A reform-oriented approach to political parties' revealed social preferences

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January 9, 2024

This paper in a nutshell

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estimate MVPFs for German parties' tax-transfer proposals

- examine more than 300 party election proposals related to the tax-transfer system

- use microsimulation (ifo-MSM) to compute their hypothetical impacts

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- examine more than 300 party election proposals related to the tax-transfer system

- use microsimulation (ifo-MSM) to compute their hypothetical impacts

estimate German parties' social welfare preferences

- use inverted MVPF to recover implied welfare weight for reform beneficiaries

- aggregate welfare weights of single proposals for each party in each election year

Roadmap of Talk

MVPF and parties' social welfare weights - method

MVPF and parties' social welfare weights - results

Conclusion and next steps

Microsimulation for Reform Proposal Evaluation

Problem: large majority of reform proposals never implemented, let alone evaluated

Solution: ifo Microsimulation Model to generate a counterfactual post-reform state

- based on microdata from the German Socio-economic Panel (SOEP)

- ifo MSM's comprehensive representation of the German tax and transfer system
  $\rightarrow$ obtain accurate measures of individuals' taxes, transfers and disposable income

MVPF and welfare weights

MVPF for tax reform j (Hendren and Sprung-Keyser 2020): ▸ how to get y^1

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mean mechanical change in disposable income due to reform

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change in mean tax revenue inclusive of behavioral responses

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welfare weight for tax reform j: ▸ details

$$\bar{\eta}_j = \frac{1}{MVPF_j} = \frac{E[T^0(y_i^0)] - E[T^1(y_i^1)]}{E[T^0(y_i^0) - T^1(y_i^0)]}$$

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$\Rightarrow \bar{\eta}_j$ the same for all reform beneficiaries

Roadmap of Talk

Reform MVPFs

Example: Greens 2013 ▸ Left ▸ SPD ▸ CDU ▸ FDP
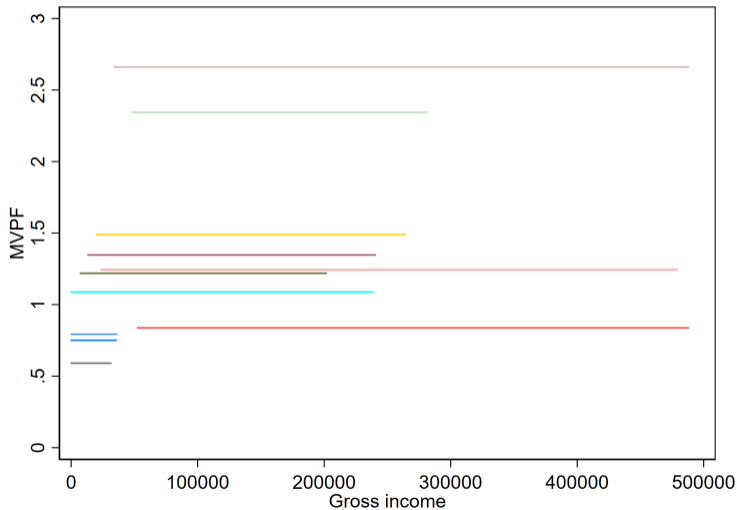
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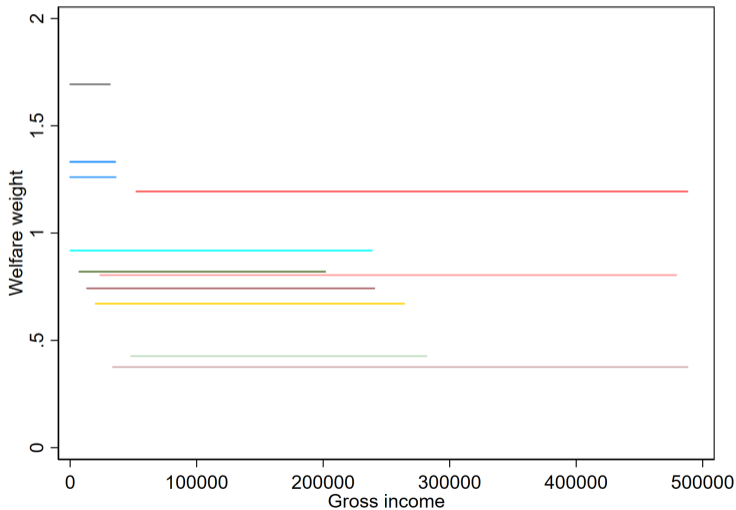
Aggregated welfare weights

