

The Efficiency-Equity Tradeoff of the Corporate Income Tax: Evidence from the Tax Cuts and Jobs Act

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 - Microdata not previously available to researchers
 - Challenging to find credible counterfactuals

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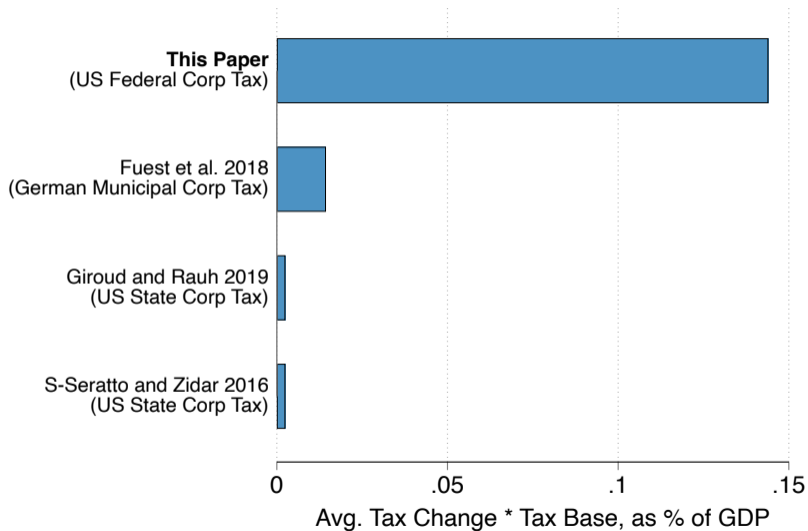
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3. Stylized Model

- Use reduced form elasticities to quantify efficiency gains, incidence

Large Shock Relative to Recent Studies



Empirical Design: C vs. S Corps

DiD comparing two legal entity types:

	C Corps	S Corps
Legal Differences		
Taxes	Pay corp, dividend taxes on profits	Owners pay personal taxes on profits
Shareholders	No restrictions	≤ 100 owners; must be individual US citizens
TCJA Changes		
Top Rate Cut	35% \rightarrow 21%	39.6% \rightarrow 37%; 20% QBI deduction

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IRS Microdata

Sample: Employer-employee linked federal tax records, 2013-2019

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Business Tax Returns (SOI 1120, 1120s)

- Sales, profits, investment, taxes, firm characteristics
- Restrict to med/large firms, balance panel, drop C↔S switchers

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Measurement

- S corp MTR constructed as weighted average of shareholder MTR's
- Scale outcomes by 2016 sales to account for potentially non-positive values

Empirical Strategy

Estimate:

$$y_{ft} = \sum_{t \neq 2016} \beta_t C_f * \mathbf{1}(\text{year} = t) + \gamma_f + \alpha_{is(f),t} + \epsilon_{ft}$$

- y_{ft} is an outcome for firm f in year t
 - $y \in \{\text{MTR, taxes, profits, payouts, investment, employment, workers' earnings}\}$
- C_f is an indicator = 1 if firm f is a C corp
- γ_f is a firm fixed effect
- $\alpha_{is(f),t}$ is an industry \times size-bin \times year fixed effect
- Cluster standard errors by firm

Identification and Interpretation

$$y_{ft} = \sum_{t \neq 2016} \beta_t C_f * \mathbf{1}(\text{year} = t) + \gamma_f + \alpha_{is(f),t} + \epsilon_{ft}$$

