of Austrian fiscal policy as part of the concept of "Austro-Keynesianism". The development of public debt in Austria seems to be driven not primarily by ideology, but by structural causes and a shift of the budgetary policy paradigm. We find some empirical evidence that governments in Austria dominated solely by one party run higher deficits than coalitions of the two large parties or the two conservative parties. There are no indications of a political business cycle.

2:00 pm - 4:00 pm
Room 354, Main Building
Session Chair: Tom Van Veen, Maastricht University/Nijenrode Business University
FiscPol 2: Public debt II
The perils of sovereign default: Looking for the right haircut.
Michel Guillaud1, Hubert Kempe2
1U. Evry, 2ENS-Cachan, France
Abstract: We address three issues related to sovereign default in a macroeconomic model: its cause, its frequency and the policy response after default. Taking into account a default rule, we distinguish the "default threshold" from the "unsustainability threshold". The former one corresponds to the upper limit to public debt beyond which it becomes unsustainable; the latter one to the level above which, absent any further shock, the dynamics of public debt leads to future default. The unsustainability threshold increases with the level of debt and specified by the default rule agreed by the contractors. We show that a "successful" default rule is such that the post-default risk premium is small enough and contributes to a decreasing debt-to-output ratio. This implies that the haircut on public debt must be sufficiently high.

Money Overhang, Credit Overhang and Financial Imbalances in the Euro Area
Tom Van Veen1, Clemens Kool2, Erik de Regt3
1Maastricht University/Nijenrode Business University, Netherlands; 2Utrecht School of Economics, Utrecht University, Netherlands; 3School of Business and Economics, Maastricht University, Netherlands
This paper focusses on the relation between external imbalances and domestic money and credit growth in the euro area. We compute money and credit overhang both for the euro area as a whole and for individual member countries. Our results show that both aggregate money and credit overhang have trend-like increased since the early 2000s. The increase in money overhang has been rather evenly spread over the member states but the increase in credit overhang has been unevenly spread and has made the most pronounced for the GIPS countries in isolation, net debt flows do play a significant role to explain money and credit overhang.

Holdout: Rogue behaviour or rational decision?
Maximilian Stephan, Janine-Denise Tamme
University of Freiburg, Germany
The model presented here serves to illustrate that a holdout is by no means destructive investor behaviour but a rational investment decision. This investment decision is characterised by the mean-variance approach. We will demonstrate that at some point during the Greek (2012) and Argentine (2005) debt restructuring programs it was reasonable for the investor to hold out.

2:00 pm - 4:00 pm
A 13, Palazzo Rosso
Session Chair: Marco Sahm, Technische Universität München
FiscPol 3: Financing of public spending
Advance-Purchase Financing of Projects with Few Buyers
Marco Sahm
Technische Universität München, Germany
I investigate a simple model of advance-purchase contracts as a mode of financing costly projects. The analysis can easily be reinterpreted as a model of monopolistic provision of excludable public goods under private information. A monopolist has to meet some capital requirement in order to start production and sell the related good to a limited number of potential buyers. The potential buyers are privately informed about their willingness to pay. I find that advance-purchase arrangements allow to finance more costly projects than traditional funding sources. The monopolist is able to use advance-purchase surcharges as a price discrimination device. He will prefer advance-purchase financing over traditional funding if the capital requirement is sufficiently large. However, the discriminatory power is limited by the problem of free-riding which aggravates for an increasing number of potential buyers.

Manipulating discretionary grants: Evidence from a German state
Markus Reischmann
Ifo Institut, Germany
We investigate whether politicians manipulate intergovernmental grants. Our unique dataset contains information on discretionary consumption grants and discretionary investment grants in a German state over the period 2009-2011. The results show that the incumbent state government manipulated grants to the municipalities. Consumption grants are higher in municipalities where the election outcome is close (swing electorates). Investment grants are higher in state electorates where the dominant government is on government. The grant pattern indicates that government ideology and tactical considerations influence the grant distribution.

Geographical Allocation of Budget Adjustments under a Discretionary Executive
Cecilia Rumi1, Walter Contr1,2
1Universidad Nacional de La Plata, Argentine Republic; 2FIEL, Argentine Republic
Taking the allocation of budget credits as given, this paper presents a model in which a central government adjusts and allocates accrued expenditures among provinces by minimizing a loss function that weights different jurisdictions in different fashion. Using unexplored information of the Argentine federal budget process for the period 1997-2005, we test a simple condition on the allocation of budget adjustments among provinces and present evidence that these adjustments are correlated with (i) macro (and revenue) forecast errors incurred in the formulation phase of the budget process and (ii) the political alignment between the president and the provincial governments, suggesting a tacit redistribution of funds under the president's discretion.

2:00 pm - 4:00 pm
A 14, Palazzo Rosso
FiscPol 4: Decentralisation
Session Chair: Willem Sar, KU LEUVEN
Fiscal adjustment and balanced-budget-rules: Evidence from a Norwegian reform
Arend Ove Høiland, Lars-Erik Borge
Norwegian School of Economics, Norway
In Norway, central control of local government borrowing and budgeting was relaxed in 2001. Prior to 2001 budgets and borrowing in all local governments had to be approved by the central government. Since 2001, control has been more selective and applies only to local governments that have violated the balanced-budget-rule. Local governments subject to control are placed in a register. This register receives large attention in the public debate and works as a "fit of shame". We investigate possible disciplinary effects of the register. The main
hypothesis is that local governments that run deficits and thereby are in danger of being placed in the register will take actions to avoid this. An implication of this hypothesis is that the current deficit will be more affected by past deficits after the reform. The empirical analysis confirms a change in deficit dynamics.

**Decentralization and progressive taxation**

Simon Berret, Mark Schelker  
University of Fribourg, Switzerland

While an important strand of the literature argues that decentralization might enhance allocative efficiency, standard theory of fiscal federalism also suggests negative redistributive effects. For this reason, centralized redistribution is proposed. The assignment of these two public sector functions, i.e., resource allocation at the local level and income redistribution at the upper level of government, is thus well established. Based on the joint direct taxation system in force in Switzerland – the separation of the decision to set the rate of progression at the cantonal level from the decision to set the 'level' of taxation at the municipal level – we investigate the influence of varying degrees of decentralization on the general 'level' as well as the degree of redistribution in the cantonal income tax schedules. Our empirical results indicate that more decentralized jurisdictions feature generally lower income taxes and impose higher rates of progression.

**Fiscal decentralization and regional income in Korea**

Hyuna Kim  
Korea Institute of Public Finance, Korea, Republic of (South Korea)

Fiscal decentralization in Korea changed significantly since the 1991 push towards local autonomy; policy makers are still assessing the effects of this devolution. This paper attempts to examine how local fiscal share out of national expenditure (decentralization) affects the growth of regional incomes. It will show the relationship between fiscal decentralization and economic growth with more recent data and with careful attention to the effects of the components of fiscal structure. The empirical results support the ideas that the expansion of local expenditure and the degree of tax-benefit ratio may encourage the growth of regional income. These findings demonstrate the importance of the specification of the local expenditure structure variables, including transfer payments. In Korea, fiscal decentralization may be evaluated as an instrument in economic growth.

**Soft budget constraints in a federation: The effect of regional affiliation**

Willem Sas  
KU LEUVEN, Belgium

This paper revisits the soft budget constraint problem, pushing sub-central (states) borrowing to the limit in multi-tiered countries. Accounting for the institutional design and political practice common to many federations, bargaining and log-rolling are introduced to the analysis. In our intertemporal model, a federal legislature of locally elected representatives bargains on federal grants going to the states. As a result, voters can affect federal candidates' in favour of looser state public spending than otherwise expected. This strategic voting not only leads to overly generous bailout policies. Also, and compared to a setting where federal decision making does not follow from bargaining and regional affiliation, states over-borrow more inefficiently. Allowing for heterogeneity in state income and population does not affect this inefficient outcome. Lower relative per capita incomes even boost federal generosity and subsequent over-borrowing by the states.

**Retired but not withdrawn: Does Retirement Induce Participation in Social Activities ?**

Anne Laferrère  
INSEE, CREST, France

In old age retirement rules. We show negative and significant effect of retirement on both health and cognitive abilities. We also show evidence of significant heterogeneity across occupational groups. In particular, the negative effect of retirement disappears and turn to be even positive for those working in very physically demanding jobs.

**Optimal Health and Pension Policy with Biologically Founded Human Ageing**

Volker Grossmann¹, Holger Strulik²  
¹University of Fribourg, Switzerland; ²University of Göttingen, Germany

This paper integrates into public economics a biologically founded, stochastic process of individual ageing. The novel approach makes it possible to investigate theoretically and quantitatively the interaction between health and retirement policy for welfare and from a budgetary point of view. In particular, we derive the optimal design of the public insurance system behind the veil of ignorance and its implications for health inequality. Calibrating our model to Germany, we find that the health contribution rate and particularly health spending for the elderly may be considerably too low. Interestingly, spending more on health of the elderly is predicted to lead to more health inequality, however. Moreover, this strategic voting not only leads to overly generous bailout policies. Also, and compared to a setting where federal decision making does not follow from bargaining and regional affiliation, states over-borrow more inefficiently. Allowing for heterogeneity in state income and population does not affect this inefficient outcome. Lower relative per capita incomes even boost federal generosity and subsequent over-borrowing by the states.

**How Local Electoral Systems Shape Intergovernmental Relationships: Some Empirical Evidence from Italian Municipalities**

Emanuele Bracco¹, Alberto Brugnoli²  
¹Lancaster University, United Kingdom; ²Università di Bergamo

Different electoral systems offer very different incentives to parties and coalitions of voters, and demand different political strategies from potential candidates and chief executives. Italian mayors and city councils are elected through two different electoral systems according to the
Do Electoral Rules Alter the Effect of Fiscal Transfers? Evidence from German Municipalities

Marko Koestenbauer1, Peter Egger2, Michael Smart2

1ETH Zurich, KOF, Switzerland; 2University of Konstanz, Germany

The paper empirically analyses whether electoral rules make legislators differently responsive to changes in fiscal incentives. Key to the analysis are two unique reforms in the German state of Lower Saxony which changed (i) the municipal charter by replacing the council-manager system (featuring appointed mayors) with a mayor-council system (with directly-elected mayors) and (ii) the fiscal incentives inherent to the equalization system. We find that municipalities with appointed mayors react less strongly to changes in fiscal incentives. The change in municipal tax rates is three times smaller compared with a system of direct mayoral elections. We point to the different electoral incentives of mayors in the two systems to explain the result.

The allocation of grants to Brussels municipalities: the effect of partisan alignment

Geert Jennes

KULeuven, Belgium

This paper is one of the first to our knowledge to investigate the politicisation of intergovernmental grants per individual party in a coalition, hence distinguishing between the effect of being a large versus the effect of being a small coalition partner. Rather surprisingly it finds that municipalities of the Brussels Region that are party-politically aligned with small parties in power at one or more of the Brussels municipalities’ subsidising levels receive more discretionary grants than municipalities that are aligned with larger parties. This finding is obtained by instrumentalising power in the electoral system at the municipal level with cases of being in power after the formation of an anti-coalition, i.e. a coalition from which the dominant party in a municipality has been excluded, and with 1st ever municipal coalition participation of a political entity, both deemed exogenous to grants received.

The Business of American Democracy: Citizens United, Independent Spending, and Elections

Tilman Klumpp1, Hugo M. Mialon2, Michael A. Williams3

1University of Alberta, Canada; 2Emory University; 3Competition Economics, LLC

In Citizens United v. FEC (2010), the U.S. Supreme Court ruled that restrictions on independent political expenditures by corporations and labor unions are unconstitutional. We analyze the effects of Citizens United on state election outcomes. We find that Citizens United is associated with increases, spending on roads decreases, consistent with the hypothesis that large municipalities to a larger degree internalize the costs of local roads in terms of less available resources for other public services. I do not find differences in preferences can explain the finding.


NovoPark

Korea Institute of Public Finance, Korea, Republic of (South Korea)

Presidential elections in Korea in the eighties and nineties provide an opportunity to examine the role of political patronage in a newly formed democracy. We examine whether the bureaucratic reshuffling which accompanies presidential changes depends on the political connections of the public officials. We use data on all public prosecutors in Korea between 1992-2000 and find that ranking in the public prosecutor’s office depends on the particular political connections of the public prosecutor. We find that the transfer policy of left-wing state governments favors aligned municipalities, while that of right-wing state governments favors unaligned municipalities. The explanation is that the right-wing state governments faced only few aligned municipalities during their tenure, while the left-wing governments had stronger local support. The fact that high-level governments with weak support at the local level use transfers to buy off unaligned municipalities is a novel finding and suggests that prevailing theories on the political economy of intergovernmental transfers are incomplete.

Political alignment and intergovernmental transfers in parliamentary systems

Thushyanthan Baskaran1, Zolah Hessami1

1University of Konstanz, Germany; 2University of Goettingen, Germany

This paper explores the causal relationship between state-municipality political alignment and the allocation of discretionary transfers. Our dataset covers municipalities from the German federal state of Hesse over the 1989-2010 period. Since Hessian municipalities have a parliamentary system, we use a perturbation procedure to classify close election outcomes. One of our methodological contributions is to adapt existing regression discontinuity designs to this particular setting. We find that the transfer policy of left-wing state governments favors aligned municipalities, while that of right-wing state governments favors unaligned municipalities. The explanation is that the right-wing state governments faced only few aligned municipalities during their tenure, while the left-wing governments had stronger local support. The fact that high-level governments with weak support at the local level use transfers to buy off unaligned municipalities is a novel finding and suggests that prevailing theories on the political economy of intergovernmental transfers are incomplete.

Tax Morale and Reciprocity. A Case Study from Vietnam

Bjorn Jahnke

Leibniz University Hannover, Germany

The intention of this paper is to analyze the impact of horizontal and vertical reciprocity on tax morale in Vietnam. To the knowledge of the author it is novel in the tax compliance literature to study both dimensions of reciprocity for a developing country. The analysis is based on a consumer survey in the City of Hue which combines and extends questions from previous versions of the European and the World Value Survey. The result of this study is that both...
measures significantly affect tax morale in Vietnam but that vertical reciprocity has a higher impact. The paper also observes a high level of tax morale and largely positive attitudes towards paying taxes in Vietnam while cheating on taxes is perceived to be widespread.

**Effectiveness of Fund Management at Local Government Bodies in Nepal**

*Narayan Premad Paudel*
Kathmandu University School of Management, Kathmandu, Nepal, Nepal

**Abstract**
The study has examined the effectiveness of fund management at local government bodies in Nepal. Many problems could be observed at the local level, lack of management units, in terms of management of fund, lack of capacity, lack of elected representatives at grassroots level, political transition, lack of capacity to use information, and weak institutional mechanism. The study reports that the fund usage should be easily available and comprehensible to the general public so that people can extract data, compare them, analyze them, and use them as per their needs. The study further highlights that the government need to accommodate on the adequacy of the fund, proper mechanism of budget spent, and further focus on enhancing the efficiency of financial planning and budgetary process at the local level.

**Elections and Economic Development**

*Thushyanthan Baskaran*, *Brian Min*, *Uppal Yogan*  
1University of Goettingen, Germany; 2University of Michigan, Ann Arbor; 3Youngstown State University

We study at the constituency level whether Indian state governments induce political business cycles. Our dataset encompasses 600,000 Indian villages, which are consolidated into 66,618 state-level electoral constituencies. Using various light output measures as proxies for economic conditions in a constituency, we explore whether light output increases in election years. Our main contribution is a credible identification of electoral cycles by focusing on bye-elections held in selected constituencies for exogenous reasons. Our results show that state governments induce large electoral cycles. Single-party governments manipulate more than coalition governments. Manipulation is also stronger in contested constituencies.

**Taxation of Walloon Municipalities: is there room for yardstick competition, intellectual trend and partisan monopoly effect?**

*Marcel G. Gerard*, *Laurent van Malderen*  
1Université catholique de Louvain, Belgium; 2Université catholique de Louvain, Belgium

Three sources of tax interactions among local jurisdictions are usually considered: expenditure spillover, tax competition and yardstick competition. However, another source is the Intellectual Trend. According to that hypothesis, politicians of the same party behave similarly: they mimic each other’s policies. Moreover partisan politics also act through a monopoly power effect linked to several terms of power for the same party.

The paper proposes an empirical analysis of taxation of Walloon municipalities. Yardstick hypothesis, intellectual trend hypothesis and potential partisan monopoly power effect are tested. Spatial econometrics tools are used along a panel of local taxes data from 1983 to 2008 and political data. Results confirm yardstick competition among Walloon municipalities but not behaviors in line with the intellectual trend hypothesis. Moreover evidence is found of a partisan monopoly power effect for the local personal income tax. Finally the presence of an electoral cycle is also clearly documented.

**Tax Competition and “Race to the Bottom” in Tax Rates: Evidence from India**

*Sithanu Nair*
Indian Institute of Management, Kolkata (IIMK), India

One of the major conclusions of the theoretical literature on tax competition among sub-national governments is that it ends up in inefficiently low level of taxes – or a “race to the bottom” in tax rates – on mobile bases in the competing jurisdictions. However, the empirical evidence on this phenomenon is practically non-existent, provoking some scholars to consider the description of tax competition as involving a race to the bottom in tax rates as “quite misleading” (Oates, 1999; Brueckner, 2000). This paper is a modest attempt to prove that a race to the bottom in tax rates indeed emerges as a result of tax competition among sub-national governments in the context of tax-based competition for cross-border shoppers/entrepreneurs.

**Economic Fiscalization, Tax Salience, and Tax Competition**

*Martin Affeney-Bartlischer*
IWH, Germany

In this paper we are going to analyze decentralized revenue policies in a federal state if taxpayers are inattentive to some tax instruments. Jurisdictions try to attenuate the pressures of inter-regional competition for mobile factors by substituting tax instruments that stand in the limelight and attract taxpayers’ attention with less salient ones. Accordingly, with an appropriate assignment of revenue functions jurisdictions engage in broadening their tax bases in order to gain a margin for cuts of the statutory tax rates. In this connection, we address the question to which extent substitution effects that stems form tax salience effects may suppress the under-exploitation of tax bases that typically goes along with fiscal equalization.

**International Tax leadership among Asymmetric Countries**

*Jean Hindriks*, *Yukihiko Nishimura*  
1Universite Catholique de Louvain, Belgium; 2Osaka University, Japan

Multinational companies can shift profit and income between branches in order to reduce the overall tax liabilities of the company. The result is a low level of taxes – or a “race to the bottom” in tax rates – on mobile bases in the competing jurisdictions. However, the empirical evidence on this phenomenon is practically non-existent, provoking some scholars to consider the description of tax competition as involving a race to the bottom in tax rates as “quite misleading” (Oates, 1999; Brueckner, 2000). This paper is a modest attempt to prove that a race to the bottom in tax rates indeed emerges as a result of tax competition among sub-national governments in the context of tax-based competition for cross-border shoppers/entrepreneurs.

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**Testing the Capitalization Theory in a Transitional Economy: Education Quality and Property Value in Urban China**

*Yilin Hou1, Qiang Ren2, Haitao Ma2*  
1Syracuse University, United States of America; 2Central University of Finance and Economics, China

This research extends the capitalization theory into a new context, enriching the literature with theoretical modifications and empirical evidence. This research uses a recent pilot local property tax in China and a multi-wave hedonic data set of residential property in China’s megacities: the quality of education and real property values in China’s megacities: the quality of elementary education is a key determinant of the marginal differences of property value.
Local infrastructure and property taxation have been examined by scholars, the connection between them is not. This paper assembles a set of county level data and parcel data in the state of Georgia, employs two-stage method with instruments and OLS estimators, and connects local infrastructure and property tax in local public finance. We find: for rural and small urban counties, a one dollar increase of property tax revenue returns to residents 40 cents in local infrastructure expenditure; for medium and large urban counties it is 60 cents. Our results argue that the effect is much larger for rural parcels. The land price elasticity on infrastructure investment is 1.42 for rural parcels compared to 0.57 for urban parcels. Different from studies using data in different states, our analyses are in the same institutional and legal circumstances; we extend results from metro cities to a comparison between urban and rural counties.

Who’s Taxing Whom? Empirical Evidence on Place-Based Policy Making when Industries are Agglomerated

Marius Brülhart1, Helen Simpson2
1University of Lausanne, Switzerland; 2University of Bristol, UK

We examine whether firms and governments take account of agglomeration economics as predicted by models of economic geography. Specifically, we study the generosity of governments in allocating plant-specific subsidies which aim to create jobs in economically lagging regions. Using administrative data on both grant applications and offers from a major place-based policy in Great Britain, we test the hypothesis that in the magnitude of their offers, governments internalise the fact that firms in more agglomerated industries should be less sensitive to financial inducements. We find that firms appear to some extent to internalise localisation benefits in their grant applications, and that government agencies reflect this in the generosity of their subsidy offers. However, we also find evidence that local government agencies structure their offers so as to try and preserve existing employment in more agglomerated industries in areas with a higher percentage of industry employment.

