

Scientific Project: Optimal Nonlinear Income Taxes with Compensation

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Dworkin (1981) argues that there is a cut between the characteristics of a person's environment, genetic and social, for which a person should not be held responsible for, and those for which she should be. This distinction and Dworkin's responsibility-sensitive arguments have been largely discussed in the egalitarian literature in philosophy but has also been exploited in economics. For instance, based on this cut between characteristics people are responsible and those for which they are not, Roemer (1993, 1998), Fleurbaey (2008), and Fleurbaey and Maniquet (2009) propose distinct normative approaches to the compensation responsibility dyad.

This project investigates how the optimal income tax schedule should be designed when taking into consideration the compensation-responsibility couple. Building up on our survey of the previous approaches on this issue, we hope to offer a new interesting avenue. Fleurbaey and Maniquet (2005, 2006, 2007) use an ordinal approach and build up social ordering functions which do not require any utility comparison nor any cardinal measurement of utility. However, their approach implies that the entire optimal tax schedule cannot be characterized; results are limited to properties that the optimal tax schedule must satisfy at the bottom of the income distribution. In this paper, we aim developing an approach to fully characterize tax policies when compensation and responsibility matter. Therefore, we assume that individual utility levels are comparable and a very general social welfare function. This allows us to derive the optimal tax formula valid along the entire income distribution and the subjacent economic intuitions.

These assumptions are also used in Roemer (1993, 1998). Roemer's approach requires that individual welfare be equalized across skills for those people who have the same preferences for leisure and so belong to the same preference group. At the same time, there would be no redistribution between preference groups. However, the policy instruments that are available do not generally allow the government to achieve such an equality, and even if they are available the redistributive policy that would achieve it would generally depend upon the preference group. This calls for some compromise and Roemer (1998) proposes that the redistributive policy should be chosen so as to maximize the weighted sum of utilities of the worst-off individuals within each preference group, the weights being the shares in the population of the preference groups. After Fleurbaey (2008), this objective function is called the mean of mins and the way of aggregating across preference groups is called utilitarian reward. Implicitly, the latter provides an ethical criterion of what comprise the proper rewards to effort. This paper builds up on Roemer's approach regarding the compensation principle since it assumes a weighted sum of utilities of the worst-off individuals within each preference group. However, differing from Roemer's approach, we will allow the government to have varying attitudes towards persons of different preferences by possibly attaching distinct weights on individuals with distinct

preferences for leisure. We study how the tax schedule is modified with these weights and we also relate the weights we use to those (implicitly) used in Fleurbaey and Maniquet's works.

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