Identification

- Key assumption is parallel trends in counterfactual with no MTR shocks

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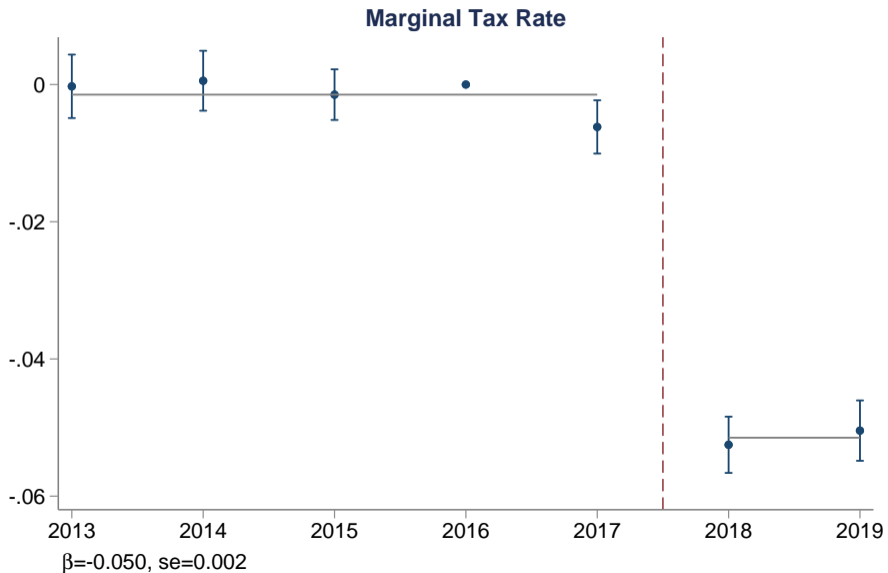
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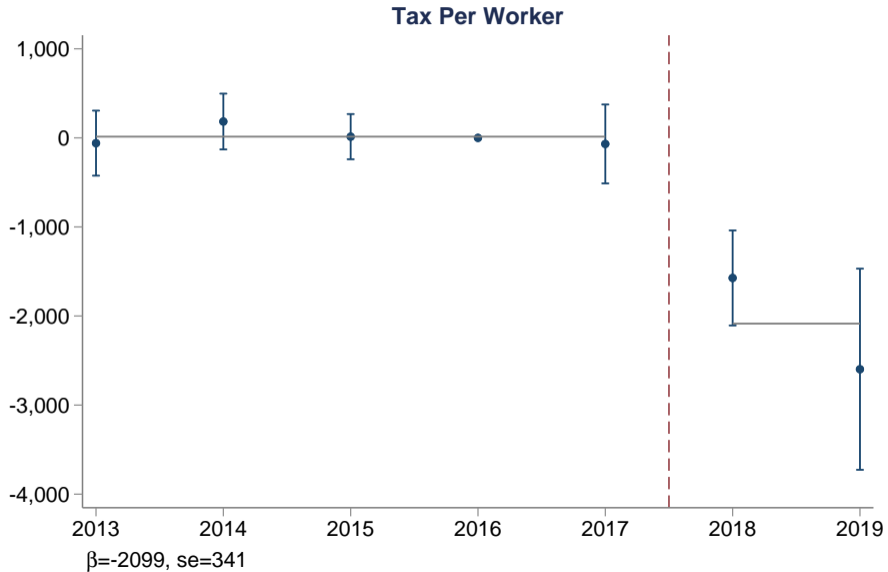
Defending parallel trends:

- TCJA was unexpected prior to 2016 elections
- Compare outcomes in narrow industry-size-year bins
- Yagan (2015) finds C and S firms historically trended similarly
- Examine pre-trends to assess plausibility