The determinants of local tax setting in the event of a tax system under reform: the case of Italian municipal property tax

Alberto Zanardi3, Cerrado Pollastri2
1University of Bologna, Italy; 2Istat, Italy

We develop a theory of cross-border income shifting in response to personal taxation, and examine its implications for the revenue potential estimates, shifting taxable income between provinces accounts for about two-thirds of total tax avoidance in response to unilateral provincial tax reforms. Using data on top income shares for Canadian provinces around a significant reform in subnational taxation in Canada. According to our estimates, shifting taxable income between provinces accounts for about two-thirds of total tax avoidance in response to unilateral provincial tax changes. Implications for design of federal income tax policies are discussed.

The long run effects of taxes and tax competition on top income shares: an empirical investigation

Christian Frey, Christoph Gorgas, Christoph André Schaltegger
University of Lucerne, Switzerland

We provide empirical evidence on the effect of tax policy on income concentration in Switzerland over the long run. Swiss cantons enjoy considerable autonomy with respect to taxation, which makes it possible to study the impact of the income tax burden as well as the influence of tax competition. Using panel regressions covering all Swiss cantons over the years from 1917 to 2009 we find the expected negative effect of the cantonal tax burden on the income share of top earners. Further we find evidence that tax competition is a driving force behind the income shares of the top 1 and 0.5 percent. Lower tax rates in neighbor cantons increase the competitive pressure and cantons paribus reduce top income shares in the respective canton. For the very top incomes (the top 0.1 and 0.01 percent) tax competition seems to be an issue of the last 30 years.

The Fixed-Bracket Average Treatment Effect: A Constructive Alternative to LATE Analysis for Tax Policy

Caroline E. Weber
University of Oregon, United States of America

This paper analyzes the conditions under which it is possible to obtain a causal average treatment effect of a tax policy change, which I term the Fixed-Bracket Average Treatment Effect (FBATE). Local Average Treatment Effect (LATE) analysis does not apply in this context. FBATE identifies the average treatment effect for individuals with no incentive to switch tax brackets in response to a tax reform or other shock that affects the bracket in which an individual is located. The fact that the estimate is only informative for this subpopulation has important implications for the policy relevance of this parameter. The paper also shows that using an alternative definition of treatment relative to what is usually employed in the literature obtains a causal average treatment effect for a larger subpopulation under weaker assumptions. This paper has important implications for all policy analysis with simulated instruments.

Keynote II: Wealth Inequality, Savings, and Bequest Motives

Session Chair: Katherine Cuff, McMaster University

Wealth Inequality, Savings, and Bequest Motives
Mariacristina De Nardi
University College London, United Kingdom

Slides for Prof. Mariacristina De Nardi’s plenary lecture

IIPF Members GA: General Assembly of IIPF Members

5:30pm - 7:00pm
Aula Magna, Main Building

Print View
Overview and details of the sessions of this conference. Please select a date or room to show only sessions at that day or location. Please select a single session for detailed view (with abstracts and downloads if available).

Date: Thursday, 21/Aug/2014  
9:00am - 11:00am  
A 11, Palazzo Rosso

**Session Chair:** Arjan Lejour, CPB Netherlands Bureau for Economic Policy Analysis

**Tax treaties and the Allocation of Taxing Rights with Developing Countries**

Dimitri Paolini1, Pasquale Pistone2, Giuseppe Pulina3, Martin Zagler4  
1University of Padova, Italy; 2University of Milan, Italy; 3University of Salerno, Italy; 4University of Luxembourg

We examine the impact of bilateral and multilateral tax treaties on bilateral FDI stocks. First, we regress the effects of treaties on FDI based on an extensive database of all OECD countries from 1985 onwards. We use geographic and institutional instruments to correct for the endogeneity of treaties. We show that the impact of treaties on bilateral FDI is significant and increases by about 50 percent. Moreover, the EU parent subsidiary directive doubles bilateral FDI stocks.

**The Effect of Moving to a Territorial Tax System on Profit Repatriations: Evidence from Japan**

Makoto Hasegawa1, Kozo Kiyota2  
1National Graduate Institute for Policy Studies (GRIPS), Japan; 2Keio Economic Observatory, Keio University, Japan

The design of international tax policies, regarding whether and how to tax corporate incomes earned in foreign countries, has received a great deal of attention from policymakers and economists. Japan's worldwide tax system taxed foreign source income upon repatriation. To stimulate dividend repatriations from Japanese-owned foreign affiliates, Japan introduced a foreign dividend exemption in 2009 that exempts from home country taxation dividends remitted by Japanese-owned foreign affiliates to their parent firms. This paper examines the effect of dividend exemption on profit repatriations by Japanese multinationals. We find no evidence that the dividend exemption system stimulated dividend repatriations of the foreign firms is likely to be beneficial for banks, consumers, and taxpayers alike. In this setting we consider two types of financial integration. A reduction in the transaction costs of cross-border banking reduces aggregate taxpayers in the bank's home country. Moreover, each bank chooses the share of lending allocated to domestic and to foreign firms, respectively. Competitive firms in each country produce goods in an uncertain productive environment and borrow either from the domestic or the foreign bank. Domestic banks can choose their levels of monitoring firms, and thus the level of risk-taking, but risks are ultimately borne by taxpayers in the bank's home country. Moreover, each bank chooses the share of lending allocated to domestic and foreign banks, respectively.

**International Fiscal Policy Coordination and GDP Comovement**

Nicholas Sly, Caroline Weber  
University of Oregon, United States of America

In this paper we demonstrate that international coordination on fiscal policy is an important avenue by which national economies become more integrated, thereby influencing the transmission of macroeconomic shocks between countries. Using a 30-year panel of quarterly GDP fluctuations from a broad set of countries, we find that coordinated changes in fiscal policy rules -- as indicated by the signing of a bilateral tax treaty -- increase business cycle comovement by 1/2 a standard deviation. Bilateral tax treaties also increase comovement in shocks to nations' GDP trends, demonstrating the permanent effects of coordination on fiscal policy rules. We estimate trend and business cycle components of GDP trends, demonstrating the permanent effects of coordination on fiscal policy rules. We estimate trend and business cycle components of GDP trends, demonstrating the permanent effects of coordination on fiscal policy rules. We estimate trend and business cycle components of GDP trends, demonstrating the permanent effects of coordination on fiscal policy rules.

**Dodging Robin Hood: Responses to France and Italy's Financial Transaction Taxes**

Maria Coetti  
University of California, Berkeley, United States of America

I look at the effect of the introduction of financial transaction taxes in equity markets in France and Italy in 2012 and 2013, respectively, on asset returns, trading volume and market volatility. Using two natural experiments in a difference-in-differences design, I identify the 'after-tax' and 'pre-tax' returns on four broad categories of assets, and am able to account for as much as 60% of the reported revenue shortfalls. By far the strongest behavioral response comes from high-frequency trading lock-in on regulated exchanges, with an extraordinarily high tax elasticity in the order of -9. The results shed light on previously neglected features of optimal FTT design.

**Capital regulation and trade in banking services**

Andreas Hauffel1, Ian Wooton2  
1University of Munich, Germany; 2University of Strathclyde, U.K.

We set up a two-country model of trade in financial services where banks' overall loan volume is fixed by a capital requirement set in its home country. Competitive firms in each country produce goods in an uncertain productive environment and borrow either from the domestic or the foreign bank. Domestic banks can choose their levels of monitoring firms, and thus the level of risk-taking, but risks are ultimately borne by taxpayers in the bank's home country. Moreover, each bank chooses the share of lending allocated to domestic and to foreign banks, respectively.

In this setting we consider two types of financial integration. A reduction in the transaction costs of cross-border banking reduces aggregate output and increases risk-taking, thus harming consumers and taxpayers in both countries. In contrast, a reduction in the costs of screening foreign firms is likely to be beneficial for banks, consumers, and taxpayers alike.

**The Taxation of Bilateral Trade with Endogenous Information**

Tri Vi Dang1, Florian Mounath2  
1University of California, Berkeley, United States of America; 2University of Strathclyde, U.K.

We examine the effect of the introduction of financial transaction taxes in equity markets in France and Italy in 2012 and 2013, respectively, on asset returns, trading volume and market volatility. Using two natural experiments in a difference-in-differences design, I identify the 'after-tax' and 'pre-tax' returns on four broad categories of assets, and am able to account for as much as 60% of the reported revenue shortfalls. By far the strongest behavioral response comes from high-frequency trading lock-in on regulated exchanges, with an extraordinarily high tax elasticity in the order of -9. The results shed light on previously neglected features of optimal FTT design.

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This paper analyzes the effects of taxation on trade in a decentralized market. We show that a tax on profits and a transaction tax have opposite implications for information acquisition and trade in the canonical take-it-and-leave-it bargaining model. A (marginal) increase of a transaction tax can lead to more information production and lower the probability of efficient trade. In contrast, a (marginal) increase of a profit tax can reduce the incentive to produce information and increase the probability of efficient trade. The taxation of profits can be efficiency enhancing when information is endogenous, while it has no effect when private information is exogenous.

### Economic Effects of the Taxation of Banks as Corporations: An Analysis in a Simple Industrial Organization Model

**Timothy J. Goodspeed**

Hunter College and Graduate Center - CUNY, United States of America

Taxation of the banking sector is an under-researched area in public economics. Our goal here is to partially fill this gap by analyzing different ways to tax banks as a corporation. As discussed in Freixas and Rochet (1999) Arrow-Debreu models (with perfect financial markets) are not very useful for analyzing the banking sector as banks become redundant and essentially serve no useful purpose in such models. Two distinct types of models have been developed to explain the usefulness of banks, one relying on incomplete information, and a second that emphasizes the role of banks in providing services such as the management of loans and deposits, associated with Monti (1972) and Klein (1971). We analyze three types of taxes (a tax on bank assets, a tax on bank deposits, and a tax on bank profits) in this model under different types of market structure.

### BusTax 5: Taxation and innovation

**Session Chair:** Diego d’Andria, Friedrich Schiller University of Jena

**Taxation and incentives to innovate: a principal-agent approach**

Diego d’Andria

Friedrich Schiller University of Jena, Germany

A principal-agent multilending model is used to explore the effects of different tax schemes on innovation in a pure knowledge economy. Corporate taxes and labor income taxes can affect both the firm owner's and the employee's incentives to commit to innovative tasks, when the former compensates the latter (a manager, technical or R&D employee) by means of variable pay tied to measures of the company's success. Results point to a complementary role between "patent box" tax incentives and reductions in the tax rate levied on profit sharing schemes. This complementarity holds, albeit with different relative importance for the two tax incentives, also with non-deductible labor costs, with a stochastic innovation value coupled with a risk-averse agent, and with multiple principals competing for talented agents.

### The Global Effects of R&D Tax Incentives: Evidence from Micro-Data

**Martin Baumann, Bodo Knoll, Nadine Riedel**

University of Hohenheim, Germany

A growing empirical literature suggests that R&D tax incentives are instrumental in raising domestic R&D activity. In policy debates this finding is often interpreted to lend support to the notion that R&D tax incentives increase national welfare by internalizing knowledge spillovers to other agents in the economy and raising inefficiently low R&D levels. Our paper stresses that much of the observed increase in R&D activity in response to R&D tax incentives is in fact related to R&D activities that are facilitated by European multinational firms, we find a positive impact of domestic R&D tax incentives on affiliates' R&D activity and a negative one for foreign tax incentives provided at other group locations. Quantitatively, the findings suggest that around 80% of the observed increase in R&D activities is related to relocations of R&D across country borders.

### The Impact of Corporate Taxes on R&D and Patent Holdings

**Tobias Böhni, Nadine Riedel, Bodo Knoll**

University of Münster, Germany

We provide evidence that patenting strategies are exploited as a device to transfer income to low-tax jurisdictions. Using data on the population of corporate patent applications to the European Patent Office, we show that the location of R&D investment and patent ownership is geographically separated in a non-negligible number of cases. Moreover, our results suggest that this geographical split is partly motivated by tax considerations. We find that countries which levy low patent income taxes attract ownership of foreign-invented patents, especially those of relatively high quality.

### The Trickle-Down Growth Hypothesis Revisited: Publicly Financed Higher Education versus Redistributive Transfers

**Sebastian Böhm1, Volker Grossmann2, Steger Thomas M.1**

1Leipzig University, Germany; 2University of Fribourg, Switzerland

This paper applies dynamic general equilibrium theory to shed light on two related research questions: (i) Does growth, triggered by an increase in public education expenditure on behalf of those with high learning ability, eventually trickle down to low ability workers and serve them better than redistributive transfers? (ii) Does expanding education of wealthy, high-ability households inevitably raise inequality of earnings and income over time? Our results suggest that, in the shorter run, low-ability workers lose from expanding others' educa- tion. For an extensive period, they are better off from promoting redistributive transfers. In the longer run, however, low-skilled workers eventually benefit more from the education policy. It leads to sustained increases in the skill premium and an inverted U-shaped pattern of income inequality.

### Endogenous Growth and Welfare Effects of Education Subsidies and Intergenerational Transfers

**Elena Del Rey1, Miguel-Angel Lopez-Garcia2**

1University of Girona; 2Autonomous University of Barcelona

In this paper we investigate the welfare effects of education subsidies and intergenerational transfers along an arbitrary, non-optimal balanced growth path in an overlapping generations model with both physical and human capital. An increase in the lump-sum tax paid by the working middle-aged translates into a lower accumulation of both physical and human capital (and thus a smaller growth rate). However, there can be non-monotonicities in the welfare effects of this policy change. An increase in the rate of education subsidy can either have a positive or a negative effect on the accumulation of both physical and human capital, but conditions that guarantee a clear-cut sign of the effect of education subsidies on welfare are derived. Some attention is given to the asymmetric comparative dynamics of introducing pay-as-you-go social security at the laissez faire equilibrium balanced growth path.

### Intergenerational Income Path with Physical Transfers and Human Capital Investment

**Joongho Kook**

Yokohama City University, Japan

This paper investigates an intergenerational income path with physical transfers as well as human capital investment. The latter, or the investment in education from parent to child, increases child income indirectly through the enhancement of the earnings capacity of child. According to the result, increasing investment in education raises the steady state income only when the contribution to income of earnings capacity is high. We examine the effects of investment in education on the steady state income by a simple simulation and provide some examples on how the intergenerational income path relates to income growth and distribution.

### A normative justification of compulsory education

**Alessandro Balestrino1,2, Lisa Grazzini3, Annalisa Luporini1,2**

1University of Pisa, Italy; 2CESifo, Germany; 3University of Florence, Italy

Using a household production model of educational choices, we characterise a free market situation in which some agents ("high-agers") send their children full-time and spend a sizable amount of resources on them, while others ("low-agers") educate them only partially. The free-market equilibrium is iniquitous. Public policy is thus called for, either for vertical or horizontal equity purposes (or both). Redistributive taxation may be counter-productive, especially in horizontal equity terms, as it forces some agents to move away from full-time education for their kids, and price subsidies are only moderately effective, since they only work on the intensive margin. A compulsory education package, financed by a redistributive tax system, may help achieve both types of equity. Redistributive taxation and compulsory education are therefore best seen as complementary policies.
9:00am - 11:00am
A 21, Palazzo Rosso

FiscPol 5: Fiscal stimulus
Session Chair: Jan- Egbert Sturm, ETH Zurich

On the Identification and Macroeconomic Effects of Fiscal Stimulus
Christian Breuer
Ifs Institute, Germany

Empirical studies on the effects of fiscal adjustments apply different approaches to identify discretionary changes in fiscal policy. The results of one strand of literature suggest that the effects of fiscal adjustments on GDP are small or even positive, particularly for spending cuts (expansionary austerity). I compare the macroeconomic effects of fiscal adjustments using alternative identification strategies for a panel of 30 OECD countries over the period 1980 to 2012 and show that the strategy chosen for identifying fiscal policy has a crucial impact on the estimated effects. My results suggest that large fiscal adjustments (both revenue and spending based) lead to economic contractions, after appropriate controlling for cyclical effects and one-off capital transfers. These findings rule out that fiscal stimulus and expansionary austerity is based on an incorrect measure of fiscal policy and needs to be reevaluated.

Investigating the Effect of Fiscal Stimulus under Zero Lower Bound in Japan
Kazuki Hiraga1, Hiroshi Morita2
1Tokai University, Japan; 2Hitsuhsusashi University, Japan

This paper investigates the effects of fiscal stimulus under zero lower bound using Japanese data and Regime-Switching structural VAR model. Theoretically, effect of fiscal stimulus is propagated under zero lower bound, such as Consumer Expenditure and Rebele (2011), Eggertson (2011) and Werning (2011). On the other hand, our result contradicts the theoretical prediction; i.e., fiscal multiplier in zero lower bound is smaller than that in positive interest rate regime. We obtain the results that the effects of government expenditure under the zero lower bound are not different from that under positive interest rate.

Substitution and income effects at the aggregate level: The effective budget constraint of the government and the flypaper effect
Cristian F. Sepúlveda
Tulane University, United States of America

This paper explains the effects of a change in lump-sum (private) income on the tax and expenditure decisions of a government constrained by taxpayers' behavioral responses to taxation. We show that pure income effects at the individual level can lead to three distinguishable effects on government decisions at the aggregate level. Fiscal responses can be broken up into a "net substitution effect," associated with a change in the marginal cost of public funds, a "private income effect," associated with the increase in private consumption, and a "public income effect," which is equivalent to the effect of intergovernmental transfers. It follows that the effects of lump-sum income and intergovernmental transfers on fiscal decisions are generally different, but they are consistent with empirical findings of the literature on the flypaper effect.

FiscPol 6: Fiscal rules
Session Chair: Stuart K Landon, University of Alberta

Stuart K Landon, Constance Smith
University of Alberta, Canada

The growth of debt and deficits has led many jurisdictions to consider fiscal rules. While there is considerable interest in rules, there is little evidence on the benefits of different types of fiscal rules. We use Monte Carlo techniques to examine the impact on welfare of several types of government expenditure rules. The simulation employs an expected intertemporal welfare function and the parameters of a three-variable structural VAR estimated using data for European countries. The VAR captures the interaction effects between spending, output and revenue. Welfare depends on the level and volatility of both government spending and private consumption. Most, but not all, of the fiscal rules examined increase welfare. The best fiscal rules also reduce government expenditure volatility by about one third. A simple rule, where government expenditure is set equal to a one-period ahead forecast of current revenue, performs as well as a more complicated Swiss-type rule.

Incentive Effects of Fiscal Rules on the Finance Minister's Behaviour: Evidence from Revenue Projections in Swiss Cantons
Florian Chatagny
ETH Zurich, Switzerland

In the current paper we explore the effect of the ideology of the finance minister on tax revenue projection errors and assess how fiscal rules alter this relationship. We use a panel dataset on 26 Swiss cantons over the period 1980-2007 as well as a new dataset on 99 finance ministers at the cantonal level. We find a positive effect of ideology on projection errors in the sense that a left wing finance minister produces more conservative forecasts. We also find negative interaction effect between fiscal rules and ideology. These results suggest that left wing finance ministers need to curb deficits more in order to signal the same level of competence than a right wing finance minister. It also suggests that fiscal rules render the signal less informative and reduce the incentive for left wing finance ministers to be more conservative.

The Maywood effect: On the mechanics of fiscal rules efficiency
Etienne Farvacque1, Martial Foucault2,3, Marcelin Joanis4
1Université de Haute, France; 2Sciences Po Paris, France; 3ORANO, Canada; 4Polytechnique Montréal, Canada

The paper looks at the effectiveness of fiscal rules in the American states. A first contribution is to examine how efficient fiscal rules are in achieving fiscal discipline, using a newly defined stringency index that decomposes rules in their political vs. legal procedural components. Then, a second contribution is to go deeper into the details of fiscal adjustments, by looking at the ways and means of fiscal rules. More particularly, we look at the expenditure programs that are most susceptible to suffer from cuts: we assess if and how decisions cut on, for example, education, wages or infrastructures. We finally assess which of the different revenue bases US states use to get their way out of a deficit. A third contribution is to explain the empirical features by a model of spending cuts and fiscal revenues adjustments.

