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## What Drives Tax Policy Choices?

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### **Abstract**

Economists have put forth many specific tax design recommendations over the years, both for piecemeal changes to the tax system and for more fundamental reforms. These recommendations have typically been timely, plausible, and even elegant, and they often have had widespread agreement among economists, even those of greatly differing political sentiments. However, many – indeed perhaps most – of these proposals have gone nowhere in the actual policy implementation stage. Why is this? I argue here that the main reason for this lack of impact is politics – and a failure by economists to consider fully the central role of politics in policy making. Of course, all policy changes in democracies, including those that involve taxes, necessarily revolve around political considerations by elected politicians as policy makers. However, my argument goes beyond this obvious truism. Instead, I emphasize one specific aspect of politics: Who gains and who loses from a tax policy change? I argue that these are the types of political considerations that are decisive because it is the distributional effects of policies that determine how people vote and so that also determine how their elected representatives vote. I illustrate these points with a brief – and a deliberately selective – history of what I term ‘clever’ policy recommendations made over the years by major figures in the broad field of public economics and the narrower field of taxation, I then discuss the many possible reasons for this lack of policy impact, and I identify the factor that seems most likely to drive actual tax policy choices – the effects of tax policies on the winners and losers of the policies, as determined by broadly defined ‘distributional effects’. I finish with a discussion of the ways in which economics – and other disciplines – might more productively contribute to the policy discussion. Along the way, I indicate the ways in which the chapters in this volume contribute to the ongoing policy discussion.

Keywords: Taxation; tax policy; tax incidence; distributional effects; voting; political economy  
JEL codes: H20; H22; H50; D30; D72; D78

# What Drives Tax Policy Choices?

JAMES ALM\*

## ABSTRACT

Economists have put forth many specific tax design recommendations over the years, both for piecemeal changes to the tax system and for more fundamental reforms. These recommendations have typically been timely, plausible, and even elegant, and they often have had widespread agreement among economists, even those of greatly differing political sentiments. However, many – indeed perhaps most – of these proposals have gone nowhere in the actual policy implementation stage. Why is this? I argue here that the main reason for this lack of impact is politics – and a failure by economists to consider fully the central role of politics in policy making. Of course, all policy changes in democracies, including those that involve taxes, necessarily revolve around political considerations by elected politicians as policy makers. However, my argument goes beyond this obvious truism. Instead, I emphasize one specific aspect of politics: Who gains and who loses from a tax policy change? I argue that these are the types of political considerations that are decisive because it is the distributional effects of policies that determine how people vote and so that also determine how their elected representatives vote. I illustrate these points with a brief – and a deliberately selective – history of what I term ‘clever’ policy recommendations made over the years by major figures in the broad field of public economics and the narrower field of taxation, I then discuss the many possible reasons for this lack of policy impact, and I identify the factor that seems most likely to drive actual tax policy choices – the effects of tax policies on the winners and losers of the policies, as determined by broadly defined ‘distributional effects’. I finish with a discussion of the ways in which economics – and other disciplines – might more productively contribute to the policy discussion. Along the way, I indicate the ways in which the chapters in this volume contribute to the ongoing policy discussion.

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\* Tulane University. I have received many helpful comments from Yvette Lind and the participants in the seminar “Tax in Politics, Politics in Tax – A Dialogue on the Political Economy of Tax Laws”, held in Oslo, Norway in May 2025. Please address any correspondence to James Alm, Professor Emeritus, Department of Economics, Tulane University, New Orleans, LA 70118 USA (jalm@tulane.edu).

## INTRODUCTION

What do we want a tax system to achieve? Tax policy choices involve the pursuit of multiple goals.<sup>1</sup> Taxation must generate the revenues necessary to finance government expenditures, what might be termed ‘adequacy’. It must raise these revenues in a way seen as fair, or the goal of ‘equity’, where individuals or businesses pay their ‘fair’ share of taxes. It must not unduly distort the decisions of individuals and firms (‘efficiency’), although there may be circumstances in which changing these decisions is in fact the intention of taxation. Other possible goals include encouraging economic growth, achieving political acceptance, being easy to collect and to pay, generating equity by race or gender or ethnicity, or promoting economic stabilization. Balancing these goals in making tax policy choices in an ‘optimal’ way is an enduring challenge, and one for which there is never a unique, one-size-fits-all answer.

Over the years, these many goals have generated many specific tax design recommendations from economists and others, both for piecemeal or incremental changes to the tax system and for more fundamental and more radical reforms. These recommendations are wide-ranging, covering proposals for optimal income and commodity taxes, lifetime income averaging, personal consumption taxation, capital income and capital gains taxation, a destination-based cash flow tax on corporations, a world-wide wealth tax, a world-wide minimum corporate income tax, an income tax on unrealized income, carbon taxation, earmarked taxes, and the like. Indeed, economists like to believe that their recommendations influence heavily the tax policy choices ultimately made by governments, perhaps in line with the famous

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<sup>11</sup> Many of these same issues are discussed in several chapters in this volume. See: Natalia Pushkareva, ‘The Limits of Tax: On the Need for a Comprehensive Approach to Fiscal Policy’, Chapter 2; and Sam Jacob van der Vlugt, ‘Legality and Legitimacy in Tax Law-making’, Chapter 3.

quotation from John Maynard Keynes in his *The General Theory of Employment, Interest, and Money*:<sup>2</sup>

‘Practical men who believe themselves to be quite exempt from any intellectual influence, are usually the slaves of some defunct economist. Madmen in authority, who hear voices in the air, are distilling their frenzy from some academic scribbler of a few years back.’

However, the reality surrounding the actual policy impact of these many recommendations is much different than suggested by Keynes. It is this reality that I examine in this chapter.

Now there are certainly many aspects of tax policy choices that command widespread agreement, even among economists of greatly differing political sentiments. However, many – and I argue that it is probably more accurate to use ‘most’ rather than ‘many’ – of these plausible, timely, and elegant proposals by economists have gone nowhere. Indeed, the same can be said of the many recommendations made by experts from many other disciplines.

Why is this?

I argue here that, while there are many reasons for this lack of impact, the main reason is politics – and a failure by economists to consider fully the central role of politics in policy making. Of course, it is accurate, as well as convenient, to argue that politics drives policy choices in democracies. Indeed, all policy changes in democracies, including those that involve taxes, necessarily revolve around political considerations by elected politicians as policy makers. However, my argument goes beyond this obvious truism. Instead, I emphasize one specific aspect of politics: Who gains and who loses from a tax policy change? I argue that these are the types of political considerations that are decisive because it is the distributional effects of

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<sup>2</sup> John Maynard Keynes (1936), *The General Theory of Money, Interest, and Prices*, London, UK: Palgrave Macmillan.

policies that determine how people vote and so that also determine how their elected representatives vote. These distributional effects clearly start with the ways by which a tax policy affects the income of individuals. This is an area in which economists have much to say, as identified by their standard fiscal incidence studies. Importantly, however, I argue that these distributional effects go well beyond a change in the income but that also they should incorporate any change in broader aspects of individual welfare. Does the enactment of a policy stigmatize individuals of certain types, while commending other types of individuals? Does the policy reflect a political class that treats them with disdain, while praising other individuals? Does the policy impose emotional costs on individuals, but only on individuals of some types? Does the policy suggest a rejection of their culture of certain classes of individuals, but an embrace of the culture of other classes of individuals? Is the policy inconsistent with the ideology of some types of individuals, while endorsing the ideology of other types? Does the policy generate anger and resentment from some individuals, but not from others? I argue that it is these types of broadly defined ‘distributional effects’ for which policies create winners and losers, it is these types of ‘distributional effects’ that fundamentally drive political considerations, and it is these types of ‘distributional effects’ about which economists have had little to say. As a result, there is a general failure of economists to say much that politicians consider relevant or useful about winners and losers, and it is this failure that largely relegates economists to the sidelines in many policy discussions.