Example: 2013 (dpi-weighted smoothed average) ▸ smoothed ▸ simple ▸ all years
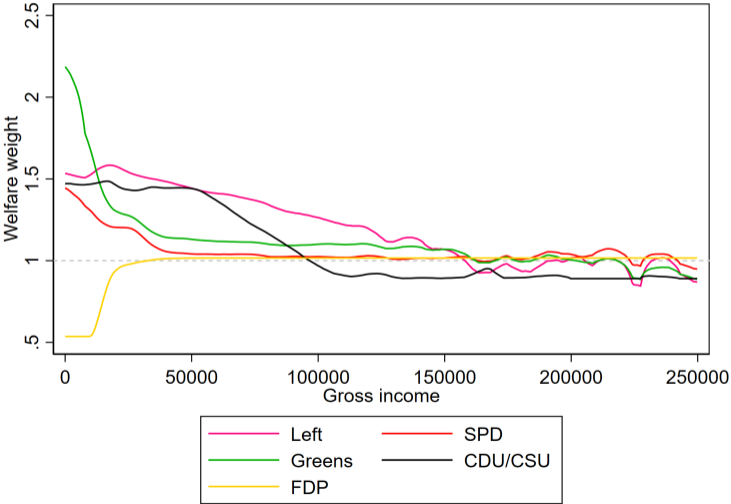
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Conclusion & Outlook

Takeaways:

1. microsimulation can help us compute MVPFs of hypothetical reforms

2. MVPF framework can be used to recover parties' social preferences

Outlook:

- compare to inverse-optimum tax approach [Jacobs et al. 2017]
- take statements favoring the status quo into account
- simulate a '*marginal reform on top*'
- what if parties disagree on elasticities?
- *extension to political economy*: are parties' election proposals informative for policies enacted by a coalition government? ▸ Hypotheses

Thank you!

Comments and suggestions very welcome!

Post-reform income and revenue effects

$$y_i^1 = (1 - \frac{\tau_i^1 - \tau_i^0}{1 - \tau_i^0} \varepsilon_i) y_i^0$$

$$\Delta T_i = (1 - \pi_i \frac{t_i^1 - t_i^0}{1 - t_i^0}) t_i^1 y_i^1 - t_i^0 y_i^0$$

Assumptions: π = 0.2 ; ε = 0.25

▸ MVPF

MVPF and welfare weights

social welfare impact of policy j:

$$\frac{dW}{d\tau_j} = \bar{\eta}_j \sum_i WTP_i^j + \frac{dR}{d\tau_j}$$

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$\Rightarrow \bar{\eta}_j$ the same for all reform beneficiaries
$\Rightarrow$ identify $\bar{\eta}_j$ for all reform proposals of party p
$\Rightarrow$ construct social welfare function by combining $\bar{\eta}_j$'s along the income distribution

▸ MVPF

Reform MVPFs

Example: Left 2013 ▸ Greens
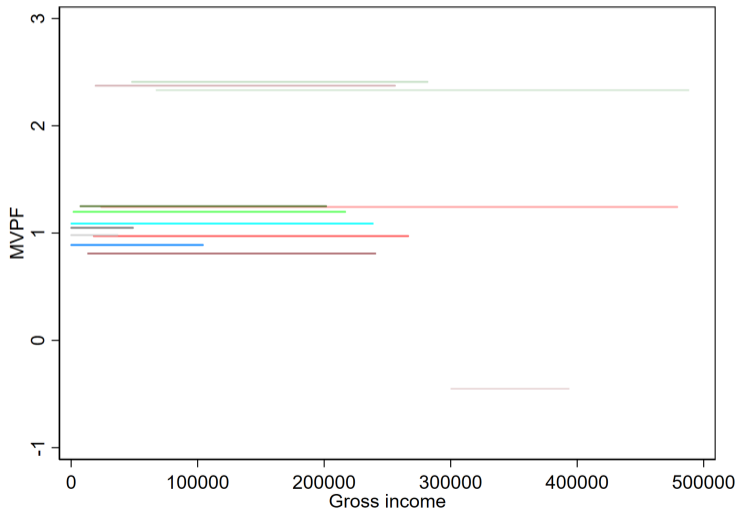
Reform MVPFs