The effects of fiscal rules on public finances and their identification
Mustafa Yeter, Friedrich Heinemann
ifo Institute, Germany

Many economic studies analyse the impact of fiscal rules and discuss their effectiveness in limiting excessive debt. A majority of these studies, however, neglect the crucial threshold issue of endogeneity. I propose a new identification approach which identifies the impact of fiscal rules free from effects driving simultaneously the fiscal performance and the existence or strength of rules at the country level. In its core, the approach relies on unexpected shocks in long-run growth in order to derive a setting free from unobserved fiscal preferences and to allow for causal interpretation.

Health 4: Health systems
Session Chair: Antti Moisio, Government Institute for Economic Research

Consolidating bureaucratic supply? The case of Italian health care (1982-2008)
Silvia Fedeli1, Leone Leonida2, Michele Santoni3
1Sapienza - University of Rome, Italy; 2Queen Mary University of London; 3Università degli Studi di Milano

The Italian National Health Service is characterised by a bureaucratic structure organised at a regional level, financed by central government. We develop a two-stage model showing how the preferences of a regional government for health care services shape the regional organisation. The model shows that a regional government prefers the supply by one consolidated agency if it demands services perceived as complements,
whereas it prefers the supply by two independent agencies if it demands services perceived as substitutes. We use this prediction for empirical analysis of the organisation of the Italian health care system, with a regional-panel from 1982 to 2008. We show that the number of regional agencies, taken as a proxy for health care decentralisation, is affected by complementary/substitute health care services demanded at a regional level. Our estimates show a positive (negative) correlation between the number of independent regional agencies and proxies of the government demand for substitutes/complements.

Break-Ups of Municipal Health Centre Federations: Expenditure and Efficiency Effects

Antti Moisio, Mika Kortelainen, Kalevi Luoma

Government Institute for Economic Research, Finland

Empirical evidence on economies of scale in healthcare is mostly based on the cost effects of hospital mergers. This paper approaches the economies of scale issue by analysing the break-ups of health centre federations. We use the difference-in-difference models to evaluate the break-up impacts on costs, outputs and efficiency of health centres in Finland between 1990 and 2013. To address potential non-random or endogenous treatment assignment we also utilize propensity score difference-in-difference approach. For cost efficiency estimation we use the non-parametric order-alpha method that is more suitable for small samples than the traditional efficiency estimators. Our results show that healthcare costs have grown considerably faster for the seceded health centres than for the similar non-seceded ones, while outputs have increased more for the former than for the latter group. Interestingly, we find the impact of break-ups to be insignificant on the productive efficiency of health centres.

Is Chinese government health expenditure ready for ageing society? - Evidence from Chinese healthcare equality data analysis

Mike Xu1,2, Diana Ooi1,3

1Hong Kong (Institute of Health Economics, Hong Kong S.A.R. (China)), 2University of Bayreuth, Germany, 3Hong Kong Polytechnic University, Hong Kong S.A.R. (China)

Chinese economic has growing rapidly for over 30 years but social welfare did not improve in same speed. Distinctions between different Chinese regions exist in healthcare government expenditure and this potential risk may lead to difficulties to Chinese healthcare universal coverage for sufficient health resource in era of ageing society. The paper aims to fill the blind points of previous researches focus on imbalance between elderly age group and government health expenditure in future simulation of ageing society, attend to provide reference for Chinese government in evaluating current status and proposed countermeasures. The results shows current Gini coefficient has already crossed threshold from relative equality (0.1495) to acceptable inequality (0.1856) in 2010. The situation will be further deteriorated in 2020, as Gini coefficient will skymneted to 0.3075 if Chinese government still maintain current configuration of health fund, and present arrangement will not be sustainable to encounter ageing society impact.

9:00am - 11:00am
A 32, Palazzo Rosso

PoI Econ 4: Voting behavior

Session Chair: Klaas Staal, University of Bonn

Lisbon and the Coherence of Council Votes

Klaas Staal1, Marco Fantoni2

1University of Bonn, Germany; 2DG-TAXUD, Belgium

This paper explores patterns of voting in the Council of the European Union. We analyze the full set of voting records for this institution between 2003 and 2009, i.e., under the Treaty of Nce. The relationship in voting behavior between two countries is measured by Spearman's rank correlation coefficients. Based on this relationship, we determine the support for the positions members states take in the Council. We evaluate whether these correlations can also be used as a prediction of future voting behavior, and we identify the effect the Treaty of Lisbon has on the support for the positions of the member states.

Voter Turnout and City Performance

Anna Lo Prete, Federico Revelli

University of Turin, Italy

We study the impact of exogenous variation in Italian municipal elections' voter turnout rates on city performance scores and elected mayors' indicators of valence: In a simple model of voluntary and costly expressive voting, we show that the cost of voting depresses voter turnout, yet can raise the chances of selecting higher valence candidates and thereby improve government performance. Empirically, we exploit exogenous variation in voter turnout rates through the 2000s due to the presence of concomitant regional, general and European parliament elections, and to weather conditions (rainfall) on the election day. The results from a number of specifications and quality of policy-making indicators consistently point to a negative causal impact of voter turnout rates on the performance of cities and the valence of mayors.


Benno Torgler1, David Stadelmann2, Marco Portmann3

1University of Fribourg, Switzerland; 2University of Bayreuth, Germany; 3Queensland University of Technology Brisbane, Australia

In Switzerland, two key church institutions – the Conference of Swiss Bishops (CSB) and the Federation of Protestant Churches (FPC) – make public recommendations on how to vote for certain referenda. We leverage this unique situation to directly measure religious organizations' power to shape human decision making. We employ an objective measure of voters' commitment to their religious organization to determine whether they are more likely to vote in line with this organization's recommendations. We find that voting recommendations do in fact matter, implying that even in a secularized world, religion plays a crucial role in voting decisions.

9:00am - 11:00am
A 31, Palazzo Rosso

PubEcon 4: Intermunicipal cooperation and competition

Session Chair: Sam Bucovetsky, York University

Centralization and Incentive Compatibility

Sam Bucovetsky

York University, Canada

Direct central government provision may guarantee the incentive compatibility of the optimal allocation, under asymmetric information about the cost of the public output in different jurisdictions. To achieve this, a low "basic" level of public output should be provided uniformly to all jurisdictions, but only those jurisdictions identifying themselves as low-cost should be allowed to "top-up" this basic level.

Interjurisdictional Competition with Adverse Selection

Ruben Hernandez-Murillo

Federal Reserve Bank of St. Louis, United States of America

We study the welfare consequences of imposing alternative regimes of competition between non-benevolent governments that compete for mobile firms which have private information on their degree of home bias. We find that a system of coarser policy instruments may improve welfare relative to competition with discretionary instruments, even when politicians are benevolent, because it reduces the costly rents that are granted to firms in equilibrium—at the cost of distorting output choices. We also find that the gains from resorting to constitutional constraints are maximal when communities are identical, but if the extent of asymmetry between locations (in terms of local market size or technological complementarities) increases, the advantages of the constrained regime decrease and can be overturned.

Identifying the Effects of Grants on Local Policies in the Presence of Grant Endogeneity and Grant Effect Heterogeneity

Diana Qiu1,3

1University of Bonn, Germany; 2DG-TAXUD, Belgium

We study the impact of exogenous variation in Italian municipal elections' voter turnout rates on city performance scores and elected mayors' indicators of valence: In a simple model of voluntary and costly expressive voting, we show that the cost of voting depresses voter turnout, yet can raise the chances of selecting higher valence candidates and thereby improve government performance. Empirically, we exploit exogenous variation in voter turnout rates through the 2000s due to the presence of concomitant regional, general and European parliament elections, and to weather conditions (rainfall) on the election day. The results from a number of specifications and quality of policy-making indicators consistently point to a negative causal impact of voter turnout rates on the performance of cities and the valence of mayors.
IIPF 2014 - ConfTool Pro - BrowseSessions

9:00am - 11:00am
A 33, Palazzo Rosso

Gender preferences
Session Chair: Bjørne Strom, Norwegian University of Science and Technology

Spill-over effects of affirmative action: political representation and the power of the elderly
Audilea Batranuță¹, Alessandro Casarici², Paola Profeta²
¹Institute for International Economic Studies (IIES) Stockholm University; ²University of Ferrara, Italy

There is evidence that age matters in politics. We study whether implementation of affirmative action policies on gender can generate additional effects on an alternative dimension of representation, namely, the age of politicians. We consider an Italian law which introduced gender quotas in candidate lists for local elections in 1993, and was abolished in 1995. As not all municipalities went through elections during this period, we can identify two groups of municipalities and use a Difference in differences estimation to analyze the effect of gender quotas on the age of elected politicians. We find that gender quotas are associated with election of politicians that are younger by more than one year. This effect is mainly due to the reduction in age of elected male politicians.

The casual effects of voting franchise on fiscal and election outcomes
Bjørne Strom¹, Torberg Falch², Per Tovmo³
¹Norwegian University of Science and Technology, Norway; ²Norwegian University of Science and Technology, Norway; ³Norwegian University of Science and Technology, Norway

The paper studies the effects of removing socioeconomic and gender restrictions on voting on fiscal and election outcomes. We use national voting reforms in Norwegian local and national elections in the beginning of the 20th century and exploit that the title of the reforms varied across municipalities to estimate causal effects. We find that extension of the voting franchise has small positive effects on some municipal expenditures, while the total spending effect is negative. Further, removing socioeconomic restrictions on female voting rights appears to have a negative effect. Finally, we find no robust evidence that removing socioeconomic restrictions on voting rights for women in parliamentary elections contributed to the growth of the Social democratic party.

Is there a Gender Gap in Preferences for Public Spending? Evidence from Germany
Tina Haussen
Freiburg-Schiller-University of Jena, Germany

In several empirical contributions researchers have found a gender gap in preferences for public spending. This paper analyzes the persistence of these gender gaps when income differences between individuals are taken into consideration. Using survey data from the years 1996 and 2006 of German respondents, we show that gender gaps in preferences vanish when we control for individual income relative to the German median income. The larger this income ratio, the lower the preferences for social security (health care, retirement and unemployment) but the larger the preferences for education spending. Controlling for pseudo individual income (the actual available income if income is shared between all household members), gender gaps in health care and retirement reappear. This may reflect an insurance motive of women who fear to lose the benefits from sharing income within the household.

9:00am - 11:00am
A 22, Palazzo Rosso

Efficiency in public input provision in two asymmetric jurisdictions with imperfect labour markets
Holger Gilitz¹, Johannes Pausaer²
¹Ministry of Economics, Labour, Energy and Transport of Saarland, Germany; ²Institute for Employment Research (IAB), Germany

This paper examines efficiency in public input provision in two large jurisdictions with imperfect labour markets. It analyses how equilibrium capital tax rates and public input provision levels differ between asymmetric jurisdictions that can strategically influence the interest rate on the common capital market in an international tax competition setting. In contrast to the scenario assuming competitive labour markets, the non-cooperative equilibrium is inefficient also when governments have capital and head taxes at disposal. As a source of the distortion in the tax structure between jurisdictions and the inefficiency in public input provision, which can be determined in at least one of the jurisdictions, we identify the governments' incentives to decrease unemployment, and a pecuniary externality in both jurisdictions. Efficiency in public input provision can be restored, however, if the set of fiscal instruments available for regional policy makers is extended by a labour tax.

Pareto improvements under Matching Mechanisms: General Preferences and An example
Weifeng Liu
Australian National University, Australia

Matching mechanisms have been proposed to mitigate underprovision of public goods in voluntary contribution models. This paper investigates Pareto-improving equilibria under various matching schemes with two heterogeneous players. The paper finds that: First, this two-stage matching mechanism avoids free riding and each player has incentives to provide matching contributions because the matching player is better off while the matched is worse off. Second, given any income distribution within the interior zone players can always implement small matching schemes to make them both better off. This finding is useful for cooperation, particularly in the context without complete information of global preferences or at the international level without a central government.

9:00am - 11:00am
A 23, Palazzo Rosso

Local infrastructures and externalities: does the size matter?
Massimiliano Ferraresi¹, Umberto Galmirin², Leoncio Rizzo³
¹University of Ferrara, Italy; ²University of Insubria, Italy; ³University of Trieste, Italy

We setup a simple theoretical model where citizens consume two local public goods, one provided by their own jurisdiction and the other provided by the neighboring jurisdiction. Solving the model leads to a strategic interaction between the two jurisdictions whose sensitivity depends on the jurisdiction’s size. We test the model by using financial and socio-economic data of the Italian province of Trento. In particular we estimate determinants of infrastructure stock by explicitly introducing the spatial lag and exploring its differential impact according to the population size of the considered municipality. We find that jurisdictions positively react to an increase in infrastructure, but the effect tends to vanish after a given population threshold.

Efficiency may improve when Defectors Exist
Takako Fujisawa-Grave¹, Masahiro Okuno-Fujimura², Nobue Suzuki³
¹Komazawa University, Japan; ²Keio University, Japan; ³Murashiro University, Japan

Voluntarily Separable Repealed Prisoner's Dilemma (Fujisawa-Grave and Okuno-Fujimura, 2009) has many kinds of equilibria. Focusing on monomorphic and bimorphic equilibria, we show that a bimorphic equilibrium consisting of cooperators and defectors is most efficient, under a mild payoff condition. This is a striking contrast to ordinary repeated Prisoner’s Dilemma, where the symmetric efficient payoff is achieved by the symmetric C-trigger equilibrium. Our result indicates that behavioral diversity can be beneficial for the society, when players are free to escape from personalized punishments.
We study deception choices and deception detection in a tax compliance experiment. We find large systematic differences in individual deception abilities. Tax payers are conscious about their own deception abilities. The empirical outcomes are in line with a theory suggesting that tax payers make their choices whether to underreport or report truthfully on the basis of their own deception ability. Tax payers with high deception ability are more likely to underreport. This selection effect is stronger if the fines for underreporting are higher. These results provide an (additional) reason why random audits are superior to audits based on discretionary choice.

**Committing-to-Rules and Compliance: Combined Laboratory and Field-Experimental Evidence**

### Ulrich Glogowsky, Tobias Cagali, Johannes Rincke

University Erlangen-Nuremberg, Germany

Requesting commitments to rules is a widespread instrument to foster rule compliance via promoting individuals' intrinsic motivations. This paper combines a randomized field experiment on cheating in exams, laboratory experiments, and survey techniques to identify the effects of commitments and close monitoring on compliance decisions. We find evidence that individuals cheat when detection probabilities are low, but do not fully exploit cheating possibilities. This evidence is that individuals are intrinsically motivated to comply. Commitments, aiming at promoting intrinsic motivations, do not have any effect on cheating. Close monitoring, as strong external incentive, eliminates cheating.

**A Factorial Survey on the Inheritance Tax, Social Norms, and Social Justice**

### Friedemann Richter, Martin Abraham, Kerstin Loret, Matthias Wrede

FU Berlin, Germany; 2Oslo Business School; 3Free University Brussels

This paper theoretically and empirically analyzes the acceptability of inheritance tax evasion. In the theoretical part, it builds on three different strands of literature from economics and sociology, namely on the tax evasion literature as initiated by the work of Becker (1968) and Allingham and Sandmo (1972), on recent developments in optimal taxation theory, and on the literature on social norms and institutions. To test the hypotheses, a Factorial Survey Design (Vignettes) was employed. It empirically confirms that closeness of kinship (protection of the family), asset type of inheritance and scope of evasion play a role for the acceptability of evasion. The results indicate that violating a compliance norm is to some extent justifiable if the underlying goal of the tax is not infringed by the evasion. In contrast, the norm violation is less acceptable, if the underlying goal is at stake.

### Tax reform evaluation using status quo based welfare comparison: An application to a consumption based income tax

Tanja Kim

Universität Liechtenstein, Liechtenstein

A necessary condition of equitable reforms is the principle of "equal treatment to equals", which can be tested with the "status quo based social welfare analysis" (Bourguignon, 2011a). This paper reviews the restrictions of such an approach, by applying it on a consumption tax. The comparative analysis reveals, that the "status quo based" welfare analysis shows no dominance in terms of social welfare – which is in contrast to the result of the standard utilitarian approach. This finding confirms the importance to flank the standard utilitarian analysis with a "status quo based" welfare analysis. Additionally is the approach of Bourguignon (2011a) extended towards a dynamic framework, which allows studying long-term welfare effects.

### What makes personal income taxes progressive? A decomposition across European countries

Francesco Fasigl, Gerlinde Verbit

University of Innsbruck, Italy

Over the last few years concern for income inequality has increased remarkably and the redistributive role played by taxation is of utmost importance in shaping the distribution of disposable income. We investigate the redistributive role of personal income taxes, with a focus on the EU-15 countries, using EUROMOD, the EU-wide tax-benefit model. In most of these countries the top tax rates have been reduced, as well as the number of tax bands. Hence, it is commonly thought that the progressivity of these taxes is lost. However, its effects on overall progressivity are less obvious than they may appear at first sight, as progressivity is not only determined by the bands and rate structure, but also by tax exemptions, tax allowances, deductions and credits. Cross-country comparison of the extent of progressivity and the ways in which this is obtained confirms the heterogeneity of the policy options adopted in different countries.

### Religios Heterogeneity and Fiscal Policy: Evidence from German Reunification

Ronny Freier\(^1\), Benny Gey\(^2\), Joshua Holm\(^3\)

\(^1\)DIW Berlin Germany; \(^2\)Free University Brussels

This paper theoretically and empirically analyzes the acceptability of inheritance tax evasion. In the theoretical part, it builds on three different strands of literature from economics and sociology, namely on the tax evasion literature as initiated by the work of Becker (1968) and Allingham and Sandmo (1972), on recent developments in optimal taxation theory, and on the literature on social norms and institutions. To test the hypotheses, a Factorial Survey Design (Vignettes) was employed. It empirically confirms that closeness of kinship (protection of the family), asset type of inheritance and scope of evasion play a role for the acceptability of evasion. The results indicate that violating a compliance norm is to some extent justifiable if the underlying goal of the tax is not infringed by the evasion. In contrast, the norm violation is less acceptable, if the underlying goal is at stake.

### The Political Economy of Labour Market Policies in Western and Eastern European countries

Koen Caminada, Kees Goudswaard, Olaf Van Vliet

Department of Economics, Leiden University, The Netherlands

In this paper we investigate the cross-country variation in net unemployment benefit replacement ratios, both for Western and Eastern European countries. Unemployment benefits are an important indicator for labour market policies. Especially on the roles of partisan politics and of corporatism. These factors have been extensively studied in the literature, but hardly for Eastern European countries, because of a lack of data. For this reason we assembled a dataset for 34 welfare states (1971-2009).

We find a significant positive correlation between left-wing governments and unemployment protection for both Western and Eastern European countries, but this linkage is conditional on the economic situation. Corporatism is also positively and significantly related to unemployment benefits. Surprisingly, this relationship is relatively strong for the group of Eastern European countries. Finally, within the EU we find a trend of convergence of unemployment benefit levels in the period 1990-2009.

### Employment protection and the market for innovations

Andreas Basset\(^1\), Christian Holm\(^2\)

\(^1\)Ludwig Maximilians Universität Munchen, Germany; \(^2\)ifo Institute of Economic Research

Can employment protection increase innovations and decrease output at the same time? To answer this question we develop an equilibrium matching model with an imperfect labor and innovation market. We calibrate our model to match US labor and product market statistics. We...
then take the calibrated model, switch on employment protection and show that our comparative static results are in line with the estimated impact of the adoption of wrongful dismissal laws in 13 US states on total factor productivity and innovation found in the literature. Our calibration results suggest that employment protection decreases output and total factor productivity despite the fact that it shifts economic activity towards innovation.

Health, Incentives and Activation
Caroline Hail1, Kaisa Kotakorpi2, Linus Liljeborg1, Jukka Pirttilä2
1Institute for Labor Market Policy Evaluation (IAFU), Sweden; 2University of Turku, Finland; 3University of Tampere, Finland
We study individual reactions to a labour market programme targeted at young unemployed in Sweden in 2007. The programme involved both monetary incentives i.e. changes in the tax transfer system designed to increase employment, as well as mandatory activation. We use a difference-in-difference strategy to analyse whether there are differences with respect to past health and school drop-out status in the way individuals reacted to the incentives and/or activation associated with the programme. Our hypothesis is that individuals who are in a difficult overall life situation may not be in a position to react to monetary incentives, and may be better helped by actual activation; whereas other individuals may respond to monetary incentives or the threat of activation (in which case activation programmes work more as a screening device). We use register data covering the entire Swedish population, including very detailed information on health.