To illustrate these points, I first present in this chapter a brief – and a deliberately selective – history of what I term ‘clever’ policy recommendations made over the years by major figures in the broad field of public economics and the narrower field of taxation, people who include Nobel Prize winners in economics like Peter Diamond, James Mirrlees, Paul Samuelson,

Joseph Stiglitz, and William Vickery, among many others. While some of these recommendations have had some impact on actual and enacted policies, most have not. I discuss the many possible reasons for this lack of policy impact. I then identify the factor that seems most likely to drive actual tax policy choices – the effects of tax policies on the winners and losers of the policies, as determined by broadly defined ‘distributional effects’. I finish with a discussion of the ways in which economics – and other disciplines – might more productively contribute to the policy discussion. Along the way, I indicate the ways in which the chapters in this volume contribute to the ongoing policy discussion.

Note some limitations of my discussion. My focus is on a representative selection of ‘clever’ proposals by prominent economists, proposals that often command widespread support within the economics profession, that are based on sound and even innovative economic reasoning, but that have had a decidedly mixed record in actual real-world policy implementation. I also focus on tax recommendations originating in democracies, especially the United States and United Kingdom, as well as on proposals other than simple tax cuts given the obvious popularity of most all recommendations that simply lower taxes. Finally, I examine proposals by economists, even though I emphasize throughout that economics is not the only discipline whose recommendations are often ignored in the policy implementation stage, for many of the same reasons that recommendations by economists are typically ignored.

### **A BRIEF HISTORY OF ‘CLEVER’ POLICY RECOMMENDATIONS<sup>3</sup>**

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<sup>3</sup> This section is based in part on a presentation made by Jim Hines at the 20<sup>th</sup> anniversary celebration of the Office of Tax Policy Research at University of Michigan in 2018, entitled “Tax Research: Motivation and Consequences”. I am grateful to Jim for sharing his presentation.

Tax policy recommendations come in many shapes and sizes. I discuss some of the better known recommendations from some of the better-known economists that have emerged over the last century.

*Choosing Optimal Commodity Taxes.* In 1927, Frank A. Ramsey was the first economist to analyze formally the optimal commodity tax structure – more accurately, the efficient commodity tax structure. He found that efficiency considerations required that a good whose (compensated) elasticity of demand was greater in absolute value be taxed at a lower rate than a good whose elasticity was lower; that is, the most efficient commodity tax structure is, under some conditions, one in which tax rates are inversely proportional to elasticities of demand, the so-called ‘Ramsey Rule’ for optimal commodity tax rates.<sup>4</sup> Imposing commodity taxes in this manner would generate a lower excess burden of taxation (and so be more efficient) because the excess burden of a tax increases with the good’s elasticity of demand. This insight attracted so little attention over the years that Paul A. Samuelson independently rediscovered this result in a 1951 report for the U.S. Department of the Treasury, subsequently republished in 1986.<sup>5</sup> Overall, the basic result of these analyses suggests that proportional (or uniform) commodity tax rates are not in general the most efficient tax structure.

However, this insight has had little practical impact on commodity tax rates, in part because goods with an inelastic demand (e.g., necessities) are often consumed disproportionately by lower income individuals, while those with an elastic demand (e.g., luxuries) are often consumed in greater amounts by higher income individuals.

Perhaps as a result, in 1975 Peter Diamond extended the basic Ramsey Rule to incorporate distributional (or equity) considerations in addition to the efficiency goals of the

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<sup>4</sup> Frank A. Ramsey (1927), ‘A Contribution to the Theory of Taxation’, *Economic Journal*, 37 (145), 47-61.

<sup>5</sup> Paul A. Samuelson (1986), ‘Theory of Optimal Taxation’, *Journal of Public Economics*, 30 (2), 137-143.

original Ramsey and Samuelson analyses, leading to a ‘Many-person Ramsey Rule’ in which optimal commodity tax rates balance the efficiency gains of higher tax rates on inelastic goods consumed more by the ‘poor’ (or the ‘more deserving’ households) with the equity gains of higher tax rates on elastic goods consumed more by the ‘rich’ (or the ‘less deserving’ households).<sup>6</sup>

Again, this modified recommendation has had little practical impact on tax design. Indeed, a far more common policy recommendation is that tax rates should be uniform, rather than differentiated in ways that balance efficiency and equity considerations, even though proportional tax rates are seldom actually seen in practice.

*Choosing Optimal Income Taxes.* There is also a large literature in which income tax rates are chosen to balance the equity gains from redistributing income taxes from the rich to the poor, with the efficiency losses of imposing income taxes that distort labor supply choices.<sup>7</sup> This recommendation emerged from the work of James A. Mirrlees,<sup>8</sup> which built upon his 1971 work with Peter Diamond.<sup>9</sup> On equity grounds, these analyses typically conclude that income tax rates should be higher on those with higher income; indeed, under some special conditions (e.g., labor supply decisions are fixed and unresponsive to tax rates), income taxes should be chosen to equalize after-tax incomes, thereby implying marginal tax rates of 100 percent on higher income individuals. However, on efficiency grounds, these analyses conclude that marginal tax rates

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<sup>6</sup> Peter A. Diamond (1975), ‘A Many-person Ramsey Tax Rule’, *Journal of Public Economics*, 4 (4), 335-342.

<sup>7</sup> One aspect of these efficiency losses stems from the potential mobility of individuals in response to differences in tax rates across jurisdictions. For discussion of this issue, see Chapter 4 in this volume: Yvette Lind, ‘Insiders, Outsiders, and Those in Between: Legal Opportunities and Boundaries Pertinent to Cross-border Mobility of Individuals’.

<sup>8</sup> James A. Mirrlees (1971), ‘An Exploration in the Theory of Optimum Income Taxation’, *The Review of Economic Studies*, 37 (2), 323-349; and James A. Mirrlees (1976), ‘Optimal Tax Theory: A Synthesis’, *Journal of Public Economics*, 6 (4), 327-358.

<sup>9</sup> Peter A. Diamond and James A. Mirrlees (1971), ‘Optimal Taxation and Public Production, Part II: Tax Rules’, *The American Economic Review*, 61 (2), 261-278.

should be lower the more responsive are individuals in their labor supply decisions. Overall, a striking result of the analyses in which tradeoffs between equity and efficiency are present is that the optimal income tax structure typically imposes progressive tax rates, but only up to some level, after which tax rates fall. Indeed, under some circumstances, Efraim Sadka (1976) showed that the optimal marginal tax rate on the very rich is zero,<sup>10</sup> although Peter Diamond later identified cases in which this result does not hold.<sup>11</sup>

Relatedly, William Vickrey proposed in 1947 a scheme for lifetime income averaging, along with an expanded income tax base that included many types of provisions that were then untaxed and also with an accompanying progressive income tax rate structure.<sup>12</sup> This proposal was widely viewed as clever, efficient, and equitable. It was also incredibly complicated, so much so that no country has contemplated its enactment. Indeed, in a 1992 retrospective and updated commentary, Vickrey wrote that ‘[s]ince the publication of the Agenda in 1947, remarkably little of its recommendations have seen implementation.’<sup>13</sup>

Overall, these various recommendations are so varied and so complicated that they have had virtually no practical impact on income tax rates. In particular, the recommendation of zero marginal income tax rates on the very rich is far afield from any real-world income tax.<sup>14</sup>

*Choosing the Optimal Mix of Commodity and Income Taxes.* Of course, most all tax systems consist of a mix of commodity and income taxes. In 1976 Anthony B. Atkinson and

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<sup>10</sup> Efraim Sadka (1976), ‘On Income Distribution, Incentives Effects, and Optimal Income Taxation’, *The Review of Economic Studies*, 43 (2), 261-268.