Example: Social Democrats 2013 ▸ Greens
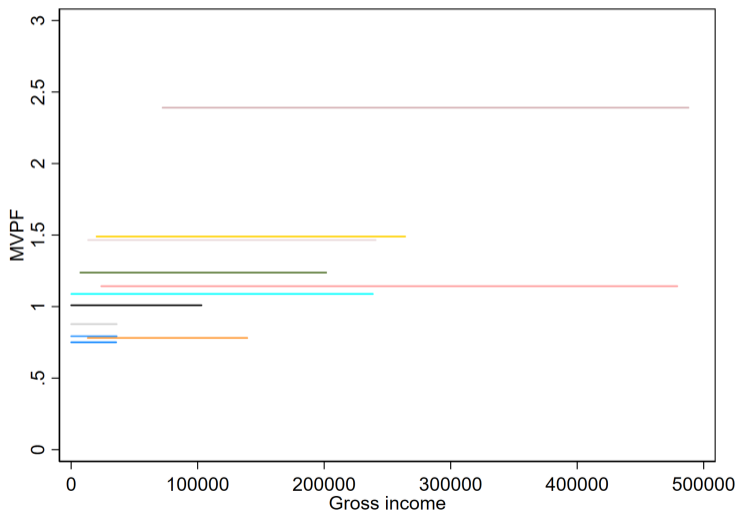
Reform MVPFs

Example: Christian Democrats 2013 ▸ Greens
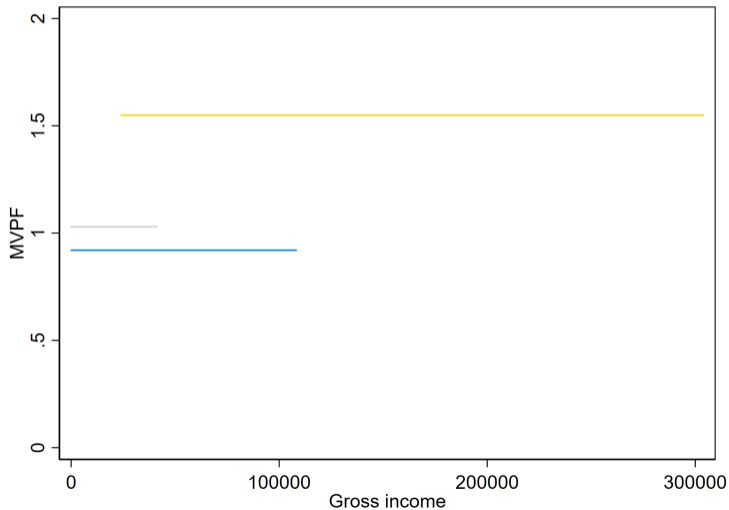
Reform MVPFs