9:00am - 11:00am
Welfare 5: Bequests, transfer and charity
Session Chair: Oscar Erikson, Research Institute of Industrial Economics
Estate division: Equal sharing as choice, social norm and legal requirement
Oscar Erikson1, Henry Ohlsson2
1Research Institute of Industrial Economics, Sweden; 2Upsala University, Upsala Center for Fiscal Studies, Sweden
This paper studies to what extent parents divide their estates unequally between their children and the determinants of this decision. Using a new dataset based on the estate reports for the entire population of deceased Swedes for 2002-2004 we find that only 2-12 percent of the estates are unequally divided. The relatively low frequency of unequal sharing in Sweden compared to for example the US could potentially be explained by contextual factors such as the inheritance law, the transfer tax system, the income distribution, and the welfare state. Results from models with family fixed effects show that bequests do not need to be used to compensate for income differences between children, suggesting that bequests are not guided by altruistic motives. Children who are likely to have provided services to the parent receive more than their siblings however. This suggests that, at least some bequests are guided by exchange motives.

Does Income Inequality Increase Charitable Giving?
A. Abigail Payne1, Justin Smith2
1McMaster University, Canada; 2Wilfrid Laurier University, Canada
Do households react to changes in the distribution of income in their neighbourhoods and localities in their charitable donations? The theoretical prediction of the effects of income inequality on giving is unclear. We study how the change in income inequality as measured at the neighbourhood and locality (municipality) levels affects reported giving by households in Canada between 1991 and 2006. We find, on average, that an increase in inequality will increase charitable giving. These results, however, are sensitive to the geographic dispersion of low and high income households in neighbourhoods that form a locality. There is evidence to suggest that the effect on donations is smaller in areas with high levels of inequality at both the neighbourhood and locality levels.

Does Welfare Spending Provide Labor Supply Disincentives?: The Case of Korean Social Assistance Program and Social Insurance
Seng Eun Choi
Korea Institute of Public Finance, Korea, Republic of (South Korea)
The paper analyzes labor supply effect of income transfer payments, using the second to eleventh waves of the KLIPS data for the period of 1999 to 2008. The estimated results show that transfer payment, National Basic Livelihood Security System, pension, and social insurance discourage labor supply, reducing both labor participation rate and hours of labor. The magnitudes of the estimates indicate that Korean social assistance program to provide work incentives are not enough to offset negative income and substitution effect of social insurance. The findings imply that earnings disregard and work fare features of social assistance program provides larger work disincentive than social insurance. The paper analyzes labor supply effect of income transfer payments, using the second to eleventh waves of the KLIPS data for the period of 1999 to 2008. The estimated results show that transfer payment, National Basic Livelihood Security System, pension, and social insurance discourage labor supply, reducing both labor participation rate and hours of labor. The magnitudes of the estimates indicate that Korean social assistance program provides larger work disincentive than social insurance. The findings imply that earnings disregard and work fare features of social insurance. The magnitudes of the estimates indicate that Korean social assistance program to provide work incentives are not enough to offset negative income and substitution effect of social assistance program to provide work incentives are not enough to offset negative income and substitution effect of social assistance program.

Rotten spouses, family transfers and public goods
Helmuth Cremer1, Kerstin Roeder2
1Toulouse School of Economics; 2LMU, Munich, Germany
We show that once interfamily exchanges are considered, Becker’s rotten kids mechanism has some remarkable implications that have gone hitherto unnoticed. It is not just beneficial for efficiency but it may have dramatic redistributive implications. Combined with a contribution game to a household public good, it may lead to an astonishing equalization of consumptions between spouses and parents, even when parents’ wealth levels differ. The most striking results obtain when wages are equal and when parents’ initial wealth levels are not too different. When wages are different but similar the outcome will be near efficient (and near egalitarian).

11:30am - 12:30pm
Aula Magna, Main Building
Keynote III: Financing Retirement: Where Have We Come From, and Where Do We Go from Here?
Session Chair: Monika Bittler, University of St. Gallen
Keynote Lecturer: Brigitte Madrian (Harvard University, USA)
Financing Retirement: Where Have We Come From, and Where Do We Go from Here?
Brigitte Madrian
Harvard University, United States of America
Slides for Prof. Brigitte Madrian's plenary lecture

7 von 7 05.03.2015 11:42
Redesigning the Welfare State for Aging Societies
August 20th – 23rd, 2014 – Lugano, Switzerland

Conference Agenda
Overview and details of the sessions of this conference. Please select a date or room to show only sessions at that day or location. Please select a single session for detailed view (with abstracts and downloads if available).

Date: Friday, 22/Aug/2014
9:00am - 11:00am
A 11, Palazzo Rosso

Session Overview

Envir 2: Fuel taxes
Session Chair: Massimo Filippini, Università della Svizzera Italiana / ETH Zurich

Does the Swiss Car Market Reward Fuel Efficient Cars? Evidence from Hedonic Pricing Regressions, a Regression Discontinuity Design, and Matching
Massimo Filippini1, Anna Alberini2, Markus Bareit3
1Universita della Svizzera Italiana / ETH Zurich, Switzerland; 2University of Maryland; 3ETH Zurich

To correct market failures due to the presence of negative externalities associated with energy consumption, governments have adopted a variety of policies, including taxes, subsidies, regulations and standards, and information-based policies such as labels. In 2003, Switzerland introduced a system of fuel economy labels, based on grades ranging from A to G, where A is best and G is worst. We use a rich dataset for Switzerland on cars and several methods (hedonic pricing regressions, regression discontinuity and a matching estimator) to answer three key research questions. First, what is the willingness to pay for fuel economy? Second, do Swiss drivers—or Swiss auto importers on their behalf—appear to do a one-to-one tradeoff between car purchase price and savings on fuel costs over the lifetime of the car? Third, does the label have an additional effect on price, all else the same, above and beyond that of fuel efficiency alone?

Fuel tax incidence in the EU: the interplay of ad valorem and specific taxation under imperfect competition
Marina Di Giacomo, Massimiliano Piacenza, Francesco Scervini, Gilberto Turati
Università di Torino, Italy

Fuel taxation is an important fiscal mechanism, that allows EU countries to implement transport policies, environmental actions, general energy policies, but also budget deficits control, agricultural and employment policies. The European heterogeneity in the structure and levels of taxes on mineral oils allows for the identification of the effects of fuel taxes on energy prices and public policies. Fuel taxation is an easy way for raising fiscal revenues. Its administrative costs are quite low, compliance costs for consumers are almost nil, and tax evasion is limited. The aim of the paper is breaking new ground in understanding the characteristics of the European fuel taxation system, and how they influence consumers, producers and public bodies decisions. We expect to contribute to: 1) the fuel tax incidence literature; 2) the policy debate on the effects of fuel taxes as fiscal mechanisms able to stabilize oil price peaks and to reach environmental targets.

Effects of a mileage tax for trucks
Simon Luechinger, Florian Roth
University of Lucerne, Switzerland

We evaluate the effect of the introduction of a mileage tax for trucks in Switzerland in 2001 on traffic volume and externalities. Using a regression discontinuity design, we find a reduction in overall truck traffic of around 4-6%, no effects on car traffic and time-shifted placebos, suggestive evidence for traffic substitution towards rail, and negative effects on nitrogen oxides at curbside monitors. With the synthetic control method, we find insignificant short-run reductions in traffic density similar to the regressions discontinuity results, but substantially larger effects for some later years.

Terminal peak in nonrenewable resource use
Hagen Schwerin
ETH Zürich, Switzerland

Increased fossil energy use is explained by sustained investment in production capacity. A continued increase is predicted to halt at the latest date of investment in this technology without a technology revolution or climate policy—in the early 22nd to the early 23rd century depending on the resource endowment, before renewable energy fully provides energy of consumption goods. The fossil energy use peaks locally at the latest period before efficiently stabilizing atmospheric carbon dioxide—in the 2080's to limit the carbon dioxide amount by 720 ppmv, so that renewable energy production gradually increases in a medium time interval.

9:00am - 11:00am
A 23, Palazzo Rosso

Session Overview

FiscPol 7: Spending and growth
Session Chair: Atsuyoshi Morozumi, University of Nottingham

Government spending shocks, sovereign risk and the exchange rate regime
Jasper Luukasen, Dennis Bonam
CPB, Netherlands, The Netherlands

Keynesian theory predicts output responses upon a fiscal expansion in a small open economy to be larger under fixed than floating exchange rates. We analyse the effects of fiscal expansions using a New Keynesian model and find that the reverse holds in the presence of sovereign default risk. By raising sovereign risk, a fiscal expansion worsens private credit conditions and reduces consumption; these adverse effects are offset by an exchange rate depreciation and a rise in exports under a float, yet not under a peg. We find that output responses can even be negative when exchange rates are held fixed, suggesting the possibility of expansionary fiscal consolidations.

Public expenditure composition and economic growth: the role of government accountability
Atsuyoshi Morozumi1, Francisco Veiga2
1University of Nottingham, United Kingdom; 2University of Minho, Portugal

This paper examines the role of institutions in the nexus between public spending and economic growth. Using a newly assembled dataset of 80 countries over the 1970-2010 period with disaggregated public spending, we show that only when institutions prompt governments to be accountable to the general public does the capital component of public spending significantly promote growth. Meanwhile, a rise in current spending does not allow robust growth-promoting potential, regardless of the level of government accountability. Our interpretation of these findings is that, while capital spending innately has a larger growth-fostering effect than current spending, inefficiencies in the former type of spending, caused by officeholders' rent-seeking behavior under unaccountable governments, mitigate its fostering effect.

Fiscal Policy Sustainability: New Evidence from State-Varying Models with Non-linear Thresholds
Gabriella Deborah Legrand1, Roberto de Santis2, Costas Milas3
1Keele University, CESifo, Rimini Centre for Economic Analysis, United Kingdom; 2European Central Bank, Fiscal Policy Division; 3University of Liverpool

We introduce non-linear sustainability tests conditional on endogenously estimated state-varying thresholds. These thresholds vary with fiscal disequilibria, the economic cycle and financial market conditions. Applied to fiscal policies pursued by the GIPS, our empirical results provide evidence of threshold behavior in terms of large versus small budgetary imbalances. Financial market pressure relaxes the debt-to-GDP
Fiscal consolidation with a view on economic growth
Carsten Colombier
Federal Finance Administration, Switzerland

crisis-ridden European countries such as Spain and Greece are struggling to make public finances sustainable. This has sparked a debate on whether a thrift-based or a growth-based consolidations strategy should be adopted. So far the debate has revolved predominantly around the short-term effect of fiscal consolidation measures. This paper switches the focus on the long-run impact by estimating how the composition of government expenditure affects economic growth. Recently, empirical research on debt consolidation is in all likelihood not successful if the growth rate of the economy is too low. This paper shows that, in particular, public expenditure on general government services, education, infrastructure and order and safety are growth-enhancing, whereas public expenditure on religion, culture and recreation is growth- retarding. Thus, policy-makers, who intend to implement austerity measures, should be aware of the fact that cutting productive public expenditure might run the risk to ‘defeat’ the consolidation strategy.

9:00am - 11:00am
A 22, Palazzo Rosso
FiscPol 8: Fiscal policy and debt
Session Chair: Estelle P. Dauchy, New Economic School
Haircut Size, Haircut Type and the Probability of Serial Sovereign Debt Restructurings
Christoph Schröder
ZEW Mannheim

This paper complements the empirical literature on sovereign debt restructurings by analyzing potential drivers of the probability of near-term follow-up restructurings. It looks for drivers of serial restructurings. I look for these drivers of serial restructurings, to ask whether there is certainly to debt renegotiation processes and outcomes that promote near-term follow-up restructurings. The probability of follow-up restructurings is estimated by means of survival models using a unique dataset that has kindly been provided by Crues and Trebesch (2013). The main findings are that more comprehensive debt remissions decrease the probability of serial restructurings significantly. At the same time, it does, in fact, seem to be important for the probability of serial restructurings whether a haircut includes outright debt relief in terms of a cut in the face value of the debt contract or whether it includes ‘only’ maturity extensions and/or interest rate reductions.

State Fiscal and Benefit Policies: A Tradeoff in Automatic Stabilization and Intergenerational Income Mobility
Estelle P. Dauchy1, Nathan Segent2
1New Economic School, Russian Federation; 2University of Utah, USA

We contrast the effectiveness of government interventions to dampen income shocks with their costs of distorting intergenerational income mobility. On the one hand, the occurrence of income and consumption shocks has increased over the past decades. On the other hand, individuals’ ability to smooth consumption against income shocks has decreased, and this has been linked to decreases in the insurance provided by the federal income tax. However, there is a tradeoff in government interventions meant to smooth income shocks. If income shocks are random then the tax and benefit system can provide insurance and increase welfare. However, it can also dampen income mobility both mechanically by dampening after-tax income growth and through distorting behavior. We use the PSID to decompose the impact of federal and state government interventions on the variance of intergenerational income and consumption into the part that captures insurance against income shocks and the part that distorts income mobility.

Debt brakes in the German states: Which governments take budget consolidation seriously?
Niklas Potratzek, Marina Riem, Christoph Schinke
Ifo Institute, Germany

In 2009 a new law on German debt brakes was passed – state governments are not allowed to run structural deficits after 2020. We investigate whether government ideology influences how state governments consolidate budgets. The results show that leftwing governments ran higher structural deficits than rightwing governments between 2010 and 2013. When controlling for the debt level, we find strong support for partisan politics. Left governments seem to overestimate tax revenues more than right ones to satisfy their electorate with additional expenditure plans. We find that more fragmented governments tend to produce more pessimistic tax revenue forecasts. One reason might be that at least one of the coalition members will be part of the next government, too. We do not find empirical evidence for political business cycles at all.

A debt management rule, fertility, and growth
Kazutoshi Miyazawa
Doshisha University, Japan

By introducing a debt management rule into an extended model of Japan and Enders (1990), we analyze a dynamic relationship between public debt, fertility, and per capita income growth. The rule proposed is simple and intuitive: public debt newly issued is an increasing function of the government’s primary balance. We show that the public debt-GDP ratio decreases monotonically toward zero, and both fertility rate and per capita income growth rate continue to increase in transition, if an initially indebted government adopts a tight management rule. Unfortunately, the long-run growth rate is low and the long-run fertility rate is high relative to the social optimal because of capital externality and a trade-off between fertility and bequests. The optimal policy requires an additional policy instrument, that is, a subsidy for bequests.

Analysis of Creative Accounting and its Impacts on Governments’ Financial Performance. The Case of the Swiss Cantons.
Maxima Clémenceau, Nils Soguel
University of Lausanne, Switzerland

This research aims at empirically identifying a possible impact of creative accounting on public deficits. More precisely, local governments may have incentives to resort to financial tricks in order to hide public surpluses. Such loopholes allow local governments to put expenditure under pressure and to justify higher tax rates than needed. In turn, these high tax rates should generate additional cash-flows that could be used in order to repay debt or to bail out cookie-jar reserves. Considering the second case, money accumulated into these reserves could be used in order to smooth fiscal balance over time. Using panel data relative to the 26 Swiss cantons over the period 1980 - 2012, we show that creative accounting operations allow to significantly decrease public deficits.

Bailouts and austerity
Thushyanthan Baskaran
University of Goettingen, Germany

This paper studies with disaggregated budget data how expenditures, revenues, and borrowing evolve in municipalities that receive bailouts. It asks, in particular, whether higher-level governments enforce austerity measures after bailing out indebted municipalities. The sample consists of 421 municipalities in the German federal state of Hesse over the 1997-2010 period. The results indicate that municipalities cut personnel, construction, and social expenditures, increase tax revenues and property tax rates, and reduce deficits after they receive a bailout from the state government. The state government appears to be both able and willing to enforce austerity after granting a bailout.

On the political economy of tax revenue forecasts – Evidence from OECD countries
Beate Jochimsen1,2, Robert Lehmann3
1Berlin School of Economics and Law, Germany; 2DIW; 3ifo

Today, a solid budget serves as an important quality signal for the electorate. Therefore, politicians might face an incentive to influence tax revenue forecasts which are widely regarded as a key element for budget setups. Looking at the time period from 1996 to 2012, we systematically analyze whether national tax revenue forecasts in 18 OECD countries are biased through political distortions. Based on several theoretical approaches drawn from the theories of political economy, we test four hypotheses using panel data estimation techniques. We find strong support for partisan politics. Left governments seem to overestimate tax revenues more than right ones to satisfy their electorate with additional expenditure plans. We find that more fragmented governments tend to produce more pessimistic tax revenue forecasts. One reason might be that at least one of the coalition members will be part of the next government, too. We do not find empirical evidence for political business cycles at all.
Panel 1: GIZ Policy Panel

New rules for global taxation - Challenges for developed countries

Session Chair: Matthias Witt, GIZ
Panellists:

- Michael Devereux, President of IIPF, Oxford University
- Stefania Knoth, German Federal Ministry of Finance (BMF)
- Logan Wort, African Tax Administration Forum (ATAF)

Panel 2: Long term impacts of early events in life

Session Chair: Monika Bütler, University of St. Gallen

Panelists:

- James P. Smith, Rand Corporation
- Christoph Weise, European Investment Bank
- Radim Bohacek, CERGE-EI

Trade and the Political Economy of Redistribution

Eckhard Janeba¹, Gonzague Vannooorenbergh²

¹University of Mannheim, Germany; ²Tiburg University

This paper analyses the effects of trade liberalisation on the political support for policies that redistribute income between workers in different sectors. We allow for worker heterogeneity and imperfect mobility of workers across sectors, giving rise to a trade-off between redistribution and the ineciency of the labor allocation. We compare two environments, autarky and small open economy, and present three main findings. First, redistributive policies are more likely to arise in a small open than in a closed economy. Second, if a redistributive policy is adopted in both situations, its nominal level is higher in autarky than in the small open economy. Third, even though voters choose redistributive policies with lower nominal value in open economies, the actual extent of redistribution in equilibrium is larger in the open than in the closed economy. We discuss our results in the context of the debate about the effects of globalisation on government activity.

Government ideology, Globalization, and Top Income Shares in OECD Countries

Christoph Schinke
Ifö Institute, Germany

I investigate how government ideology and globalization are associated with top income shares in 16 OECD countries over the period 1970 to 2010. I use the new World Top Incomes Database. Globalization is measured by the KOF index of globalization. The results show that the top 1% income share increased more under right-wing than under left-leaning governments. The effect was stronger when globalization proceeded more rapidly.

Aging and Deflation from a Fiscal Perspective

Hiduki Konishi, Koos Ueda
Waseda University, Japan

Negative correlations between inflation and demographic aging have been observed across nations recently. To understand the phenomenon from a political economy perspective, we embed the fiscal theory of the price level into an overlapping-generations model. We suppose that short-lived governments successively choose income tax rates and bond issues, considering political influence from existing generations and the expected policy responses of future governments. Our analysis reveals that the effects of aging depend on its causation; aging is deflationary when caused by an unexpected increase in longevity, but is inflationary when caused by a decline in the birth rate. Our analysis also sheds new light on the traditional debate about the burden of national debt. Because of price adjustment, the accumulation of government debt imposes no burden on future generations.

Redistributive Politics and Regional Economic Growth: Evidence from Japanese Prefectures

Hario Konosh
Seinan Gakuin University, Japan

This paper clarifies whether or not the distribution of interregional transfer or public investment to each region is affected by political influences and whether or not its expenditure contributes to regional economic growth. I employ a simultaneous-equation approach in order to obtain this aim, and estimate the regional distribution functions and the regional growth regression using a panel of Japanese prefectural level data for a period of 1989 to 2010. Empirical results show that (1) regional distribution of public investment or interregional transfer is affected by political factors such as governing party(LDP)'s incentive to buy votes and pressure by a local interest group, (2) the funds distributed to each region do not necessarily contribute regional economic growth. This finding may indicate that funds distributed to each region are not beneficial for citizens and become a kind of transfers for rent-seekers.

The Costs and Benefits of Mandatory Securities Regulation: Evidence from Market Reactions to the JOBS Act of 2012

Dhammika Dharmapala¹, Vic Khanna²
¹University of Illinois, Urbana, Illinois, United States of America; ²University of Michigan, Ann Arbor, Michigan, United States of America

The effect of mandatory securities regulation on firm value has been a longstanding concern across law, economics and finance. In 2012, Congress enacted the Jumpstart Our Business Startups (‘JOBS’) Act, relaxing disclosure and compliance obligations for a new category of firms known as “emerging growth companies” (EGCs). The JOBS Act’s definition of an EGC involved a limited degree of retroactivity, extending its application to firms that conducted initial public offerings (IPOs) between December 8, 2011 and April 5, 2012 (the day the bill became law).

