Three Essays in Taxation

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Chapter 1: “Does the Earned Income Tax Credit Reduce Saving by Low-Income Households?”

This paper analyzes the effect of the Earned Income Tax Credit (EITC) on non-labor income, particularly investment income. Policy-makers have devoted substantial time and resources toward increasing the saving rate of low-income households with programs like the Saver’s Credit and Individual Development Accounts. Yet the EITC—the largest federal cash transfer program in the U.S.—provides a substantial disincentive for individuals to save and realize investment income because EITC benefits decline as investment income rises over certain income ranges. I find a significant response of investment income to these disincentives both when I semi-parametrically estimate the change in investment income in the region in which non-labor income begins being taxed, and also when I estimate the parameter parametrically using differences in tax rate changes between taxpayers with differing numbers of dependents for identification. A one percent increase in the after-tax return to saving causes a 3.05 percent increase in investment income. Nearly 40 percent of the decline over the last two decades in the fraction of EITC recipients with savings in income-bearing accounts can be explained by changing EITC incentives.

Chapter 2: “Identifying the Causal Effect of a Tax Rate Change When There Are Multiple Tax Brackets”

Empirical researchers frequently confront situations in which tax reforms affect taxpayers differentially based on their individual characteristics and tax situations. This paper analyzes the conditions under which it is possible to obtain a causal average treatment effect using pre-reform characteristics as instruments, which I term the Fixed-Bracket Average Treatment Effect (FBATE). Previous literature has assumed that only one of these conditions is sufficient to identify a causal parameter. 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. FBATE is the relevant parameter for welfare analysis if taxpayers whose response is identified by the FBATE estimate will have the same long-run response as the rest of the population, which is often a reasonable assumption. FBATE also highlights new tradeoffs between different sources of identification; for example, an oft-touted source of identification—bracket creep—cannot yield a causal estimate. 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.

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Chapter 3: “The Lock-In Effect of Housing Transfer Taxes: Evidence from a Notched Change in D.C. Policy” (with Joel Slemrod and Hui Shan)

This paper estimates the lock-in effect in Washington D.C. of residential real estate transfer taxes using a notched tax rate change that only applies above a certain threshold in the tax base (the tax base is the sales price and it determines the amount of tax owed) as identifying variation. A tax notch, unlike a tax kink, imposes a discrete change in tax liability. While states often impose transfer taxes, they have received little attention in the literature. We provide evidence that there is substantial manipulation of the sales price in the region around the notch. We estimate the amount of manipulation as well as how manipulation changes depending on the location of house value relative to the tax notch. Ignoring this manipulation would lead us to substantially overstate the lock-in effect. We address this manipulation using a new estimation approach, which avoids the difficulties of commonly used resolutions to this problem, such as instrumental variables.