Example: Liberals 2013 ▸ Greens
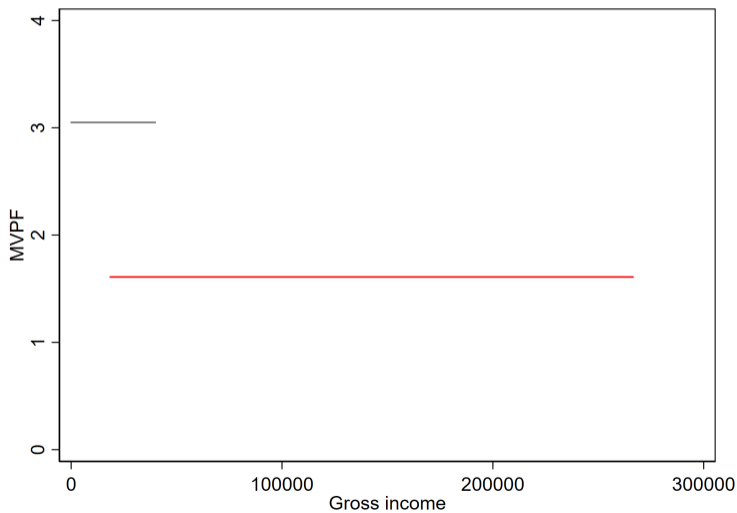
Reform welfare weights
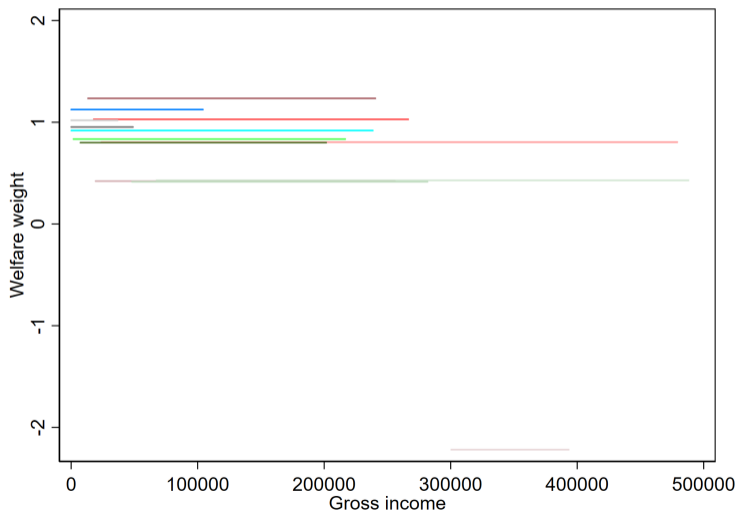
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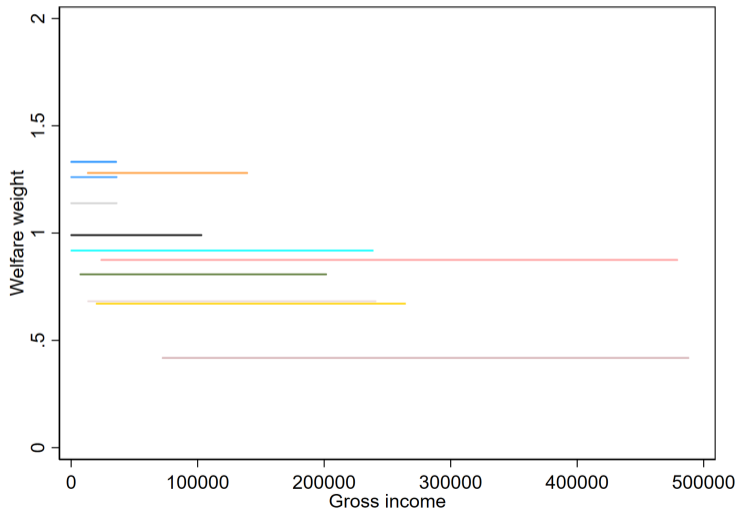
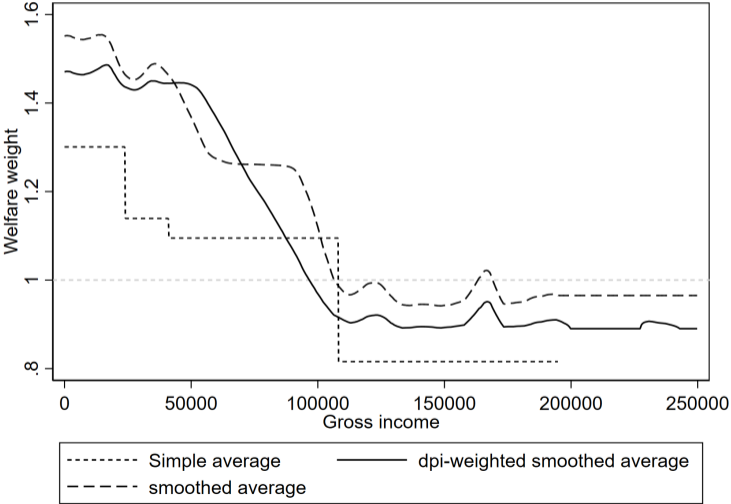# Reform welfare weights