The persistent effects of regional policy: Evidence from the West-German Zonenrandgebiet

Maximilian von Ehrlich¹, Tobias Seidel²
¹University of Bern, Switzerland; ²University of Duisburg-Essen

In this paper, we provide evidence on the contemporaneous and persistent effects of regional policy. We apply a quasi-experimental identification strategy exploiting the fact that municipalities in the West-German Zonenrandgebiet (ZRG) were eligible for substantial regional transfers during the Cold War. The ZRG was an approximately 40km-band adjacent to the Iron Curtain. Apart from determining transfer eligibility, this pure geographic threshold did not have any relevance. Using municipal data and satellite night light data, we find that the ZRG treatment led to an increase of income per km² of about 50 percent in 1986. Importantly, economic density remained high 16 years after the transfers had phased out. This speaks against unique equilibria determined by locational advantage, but rather strengthens market externalities as an important explanation for the spatial distribution of economic activity. We also examine several potential channels finding strong contemporaneous and persistent effects of transfers on population density and the business tax base.

Reaching the Poor in Nigeria: A Comparative Analysis of the Role of Microfinance Banks and Cooperatives

Adebayo Adedokun¹, Abiodun O. Folawewo²
¹McPherson University, Seriki Sotayo, Ogun State, Nigeria; ²University of Ibadan, Ibadan, Oyo State, Nigeria

This study investigates the role of microfinance banks and cooperatives in reaching the poor in Nigeria. Analyses are carried out in relation to how accessible and effective the two institutions' loans are to people in the country, especially the poor. Findings reveal that loan accessibility of microfinance banks is not certain for the poor. Likewise, loan effectiveness analysis confirms that the poor do not stand a chance to benefit from loans by the banks, giving loan credibility criteria and interest rate charged. However, cooperatives’ loans are more accessible to the poor; and loan effectiveness analysis reveals that the poor can grow above the poverty line and interest rate charged by cooperatives. The results of this study have important implication for poverty reduction, thereby recommends that cooperatives movement should be rekindled in Nigeria.

Panel 5: Political economy of redistribution

Session Chair: Eckhard Janeba, University of Mannheim

PolEcon 5: Political economy of redistribution

The actual extent of redistribution in equilibrium is larger in the open than in the closed economy. We discuss our results in the context of the debate about the effects of globalisation on government activity.

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Elites and Bank-Based Finance - A political economy model on the emergence of financial systems

Florian Buck1, Nikolaus Hildebrand2
1Center for Economic Studies, Germany; 2Ludwig Maximilians University

Why do some economic systems depend on bank financing while others rely on capital markets and bond financing? We propose a political economy model in which elites favor a bank-based system, which increases their rents due to reduced competition. If suffrage is restricted to the elite, this will result in poor corporate rights and more reliance on banks that offer substitute mechanisms of corporate governance. The lack of legal rights in history triggers path dependencies and explains the dominance of banks. We test the model's predictions by tracking the emergence and evolution of the bank-based financial system in Germany since the 19th century.

Common Pool Problems in Voluntary Municipal Mergers

Tuukka Saarimaa, Janne Tuukalainen
Government Institute for Economic Research, Finland

We analyze free-riding behavior of Finnish municipalities prior to municipal mergers. The merger process creates a temporary common pool problem, which arises because of a delay from the initial merger decision to the actual merger. Using a difference-in-differences strategy, we find large responses to free-riding incentives. Consistent with the "law of 1/n", the stronger free-riding incentive a municipality faced the more it increased its per capita debt and used up its cash reserves. These funds were spent mostly on investment and current expenditures. The results are somewhat surprising because the mergers were agreed upon voluntarily.

Cooperation and Trustworthiness in Repeated Interaction

Tobias Caepka, Ulrich Glogowsky, Johannes Rincke
Friedrich-Alexander-University Erlangen-Nürnberg, Germany

Cooperation in public good provision often depends on the trustworthiness of an administrator who may reduce contributors' returns from cooperation to her own benefit, and who herself may respond to the degree of cooperation among contributors. This paper analyzes the interdependencies between cooperation and trustworthiness in a repeated game that replaces the mechanical public good administration in the Public Good Game with a human administrator. We present a new approach for visualizing conditional behavior in repeated sequential games. Our approach identifies the causal effects of cooperation on trustworthiness and vice versa by combining standard methods from time-series analysis with a design based identification strategy. We find that contributors and the administrator strongly respond to each other, resulting in cooperation and trustworthiness being strongly mutually independent. Furthermore, cooperation and trustworthiness are rather driven by changes in cooperation than by changes in trustworthiness.

Cultural Biases in Government Make-or-Buy Decisions: Evidence from a Regression Discontinuity Approach

Laure Athiès1, Pascal Wicht2
1University of Lausanne, Switzerland; 2University of Lausanne, Switzerland

What determines governments' decisions for the mode of provision of their services? While the theoretical and empirical literature on this issue has mostly considered technical dimensions (contractual and public choice aspects), this paper emphasizes the role of culture and quantifies it. We build a representative database for contracting choices of municipalities in Switzerland and exploit the discontinuity at the Swiss language border at identical actual set of policies and institutions to analyze the causal effect of culture on the choice of how public services are provided. We find that French-speaking border municipalities are 50% less likely to contract with the private sector than their German-speaking adjacent municipalities, and this effect prevails over the effect of any technical dimension. Systematic differences in the level of confidence in public administration and private companies potentially explain this discrepancy in private sector participation in public services provision.

Teams Punish Less

Helke Auerwald1, Carsten Schmidt1, Marcel Thum1, Gaute Torsvik2
1TU Dresden, Germany; 2University of Bergen, Norway

Many decisions in politics and business are made by teams rather than by single individuals. In contrast, economic models typically assume an individual rational decision maker. A rapidly growing body of experimental literature investigates team decisions in different settings. We study team decisions in a public goods contribution game with a costly punishment option and compare it to the behavior of individuals in a laboratory experiment. We also consider different team decision-making rules (unanimity, majority). We find that teams contribute significantly more and punish less than individuals, regardless of the team decision rule. Overall, teams yield higher payoffs than individuals.

Local income tax competition and public goods with imperfect spillovers

Florian Kuhlig, Beat Hintermann
University of Basel, Switzerland

We extend the literature on income tax competition by allowing for inter-jurisdictional spillovers of public goods, which so far have been analyzed in a completely separate framework. Introducing spillovers to the tax competition model adds an inefficiency of decentralization in the form of underprovision of the public good. At the same time, it reduces incentives for tax competition and the resulting income segregation, and thus increases welfare. This is due to a redistribution pathway absent in models based on purely local public goods: Richer jurisdictions effectively subsidize poorer jurisdictions in the form of transboundary spillovers. This effect increases with the degree of spillovers and is maximized for the case of a pure public good.

Global Public Goods and Coalitions under Matching Mechanisms

Weifeng Liu
Australian National University, Australia

Matching mechanisms have been proposed to mitigate underprovision of public goods in voluntary contribution models. This paper investigates coalition formation under matching mechanisms with multiple players who have the same preference but different incomes. Given income heterogeneity within a certain range, there always exist small matching rates which make all members in the coalition better off. However, given other players in the coalition players have incentives to take free rides and the matching coalition does not exist. If players value their reputation, they would stay in the coalition when the gain of free riding is lower than the reputation loss. Due to heterogeneity, the matching coalition faces trade-offs between matching depth and breadth. The policy implication is that the matching rate can be flexibly set to compromise between cooperation depth and breadth and, more importantly, it may achieve Pareto-improving outcomes while avoiding international side payments.

The Dilemma of Delegating Search: Budgeting in the Public Employment Service

Thomas Karl Kuhn1, John Addison2, Martin Attemayer-Bartelscher2
1Chenrezing University of Technology, Germany; 2Moore School of Business, University of South Carolina; 2WH Halle

We propose an incentive scheme to overcome moral hazard inherent in local job centers' search efforts. The key idea is to link future staff capacity in a job center to its past performance. Staff capacity and effort are complimentary in the production of job matches. If the central
agency can commit to providing additional staff to reward a high match rate, caseworkers will respond when deciding on their supply of effort. They can then be incentivized to offer an efficient level of service even if effort is not verifiable and where, as in Germany, alternative (monetary) mechanisms are effectively precluded.

9:00am - 11:00am A 24, Palazzo Rosso

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Cost escalation in defence and public administration

Lars-Erik Borges1, Kittel Hove1, Tobias Lillevikeland2, Per Per Tommo1

1Norwegian University of Science and Technology, Norway; 2Norwegian Defence Research Establishment

The Bauml hypothesis predicts a steady increase in public sector costs relative to the private sector because of relatively slow productivity growth. In this paper we analyse cost escalation in the public sector with particular attention to defence using data from Norway. There is strong support for the Bauml hypothesis in the sense that relative public sector costs are non-stationary and growing over time. The Bauml effect is weaker in defence than in the rest of the public sector. Moreover, it is investigated to see whether the Bauml effect is driven by GDP and political fragmentation, both in defence and in the rest of the public sector.

Security Gradient and National Defense – The Optimal Choice between a Draft Army and a Professional Army

Vesa Kinnalainen1, Staffan Ringmo2

1University of Helsinki, Finland; 2Hanken School of Economics

The earlier work on the optimal design of the national security has focused on the opportunity cost of the draft in terms of foregone human capital formation. The current paper introduces the national security into the welfare analysis missing from the earlier work. This creates a trade-off between the private goods and the security as a public good in the social cost-benefit analysis. There are three major results. First, and arising from the intergenerational interaction, it is optimal to introduce a pay to the young generation when in duty even by resorting to a distortive tax. Second, when optimizing the size of the army, the optimal choice between the draft army and the professional army depends on the risk class of the country. A security gradient arises. Third, the choice is linked to the size and the quality of the reserve generated by the two approaches.

International Security, Insurance, and Protection: Negative Spillovers within Alliances

Toshihiro Ihori1, Martin McGuire2, Shintaro Nakagawa3

1University of Tokyo, University of California-Irvine, 2Shimonoseki City University

Over forty years ago Olson and Zeckhauser (1969) proposed a new famous theory of security alliances. We consider multiple pure public goods in the sense that “defense” or “security” is disaggregated into the more realistic categories of both self-insurance and self-protection at simultaneous optimization. We show how the two public goods are provided by the countries constituting an alliance critically influences what impacts a change in income of countries has. An increase in income in a country may reduce the provision of the public goods, and deteriorate the welfare of the allies. Such negative spillovers are more likely to occur than under the conventional standard due to goods inferiority. We show how economic growth and redistribution explore negative spillovers and other difficulties among allied countries managing insurance and protection at corner solutions although the nature of public goods itself should have positive spillovers.

Military Spending and Political Institutions: Lessons for the Iran’s Sanctions

Mohammad Reza Farzanegan1, Sajjad F. Dizaj2

1Pnps-University of Marburg, CNM, Germany; 2Tarbiat Modares University, Tehran, Iran

This study examines how quality of political institutions affects the distribution of government budget and how development of government spending in major sections shapes the political institutions in Iran. This question has become especially important due to recent international sanctions, aiming to change the political behavior of Iran. We use the impulse response functions (IRF) and variance decomposition analysis (VDC) on the basis of Vector Autoregressive (VAR) model with annual data from 1960 to 2006. Our results show the importance of political institutions in patronage (e.g., military) and public goods provision spending (e.g., education and health) in Iran. The results imply that a shock in positive changes of democratic quality of institutions leads to negative and statistically significant response of military spending and positive and statistically significant response of education expenditures in short term.

9:00am - 11:00am A 33, Palazzo Rosso

Assessment Limits and Timing of Real Estate Transactions

Sebastien Bradley

Drexel University, United States of America

Michigan homebuyers face large potential tax discontinuities for purchases made around January 1 and May 1 under the State's application of acquisition-value based assessment limits and principal residence (homestead) exemptions, respectively. Consistent with incentives, roughly 7.9 percent of sales concluded in the first 10 business days of January are thus attributable to timing responses. Underlying this effect is a willingness to stretch the number of days between offer acceptance and closing dates by an average of 2 to 2.3 business days per $1000 of tax savings among transactions otherwise likely to close immediately prior to the end of the year. Results involving sale patterns around May 1 provide no evidence of timing for purposes of ensuring homestead exemption eligibility. A small proportion of taxpayers hence appear to respond in a sophisticated manner to the timing incentives associated with near-immediate increases in taxable basis.

Property Taxes and Rental Housing

Max Löffler1, Sebastian Siegloch2

1ZEW and University of Cologne; 2ZFA

Although being heavily analyzed and discussed, there is neither a theoretical nor an empirical consensus on the incidence of the property tax. In this study, we exploit the advantageous institutional setting of property taxation in Germany to provide a clean estimate of the incidence. Using a panel of roughly 540 communities over up to 20 years, we show that landlords and tenants share the burden of property taxes. Although the property tax can legally be shifted to 100 % onto tenants, landlords bear parts of the tax burden depending on the construction type, the year of construction and the quality of the apartment. Moreover, tax shifting increases substantially over time.

The Tax Treatment of Housing: A Missed Opportunity?

Kristin Elle Bre

Statistis Norway, Norway

In many countries the favorable tax treatment of housing has been reduced since the 1970s. This has not happened in Norway. In this paper I use a tax benefit model, and data covering the whole Norwegian population to impute the cost of treating owner-occupied housing as it is treated today. I look at tax revenue and distributional effects of changing the treatment of housing in the direct tax system: taxation as of other types of capital assets, i.e. a flat tax on income and tax valuation of 100 percent of market value.

I find that a tax reform increasing the taxation of housing increases the progressivity of the tax system, but only when imputed housing income is treated today. I look at tax revenue and distributional effects of changing the treatment of housing in the direct tax system: taxation as of other types of capital assets, i.e. a flat tax on income and tax valuation of 100 percent of market value.

Property taxation, bounded rationality and housing prices

Mikael Elinder1,2, Leivisa Persson1

1Uppsala University, Sweden; 2The Research Institute of Industrial Economics (IFN)

In 2008, the Swedish property tax was reformed through the introduction of a cap on yearly tax liabilities. A large portion of properties experienced a large proportional decrease in the tax rate. At the time when the reform was announced, politicians and economists projected - in line with tax cap literature - that the tax decrease would lead to significant negative spillovers. The empirical analysis in this paper runs counter to these projections, as we find no significant price increases for houses that received a generous tax reduction, compared with houses that received a more modest reduction. We explore various theories of bounded rationality in order to explain why house buyers fail to take the tax decrease into account when settling on a price.
**Mobility and Progressive Taxation**

Marcus Roller, Kurt Schmiederheim  
University of Basel, Switzerland  
  
In fiscally decentralised countries with varying local tax schedules, the effective tax progressivity depends on the distribution of taxpayers across local jurisdictions as well as on local income distributions. The latter matter differs systematically because high income households can partly or fully avoid high tax rates by sorting into low tax locations. This paper develops an empirical approach in order to quantify the effective tax progressivity in a highly fiscally decentralised country - Switzerland - taking the relative size of jurisdictions and the actually observed income sorting into account. Exploiting data on the universe of Swiss taxpayers, we find that rich households encounter significantly lower tax rates and lower progressivity than in the benchmark case that does not take the income sorting into account. Furthermore, we find suggestive evidence that the Swiss income tax system is not only less progressive but even regressive for single households with very high incomes.

**Fiscal Progression and Income Instability**  
Jean-François Wen1, Cecilia Medina-García2  
1University of Calgary, Canada; 2Banco de Mexico  
  
We construe the ratio of the post-fisc transitory income variance to the pre-fisc transitory income variance as a measure of the extent to which the progressive tax and transfer system protects families against income risks in Canada between 1993 and 2009. To obtain an annual time series of pre- and post-fisc instability variances, we use the method of multi-year rolling windows introduced by Beach et al. (2010), in an otherwise standard non-parametric decomposition of the total income variance of longitudinal data into "permanent" and "transitory" components. We find that the reduction in the protection against risk that is evident following the provincial and federal tax reforms from 1999-2001 are driven by changes occurring for families headed by individuals with less than high school education.

**Non-linear tax with two tax bases – Static income shifting vs. dynamic tax planning**  
Sappo Karl1, Jussi Laitila2  
1VATT, Finland; 2Department of Biosciences, University of Helsinki  
  
We study the effects of non-linear taxation of entrepreneur's income in a dual income tax. Previous analyses show that a non-linear tax generates incentives to start distributions early (early distribution incentive, EDI). We confirm that without carry forward EDI applies to both income types. Allowing carry forward, EDI disappears and dividend payments are deferred to the steady state phase. As a result pay-out policies for dividends and labor income differ much and static income shifting disappears. A high interest rate used to compound the unutilized income types. Allowing carry forward, EDI disappears and dividend payments are deferred to the steady state phase. We study the effects of non-linear taxation of entrepreneur's income in a dual income tax. Previous analyses show that a non-linear tax generates incentives to start distributions early (early distribution incentive, EDI). We confirm that without carry forward EDI applies to both income types.

**Groupings and the Gains from Tagging**  
Matti Toomaala, Ravi Kanbur  
1University of Tampere Finland; 2Cornell UniversityUSA  
  
The large literature on "tagging" shows that group specific tax and transfer schedules improve welfare over the case where the government is restricted to a single schedule over the whole population. The central assumption, however, is that the groupings available to the government are given and fixed. But how many and which types of groups should the government choose to tag? This is the question addressed in this paper. Starting with a simple framework and ending with numerical simulations based on data from Finland, we show how groupings should be formed for tagging, and provide a quantitative assessment of how group differences affect the gains from tagging. We also provide a quantitative assessment of the welfare gains from increasing the number of tagged groups. In particular, we find that the gains from increasing the number of groups fall off quite rapidly.

**Welfare 6: Family**  
Session Chair: Paola Profeta, Bocconi University  
  
Childcare and the division of parental leave - Evidence from a Swedish reform  
Anna Norén  
Uppsala University, Sweden  
  
The purpose of the paper is to investigate whether access to childcare for older siblings during parental leave affects the division of paid parental leave between mothers and fathers. Access to pre-school can be regarded as a decision in the care burden, or decreased non-monetary cost, of parental leave which may affect how the leave is divided between parents. Using the regional heterogeneity of the implementation of a childcare reform in Sweden in 2002 the effects of access to childcare will be evaluated through a difference-in-differences strategy. Preliminary results suggest that the availability of childcare for an older sibling during parental leave has no effect on the father's take-up with the second born child, but there is suggestive evidence of an increase in the father's share, that is in the division of the total parental leave relative to the first born child.

**The Impact of Targeting Policy on Spouses' Demand for Public Goods, Labour Supplies and Sharing Rule**  
Panayota Lyssiotou  
University of Cyprus, Cyprus  
  
This paper studies the impact of targeted unconditional cash transfers on the spouses' demand for public goods, labour supplies and sharing of resources. We estimate a collective labour supply model with distributional factors which is extended to include preferences over marketable public goods (including child goods). In this way, unlike previous research, we consider the impact of such transfers on the household allocation of resources and distinguish between the labeling and recipient effects. We exploit the UK experience and find evidence in favor of the collective model with separable preferences over labor supplies and public goods. This finding implies a reciprocal effect and not a labeling effect of child benefits. Given the household's unearned income, the bigger the wife's bargaining power the more the resources allocated to public goods (including child goods) and the wife's private consumption. The results are useful in the design of family policy to alleviate intra-household consumption inequality and poverty.

**Cohort at Risk: The Effects of Divorce Laws on Household Retirement Security**  
Luca Stella  
University of Padua, Italy  
  
This paper investigates the effect of the increase in the risk of divorce on the retirement security of married couples. My empirical strategy exploits the variation in unilateral divorce law reforms occurring between the late 1970s and the 2000s in Europe as an exogenous shock to the risk of marital breakup. Across countries and over time, these reforms shifted the ground for divorce from mutual consent to unilateral choice. By employing a unique dataset, which contains detailed work and marital histories, I discuss and test the potential mechanisms by which the introduction of unilateral divorce legislation affects the retirement well-being of households. Overall, my results suggest that increased exposure to divorce risk results in a significant wealth accumulation of married couples around retirement, thus lending support to the precautionary effect of child benefits. Given the household's unearned income, the bigger the wife's bargaining power the more the resources allocated to public goods (including child goods) and the wife's private consumption. The results are useful in the design of family policy to alleviate intra-household consumption inequality and poverty.

**Old Money, the Nouveau Riche and Brunhilde’s Marriage Dilemma**  
Anne-Katrin Brosson1, Kai A. Konradi1, Amihai Glazer2  
1Max Planck Institute for Tax Law and Public Finance, Germany; 2Department of Economics, University of California, Irvine, USA  
  
This paper proposes a screening approach to explain why dating is associated with purchasing status products and conspicuous gift giving. A potential bride searching for a husband may seek to screen candidates whose income is only partially observable. Taking into account that she also bears part of the screening costs, she can sort candidates by offering a menu of contracts that triggers but also constrains conspicuous consumption.