<sup>11</sup> Peter A. Diamond (1998), ‘Optimal Income Taxation: An Example with a U-Shaped Pattern of Marginal Tax Rates’, *The American Economic Review*, 88 (1), 83-95.

<sup>12</sup> William Vickrey (1947), *Agenda for Progressive Taxation*, New York, NY: The Ronald Press Company.

<sup>13</sup> William Vickrey (1992), ‘An Updated Agenda for Progressive Taxation’, *The American Economic Review*, 82 (2), 257-262.

<sup>14</sup> For somewhat dated but still relevant discussions of the relevance – and mainly the practical irrelevance – of optimal tax theory to actual real-world tax policy design, see: Joel Slemrod (1990), ‘Optimal Taxation and Optimal Tax Systems’, *The Journal of Economic Perspectives*, 4 (1), 157-178; and James Alm (1996), ‘What is an “Optimal” Tax System?’, *National Tax Journal*, 49 (1), 117-133.

Joseph E. Stiglitz analyzed this optimal ‘tax mix’, and concluded that both income and commodity taxes should be used in general.<sup>15</sup> However, under some restrictive conditions, the optimal form of commodity tax rates that are imposed in the presence of an optimal income tax requires that uniform commodity tax rates, so that taxation of commodities at different rates is not optimal and that, effectively, only the optimal income tax is used.<sup>16</sup> This recommendation of using only an optimal income tax is of course routinely ignored.<sup>17</sup>

*Replacing the Individual Income Tax with a Personal Consumption Tax.* Income is not the only possible choice for a tax base. Indeed, there have been many proposals for replacing the individual income tax with a personal consumption (or expenditure) tax, due largely to the belief that a tax on consumption rather than on income is both more equitable (because it is fairer to tax someone on what they consume) and also more efficient (because it eliminates the intertemporal distortion caused by an income tax that taxes interest income). A personal consumption tax has been advocated by such prominent economists as John Stuart Mill, Alfred Marshall, and A.C. Pigou, and detailed proposals have been made by Irving Fisher and Herbert W. Fisher,<sup>18</sup> Nicholas Kaldor,<sup>19</sup> William D. Andrews,<sup>20</sup> and David F. Bradford.<sup>21</sup> More recently, then-President George W. Bush, fresh from his 2004 re-election to the presidency, appointed an Advisory Panel on Federal Tax Reform to recommend ways of reforming the federal tax system, and one of its

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<sup>15</sup> Anthony B. Atkinson, and Joseph E. Stiglitz (1976), ‘The Design of Tax Structure: Direct Versus Indirect Taxation’, *Journal of Public Economics*, 6 (1), 55-76.

<sup>16</sup> For a related analysis that reaches much the same conclusions, see: Robin Boadway, Maurice Marchand, and Pierre Pestieau (1994), ‘Towards a Theory of the Direct-Indirect Tax Mix’, *Journal of Public Economics*, 55 (1), 71-88.

<sup>17</sup> For a related analysis that reaches much the same conclusions, see: Robin Boadway, Maurice Marchand, and Pierre Pestieau (1994), ‘Towards a Theory of the Direct-Indirect Tax Mix’, *Journal of Public Economics*, 55 (1), 71-88.

<sup>18</sup> Irving Fisher and Herbert W. Fisher (1942), *Constructive Income Taxation – A Proposal for Reform*, New York, NY: Harper & Brothers Publishing.

<sup>19</sup> Nicholas Kaldor (1955), *An Expenditure Tax*, London, UK: George Allen & Unwin Ltd.

<sup>20</sup> William D. Andrews (1974), ‘A Consumption-type or Cash Flow Personal Income Tax’, *Harvard Law Review*, 87 (6), 1113-1188.

<sup>21</sup> David F. Bradford (1977), *Blueprints for Basic Tax Reform*, Washington, D.C.: U.S. Department of the Treasury.

recommendations was for a ‘Progressive Consumption Tax Plan’ whose basic form was similar to those for a personal consumption tax.<sup>22</sup> Also, the ‘Flat Tax’ proposed by Robert E. Hall and Alvin Rabushka is much like a personal consumption tax, despite its name.<sup>23</sup> All of these proposals essentially call for something like an individual income tax but with a deduction for new saving, leaving consumption as the tax base.<sup>24</sup>

Despite the impressive pedigree and the potential appeal of a tax on consumption rather than income, such a tax has only rarely been used, in Ceylon (now Sri Lanka) and India in the 1950s and 1960s, before being abolished due to administrative problems in both countries.

*Taxing Capital Gains.* A criticism of the common practice of taxing realized capital gains is that the tax might lead individuals to hold on to their assets in order to avoid being taxed on any realized capital gains, termed the ‘lock-in effect’. Alan J. Auerbach proposed in 1991 a method for taxing capital gains that avoided the lock-in effect, as an alternative to the inefficiencies generated by the current system of realization-based capital gains taxation, making

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<sup>22</sup> President’s Advisory Panel on Federal Tax Reform (2005), *Simple, Fair, and Pro-Growth: Proposals to Fix America’s Tax System*, Washington, D.C.: President’s Advisory Panel on Federal Tax Reform.

<sup>23</sup> Robert A. Hall and Alvin Rabushka (2007), *The Flat Tax* (2<sup>nd</sup> Edition), Palo Alto, CA: Hoover Institution Press. To be more precise, the Hall and Rabushka ‘Flat Tax’ combines an ‘Individual Wage Tax’, or a flat rate tax imposed at the individual level on wage (and pension) income with no itemized deductions, with a ‘Business Tax’, or a flat rate tax on the difference between a firm’s gross receipts and the costs of all intermediate inputs (including the cost of capital goods and also including wages, both of which are therefore allowed as deductions against the firm’s gross receipts). Now the tax base of a standard value-added tax (VAT) equals the difference between a firm’s gross receipts and the costs of all intermediate inputs, including the cost of capital goods but excluding wages, so the base of a standard VAT equals the sum of wages, interest, rents, and profits of the firm, all taxed at the business level. By taking wages out of the Business Tax by allowing them as a business deduction while still taxing interest, rents, and profits of the firm, and then taxing wages at the individual level with the Individual Wage Tax, the base of the resulting Flat Tax becomes identical to the base of a standard VAT; that is, the total tax base on businesses and individuals is still consumption, equal to the sum of wages, interest, rents, and profits, but the collection of the tax is now done both at the business and at the individual level. The Business Tax in the Flat Tax is similar to a VAT, except that labor costs (e.g., wages) are allowed as a business deduction, along with other input costs and capital costs. The “Individual Wage Tax” in the Flat Tax is imposed at the individual level on wage (and pension) income.

<sup>24</sup> For a discussion of various issues in consumption taxes, see: Rita de la Feria and Michael Walpole (2020), ‘The Impact of Public Perceptions on General Consumption Taxes’, *British Tax Review*, 67 (5), 637-669; and Artur Swistak and Rita de la Feria (2024), ‘Designing a Progressive VAT’, IMF Staff Working Paper WP/24/78, Washington, D.C.: International Monetary Fund.

it a compelling alternative to realization-based taxation.<sup>25</sup> This proposal has had no impact on the practice of capital gains taxation, due largely to its complexity.<sup>26</sup>

*Taxing Capital Income.* Both Kenneth L. Judd and Christophe Chamley have argued that capital income taxes should be zero (and firm purchases of capital goods should even be subsidized at the margin), in order to overcome distortions in capital markets due to imperfect competition and to intertemporal distortions in income taxation.<sup>27</sup> Their work shows that this policy would generate large dynamic efficiency gains generated by greater economic growth. This proposal has had little impact on the taxation of capital income; that is, capital income remains subject to individual and corporate income taxes in most all countries. The slight exception here is the presence in some tax systems of allowing capital purchases as deductions from corporate income taxes.