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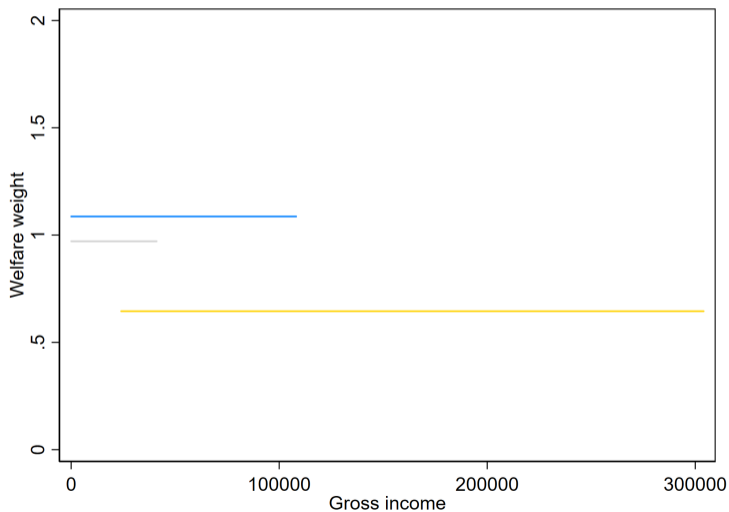
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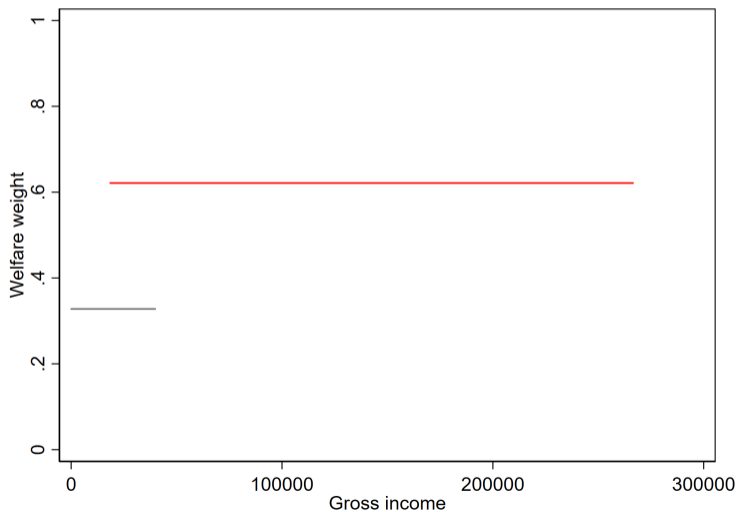
Aggregated welfare weights

Example: 2013 (smoothed average) ▸ dpi-weigthed smoothed
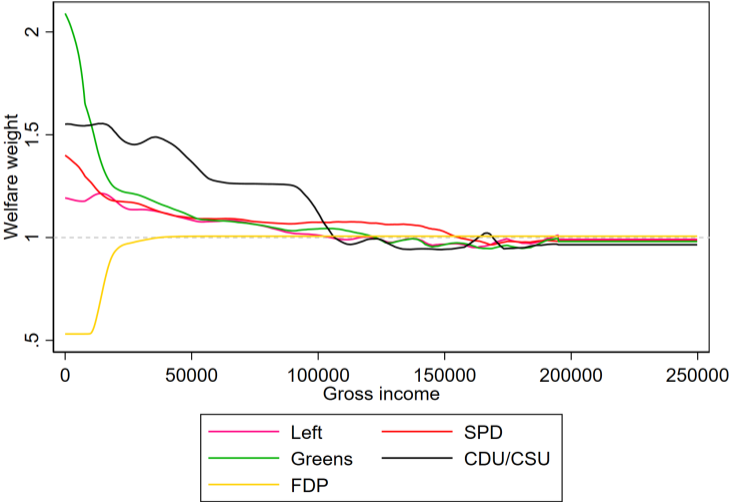
Aggregated welfare weights