**Public investment when capital is back – distributional effects of heterogeneous savings behavior**  
Linus Mattausch, Oltram Edenhofer1,2,3, David Klener, Sophie Benard3  
1MCC Berlin, Germany; 2Potsdam Institute for Climate Impact Research; 3TU Berlin  
  
We study the impact of heterogeneous savings behavior on the distributional effects of public investment. A capital tax is levied to finance
productive public capital in an economy with two types of households: high income households who save dynastically and middle income households who save for retirement. We find that inequality is reduced the higher the capital tax rate and that low rates constitute a Pareto-improvement. There is thus no clear-cut trade-off between efficiency and inequality: middle income households’ consumption is maximal at a higher capital tax rate than high income households’ consumption.

Trade Openness and Interregional Inequality

Christian Lassmann1, Georg Hirt1
1FAU Erlangen-Nuremberg, CESifo, Ifo, IWG, 2TU Dresden
We study the effect of international trade on interregional inequality within countries. We estimate a model derived from a structural economic geography approach where interregional inequality depends on weighted trade shares and trade costs. These are instrumented based on constructed trade shares and trade costs fitted from a gravity model of bilateral trade, which covers 208 countries for the period 1948–2006. We analyze a cross country data set of regional inequality within countries, which covers 151 countries (1869 sub-national regions) for the year 2005, and a panel data set, which covers 56 countries (835 sub-national regions) for the period 1980–2009. Instrumental variable regressions show that openness increases interregional inequality within countries.

Should income inequality be in praise? Multiple public goods provision, income distribution and social welfare

Jun-ichi Itaya1, Atsue Mizushima2
1Hokkaido University, Japan, 2Otaru University of Commerce, Japan
We investigate how income inequality affects social welfare in the model of voluntary contributions to multiple pure public goods and with altruistic preferences. Itaya et al (1997) have shown that maximization of social welfare precludes income equality in the setting of a singel pure public good. In contrast, we show that the validity of Itaya et al’s result may not hold in the setting of multiple pure public goods. We show that the presence of carrying preferences enhances our result. Our findings have implications for the design of the redistribution policy of income.

Reversal of the Kuznets curve: Study on the inequality-development relation using top income shares data

Elna Toominen
University of Tampere, Finland
This paper uses recently published top 1% income share series in studying the inequality-development association. Top income shares data are of high quality and cover about a century for some countries and thus provide an interesting opportunity to study slow development processes. Moreover, nonlinearities have not been studied sufficiently in the empirical inequality-development literature. To address the issue of functional form, this study utilizes penalized spline methods. It is found that the association between inequality and development experiences a reversal at later stages of development and is, thus, U-shaped in many advanced countries. In addition, results support an inverse-U-shaped relation between inequality and urbanization, and positive relation between inequality and service sector. In all these results there is an interpretation that is possible to fit into ideas presented by Kuznets who discussed shifts in the economy.

Natural Disasters and Macroeconomic Performance: The Role of Residential Investment

Holger Strulik, Timo Trimborn
University of Goettingen, Germany
Recent empirical research has shown that income per capita in the aftermath of natural disasters is not necessarily lower than before the event. Income remains in many cases not significantly affected or, perhaps even more surprisingly, it responds positively to natural disasters. Here, we propose a simple theory, based on the neoclassical growth model, that explains these observations. Specifically we show that GDP is driven above its pre-shock level when natural disasters destroy predominantly residential housing (or other durable goods). Disasters destroying mainly productive capital, in contrast, are predicted to reduce GDP. In the case of productive capital and residential housing in about equal proportions. We show that disasters with insignificant impact on GDP can nevertheless entail considerable losses of aggregate welfare.

Kizuna or NIMBY?: Empirical studies on strategic interaction among municipality governments over disaster wastes after the Great East Japan Earthquake of 2011

Takeshi Miyazaki1, Motohiro Sato2
1Kyushu University, Japan, 2Hitotsubashi University, Japan
Strategic interactions among governments have recently become a major focus of empirical and theoretical work in public economics. The NIMBY is one application of the literature. In the present paper, we apply NIMBY model to the disposal of disaster debris after the Great East Japan Earthquake given that there has been strong concern on radioactive contamination due to the Fukushima Daiichi nuclear power plant incident. We formulate the theoretical model and empirically tested the strategic interaction among municipality governments. We find strong evidence on such interaction. That is, in deciding whether or not to accept the disaster wastes, the municipal governments seem to keep a close eye on other governments’ choices.

Shake me the money!

Francesco Portelli1, Riccardo Treazzo2
1University of Essex, United Kingdom, 2University of Cambridge, United Kingdom
During a natural disaster, the negative supply shock due to the destruction of productive capacity is counteracted by a positive demand shock due to public grants for assistance and reconstruction, posing an identification issue in empirical work. Focusing on the 2005 “Aquilano” earthquake in Italy as a case study, we take advantage of quantified measure of damages for 75,424 buildings to estimate the negative supply shock and of a law issued to allocate reconstruction grants, which resulted in a sharp, exogenous disruption in transfers and output behavior across neighboring municipalities to estimate the positive demand shock. Off-farm shocks suggests that local output multipliers of reconstruction grants (net of marginal tax rebate) are below unity. Yet the size of the grants act as a public insurance scheme, preventing a fall in output.

Competition for Natural Resources and the Hold-up Problem

Carsten Hefeker, Sebastian Kissing
University of Siegen, Germany
We study the role of competition for the hold-up problem in foreign direct investment in resource-based industries. The host country government is not only unable to commit not to expropriate investment ex post, but is also unable to commit to the provision of local resources. In the case of competition for local resources this dual commitment problem triggers higher investment levels, increases host country revenues, but hurts profits of international investors. Domestic firms can play a similar role as an alternative instrument for host country governments to generate competition for local resources this dual commitment problem triggers higher investment levels, increases host countries revenues, but hurts profits of international investors. Domestic firms can play a similar role as an alternative instrument for host country governments to generate
### Optimal Harvesting of a Spatial Renewable Resource

**Thorsten Uhlmann, Stefan Behringer**  
University of Duisburg-Essen, Germany  

In this paper we investigate optimal harvesting of a renewable natural resource. While in most standard approaches the resource is located at a single point, we allow for the resource to be distributed spatially. Consequently, an agent who exploits the resource has to travel from one location to another. For a fixed planning horizon, we investigate the speed and the time path of harvesting chosen by the agent. We show that the agent adjusts the speed of movement so that he visits each location only once, even in the absence of travelling cost. Since he does not come back to any location for a second harvest, it is optimal for him to fully deplete the resource upon arrival. A similar type of a bang-bang solution results when we drop the assumption of a constant harvesting rate.

### The impact of fiscal rules on the stabilisation function of fiscal policy

**Anna Baczynska**, **Simone Salup**  
1University of Mercatour, Italy; 2University of British Columbia, UK

We study the relationship between discretionary fiscal policy and macroeconomic stability in 20 OECD countries over the 1985-2012 period. The novelty of our contribution lies in the use of annual panel data, whereas most of the existing evidence is cross-sectional, and more importantly in the thorough investigation of how fiscal rules affect that policy-macroeconomic stability relationship. We find that the strictness of fiscal rules is clearly related to fiscal sustainability, and that policy is output-stabilising rather than destabilising in most of the countries.

### An Unemployment Insurance Scheme for the Euro Area

**Mathias Dolls**  
1Centre for European Economic Research (ZEW), Germany; 2Université Catholique Louvain, CORE, Belgium

The Great Recession and the resulting European debt crisis revived a debate about deeper fiscal integration in the Eurozone. We discuss different alternatives how an unemployment insurance system for the euro area could be designed and run counterfactual simulations based on micro data to analyze the effectiveness of a basic scheme and a benefit extension program to act as an insurance device in the presence of asymmetric macroeconomic shocks. We find that a basic insurance scheme could be implemented with a relatively small annual budget of roughly 61 billion euros over the period 2008-2013. Not benefits would have stabilized incomes in particular in Cyprus, Estonia, Greece, Ireland, Portugal and Spain whereas Austria, Germany and the Netherlands would have been the largest net contributors.

### National Numerical Fiscal Rules: Not Complied With, But Still Effective?

**Wolf Heinrich Rauter**  
Vienna University of Economics and Business, Austria

This paper investigates the effects of (non-)compliance with national numerical fiscal rules on fiscal policy in 11 EU member states with 23 fiscal rules in place from 1990-2013. Introducing a new dataset of legal texts constituting the fiscal rules, allows a joint empirical analysis of different types and designs of numerical fiscal rules. In various empirical exercises the change in the difference between the exact variable constrained by the fiscal rule and its numerical limit is analysed. Statistics show that these results do not imply a constraint on fiscal policy in about 50% of the years. Various econometric exercises demonstrate that the introduction of fiscal rules does significantly change the behaviour of fiscal policy. If countries do not comply with their fiscal rule in the year or before forecast, there is a strong downward tendency of the constrained variable towards the numerical limit.

### Estimating the Size of the Shadow Economy: Methods, Problems and Open Questions

**Friedrich Schneider**  
1Johannes Kepler University of Linz, Austria; 2Institute for Advanced Sustainability Studies (IASS) Potsdam

This paper presents the various methods to estimate the size of the shadow economy, their strengths and weaknesses. The purpose of the paper is twofold. Firstly, it demonstrates that no ideal method to estimate the size of the shadow economy is possible. Because of its flexibility, the MIMIC method is used to get macro-estimates of the size of the shadow economy is discussed in greater detail. Secondly, the paper focuses on the definition and causal factors of the shadow economy as well as on a comparison of the size of the shadow economy using different estimation methods.

### Economic Freedom and the Shadow Economy: Empirical evidence by using international data

**Jin Kwon Hyun, Iljoong Kim**  
Korea Economic Research Institute, Korea, Republic of (South Korea)

Our main concern is to examine the impact of economic freedom on shadow economy by using country level data in 1997. As economic freedom is mostly determined by legal and administrative regulation, we include these two factors to explain the level of shadow economy. Besides, the paper focuses on the definition and causal factors of the shadow economy as well as on a comparison of the size of the shadow economy using different estimation methods.

### Shadow Economy and Political Stability: A Blessing or a Curse?

**Mohammad Reza Farzanegan**  
1Nipps-University of Marburg, CNMS, Germany; 2Philips-University of Marburg, Germany

This study examines the relationship between political stability and the shadow economy in more than 70 countries around the world from 1999-2005. The panel data fixed effects regression results show that there is a turning point in the stability-shadow economy nexus. Moderated levels of the shadow economy can act as political stabilizers while an extensive size of the shadow economy leads to political instability. Formal economies of developing countries, including the Arab world, have significant challenges in providing employment for the increasing working age population. In such a situation, a moderate level of informal economy can provide a safety net for the large army of unemployed, reducing the risk of political instability and conflict. However, massive out-of-books activities also lead to significant budget deficits, challenging the provision of public goods such as security and order.
on textbooks. Robustness analyses suggest that changes in household tutoring spending capture household behavioral responses to potential changes in school environment and teaching rather than confounding effects of other contemporaneous economic or policy changes. Reductions in household spending on tuition is homogeneous across income groups, whereas reductions in household tutoring spending come primarily from the top and bottom income groups, with the lowest-income households experiencing the largest reduction.

11:30am - 1:00pm
A 33, Palazzo Rosso

Welfare 8: Transfers
Session Chair: Mitsuyoshi Yanagiha, Nagoya University

Population Growth and the Transfer Paradox in an Overlapping Generations Model
Koijen Hamao1, Tsuyoshi Shinzo2, Mitsuyoshi Yanagiha3
1Nagoya University, Japan; 2Nigata University, Japan; 3Tohoku Gakuin University, Japan

In this paper, we use a one-sector overlapping generations model to investigate the transfer problem between a donor and a recipient that have different population growth rates. Unlike existing results obtained from models in which the two countries share the same population growth rate, we demonstrate that if the population growth rates differ, donor enrichment does not arise in the steady state under dynamic efficiency. This result suggests that the prevailing finding that donor enrichment can occur when countries have the same population growth rate is a special case. We also delineate the transfer problem on the transition path.

Optimal Decumulation of Assets in General Equilibrium
James A. Feigenbaum
Utah State University, United States of America

Conventional wisdom among economists says it is best for a household with no bequest motive to invest its assets in an annuity. However, very few people actually follow this advice, and recent work has shown that the economy can be better off in general equilibrium if households do not annuitize their savings. Though in partial equilibrium, households are better off participating in traditional annuities that assimilate assets upon death and therefore deliver higher returns than bonds, it is suboptimal for households to have access to traditional annuities. Instead, households should generally be encouraged to participate in “bond annuities”, which offer the same internal rate of return as bonds while paying a constant stream of income. Upon death, ownership of the assets in a bond annuity is retained by the household’s estate, which recirculates this wealth to a greater part of the population than would a traditional annuity.

Gender differences in volunteer activities
Marcus Dittrich, Blanka Mey
Chemnitz University of Technology, Germany

Using unique data from a large-scale online survey conducted in Germany, we examine gender differences in volunteering for charitable organisations. Our findings suggest that men are more likely than women to engage in volunteer activities. Additionally, we find that men devote more time to charitable causes than women. However, disaggregating the volunteer labour supply by dierent organisations reveals that women spend more time performing volunteer work for organisations that help the poor or elderly.

11:30am - 1:00pm
A 34, Palazzo Rosso

Welfare 9: Well-being
Session Chair: Markus Haavio, Bank of Finland

The economic-growth – subjective-well-being puzzle: The role of social ties
Jari-Petri Laamanen1, Petri Böckerman2, Esa Palosaari1
1University of Tampere, Finland; 2Labour Institute for Economic Research, Finland

Whether economic growth increases subjective wellbeing has been under debate. Studies that find such an effect document heterogeneity between countries in the magnitude of the effect. We test a model in which economic growth increases subjective wellbeing only when a large share of the population derives subjective wellbeing from mutually beneficial relationships (relational goods) and the choice between income and relational goods is determined by individuals’ early-developing schemas of self and others, which in psychology are conceptualized as the security of individuals’ attachment style. More specifically, we test whether economic growth increases subjective wellbeing more in those countries where the average attachment security is higher. We find zero.

Sin Licenses Revisited
Haavio Markus1, Kaisa Kotakorpi2
1Bank of Finland; 2University of Turku, Finland

We analyze personalized regulation in the form of sin licenses (O’Donoghue and Rabin 2003, 2005, 2007) to correct the distortion in the consumption of a harmful good when consumers suffer from varying degrees of self-control problems. We take into account demand uncertainty, which generates a trade-off between flexibility and the commitment provided by sin licenses. We also account for the possibility that consumers may trade the sin good in a secondary market, which partially erodes the commitment power of sin licenses. We show that if sophisticated-consumers are allowed to choose any general, individual, and relational goods license, then sin licenses are optimal.

Biased Perceptions of Income Inequality and Redistribution
Carina Engelhardt, Andreas Wagener
University of Hanover, Germany

When based on perceived rather than on objective income distributions, the Meltzer-Richards hypothesis and the POUM hypothesis work quite well empirically: there exists a positive link between perceived inequality and the extent of redistribution in democratic regimes – though such a link does not exist when objective measures of inequality and social mobility are used. These observations highlight that political preferences and choices might depend more on perceptions than on factual data.

11:30am - 1:00pm
A 21, Palazzo Rosso

Welfare 10: Aging and Pensions
Session Chair: Stanley L. Winer, Carleton University

Pension reform disabled
Sigurd Melter Galassen
University of Oslo, Norway

Old-age pension reform is on the agenda across the OECD, and a key target is to delay retirement. Most of these countries also have a disability insurance (DI) program accounting for a large share of labor force exits. This paper builds a quantitative lifecycle model with endogenous retirement to study how DI and old-age pension (OA-pension) systems interact to determine retirement age, with particular focus on the macroeconomic effects of OA-pension reforms. Individuals face uncertain future health status and wages, and if in bad health they are eligible for DI they choose to retire before reaching the statutory retirement age. The main contribution of the paper is that I, in contrast to standard macro pension models, include DI as another endogenous margin of retirement. I show that failure to account for this margin might severely bias the outcome of OA-pension reforms.

Diversity of labor supply incentives and retirement: evidence from Ireland
Roman Raab1, Brenda Gannon2
1Keel University, United Kingdom; 2University of Manchester, United Kingdom

This paper gives a first-time assessment of the interaction between retirement programs (public and occupational) and labor force behavior of older people in Ireland. Workers planning retirement face a trade-off between earnings from continued work and benefit payments from income security programs. The method portrayed in Gruber and Wise (1999) is used to simulate the behavioral incentives coming from these programs. Retirement pathways typical for Ireland uncover different patterns of the incentives; these patterns correspond to observed retirement behavior. A major source of variation relates to the coverage by occupational pensions.
Aula Magna, Main

Welfare 11: Employment and unemployment

Session Chair: Vincenzo Galasso, Bocconi University

Electoral Incentives and Economic Policy across Political Regimes

Vincenzo Galasso¹, Salvatore Nunnari²

¹Bocconi University, Italy; ²Columbia University

This paper provides a direct test of the link from electoral rules to an economic policy — Unemployment Benefits. Our theoretical model delivers unambiguous predictions on the interaction between electoral institutions and a time varying event, namely the unemployment rate in pivotal and non-pivotal districts. Electoral incentives induce more generous UB transfers in majoritarian than in proportional systems if the unemployment rate is higher in pivotal than in non-pivotal districts. Using a dataset with local information on electoral competitiveness and unemployment rates, and different measures of UB generosity for 21 OECD countries in the 1980-2001 period, our panel analysis strongly supports these predictions.

Follow the leader? Public and private wages in the Netherlands.

Adam C Elbourne, Annette S Zeilstra

CPSB Netherlands Bureau for Economic Policy Analysis, Netherlands. The

This study investigates wage leadership in the Netherlands. We empirically examine public and private wages using several wage definitions for the period 1980-2012. We find no evidence for public wage leadership. Moreover, public wages return to their previous equilibrium value three to four years after an exogenous shock in public wages. By contrast, an exogenous shock to private wages has a permanent influence on both private and public wages. These findings suggest that although a public wage freeze lowers public expenditure in the short-run, it is not an effective policy measure to lower public expenditure in the medium and long-run.

Unreported labor, Inequalities, and Taxation

Oceane Jeanne Brülan

University of Mannheim, Germany

This model uses heterogeneity in productivity across and within firms to generate two types of informality - full and within-firm informality - in an economy where monitoring of compliance is imperfect. Within-firm informality - unreported labor by formal firms - arises because formal entrepreneurs can increase the profitability of low-productivity segments of production by employing informal workers. I identify the welfare impact of informality on each type of occupations. I show that full and within-firm informality do not necessarily evolve similarly in reaction to changes in tax rates or labor regulations and must be analyzed separately to understand the extent of informality in an economy. The fiscal capacity of the government - the ability of the government to increase the share of taxes in firms total revenues (formal and informal) - determines whether a given tax reform increases or decreases the welfare of informal workers, which are the individuals at the lower end of the ability distribution.

11:30am - 1:00pm
A 32, Palazzo Rosso

Welfare 12: Fertility I

Session Chair: Volker Meier, University of Munich

Daddy months

Volker Meier¹,², Helmut Rank³,⁴

¹University of Munich, Germany; ²Ifo Institute for Economic Research

We consider a bargaining model in which husband and wife decide on the allocation of time and disposable income. Since her bargaining power would go down otherwise more strongly, the wife agrees to having a child only if the husband also leaves the labor market for a while. The daddy months subsidy enables the couple to overcome a hold-up problem and thereby improves efficiency. However, the same ruling harms the welfare of the couple and thereby harms the welfare of the economy.

Child Support, Pensions and Endogenous (and Heterogeneous) Fertility

Andras Simonovits

CRES HAB, Hungary

van Grooten, Leers and Melijdw (2003) analyzed the combination of public pension and child support in an OLG model. Their infinite stream of generations is simplified into three generations and the maximization of a paternalistic social welfare function yields the socially optimal tax and pension contribution rates. Negative saving is excluded and heterogeneity of rearing costs and of enjoying children is introduced. Two major results: (i) the introduction of the transfer system involves a jump over the cap created by the initial drop of welfare; (ii) the introduction of fertility-dependent pensions may strengthen heterogeneity in fertility.

2:00pm - 3:00pm
Aula Magna, Main Building

Keynote IV: Redesigning the welfare state for aging societies: what can we learn from international comparisons?

Session Chair: Kerstin Schneider, University of Wuppertal

Keynote Lecturer: Axel Börisch-Supan (MEA, Munich, Germany)

Redesigning the welfare state for aging societies: what can we learn from international comparisons?