*Taxing Corporate Income.* In a series of papers, Alan J. Auerbach and his co-authors have proposed what they call a ‘Destination-based Cash Flow Tax’ (DBCFT).<sup>28</sup> Unlike a traditional corporate income tax, the DBCFT allows firms to expense immediately their capital investments, which means that so-called normal profits are removed from the tax base, leaving only ‘pure

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<sup>25</sup> Alan J. Auerbach (1991), ‘Retrospective Capital Gains Taxation’, *The American Economic Review*, 81 (1), 167-178.

<sup>26</sup> For relevant discussion of these issues, see several chapters in this volume: Douglas Bamford, ‘Property, Ideology and Tax Scholactivism’, Chapter 6; Clinton Wallace, ‘Intellectual Foundations for Populist Tax Policy’, Chapter 8; and Harold Espeli, ‘Historical Development of Inheritance Taxation: Norway and Sweden During the 20<sup>th</sup> Century’, Chapter 9.

<sup>27</sup> Kenneth L. Judd (1985), ‘Redistributive Taxation in a Simple Perfect Foresight Model’, *Journal of Public Economics*, 28 (1), 59-83; Kenneth L. Judd (1999), ‘Optimal Taxation and Spending in General Competitive Growth Models’, *Journal of Public Economics*, 71 (1), 1-26; Christophe Chamley (1986), ‘Optimal Taxation of Capital Income in General Equilibrium with Infinite Lives’, *Econometrica*, 54 (3), 607-622.

<sup>28</sup> Alan J. Auerbach and David F. Bradford (2004), ‘Generalized Cash Flow Taxation’, *Journal of Public Economics*, 88 (5), 957-980; Alan J. Auerbach (2017), ‘Demystifying the Destination-Based Cash-Flow Tax’, *Brookings Papers on Economic Activity*, Fall 2017, 409-432; Alan J. Auerbach, Michael P. Devereux, Michael Keen, and John Vella (2017), ‘International Tax Planning under the Destination-Based Cash-Flow Tax’, *National Tax Journal*, 70 (4) 783-802; Alan J. Auerbach and Michael P. Devereux (2018), ‘Cash-flow Taxes in an International Setting’, *American Economic Journal: Economic Policy*, 10 (3), 69-94; and Michael P. Devereux, Alan J. Auerbach, Michael Keen, Paul Oosterhuis, Wolfgang Schön, and John Vella (2021), *Taxing Profit in a Global Economy*, Oxford, UK: Oxford University Press.

economic profits’ (or profits in excess of normal rates of return) subject to the tax. Also, the border adjustment aspect of the DBCFT is similar to the ways in which a value-added tax (VAT) treats cross-border transactions (e.g., exports are exempt but imports are taxed). In principal, the DBCFT eliminates incentives for multinational firms to avoid taxes through mechanisms that shift profits to low-tax countries. In essence, then, the DBCFT is a border-adjusted tax on business cash flows, broadly equivalent to a VAT that is combined with a wage subsidy.

To date, no country has enacted a destination-based cash flow tax, although such a tax was actually proposed by the Republican Party of the United States as part of its 2016 national policy platform. A primary concern with the DBCFT is the many complicated provisions required for its implementation, especially in combination with existing systems of income taxation already in place around the world.

*Taxing Corporate Income Redux.* The Organisation for Economic Cooperation and Development (OECD) has recently led efforts to tax corporate income where consumers are located (BEPS 2.0 Pillar One) and to enact a global minimum corporate income tax (BEPS 2.0 Pillar Two).<sup>29</sup> Many economists strongly endorse these efforts. However, while progress seems to be proceeding with international agreements, these ‘pillars’ have yet to be enacted.<sup>30</sup>

*Taxing Wealth.* Thomas Piketty and his co-authors have found compelling empirical evidence that modern capitalism has created widening inequality in wealth ownership (and in income distribution as well).<sup>31</sup> His solution is the imposition of a world-wide wealth tax,

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<sup>29</sup> Organisation for Economic Co-operation and Development (2021), *Fact Sheet Amount A: Progress Report on Amount A of Pillar One*, Paris, France: OECD; Organisation for Economic Co-operation and Development (2021), *The Pillar Two Rules in a Nutshell: Tax Challenges Arising from the Digitalisation of the Economy – Global Anti-base Erosion Model Rules (Pillar Two)*, Paris, France: OECD.

<sup>30</sup> Some political dimensions of international taxation are discussed in a chapter in this volume. See: Steven A. Dean, ‘Cuban Gambits/Cuban Missiles: The Cold War and Global Tax Politics’, Chapter 7.

<sup>31</sup> Thomas Piketty (2014), *Capital in the 21<sup>st</sup> Century*, Cambridge, MA: Belknap Press of the Harvard University Press; Thomas Piketty and Emmanuel Saez (2003). ‘Income Inequality in the United States, 1913-1998’, *The Quarterly Journal of Economics*, 118 (1), 1-41; Thomas Piketty (2003), ‘Income Inequality in France, 1901-1998’,

imposed with a progressive tax rate structure. Similar calls for a progressive, world-wide wealth tax have come from Emmanuel Saez and Gabriel Zucman, along with politicians like U.S. Senators Bernie Sanders and Elizabeth Warren, among others.<sup>32</sup> To date, however, such a wealth tax has not been enacted. Indeed, according to the most recent version of the OECD Global Revenue Statistics Database, the number of countries with any tax on wealth has fallen significantly over the years due largely to administrative problems, leaving at present only 5 countries in the OECD with a comprehensive wealth tax (Colombia, France, Norway, Spain, and Switzerland).<sup>33</sup>

*Taxing Carbon.* Economists are virtually unanimous in advocating a carbon tax as the most effective way of dealing with the externalities of climate change while also raising significant tax revenues.<sup>34</sup> Representative of these sentiments is a 2019 statement in *The Wall Street Journal*, signed by 3649 U.S. economists, 28 Nobel laureate economists, 15 former Chairs of the Council of Economic Advisors, 4 former Chairs of the Federal Reserve, and 2 former Secretaries of the U.S. Department of the Treasury:

‘A carbon tax offers the most cost-effective lever to reduce carbon emissions at the scale and speed that is necessary. By correcting a well-known market failure, a carbon tax will

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*The Journal of Political Economy*, 111 (5), 1004-1042; Thomas Piketty, Gilles Postel-Vinay, and Jean-Laurent Rosenthal (2006), ‘Wealth Concentration in a Developing Economy: Paris and France, 1807-1994’, *The American Economic Review*, 96 (1), 236-256; Anthony B. Atkinson, Thomas Piketty, and Emmanuel Saez (2011), ‘Top Incomes in the Long Run of History’, *The Journal of Economic Literature*, 49 (1), 3-71; Thomas Piketty, 2011. ‘On the Long-run Evolution of Inheritance: France 1820-2050’, *The Quarterly Journal of Economics*, 126 (3), 1071-1131 Thomas Piketty and Gabriel Zucman (2014), ‘Capital Is Back: Wealth-Income Ratios in Rich Countries 1700-2010’, *The Quarterly Journal of Economics*, 129 (3), 1255-1310.

<sup>32</sup> Emmanuel Saez and Gabriel Zucman (2019), *The Triumph of Injustice: How the Rich Dodge Taxes and How to Make Them Pay*, New York, NY: W. W. Norton; Emmanuel Saez and Gabriel Zucman (2019b), ‘Progressive Wealth Taxation’, *Brookings Papers on Economic Activity*, Fall 2019, 437-511.