Example: 2013 (simple average) ▸ dpi-weigthed smoothed
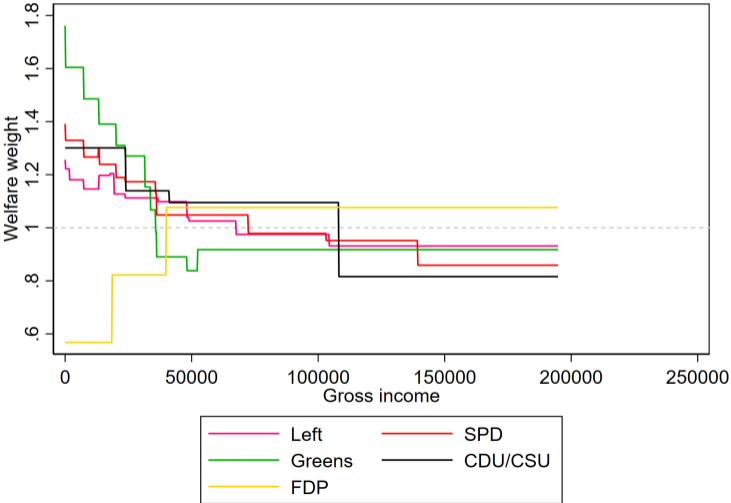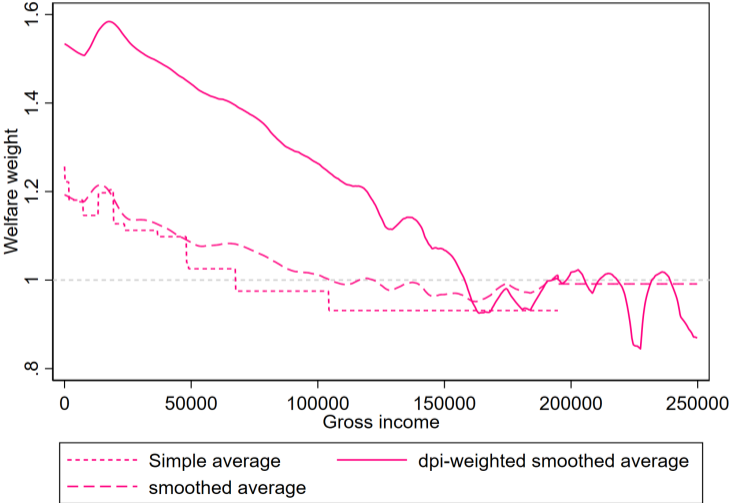
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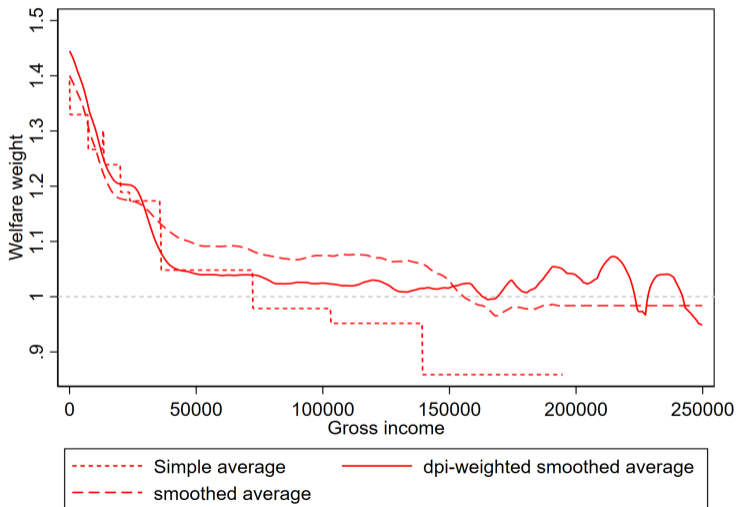
Example: Social Democrats 2013 ▸ Greens