Axel Börisch-Supan

Max-Planck-Institute for Social Law and Social Policy, Germany

Slides for Prof. Axel Boersch-Supan's plenary lecture

Trade Taxation and Entrepreneurship - Evidence from German Firm Data

Melissa Engel¹, Florian Misch², Johannes Vogel³

¹Center for European Economic Research, Germany; ²Center for European Economic Research, Germany; ³University of Mannheim, Center for European Economic Research, Germany

In this paper we study the effect of trade taxation on the creation of new firms. We use an extensive and unique data set on all entering firms between 2003 and 2012 in Germany. We exploit the specific characteristics of the German trade tax that the local multiplier is set independently by each municipality. This leads to tax differentials among municipalities. This is a key determinant of firm creations. We study the impact of tax differentials on firm creations. To analyze this data we apply a Poisson model in cross-section and panel data. Interjurisdictional Competition and Location Decisions of Firms

3:30pm - 5:30pm
BusTax 6: Location decisions

Session Chair: Agustín Redondo, University of Lugano

Trade Taxation and Entrepreneurship - Evidence from German Firm Data

Melissa Engel¹, Florian Misch², Johannes Vogel³

¹Center for European Economic Research, Germany; ²Center for European Economic Research, Germany; ³University of Mannheim, Center for European Economic Research, Germany

In this paper we study the effect of trade taxation on the creation of new firms. We use an extensive and unique data set on all entering firms between 2003 and 2012 in Germany. We exploit the specific characteristics of the German trade tax that the local multiplier is set independently by each municipality. This leads to tax differentials among municipalities. This is a key determinant of firm creations. We study the impact of tax differentials on firm creations. To analyze this data we apply a Poisson model in cross-section and panel data.
Ruben Hernandez-Murillo

Federal Reserve Bank of St. Louis, United States of America

We examine the welfare properties of alternative regimes of interjurisdictional competition for mobile firms. Alternative taxation regimes
represent restraints on the discretionary powers of taxation of local governments, and firms differ not only in terms of the degree of mobility but
also in terms of productivity.

We find that average welfare is higher under discretionary and more efficient taxation regimes (in the sense of minimizing deadweight losses
from distortionary taxation) when firms are highly mobile. In this situation, further limiting competition by imposing a system of non-discretionary
instruments can reduce average welfare by reducing the efficiency of the local governments at raising and allocating public funds.

When firms face high moving costs, on the other hand, switching to a
non-discretionary and less efficient taxation regime may increase welfare by preventing local governments from engaging in excessive
redistribution of resources from the immobile residents to the mobile firms.

Strategic Treaty Shopping
Sunghoon Hong

Korea Institute of Public Finance, Korea, Republic of (South Korea)

This paper examines treaty shopping with a game-theoretic model in a network of tax treaties. An investor can choose an investment route
across national borders to minimize tax while a tax agency can choose to audit the investor to find out the route. The audit is costly but it can
give additional revenue to the tax agency if it reveals that the investor chose an indirect route for tax avoidance. We analyze the equilibrium of this
model and calculate the tax revenue loss due to treaty shopping. I also examine the effectiveness of the suboptimal network of tax treaties
between selected countries. While about 75 percent of tax-minimizing indirect routes pass through countries with no withholding tax, about 21 percent of tax-minimizing indirect routes pass through countries with treaty networks favorable to certain residence
countries. Network centrally motivated are introduced to assess the role of pass-through countries.

Taxes and Firm’s Investment Decisions: Evidence from Swiss Municipalities
Agusin Redondo, Sergio Galletta

University of Lugano, Switzerland

Profit taxation affects firms’ investment decisions through, at least, two channels: the level of corporate taxes and the progressivity of the tax
schedule. We estimate the effect of both channels on firms’ location choices in Switzerland. We use our analysis on a unique dataset with data
for almost 2000 Swiss municipalities for the 1985-2008 period. We find that both high average tax rates and tax progressivity increase the
number of firms in a given jurisdiction. The latter result confirms the existence of an insurance effect. On the other hand, the positive impact of average tax rates should be thought in a broader context where municipalities compete to attract firms by decreasing tax rates but also in many other dimensions such as creating business-friendly environments.

The effects of personal income tax reforms on tax deductions by income source
Philipp Dörrenberg1, Andreas Peichl2, Sebastian Siegloch3

1ZEW, 2University of Mannheim, Germany; 3TZA

A large and ever growing literature focuses on the role of tax rates on taxable income as summarized by the elasticity of taxable income. Compared to multitude of studies on labor supply, the evidence on tax expenditures as a means of reducing the taxable income is remarkably
scarc. In this paper, we intend to fill this research gap by providing a thorough and comprehensive analysis of the tax effect of itemized deductions using administrative German taxpayer micro data. Our analysis explicitly accounts for the heterogeneity of the household type and its influence on the income source. For identification, we exploit several tax reforms of the German income tax system between 2000 and 2008, both in terms of tax rates and as far as the treatment of itemized deductions are concerned.

Efficiency and equity aspects of 20 years of tax benefit reforms in Belgium: microsimulation results
Toon Vanheukelom1, André Decoster1, Dieter Vandelannoote3, Gerlinde Verbist3, Sergio Pereiman2

1KU Leuven, Belgium; 2Université de Liège, Belgium; 3University of Antwerp, Belgium

Belgium has seen major changes in its tax benefit system over the past twenty years. These changes have -to a large extent- co-determined the
evolution of disposable incomes of Belgian households on the one hand, and their incentives on the other hand. In the past a range of partial
analyses have looked at different aspects of tax-benefit policy in isolation. In this paper we attempt to assess equity and efficiency aspects of all changes in tax-benefit policy over the full course of 1992-2012. In order to assess the effects of the tax-benefit policy on the different househoulds, we simulate the effects of current and past tax-benefit policies using the microsimulation model MEFISTO-EUROMOD. We find that the reforms to the system were to a large extent pro-poor, and improved equity in general. This did come at a cost: the marginal cost of public funds increased considerably over time implying increased welfare costs.

How do state owned enterprises react to taxation? Evidence from China
Clemens Fuest1, Li Liu2

1ZEW Mannheim, University of Mannheim, CESifo and IZA; 2University of Oxford

Theories about the impact of taxes on firm behaviour are divided about how taxes affect state owned enterprises. This paper exploits various
aspects of the 2006-2008 corporate tax reform in China to shed light on how taxes affect state owned and private companies. We focus on
a change in the deductibility of wage costs and find that the impact on state owned enterprises is larger than on privately owned firms.

How harmful is it to tax mobile capital?
Vidar Christiansen

University of Oslo, Norway

Assuming there is a trade-off between the harmful effects of taxing mobile capital and arguments for taxing corporate income the paper
addresses how harmful it is to tax mobile capital. In the simple single-sector economy with international capital and exogenous labour supply,
the crucial factors are the elasticity of substitution between capital and labour, the capital-labour ratio and the tax rate. It is shown that elastic
labour supply will aggravate the social loss. Where a second sector with purely domestic capital is added, a number of further effects will arise.
Typically induced substitution towards labour in the second sector will make less labour available for the international corporation and cause
further harmful outflow of international capital. Other interaction effects between the two sectors affecting the outflow of capital may be due to
changes in domestic demand for the second sector output, or changes in the allocation of domestic capital.

Capital Taxation, Investment, Growth, and Welfare
Simon Boesenberg1, Peter Egger2, Benedikt Rydzek1

1KOF ETH Zurich, Switzerland; 2ETH Zurich, CEPRE, CESifo, Leverhulme Centre for Research on Globalisation and Economic Policy (GEP) at
the University of Nottingham, and Oxford University Centre for Business Taxation (OUCBT)

This paper formulates a model of exogenous growth to study the effects of broad capital taxation (of profits, dividends, and capital gains) on
macroeconomic outcomes. The framework permits modeling countries in transition to a country-specific steady state and to discern steady-state and
transitory effects of shocks on economic outcomes. The chosen framework is amenable to structural estimation and , given the parsimony in

Text 3: 3:30pm - 5:30pm
BusTax 7: Tax reform
Session Chair: Wolfram F. Richter, TU Dortmund University

Nils aus dem Moore

RWI - Rheinisch-Westfälisches Institut für Wirtschaftsforschung, Germany

We undertake a micro-econometric evaluation of the so-called ACE corporate tax reform in Belgium based on firm-level accounting data. We
interpret the reform that came into effect in January 2006 as a quasi-experiment. We identify its causal impact on the leverage ratio of Belgian
corporations by means of a difference-in-differences (DID) approach, using corporations from the UK as a comparison group. Our results
document that the ACE reform led to a systematic pattern of heterogeneous effects on the capital structure of Belgian corporations, as the
expected reduction of the leverage ratio is limited to big firms. Estimation of quantile treatment effects further reveals that the effect gets larger
across different distribution of firm leverage. Finally, we provide evidence of sectoral heterogeneity with significant effects observed for capital-intensive, but not for labor-intensive sectors. These results are consistent with anecdotal descriptive evidence provided by experts from the Belgian tax authorities.
Capital allowances and investment: evidence from UK corporate tax returns

Giorgia Maffini1, Jing Xing2, Michael Devereux3

1Oxford University, United Kingdom; 2Oxford University, United Kingdom; 3Oxford University, United Kingdom

How do corporate tax incentives such as capital allowances affect firm investment? In this paper, we provide new empirical evidence on the effects of capital allowances on investment based on confidential UK tax returns during 2001-2009. We exploit the exogenous changes in the qualifying threshold for the first-year capital allowances in 2004 and the changes in the capital allowance rates during 2004-2007 to conduct difference-in-difference analysis. The confidential tax return data allow us to identify firms that have been affected by such changes in the tax code and also to precisely identify the types of assets affected by the policy change, that is, plant and machinery. Our preliminary results suggest that investment rate increased around 4-5 percentage points when firms became qualified for the first-year allowances in 2004, relative to firms that were never qualified.

Educ 3: Education and mobility

Session Chair: Silke Uebelmesser, Friedrich Schiller University Jena

A 12, Palazzo Rosso

3:30 pm - 5:30 pm

The Second Dividend of Studying Abroad: The Impact of International Student Mobility on Academic Performance

Katharina Suntheim, Johannes Meya

Georg-August University Göttingen, Germany

In our analysis we investigate the effect of studying abroad on the final university grade. To overcome the problem of possible self-selection into international mobility, we apply a propensity score matching strategy. Our empirical results show that a temporary study-related visit abroad improves the final university grade. In addition, we find that students who count classes taken abroad towards their degree have a significantly better final university grade than their counterparts who do not transfer any grades. This might indicate that especially the grades achieved at the foreign university are the channel through which studying abroad influences academic performance.

Educational Production Functions as of 1886: How Primary Schooling Shaped Economic Development in End-of-Nineteenth-Century Prussia

Ruth Maria Schueler1, Ludger Woessmann2,3

1ifo Institute, Germany; 2University of Munich; 3CESifo and IZA

How do educational inputs relate to economic outcomes historically? End-of-19th century Prussia, where mass expansion of schooling had arisen locally is used to estimate a historical educational production function. The first education census on primary schools from 1886 provides county-level data on schooling quality and quantity. Two measures for economic outcomes, income tax per capita and day-laborer wages, available before and after the census, allow for a value-added approach and for observing heterogeneous associations as they measure earnings of high- and low-wage earners. The findings show that teacher quality increases day-laborer wages while educational investments increase income tax per capita.

Student and Graduate Migration and its Effect on the Financing of Higher Education

Tina Haussen1, Silke Uebelmesser1,2

1Friedrich Schiller University Jena, Germany; 2CESifo

The number of tertiary students enrolled outside their home country has almost doubled in the last decade. In higher education systems that are partly tax-funded, a country's labor force might not be willing to subsidize the education of foreign students who can be expected to work abroad after graduation with high probability. This paper analyzes whether and how student mobility affects the governmental decision about the part of public funds. Based on counterfactual simulations and micro data for 27 EU member states, results suggest that the private financing share of higher education funding depends on a country's tax revenue, its GDP and the share of students enrolled in private universities.

3:30 pm - 5:30 pm

A 13, Palazzo Rosso

FiscPol 12: Fiscal federalism

Session Chair: Ekkehard A. Köhler, Walter Eucken Institut and University of Freiburg, Germany

Developing Composite Indicators for Fiscal Decentralization

Gyun Cheol Gu

Korea Institute of Local Finance (KILF), Korea, Republic of (South Korea)

The right way to measure the degree and extent of the different aspects of fiscal decentralization has been a long-debated, yet underdeveloped issue. Moreover, there has been little consensus on the right approach to developing a single indicator which is sometimes needed to show a general trend in fiscal decentralization and to reveal relationship to other variables in empirical studies. In particular, several composite indicators of fiscal decentralization have been proposed, but there are very few attempts to evaluate and compare these measures in terms of implicit biases and different weights between revenue and expenditure decentralization. Critically reviewing and comparing various types of fiscal-relations, indicators in a systematic way, this paper proposes two criteria to classify similar-looking composite indicators for fiscal decentralization while it also presents two new composite measures.

Time Series and Panel Countinestimation Estimation of Public Finance in German States: A "Second Generation" Fiscal Sustainability Analysis

Ekkehard A. Köhler, Heiko T. Burrell, Lars P. Feld

Walter Eucken Institut and University of Freiburg, Germany, Germany

This paper provides new evidence on the sustainability of public finances in German states (Laender) by exploiting a newly compiled database covering the years 1950-2011. Unlike previous studies on Germany, we analyze fiscal sustainability by applying "second generation" panel countinestimation techniques. A unique identification strategy for the selection of sub-panels improves the robustness of panel countinestimation tests and reveals that Laender finances are hardly sustainable.

Benefitting from a European "fiscal union"? Redistribution vs. stabilization

Dick Neumayer

Université catholique de Louvain, Belgium

The Great recession and the resulting debt crisis have given rise to a debate concerning deeper fiscal integration in Europe. Recent studies mostly take a macro perspective when analyzing possible steps towards a European "fiscal union". In contrast, this paper provides an evaluation method at the individual level and calculates the equivalent variation for the benchmark case of a common tax and transfer system relative to the baseline with national systems. Based on counterfactual simulations and micro data for 27 EU member states, results suggest that especially Eastern European countries would gain from such a reform, mainly due to a redistributive effect. Fiscal integration of fewer but more similar countries generally reduces redistributive and increases stabilizing effects. However, Pareto improving reforms where at least one country gains while no one loses seem to be possible only for rather severe crisis scenarios, or for high levels of individual risk aversion.

Efficient Centralized Earmarking under Decentralized Fiscal Commitments

Emilson Caputo Silva

University of Alberta, Canada
Earmarked federal grants are ubiquitous and significant. Traditional fiscal federalism is unable to explain the widespread utilization of such grants. Recent arguments focusing on the potential benefits of centralized earmarking in reducing incentives for the creation of soft budgets at sub-central government levels merit formalization. This is the main motivation for the paper. The fruits of the analysis provide a clear normative prescription: the central government should earmark its grants in order to redistribute private consumption and public expenditures incurred in the provision of all public goods that are prone to be determined strategically under decentralized fiscal commitments.

**Health 5: Health issues in aging societies**

**Session Chair:** Carsten Colombier, Federal Finance Administration

**The Fiscal Stress Arising from State and Local Retiree Health Obligations**

Byron Lutz, Louise Sheiner

Federal Reserve Board, United States of America

- Virtually all U.S. state and local governments provide health insurance to their retirees, yet these liabilities have been the focus of only limited analysis. The first portion of the paper uses the information contained in the actuarial reports for retiree health plans to reverse engineer the cash flows underlying the liabilities given in the report. Obtaining the cash flows allows us to construct liability estimates which are consistent across government state and local governments. We find that the total unfunded accrued liability of state and local governments’ retiree health care equals roughly 1/2 of total state and local government revenue. The second portion of the paper places these obligations into context by examining the budget pressures associated with retiree health on a continuing, largely pay-as-you-go basis.

**Longevity, working lives and public finances**

Jukka Lassila, Tarmo Valkonen

ETLA, Finland

- Can longer working lives bring sufficient tax revenues to pay for the growing public health and care expenditure that longer lifetimes cause? We review studies concerning retirement decisions and pension policies, the role of mortality in health and long-term care costs, and errors in mortality projections. We combine key results into a numerical OLG model where changes in mortality have direct effects both on working careers and on capital use of health and long-term care services. The model has been calibrated to the Finnish economy and demographics. Although there are huge uncertainties concerning future health and long-term care expenditure when people live longer, our simulations show that without policies directed to disability admission rules and old-age pension eligibility ages, working lives are unlikely to extend sufficiently. Importantly, with such policies it seems quite possible that generations enjoying longer lifetimes can also pay for the full costs by working longer.

**Is population ageing really dwarfed by advances in medical technology as a driver of healthcare expenditure?**

**Evidence from the Swiss case**

Carsten Colombier

Federal Finance Administration, Switzerland

- Recently it is argued that population ageing has a negligible impact on healthcare expenditure (HCE) and that no-demographic cost drivers, in particular, advances in medical technology are by far more important. This paper contributes to this debate by first, carrying out a comparison of the determinants of Swiss HCE and second, projecting Swiss HCE. Our estimations show that in advances medical technology and population ageing are interrelated and both are important drivers of HCE. In addition, the projections demonstrate that in the coming decades population ageing will increase pressure on public finances and the social health insurance. Therefore, one should be cautious to infer that population ageing is dwarfed by medical technology as a driver of HCE. Consequently, policy-makers should focus on both population ageing and advances in medical technology to mitigate cost pressures on public budgets.

**Understanding the effect of retirement on health using Regression Discontinuity design**

Peter Eibich

DWH Berlin, University of Hamburg

- This paper estimates the causal effect of retirement on health. The Regression Discontinuity design exploits financial incentives in the German pension system for identification. Self-reported health status and measures of physical and mental health are used as dependent variables. The results show an improvement in all health measures upon retirement. I investigate a wide range of health behaviors (e.g. alcohol and tobacco consumption, physical activity, diet and sleep) as potential mechanisms. The results show that retirees use their additional leisure time for behavioral adjustments. Increased leisure-time physical activity appears to be a key mechanism through which retirement affects health.

**A Political Economics Model of Subsistence Levels And The Rise of Populism**

Linus Aggabo1, Levina Persson2

1Uppsala University, Sweden; 2Uppsala University, Sweden

- The model of populism that we develop in this paper is a simple electoral accountability model where we have introduced a conflict dimension between public spending on “basic needs” and “moral needs”. Some voters are more dependent on basic public spending than others and want a minimum level of basic public goods to be supplied before any resources are put on moral public goods. There are two political parties in our model where one is the establishment’s party and the other is a populist party. The establishment party cares about upholding spending on moral goods even in times of scarce economic resources and the Populist Party never cares about the moral public spending advocated by the established political parties. Politicians from the political establishment might choose to pool with a populist politician if the long-term expected utility from being re-elected exceeds the short-term utility from implementing their preferred policy.

**Complexity of Propositions and Voting Behavior in a Direct Democracy: Evidence from Switzerland**

Sven Rensjanskii, Zohal Hessami

University of Konstanz, Germany

- This paper analyzes the effect of the complexity of direct-democratic propositions on individual participation and voting decisions. Instead of relying on subjective and potentially endogenous survey-based measures of complexity, we construct a novel objective measure of complexity based on information provided in official pre-election information booklets sent to all Swiss households. A large and unique data-set from post-election surveys of each ballot at the federal level in Switzerland since the 1980s allows us to control for respondents’ individual characteristics. We find a robust negative effect of ballot complexity on participation. Using a Heckman-selection model to correct for the participation-driven selection bias, we provide empirical evidence for a status-quo bias in the voting decision, i.e. a rejection-biased voting outcome.

**Sequential Policy Choices and the Missing Response to Reform**

Johannes Becker1, Ronald B. Davies2, Andrea Schneider3

1University of Muenster, Germany; 2University College Dublin, Ireland

- We consider a model in which governments sequentially introduce a policy, e.g. a new tax, labor market standards etc. Individuals may escape this policy by moving abroad. However, since other countries may introduced this policy as well, the migration decision may prove expensive ex post. We consider a situation in which the countries abroad will opt for the policy if there is no response to the policy reform at home. Individuals anticipate if too few of them actually move, the country abroad will introduce the policy -- which makes staying the better option. Thus, it depends on individual beliefs whether the policy reform will lead to costly responses or not.