<sup>33</sup> See <https://www.oecd.org/en/data/datasets/global-revenue-statistics-database.html>.

<sup>34</sup> See especially: Nicholas Stern (2007), *The Economics of Climate Change – The Stern Review*, Cambridge, UK: Cambridge University Press. Some of these same environmental issues are discussed in a chapter in this volume. See: Kerrie Sadiq and Ashesha Weerasinghe, ‘Australia’s Tax Response to Climate Change: Policy Drift, Political Short-Termism, and Regulatory Capture’, Chapter 10.

send a powerful price signal that harnesses the invisible hand of the marketplace to steer economic actors towards a low-carbon future.<sup>35</sup>

There are many countries around the world that have in fact enacted some form of a carbon tax, especially countries in the EU. However, despite the strong endorsement of U.S. economists, the U.S. has never come close to enacting – or even introducing in Congress – legislation that would implement the carbon tax.

*Changing Other Tax Features.* There are obviously many other more tax proposals that have been made over the last century, with little or no actual impact. Looking only at U.S. proposals, these include:

- *Reducing federal government fiscal deficits* by a combination of raising taxes and reducing spending. Most all of these proposals have been given lip-service by politicians (e.g., the 2010 Simpson-Bowles Commission), but have then typically been ignored. Indeed, it is estimated that the just-passed One Big Beautiful Bill Act of 2025 will add over USD 3 trillion to U.S. debt over the next 10 years.
- *Enacting a ‘Broad Base, Low Rates’ (BBLR) tax reform*, in which the tax base is broadened by reducing or eliminating various tax preferences, thereby allowing reduced tax rates on the expanded tax base. This approach is consistent with notion of an income tax on ‘comprehensive income’, as suggested by Georg von Schanz,<sup>36</sup> Robert M. Haig,<sup>37</sup> and Henry C. Simons,<sup>38</sup> and in fact it has sometimes been followed both in the U.S. (e.g.,

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<sup>35</sup> See <https://www.wsj.com/articles/economists-statement-on-carbon-dividends-11547682910?mod=Searchresults&pos=1&page=1>.

<sup>36</sup> Georg von Schanz (1896), ‘Der einkommensbegriff und die einkommensteuergesetze’ [Income Realized and the Income Tax Law], *FinanzArchiv*, 13 (1), 1-87.

<sup>37</sup> Robert M. Haig (1921), ‘The Concept of Income – Economic and Legal Aspects’, in *The Federal Income Tax*, Robert M. Haig (ed.), 1-28, New York, NY: Columbia University Press.

<sup>38</sup> Henry C. Simons (1938), *Personal Income Taxation: The Definition of Income as a Problem of Fiscal Policy*, Chicago, IL: University of Chicago Press.

the Tax Reform Act of 1986) and in countries around the world (e.g., New Zealand).

However, the BBLR approach has been largely ignored in recent years in the U.S., as shown in part by unsuccessful efforts to reduce the estimated USD 2 trillion in federal tax expenditures.<sup>39</sup>

- *Increasing tax enforcement.* There is recent evidence by William C. Boning, Nathaniel Hendren, Ben Sprung-Keyser, and Ellen Stuart that increasing enforcement – especially enforcement targeted at the rich – will reduce tax evasion by significant amounts, generating revenues that far exceed the budgeted cost of the enforcement, with a USD 1 increase in enforcement increasing revenues by significantly more than USD 1.<sup>40</sup> Indeed, Boning and his co-authors estimate a cumulative 10-year ‘multiplier’ from a USD 1 increase in enforcement that exceeds USD 5 across all income classes and that reaches USD 12 for enforcement spending targeted at the top 10 percent of taxpayers. In short, greater enforcement spending more than pays for itself, especially when enforcement focuses on the rich. However, the initial USD 45 billion increase in U.S. Internal Revenue Service (IRS) enforcement budgets enacted in the Inflation Reduction Act of 2022 has now been reduced to virtually zero.
- *Reducing tariffs.* Economists are virtually unanimous that tariffs on international trade should be low (even zero), and over the last century the U.S. has helped lower tariffs around the world to historically low levels. However, the Trump Administration has in

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<sup>39</sup> For a critique of the use of comprehensive income as a guide for tax policy, see: James Alm (2018), ‘Is the Haig-Simons Standard Dead? The Uneasy Case for a Comprehensive Income Tax’, *National Tax Journal*, 71 (2), 379-398.

<sup>40</sup> William C. Boning, Nathaniel Hendren, Ben Sprung-Keyser, and Ellen Stuart (2025), ‘A Welfare Analysis of Tax Audits Across the Income Distribution’, *The Quarterly Journal of Economics*, 140 (1), 63-112.

only a few months raised the average U.S. tariff from about 2 percent to over 18 percent, according to the Yale Budget Lab.<sup>41</sup>

There have also been miscellaneous and quite specific proposals for such things as: avoiding the use of tax incentives for economic development; discouraging the use of taxes for targeted, or “earmarked”, purposes; increasing local property taxes; integrating individual and corporate taxes; expanding the use of tax withholding on specific forms of income (e.g., passive income); eliminating the current 20 percent deduction for pass-through income; eliminating the exclusion of tip and overtime income from the U.S. individual income tax; eliminating ‘stepped up basis on inherited assets; and so on. Most all of these miscellaneous proposals have not been enacted.

*Summary.* There are of course numerous examples in which the advice of economists has apparently been followed by politicians, especially in areas that involve cutting individual and business tax rates. However, there is often a striking difference in the policy recommendations of economists and the policies that are actually implemented. Indeed, there are many examples in which surveys of economists demonstrate a large consensus on specific policy reforms that have never been enacted.<sup>42</sup> Even focusing only on tax issues, there are often similar results.<sup>43</sup>

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<sup>41</sup> See <https://budgetlab.yale.edu/research/state-us-tariffs-october-17-2025>.

<sup>42</sup> Although somewhat dated, there are illustrative examples of opinion surveys for U.S. economists (e.g., Richard M. Alston, James R. Kearl, and Michael B. Vaughan (1992), ‘Is There a Consensus among Economists in the 1990s?’, *The American Economic Review*, 82 (2), 203-209; and James R. Kearl, Clayne L. Pope, Gordon C. Whiting, and Larry T. Wimmer (1993), ‘A Confusion of Economists?’, *The American Economic Review*, 69 (2), 28-37) and also for European economists (e.g., Bruno S. Frey, Victor Ginsburgh, Pierre Pestieau, Werner W. Pommerehne, and Friedrich Schneider (1983), ‘Consensus, Dissension, and Ideology among Economists in Various European Countries and in the United States’, *European Economic Review*, 23 (1), 59-69; and Bruno S. Frey and Reiner Eichenberger (1992), ‘Economics and Economists: A European Perspective’, *The American Economic Review*, 82 (2), 16-20). For more recent examples of surveys, see the U.S. Economic Experts Panel at the Kent A. Clark Center for Global Markets of the University of Chicago Booth School of Business, available online at <https://kentclarkcenter.org/us-economic-experts-panel/>.

<sup>43</sup> For surveys of tax specialists, see: Mabel L. Walker (1935), ‘Opinion of American Professors of Public Finance on Important Tax Questions as of 1 January 1935’, in *Tax Systems of the World*, Tax Research Foundation (ed.). Chicago, IL: Commerce Clearing House; Joel Slemrod (1995), ‘Professional Opinions about Tax Policy: 1994 and 1934’, *National Tax Journal*, 48 (1), 121-147; Joel Slemrod (2023), ‘Three Decades of Tax Analysis, 1992-2022’, *National Tax Journal*, 76 (4), 899-908; Karlyn Bowman (2009), ‘What Do Americans Think About Taxes?’, *Tax Notes*, 123, 99-105; and Diane Lim, Joel Slemrod, and Eleanor Wilking (2013), ‘Expert and Public Attitudes Toward Tax Policy: 2013, 1994, and 1934’, *National Tax Journal*, 66 (4), 775-806. These surveys demonstrate that there are

The obvious question then becomes: What factors explain the impact – or the lack of impact – of these many ‘clever tax proposals? I speculate on these factors in the next section.