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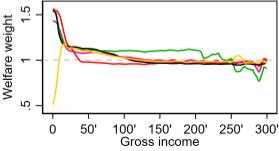
Example: Christian Democrats 2013 ‣ Greens

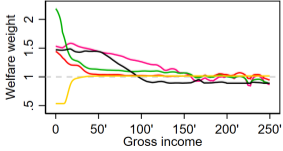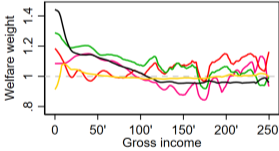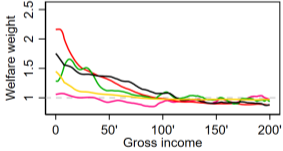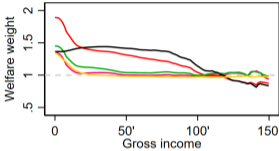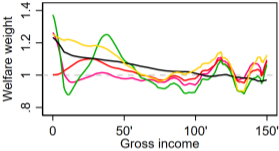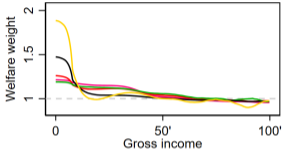# Aggregated welfare weights

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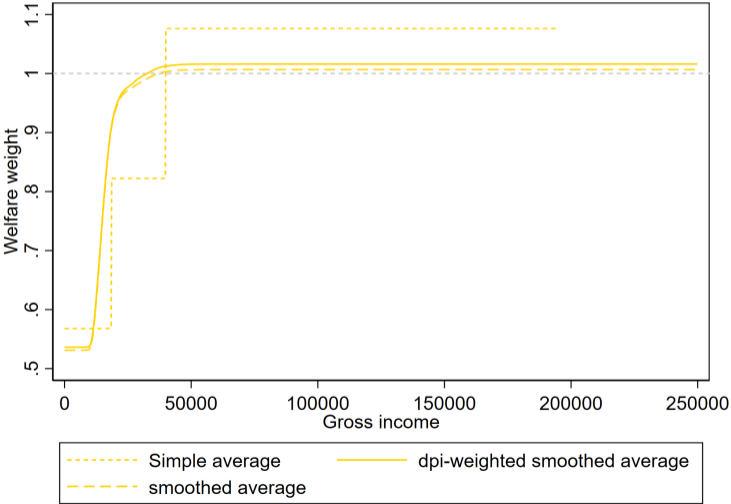
Aggregated welfare weights

1990-2021 (dpi-weighted smoothed average) ▸ 2013
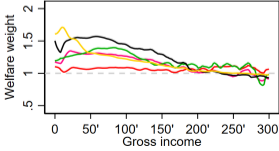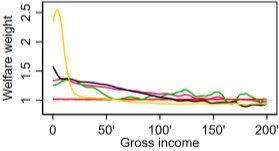
Hypotheses

1. The coalition government does not enact anything that is explicitly ruled out by one coalition partner. ▸ exclusion restrictions

2. Only such reforms, which are welfare-enhancing according to all coalition partners' revealed preferences, are enacted.

3. Only such reforms, which are welfare-enhancing for one of the coalition partners and not ruled out by any other coalition partner, are enacted.

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$\rightarrow$ results coming soon - WIP ▸ Conclusion

Hypothesis 1

The coalition government does not enact anything that is explicitly ruled out by one coalition partner.

Ex.1 CDU/CSU 2013: 'maintain income splitting and add family splitting'
     SPD 2013: 'we reject family splitting as it favors top incomes'

Ex.2 SPD 2021: '[...] we want to reinstall the wealth tax.'
     FDP 2021: '[...] we reject the reinstallment of the wealth tax.'

⇒ none of these proposals has been implemented

▸ Hypotheses