

Projekt nummer: 6

Projekt titel: Taxation and Labor Supply in OECD Countries: Hours of Work versus Labor Force Participation

Projekt deltager: Henrik Jacobsen Kleven and Claus Thustrup Kreiner.

Bevillingstidspunkt: Efterår 2002.

The aim of this research project is to improve the formulation of labor supply decisions in the theory of taxation, and to explore empirically the consequences for the optimal level and composition of income taxation. Results published in the *Economic Journal* (2007) show that for most EU (pre-enlargement) countries, because of large existing welfare programs with high phase-out rates, increasing traditional welfare is undesirable unless the redistributive tastes of the government are extreme. In contrast, in-work benefit reforms are desirable in a very wide set of cases. Some of the results from the research project were included in the report "Fremtidens velfærd – sådan gør andre lande" from the Danish Welfare Commission (March 2005).

Results published in the *Journal of Public Economics* (2006) show theoretically and numerically for EU countries that it is important to account for labor market participation responses when measuring the marginal cost of raising public funds (MCF). Estimates based entirely on intensive margin responses may substantially underestimate the size of MCF.

In an article in the *Journal of Public Economics* (2008), we propose a microsimulation method, combining intensive and extensive margin responses, to evaluate the welfare effects of tax reforms. Using this method, we examine the welfare effects on single mothers in the United States following four tax acts passed in 1986, 1990, 1993, and 2001. We find that the four tax acts created substantial welfare gains, and that the standard approaches not modeling the participation decision can make large errors.

The different results of this research program have been surveyed in an article in *Nationaløkonomisk Tidsskrift* and have been described by journalists for a broader international audience in the *NBER Digest* (2005) and in *Media Briefing of the Royal Economic Society* (2007).