## **WHY DO SO MANY POLICY RECOMMENDATIONS HAVE SO LITTLE IMPACT?**

There are many possible reasons for this lack of impact. In no particular order, these reasons center on various considerations.

Tax policy almost always involve balancing conflicting goals, and people have different goals – the goals that motivate economists in formulating their ‘clever’ tax proposals may not be the goals that drive voters or politicians.

Relatedly, these conflicting goals involve balancing tradeoffs, the ways in which these tradeoffs are balanced depends upon the weights placed on these tradeoffs, and – again – people have different weights.<sup>44</sup>

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many specific tax proposals that command strong support among tax economists. For a survey of Americans on their attitudes toward taxes, see: National Public Radio, Kaiser Family Foundation, and Kennedy School of Government (2003), ‘National Survey of Americans’ Views on Taxes’, Washington, D.C.: National Public Radio, Washington, DC, available online at [http://www.npr.org/news/specials/polls/taxes2003/20030415\\_taxes\\_survey.pdf](http://www.npr.org/news/specials/polls/taxes2003/20030415_taxes_survey.pdf).

<sup>44</sup> A recent exchange nicely illustrates the conflicting conclusions that the very best experts can draw about an optimal tax system and optimal tax reform, due to different goals, different weights, and different interpretations of the empirical evidence. N. Gregory Mankiw, Matthew C. Weinzierl, and Danny Yagan concluded that:

- The optimal marginal tax schedule could decline at high incomes.
- A flat tax, with a universal lump-sum transfer, could be close to optimal.
- Capital income ought to be untaxed.

In sharp contrast, Peter A. Diamond and Emmanuel Saez concluded, along these exact same dimensions, that:

- Very high earnings should be subject to rising marginal rates and higher rates than current U.S. policy for top earners.
- Tax and transfer policy toward low earners should include subsidization of earnings and should phase out the subsidization at a relatively high rate.
- Capital income should be taxed.

There are profound differences here between economists who are looking at the exact same evidence but who are drawing completely opposite conclusions. These conflicting conclusions are in large part because underlying assumptions and evidence about what is driving these theories and the resulting recommendations differ and also because underlying value judgments also differ. Even so, these conflicting conclusions certainly make it easier for elected politicians to ignore the policy recommendations of economists. See: N. Gregory Mankiw, Matthew C. Weinzierl, and Danny Yagan (2009), ‘Optimal Taxation in Theory and Practice’, *The Journal of Economic Perspectives*, 23 (4), 147-174; and Peter A. Diamond and Emmanuel Saez (2011), ‘The Case for a Progressive Tax: From Basic Research to Policy Recommendations’, *The Journal of Economic Perspectives*, 25 (4), 165-190.

Many times the proposal is quite elegant but much too complicated and far too impractical. As is sometimes said, mainly in derision, the proposal ‘works in theory but not in practice’.

The proposal may even work in practice in many settings, but it is unrealistic to believe a single policy will work in all settings, including the specific setting for which the tax policy is proposed. Indeed, it is certainly arguable that there is no such thing as ‘best practice’, and any ‘good’ tax policy must necessarily be tailored to a specific country, a specific time and history, a specific set of institutions, and a specific set of goals. Put differently, it is obvious that ‘one size does not fit all’, and economists often ignore this basic reality.<sup>45</sup>

Many times, the theoretical foundation for the proposal is based on assumptions whose validity is either at best relevant only to a single specific situation or at worst questionable, leading to implausible predictions.

The proposal may have no real existing empirical support because it is based entirely on theoretical propositions.

Similarly, the empirical evidence surrounding the proposal may be mixed and inconsistent.<sup>46</sup>

There are likely times in which the economist making the proposal has been hired by a special interest, so that the proposal does not have much credibility.

There may even be times when the economist making the proposal has no real interest in the actual enactment of the proposal. Rather, the economist has derived a specific policy

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<sup>45</sup> For a detailed discussion of these issues, see: James Alm (2017), ‘Is Economics Useful for Public Policy?’, *Southern Economic Journal*, 83 (4), 835-854.

<sup>46</sup> For the role of mixed and inconsistent evidence in the policy discussion, see again Chapter 4 in this volume: Yvette Lind, ‘Insiders, Outsiders, and Those in Between: Legal Opportunities and Boundaries Pertinent to Cross-border Mobility of Individuals’.

recommendation that solves a vexing theoretical or empirical puzzle, and it is the derivation of the result that is the sole purpose of the intellectual exercise.

There may also be times – indeed, many times these days – in which purely economic considerations are not the driving force in the policy debate. Instead, cultural considerations seem dominant in many political discussions in the current and highly partisan environment. As I discuss later, simply ‘defeating one’s opponents’ often seems the major motivation in much legislation, independent of the actual implications of a specific policy.

Finally, the ways in which we economists talk to policy makers may not be conducive to policy impact. Indeed, we often do not talk clearly and succinctly and unambiguously to policy makers. An example, possibly apocryphal, of this style is illustrated by a quote from then-President Lyndon Baines Johnson, who reportedly responded to an economics advisor who was giving a range of estimates about the impact of a policy by saying “Ranges are for cattle – give me a number”. The more reliably documented quote from Harry Truman (“Give me a one-handed economist”) also speaks to these tendencies. A more damaging tendency is that we economists often talk as if we are trying to impress rather than to inform others, so that we come across as self-righteous, smug, and condescending. Such an approach is hardly likely to lead to policy success.

All of these factors matter in making many recommendations of economists irrelevant in the policy domain. However, they are not, I believe, the decisive factor, as I discuss next.

### **WHAT REALLY DRIVES REAL-WORLD TAX POLICY CHOICES?**

The decisive factor, as I argued earlier, is the central role of politics – and the failure by economists to consider fully the central role of politics in policy making. Now it is certainly

accurate, as well as convenient, to argue that politics drives policy choices in democracies.

Indeed, all policy changes in democracies, including those that involve taxes, necessarily revolve around political considerations by elected politicians as policy makers. However, my argument goes well beyond this obvious truism. Instead, I emphasize one specific aspect of politics: Who gains and who loses from a tax policy change? These are the types of political considerations that are decisive because it is the distributional effects of policies that determine how people vote and so that also determine how their elected representatives vote.

These distributional effects clearly start with how a tax policy affects the income of individuals, an area in which economists have much to say, as identified by their standard fiscal incidence studies (even though these incidence studies typically lack the granular detail to be all that useful to politicians). Importantly, however, these distributional effects go well beyond a change in income to incorporate a change in broader aspects of individual welfare. I argue that it is these types of broadly defined ‘distributional effects’ where policies create winners and losers, it is these types of distributional effects that fundamentally drive political considerations, and it is these types of distributional effects about which economists have had little to say. As a result, economists typically do not contribute much that politicians consider relevant or useful about winners and losers. Indeed, I believe that our inability as economists to speak directly and meaningfully and unambiguously to politicians about all of these relevant ‘distributional issues’ has sidelined us from the policy making process.

Consider these ‘distributional effects’ in more detail, starting with narrowly defined financial issues and expanding to more broadly defined issues. I refer to financial issues as ‘economic well-being’ and the broader issues as ‘emotional well-being’.