**Happy Voters**

Federica Liberini1, Michela Redaçioni2, Eugenio Proto3

1KOF, ETH, Switzerland; 2University of Warwick, United Kingdom; 3University of Warwick, United Kingdom

- In this paper we investigate whether or not recent initiatives taken by governments and international organizations to come up with indicators of Subjective Well Being (SWB) to inform policy makers go in the same direction as citizens expectations on what policy makers should do. We test retrospective voting hypotheses by using standard measures of SWB as a proxy for utility instead of the commonly used indicators of economic and financial circumstances. Using the British Household Panel Survey Data we find that citizens who are satisfied with their life are more likely to cast their vote in favour of the ruling party, even taking into account ideological preferences. We show that SWB influences voting decision even when the event affecting the SWB is beyond the government's control, like the spouse death.

**PolEcon 10: Rent-seeking politicians**

Sven Rensjanskii, Zohal Hessami

University of Konstanz, Germany

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Petro Populism
Gisle James Natvik, Ragnar Torvik, Egil Matsu
Norwegian Bank, Norway

We aim to explain petro populism — the excessive use of oil revenues to buy political support. To reap the full gains of natural resource income, politicians need to remain in office over time. Hence, even a rent-seeking incumbent who prioritizes his own welfare above that of citizens, will want to provide voters with goods and services if it promotes his probability of remaining in office. While this incentive benefits citizens under the rule of rent-seekers, it also has the adverse effect of motivating benevolent policymakers to short-term overprovision of goods and services. In equilibrium politicians of all types indulge in excessive resource extraction, while voters reward policies they realize cannot be sustained over time.

Optimal taxation when people do not maximize well-being
Aart Gerritsen
Max Planck Institute for Tax Law and Public Finance, Munich

Most of public economics has the tendency to casually equate ‘utility’ with ‘well-being.’ This assumption is not presupposed by positive economics but is necessary for issuing policy prescriptions based upon observed behavior alone. I derive optimal tax rules when government maximizes well-being, subject to individuals maximizing utility. Compared to a standard optimal tax formula, there is an additional term which depends on the difference between the well-being-based and the utility-based marginal rates of substitution (MRS). I use British life satisfaction data to estimate the well-being-based MRS of leisure for consumption and compare this measure with the utility-based MRS. Low-income workers tend to work ‘too little,’ while high-income workers work ‘too much,’ providing a motive for lower marginal tax rates at the bottom and higher rates at the top of the income distribution.

Unconditional love? Pork barrel politics in the absence of electoral incentives
Jon H. Fiva
11Osaka University of Economics, Japan; 2Osaka University, Japan

Pork barrel spending is typically attributed to the strategic behavior of political elites hoping to be electorally rewarded for the provision of pork. We estimate the causal effect of local representation in a closed lists proportional representation system where individual candidates have no clear electoral incentives to favor their hometown. Using data from Norwegian regional governments we still find a strong hometown bias. The probability that a municipality receives transfers from the regional government increases when their representatives in the council are politically aligned with the mayor. To overcome potential endogeneity issues related to representation and spending, we exploit that in close elections it is ‘as good as random’ what political bloc that gets a seat majority, and this strongly determines which party that gets the mayor.

Heterogeneous interest rates as a reason for capital income taxation
Kevin Spitzen
KU Leuven, Belgium

Abstract: We extend the Atkinson-Sliglitz model to include heterogeneous rates of return. We find that the optimal tax on household income from savings should be higher, the more the rate of return is correlated with ability. Next we test empirically the hypothesis that such correlation is present, using panel data from PSID.

Optimal nonlinear Income Taxes with Compensation
Craig Brett, Laurence Jacquet
Queen’s University, Canada; Mount Allison University, Canada; 2THEMA University of Cergy-Pontoise

This paper investigates how an optimal income tax should be designed when individuals differ in both ability, for which they are presumed to be not responsible, and preference for leisure, which they are responsible. We propose a social objective that allows for a compromise between the principles of compensation and responsibility. This compromise is given a simple parametric form. In a second-best setting, this objective gives rise to countervailing incentives for workers at the lower end of the income distribution, thereby providing a rationale for marginal wage subsidies. At the upper end of the income distribution, the optimal tax schedule resembles the maximin optimum.
A Test of the Ricardian Equivalence Proposition in a Life-Cycle Consumption Experiment

Davud Rostam-Akheta1, Thomas Moisanner2
1Freie Universitat Berlin, Germany; 2Technical University of Berlin, Germany

This paper tests whether the Ricardian Equivalence proposition holds in a life cycle consumption laboratory experiment. This proposition is a fundamental assumption underlying numerous intertemporal choice and has important implications for tax policy. Using nonparametric and panel data methods, we find that the Ricardian Equivalence condition does not hold. Our results suggest that taxation has a significant and strong impact on consumption choice. Over the life cycle, a tax relief increases consumption on average by about 22% of the tax rebate. A tax increase causes consumption to decrease by about 30% of the tax increase. These results are robust with respect to variations in the difficulty to smooth consumption. In our experiment, we find the behavior of about 62% of our subjects to be inconsistent with the Ricardian proposition. Our results show dynamic effects; taxation influences consumption beyond the current period.

Unwilling, unable or unaware to respond? Decomposing behavioral responses to tax incentives

Tuomas Matikka, Tuomas Kosonen

Government Institute for Economic Research WATT, Finland

This paper characterizes how different behavioral factors affect individual responses to different tax incentives. We hypothesize that the characteristics of different tax systems and institutions create different reasons for responding and not responding. Our analysis compares the significance of inability to respond and awareness of the tax rules with the underlying elasticity, the willingness to respond. Within the same population and overall Finnish institutional setting, we estimate behavioral responses to tax changes across different tax systems and institutions. We find that the ability to respond is lower in individual income tax systems compared to corporate income tax systems.

Comparative Tax Information and the Choice of the Local Business Tax Rate

Thiss Blüttner1, Axel von Schwarz2
1University of Erlangen-Nuremberg, Germany; 2University of Erlangen-Nuremberg, Germany

This paper explores the role of comparative tax information in a setting with decentralized tax policy and mobile investors. We argue that investors discount tax information when evaluating the potential investment opportunities in different jurisdictions. We test our hypothesis in a laboratory experiment where participants choose between two jurisdictions, each with different tax rates and tax policies.

Fiscal equalization with hidden information and hidden action

Tanja Kim
University of Konstanz, Germany

This paper studies the local tax policy setting behavior within a federal system under hidden information and hidden action by considering the incentive effects arising from elections and yardstick competition. It differs from earlier contributions by combining auction theory with a modern approach of fiscal federalism, based on agency theory. In this framework, the yardstick competition as baseline model leads to a Pareto efficient outcome, despite private information about the costs of service provision and rent-seeking activities of local policy makers. However, a first best solution is missed, if the local governments behave non-myopic. Despite this, both results from the perspective of principals (central level, local electorate) more advantageous than the outcome of a singular yardstick competition, which is in this comparison a Pareto efficient outcome, despite private information about the costs of service provision and rent-seeking activities of local policy makers.

Electoral Rules for Mayors and Incentives to Pork-Barrel: Quasi-Experimental Evidence from German Municipalities

Zohal Hessami
University of Konstanz, Germany

This paper exploits a natural experiment in Hesse where a reform of the electoral rule from mayor appointment by the local council towards direct mayor elections was introduced during a phase-in period from 1993 to 1998. The end of the term of the last appointed mayor varies across jurisdictions. In Portugal, until 2013, mayors were not facing binding term limits and could be in office indefinitely, providing us a neighboring jurisdiction.

Unwilling, unable or unaware to respond? Decomposing behavioral responses to tax incentives

Axel von Schwerin2
University of Warwick

This paper tests the equivalence of tax-inclusive, tax-exclusive and tax-rebate prices through a series of experiments differing only in their handling of the tax. Subjects receive a cash budget and decide how much to keep and how much to spend on various attractively priced goods. Subjects spend significantly more under tax-exclusive prices whereas total purchases under tax-inclusive and tax-rebate prices are similar. These results persist throughout most of the ten rounds despite feedback and the ability to revise
purchases. The asymmetric response to tax liabilities and rebates highlights consumers’ ability both to internalize and to willfully ignore hidden price components.

JEL: C91, H20, H51

VAT Notches
Benjamin Lockwood1, Li Liu2
1University of Warwick, United Kingdom; 2CBI, University of Oxford, UK

This paper is the first to theoretically and empirically analyze the effect of VAT registration notches on firm behavior. Using UK administrative data, we show that there is excess bunching of firms below the registration threshold. Adjusting for optimization frictions and voluntary registrations, we estimate the upper bound of the bunching ratio to be around 4.01 – 5.84 during the sample period. We further split the sample to analyze heterogeneous responses to the tax notch. Finally, we show theoretically that the turnover of the firm is related to a sufficient statistic of the tax system; this theoretical relationship can be used to calculate the elasticity of the VAT tax base with respect to this sufficient statistic.

The inefficiency of reduced VAT rates: Evidence from restaurant industry
Jarkko Tapio Hari1, Toumas Kosonen2
1VATT, Finland; 2VATT, Finland

This paper provides estimates of the effects of consumption taxes on prices, demand and employment for restaurant services. We utilize a large VAT reforms affecting restaurant meals, where the VAT rate was cut in July 2010 in Finland and in January 2012 in Sweden. By comparing with restaurants in neighboring countries, these reforms offer a natural experimental approach. The results indicate that restaurants reduced their prices by only little. On average, the price reductions are approximately a quarter of the full pass-through. Remarkably, at the same time a majority of restaurants did not reduce their prices at all. We do not observe any increases in the quantity of meals sold or in wage sums paid to employees. These results imply that the demand for restaurant meals is rather inelastic and the main objective of the reforms of increasing employment in the industry was not fulfilled.

The Long Arm of the European VAT, Exemplified by the Dutch Experience
Sijbren Crossen1, Leon Bettendorf2

The harmonized EU VAT has many shortcomings, notably the numerous exemptions and the differentiated rate structures. The exemptions distort input choices and outsourcing policies; they result in the overtaxation of VAT-fable businesses and the under taxation of consumers.

Along with cut-of-scope activities, exemptions tend to skew competitive conditions vis-à-vis the private sector. The reduced rates are an ill targeted tool for reducing the regressivity of the VAT. In view of these design failures, the EU VAT is in danger of becoming an anachronism. It does not reflect the lessons that can be learned from countries with modern VATs. Fortunately, the European Commission is evaluating the performance of the common VAT. This paper contributes to the debate by illustrating its shortcomings with reference to the Dutch experience.

The paper does not break new ground, but provides a disconcerting picture of the excess burden of a major revenue source.

3:30pm - 5:30pm
A 23, Palazzo Rosso

The role of firms in retirement decisions
Wolfgang Frimmel1, Thomas Horvat2, Mario Schmalenberger1, Rudolf Winter-Etmer1
1Johannes Kepler University Linz, Austria; 2Wifo Vienna, Austria

In general, retirement is seen as a pure labor supply phenomenon, but firms can have strong incentives to send expensive older workers into retirement. Based on the seniority wage model developed by Lazear (1979), we discuss steep seniority wage profiles as incentives for firms to dismiss older workers before retirement. Conditional on individual retirement incentives, e.g. social security wealth or health status, the steepness of the wage profile will have different incentives for workers as compared to firms when it comes to the retirement date. Using an instrumental variable approach to account for selection of workers in our firms, we find that conditional on individual retirement incentives, firms with higher labor costs for older workers are associated with lower retirement age.

Income tax and retirement schemes
Philippe Chone2, Guy Laroque1
1University College London, United Kingdom; 2ENSIE-CREST

This article aims at understanding the interplay between pension schemes and tax instruments from a redistribution perspective. We are modeling extensive labor supply and retirement decisions over the life cycle, assuming a stationary environment with overlapping generations and perfect financial markets. Agents are differing in the way their productivity and opportunity cost of work evolve over their lifetime. At each date, they decide whether or not to participate in the labor force. Considering first the fiscal instrument, we characterize the shape of the optimal tax schedule and exhibit circumstances under which labor supply is distorted upwards. Second, as regards pensions, we describe various schemes, where pension transfers may depend on the retirement age, on the time spent working, or on (before or after tax) lifetime earnings. We study the interplay of the tax and pension instruments and emphasize the potential role of pensions in redistributing lifetime incomes.

3:30pm - 5:30pm
A 24, Palazzo Rosso

The introduction of disincentives for early retirement and its effect on labor market participation
Daniel Kempfert1, Timm Boenke2, Holger Luethen1,2
1DIW Berlin, Germany; 2FU Berlin, Germany

We evaluate the effectiveness of disincentives that have been introduced for early retirement in Germany, Therefore, we set up a detailed model of the German social security and tax system with special attention to the PAYG-pension system. Building on the fact that the institutional changes were phased in, we are able to estimate the parameters of a structural dynamic retirement model using high quality administrative data. This allows us to answer the question, whether and to what degree disincentives are able to steer retirement behavior of German pensioners. We also discuss the implications for the financial stability of the PAYG-pension scheme and investigate distributional effects. We try to give some insights on how a complementary private old age insurance plan (e.g. a life annuity) would have to look like, if the pre-reform level of old age income is to be retained.

Financial work incentives for disability benefit recipients:Lessons from a randomized field experiment
Monika Bütler1, Eva Deuchert1, Michael Lechner1, Stefan Staubli2, Petra Thiemann1
1University of St. Gallen, Switzerland; 2University of Calgary, Canada

This paper analyzes a conditional cash program that financially incentivizes work-related reduction of disability benefits. A randomized control group of DI beneficiaries receive the offer to claim a payment (“seed capital”) of up to CHF 72,000 (USD 71,000) if they take up or expand employment and reduce DI claims. The paper presents the results of the short-term evaluation by analyzing documented interest in taking up seed capital. Overall, interest in taking-up the financial incentive is low at only 3%. Individuals close to cash-offs react more on seed capital but the overall magnitude is small. Our results suggest that work disincentives imposed by cash-offs are unlikely the main driver for low employment and outflow from the Swiss disability insurance system, despite the fact that the partial disability insurance system generates a non-linear budget set, and bunching behavior at cash-offs are observed prior implementation of seed capital.

Welfare 14: Pension systems
Session Chair: Joachim Thøgersen, Oslo and Akershus University College of Applied Sciences

Life time pension benefits versus life time contributions
Nils Martin Stoelen, Dennis Fredriksen
Statistics Norway, Norway

Over the life course members of an insurance system normally will contribute by payments when in working age, and later receive pension
benefits as e.g. disabled or old-age pensioners. In Norway the former National Insurance Scheme was introduced in 1967, and a reform of the system started in 2011. Budgetary and distributional consequences between generations from these reforms are analysed by the dynamic microsimulation model MOSART. The effects are presented for different groups of the population by birth cohort, gender, education and for natives versus immigrants. As expected the results show that the cohorts who established the pay-as-you-go system experienced a substantial gain by letting the future generations pay.Over the life course the pension system redistributes incomes from men to women and from persons with high incomes to persons with low. Women are more affected by the pension reform from 2011 than men.

Means-testing retirement benefits in the UK: Is it efficient?
Hans Fehr1,2, Johannes Uhde3
1University of Würzburg, Germany; 2CESifo; 3Netspar
The literature has widely argued in favor of means-testing pension benefits as an efficient way to trade off distortions of labor supply and savings against distributional objectives. We construct a dynamic stochastic general equilibrium model with overlapping generations calibrated to the UK economy. In contrast to previous studies, we do not only look at the long-run welfare effects of policy reforms, but compute full transition paths and separate aggregate efficiency from intergenerational redistribution effects by means of compensating transfers. Our findings reveal that strictly means-testing benefits against pension income is optimal while welfare is deteriorated most efficiently. We show that recent cuts in the withdrawal rate of UK first pillar benefits was efficiency deteriorating. However, aggregate efficiency could be increased in the UK system by further lowering the taper rate on wealth while keeping benefits strictly means-tested against second pillar pension income.

Endogenous Retirement and Pay-as-you-go Pensions
Pan Liu1, Joachim Thaege1
1Oslo and Akershus University College of Applied Sciences, Norway; 2Iowa State University
A classic result in dynamic public economics states that a pay-as-you-go (PAYG) pension system is neither neutral nor desirable in a dynamically efficient overlapping generations economy with exogenous labor supply. This paper reevaluates this issue in a model with endogenous old-age retirement. In the model, agents respond to the pension system by optimally changing both their saving and their old-age labor supply. In such an environment, the PAYG system may be neutral. It may also be welfare improving in the long-run.

The Effect of Public Pension Wealth on Saving and Expenditure: Evidence from Poland’s 1999 Pension Reform
Marta Lachowska1, Michal Myck2
1W.E. Upjohn Institute, United States of America, Stockholm University, Sweden; 2Centre for Economic Analysis (CenEA), Poland
In order to study whether public pension systems displace private saving, we use the quasi-experimental variation in pension wealth created by Poland’s 1999 pension reform. The reform decreased pension generosity overall, but it had a differential effect on individuals depending on their year of birth. We begin by estimating difference-in-differences regressions, where we compare household saving and expenditure across time and between cohorts affected and unaffected by the reform. Next, we use the posttreatment change in pension wealth to estimate the extent of saving crowd-out and consumption crowd-in. We find that one additional Polish zloty, or PLN, of pension wealth crowds out about 0.20–0.60 PLN in household saving. We also find heterogeneity in responses. Our findings suggest that for middle-aged households, pension wealth and private saving are nearly perfect substitutes.

Welfare 15: Redistribution
Session Chair: Massimiliano Placenza, University of Torino

Individual Responsibility and Social Preferences for Redistribution: An Experimental Study
Sergio Beraldo1, Massimiliano Placenza2, Gilberto Turati3
1University of Naples "Federico II", Italy; 2University of Torino, Italy; 3University of Torino, Italy
The paper provides an experimental test to analyze the determinants of individual preferences for redistribution. Participants in the experiment face a trade-off between providing an effort on their own or free-riding on their fellows’ effort, playing in a framework where the pie and its distribution depend on circumstances which are both under and beyond the control of individuals. We find that individuals ask for more redistribution whenever differences in income levels are less dependent by personal effort. We also find complementarity among individual efforts. This means that free-riding behaviour becomes less frequent as the average level of effort in the society goes up. We also confirm that the prospect of upward mobility increases the probability that an individual asks for zero redistribution, thus providing support to the POUM hypothesis. This evidence provides insights for the ongoing debate on how reforming welfare systems to make them more sound with individual incentives.

Fiscal Demography: Age-related Redistributive Consequences of Consumption Taxation
Artur Pietr Walski
University of Economics, Katowice, Poland
Taking into account the role of consumption taxes as the source of public revenues and the growing propensity to consume characteristic at the aging society, the present paper focuses on an investigation of the consequences of the redistributive neutrality of consumption taxation in a situation when a characteristic of particular goods causes a different distribution of tax burden between consumer and seller. The study attempts to define the rule of diversification of consumption tax rates which will compensate for a different market effect (price elasticity) leading to a decrease in the wealth of consumers differentiated by age (age elasticity). The issue of the redistributive neutrality of consumption taxes is crucial because of lifetime differences in consumption. The seminal paper by Ando and Modigliani (1963) could be a good inspiration. The aim of the present paper is to construct a simple model of the redistributive effects induced by consumption taxes.

Optimal Taxation and Education Policy with Skill-Biased Technological Change
Uwe Travenmühl1, Bas Jacobs2
1Erasmus University Rotterdam, VU University Amsterdam, Tinbergen Institute, Netherlands, The; 2Erasmus University Rotterdam, Tinbergen Institute and CESifo
Abstract This paper studies optimal non-linear income taxation under the premise that increasing earnings inequality is driven by skill-biased technological change (SBTC). We employ the model by Rothschild and Scheuer (2013), while using the production function from the canonical model of SBTC (see e.g. Goldin and Katz, 2010). Using simulation, we find that marginal tax rates should decrease at the bottom of the income distribution, and increase at the top. The decrease at the bottom is driven by a drop in distributional benefits, and a trickle-down effect becoming less important. Higher marginal tax rates at the top result from lower efficiency costs, and the reduced role of the trickle-down mechanism. Our results are at odds with actual tax reforms which lowered marginal tax rates particularly at the top. We conjecture that these reforms might not have been an optimal response to SBTC.

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Register based Finnish panel data are used to examine income risk and redistribution in the working age population. The paper considers the extent of risk reduction produced by the tax-benefit system which is measured by differences between risk premia of factor and disposable household income. Social protection benefits have a positive role in reducing this difference while taxes have lost significance during the observation period. In addition, certainly equivalent income concepts are utilised to get some information on inequality and on redistribution of risk. Young adults, 20–29 years old and elderly, near retirement age 55–59 years old, seem to benefit most from social insurance. All working age groups seem to gain from redistribution in certainly equivalent income relative to redistribution of cash. Redistribution has been reduced over the sample period. The findings are robust to a particular value of the degree of risk aversion assumed.