I argue that the distributional effects most relevant to individuals clearly revolve around the ways in which a tax policy affects their personal income, or their ‘economic well-being’. Now economists often provide estimates of the incidence of tax policies that address these concerns at least in part. However, these estimates are obviously not available at the individual level but only at more aggregate levels (e.g., representative taxpayers, income deciles), and so their usefulness to voters and to politicians is limited.

Relatedly, the distributional effects most relevant for elected representative also focus upon the economic well-being of their constituents, but involving granular considerations like:

- How will ‘my’ locality be affected relative to another one?
- Will homeowners in ‘my’ jurisdiction be disadvantaged or benefited?
- How will ‘my’ elderly be affected?
- What will be the effects on urban and rural residents in ‘my’ jurisdiction?
- How will the businesses in ‘my’ jurisdiction be affected?

These types of questions are seldom considered by economists in any relevant detail. Instead, economists more typically examine – if they examine at all – the broader and more aggregate distributional effects of a policy.

It is also plausible that, even when we as economists do examine these narrowly defined distributional effects, we do not send a clear message. Our answers are highly dependent on the “models” that we use to examine these distributional effects, and we have an increasing ability to construct models that can generate quite different distributional results, depending on the specific assumptions that we make. If some politician asks whether his or her constituents may lose from a specific piece of legislation, it is certainly possible that some economist can devise some model that identifies and quantifies a loss. A politician can therefore shop around until an economist and

a model are found that justify what the politician wants to hear. The noise that is created by this bewildering and often conflicting array of models seems more likely to paralyze than to inform the policy making process. Indeed, when we as economists are able to identify a wide range of winners and losers from a tax policy change, it becomes harder for politicians to assemble the coalition necessary to pass the policy change.

Note that there is also some evidence that elected representatives may well be more concerned with the narrowly defined distributional effects that benefit mainly higher income individuals, despite the relatively small numbers of these economic elites. As demonstrated recently in separate papers by Martin Gillens and Benjamin I. Page<sup>47</sup> and by Alain Cohn, Lasse J. Jessen, Marko Klašnja, and Paul Smeets,<sup>48</sup> wealthy individuals (along with the special interests representing their businesses) have significant impacts on tax and other government policies, so that these policies often reflect the economic well-being of these affluent individuals and their businesses, generally to the detriment of those who are much less well off.

Importantly, however, I also argue that there are more broadly defined aspects of distributional effects – the “emotional well-being” of individuals – about which economists have nearly always been silent, at least until recently, and the link between voting driven by economic well-being and voting on emotional well-being is often quite tenuous. These emotional well-being aspects of individual welfare include such considerations as:

- Does the enactment of a policy stigmatize some individuals, while commending other types of individuals?

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<sup>47</sup> Martin Gillens and Benjamin I. Page (2014), ‘Testing Theories of American Politics: Elites, Interest Groups, and Average Citizens’, *Perspectives on Politics*, 12 (3), 564-581.

<sup>48</sup> Alain Cohn, Lasse J. Jessen, Marko Klašnja, and Paul Smeets (2023), ‘Wealthy Americans and Redistribution: The Role of Fairness Preferences’, *Journal of Public Economics*, 224, Article 104977.

- Does the policy reflect a political class that treats some individuals with disdain, while praising other individuals?
- Does the policy impose emotional costs on individuals, but only on individuals of some types?
- Does the policy suggest a rejection of the culture of certain classes of individuals, but an embrace of the culture of other classes of individuals?
- Is the policy inconsistent with the ideology of some types of individuals, while endorsing the ideology of other types?
- Does the policy generate anger and resentment from some individuals, but not from others?

Indeed, the roles of anger, humiliation (or shame), and resentment, clearly affect the welfare of individuals, even if these effects do not affect directly or even indirectly the income of these same individuals. It is only in recent years that the political impact of these factors has received much attention from economists. Individuals vote for politicians whom they feel listen to them with respect; individuals do not vote for politicians whom they feel look down upon them.<sup>49</sup>

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<sup>49</sup> Among economists, see especially: George Loewenstein (2000), 'Emotions in Economic Theory and Economic Behavior', *The American Economic Review*, 90 (2), 426-432; Giampaolo Bonomi, Nicola Gennaioli, and Guido Tabellini (2021), 'Identity, Beliefs, and Political Conflict', *The Quarterly Journal of Economics*, 136 (4), 2371-2411; Stefanie Stantcheva (2021), 'Understanding Tax Policy: How Do People Reason?', *The Quarterly Journal of Economics*, 136 (4), 2309-2369; Sergei Guriev and Elias Papaioannou (2022), 'The Political Economy of Populism', *The Journal of Economic Literature*, 60 (3), 753-832; Gloria Gennaro and Elliott Ash (2022), 'Emotion and Reason in Political Language', *The Economic Journal*, 132 (643), 1037-1059; and Yann Algan, Eva Davoine, Thomas Renault, and Stefanie Stantcheva (2025), 'Emotions and Policy Views', Department of Economics Working Paper, Cambridge, MA: Harvard University.. These types of considerations have long been recognized by political scientists (e.g., George E. Marcus (2002), *Sentimental Citizen: Emotion in Democratic Politics*, University Park, PA: The Pennsylvania State University Press), psychologists (e.g., Joseph P. Forgas, William D. Crano, and Klaus Fiedler (eds.) (2021), *The Psychology of Populism – The Tribal Challenge to Liberal Democracy*, New York, NY: Routledge Publishing), and sociologists (e.g., Frédéric Gonthier (2023), 'It's the Moral Economy, Stupid! Anger Toward Economic Inequality and Populist Voting', *International Journal of Sociology*, 53 (5), 351-372), among other social scientists. See also: Katherine J. Cramer (2016), *The Politics of Resentment: Rural Consciousness in Wisconsin and the Rise of Scott Walker*, Chicago, IL: The University of Chicago Press; Francis Fukuyama (2018), *Identity: The Demand for Dignity and the Politics of Resentment*, New York, NY: Farrar, Straus, and Giroux

These types of more broadly defined distributional effects that involve emotional well-being also create winners and losers, they often drive political considerations, and they are the types of distributional effects about which economists have had little to say until recently. Indeed, it seems increasingly the case the individuals often vote in favor of politicians who advocate policies that have a negative impact on their economic well-being because these same politicians pursue policies that have a positive effect on their emotional well-being. This seemingly contradictory behavior was explored in detail by Thomas Frank in his 2004 book, *What's the Matter with Kansas? How Conservatives Won the Heart of America*.<sup>50</sup> It is also evident in many other instances of voter behavior, like higher income individuals voting in favor of politicians who propose progressive taxes, Blacks voting against politicians who advocate affirmative action policies, working class individuals voting in favor of politicians who call for tax cuts that heavily favor the wealthy or regulations that weaken labor unions, low income individuals voting for politicians who propose cuts in health or food subsidies targeted to the poor, and the like. There are of course other possible reasons for such seemingly irrational voting behavior, like lack of information, partisanship, or religion. Even so, the role of emotional well-being seems likely to play an important role.

Overall, I believe that there is a general failure of economists to say much that politicians consider relevant or useful about winners and losers, whether these winners or losers are determined by the effects of tax policies on either the economic or the emotional well-being of individuals. It is, I believe, this failure that largely relegates economists to the sidelines in many tax policy discussions.

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Fukuyama (2018); and Michael J. Sandel (2020), *The Tyranny of Merit: What's Become of the Common Good?*, New York, NY: Farrar, Straus, and Giroux.

<sup>50</sup> Thomas Frank (2004), *What's the Matter with Kansas? How Conservatives Won the Heart of America*, New York, NY: Henry Holt and Company.

More generally, then, I believe that policy – and tax policy in particular – is not just about economics but about politics, and these political considerations involve mainly distributional issues, whether of economic or emotional well-being. So for tax research by economists to have a real policy impact, economists must consider both economics and politics, including these narrowly and broadly defined distributional issues (along with other issues like the process and the marketing of policy making). And this conclusion applies beyond economics to law, accounting, and indeed most other disciplines.<sup>51</sup>

Now this is not to say that economists should become political scientists. It is to say that economists need to be able to speak to the political considerations that are important both to citizens and to their elected representatives, to speak clearly and succinctly, and unambiguously about policy issues, and to speak in ways that reflect appropriate respect for those to whom we are speaking. In all of these conversations, it is especially that we speak to political considerations that involve distributional issues, both narrowly and broadly defined. We have seldom done so, with the result that our advice is typically ignored.

## **CASE STUDIES OF SUCCESSFUL AND UNSUCCESSFUL TAX REFORMS**

There are of course examples of suggested tax policy reforms that have been successfully implemented. Perhaps the most prominent example of a successful tax policy reform is the Tax

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<sup>51</sup> Note that are additional political considerations beyond distributional issues that work against ‘good’ tax proposals. For example, there is an incentive for politicians to avoid policies that impose observable costs now, with benefits hidden and in the future (e.g., reducing tax expenditures, raising taxes now to reduce deficits in the future), even when the benefits far exceed the costs. There is also an incentive to pursue policies that give observable benefits now, with costs hidden and in the future (e.g., expanding tax expenditures, increasing deficits), even when the costs far exceed the benefits. There is also the loss of a ‘felt need’ among some in the political class to talk to people on the other side. Instead, the felt need now seems to be to talk only to the partisans on one’s own side, in part to avoid provoking a primary challenge from the political fringes. There is little doubt that ideology, and ideology independent of sound economic analysis, is often the driving force in political calculations.

Reform Act (TRA) of 1986, which was a major U.S. tax reform that broadened income tax bases and lowered individual and corporate tax rates along the lines of BBLR reforms.

Now why did the TRA pass? My view is that there was a ‘perfect storm’ surrounding it:

- There was a consensus among most taxpayers – and most economists – that the tax system needed fixing.
- There was also a consensus on how to fix the system – cutting rates, expanding the base, and keeping an income base – so there were obvious and easy ‘selling points’ (e.g., reduce tax shelters, increase the corporate tax burden, lower individual marginal tax rates), and there was also even some ambiguity/uncertainty about who would actually pay for the reform.
- There was a political leader (then-President Ronald Reagan) who was popular, who was able to generate political support for reform, and who had a long track record of bipartisan legislation.

There were similar ‘perfect storms’ surrounding tax reforms in Colombia in 1970 and 2000, as well as tax reform in Jamaica in 1985.

As for example of a tax policy recommendation that was ignored, consider the recent discussion in the U.S. surrounding the state and local tax (SALT) deduction in the One Big Beautiful Bill Act (OBBBA) of 2025. Most economists see tax expenditures as inefficient, costly, and inequitable. However, efforts to reduce tax expenditures have largely gone nowhere in the U.S., even in the face of huge fiscal deficits and enormous public debt. One exception was the Tax Cuts and Jobs Act (TCJA) of 2017, which imposed a cap on how much an individual could deduct in state and local taxes and limited the SALT deduction to USD 10,000 for both single taxpayers and those filing jointly starting in tax year 2018, with the cap expiring at the end of

2025. Eliminating the SALT deduction is one obvious way of simplifying the tax code, improving its progressivity, raising revenues, and lowering tax rates (consistent with BBLR reforms). However, Democrats in high-tax states are in favor of raising, even eliminating, the cap because their residents benefit from the SALT, despite the fact that Democrats are otherwise against ‘a tax cut for the wealthy’. Similarly, Republican legislators in high-tax states also want to raise or eliminate the cap because many of their constituents benefit from the SALT, despite the fact that Republican legislators otherwise want to reduce deficits and debt. So my view is that there is no similar ‘perfect storm’ surrounding the elimination of tax expenditures generally and the SALT deduction specifically:

- There is no real consensus that the tax expenditure system is ‘broken’.
- There is no real consensus on how to ‘fix’ tax expenditures.
- There is no political leader who is pushing for reduced tax expenditures.

Indeed, the OBBBA raised the SALT cap to USD 40,000 for taxpayers making less than USD 500,000, with the cap reverting to USD 10,000 after five years.

These two examples suggest several conditions for successful tax design/reform. The tax system (or a specific feature of the tax system) must be widely seen as ‘broken’. There must be a consensus on how to fix it. There must be a strong ‘champion’ who can generate political support for the change. These conditions were clearly met in the TRA. They were not met in the OBBBA.

## **WHAT CAN ECONOMICS CONTRIBUTE TO THE POLICY DISCUSSION?**

There are, I believe, three main areas in which economists have a comparative advantage over other disciplines and can make a useful contribution to tax policy discussions.

The crucial element for determining how policies will actually ‘work’ is in most all cases identifying the incentives. Economics can identify the central role of incentives in affecting things like how the outcomes of the existing tax system are determined and how any tax policy change might work.

However, simply identifying the economic incentives is not the end of the story. Another area in which economists have a comparative advantage is identifying the tradeoffs. The decision to pursue more of one goal in taxation almost always involves the simultaneous decision to do less of another worthwhile goal. Economics can usefully identify these tradeoffs. Economics can also quantify these tradeoffs; that is, how much does, say, encouraging more investment in electric vehicles via tax incentives cost in tax revenues that could have been invested in other areas (including distribution of the subsidies directly to individuals).

A final area in which economists can make a useful contribution is identifying the winners and the losers – and doing so in a convincing way that is direct, meaningful, and unambiguous. To repeat, the crucial element for determining whether policies will actually get implemented involves politics, and it is who gains and who loses from a tax policy choice that drives these political considerations – where once again these gains and losses consider the effects of the policy on both economic and emotional well-being of individuals.

Still, many other disciplines beyond economics – accounting, law, sociology, psychology, anthropology, public administration, and beyond – clearly matter and matter a lot in determining both the effects of tax policies and the likelihood of their implementation. Tax researchers need to understand the incentives, constraints, objectives, and institutions facing policymakers before offering them pre-cut solutions, and it is especially in understanding the constraints and objectives and institutions that politics and these other disciplines can contribute, in areas like:

- Legality and legitimacy in tax law-making
- Limits on tax
- The history of property taxation, with a focus on populist tax policy
- The evolution of inheritance taxes
- Cold war politics and international taxation
- Legal opportunities and boundaries facing mobile individuals
- The role of tax expenditures
- Property ideals.

The relevance of these specific issues should be clear. These are the subjects of the other chapters in this volume, as I have mentioned throughout. I am confident that, in combination with economics, the political economy considerations that are examined in these papers will help expand our ability to understand what drives tax policy choices and what is needed to make good tax policy recommendations.

Where does all of this leave tax researchers – from any and all disciplines – who wish to influence tax policy? There are at least some times when tax research has clearly affected tax policy. There are many other times when policy makers have chosen not to act on the basis of academic recommendations. There are no doubt still other times when tax research has had important effects that may not be visible – we do not see the many bad ideas and bad proposals that have been quashed in their early stages. As our understanding keeps improving, the level of discourse and the potential impact of this discourse also improve. This is an exciting enterprise that never gets old and never stops being important.<sup>52</sup>

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<sup>52</sup> For different perspectives on the role of economists in policy advice, see: Dani Rodrik (1996), ‘Understanding Economic Policy Reform’, *The Journal of Economic Literature*, 34 (1), 9-41; James Alm (2017), ‘Is Economics Useful for Public Policy?’, *Southern Economic Journal*, 83 (4), 835-854; and Karen Dynan (2025), ‘Reclaiming a Policy Role for Economists’, *Finance & Development* (International Monetary Fund), 62 (2), 12-13.