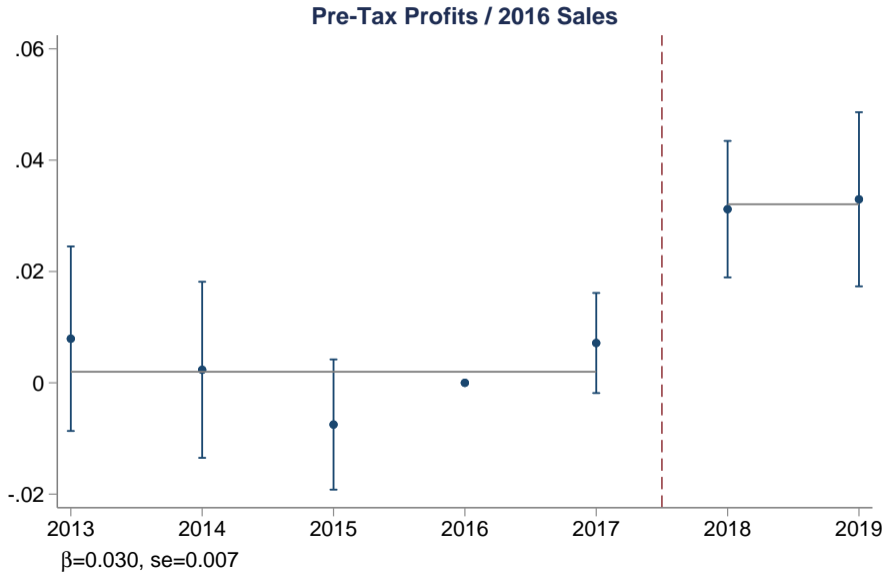
Marginal Tax Rate Wedge τ_f



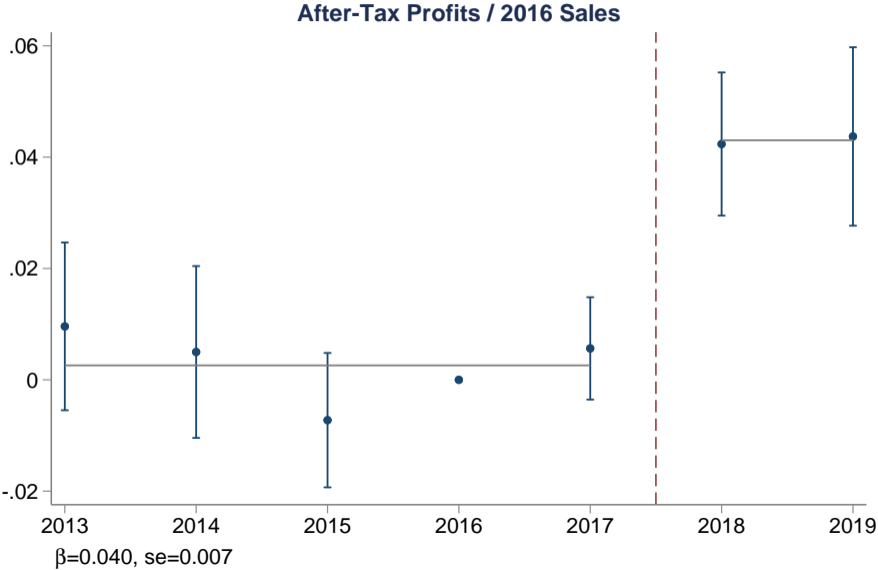
Tax Per Worker



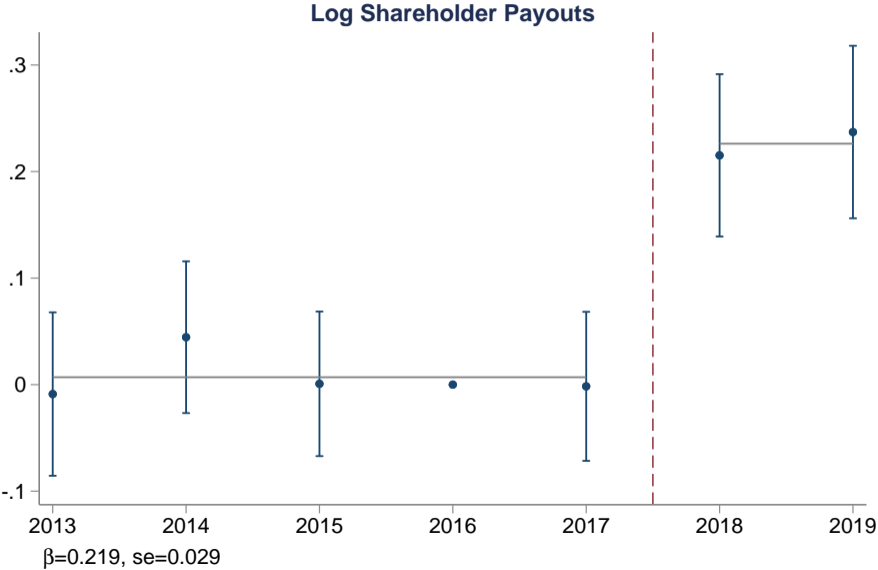
Pre-Tax Profit



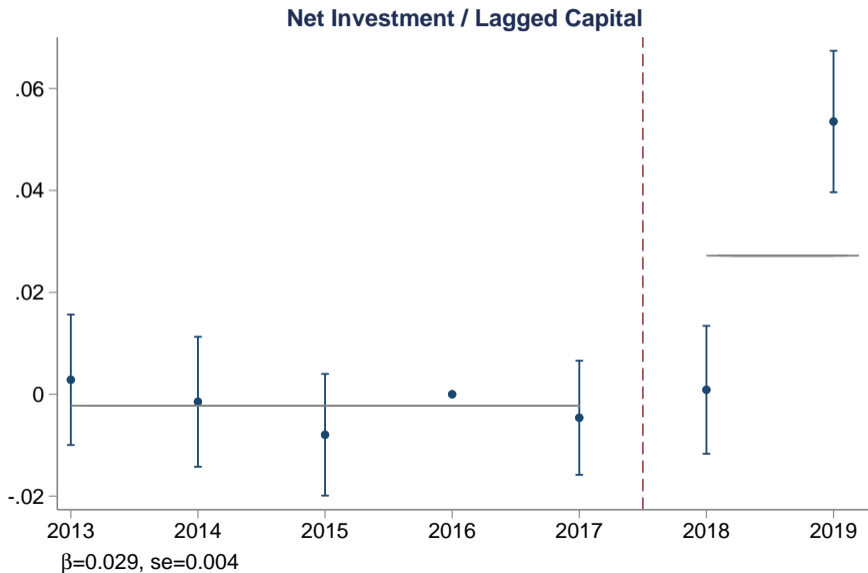
After-Tax Profits



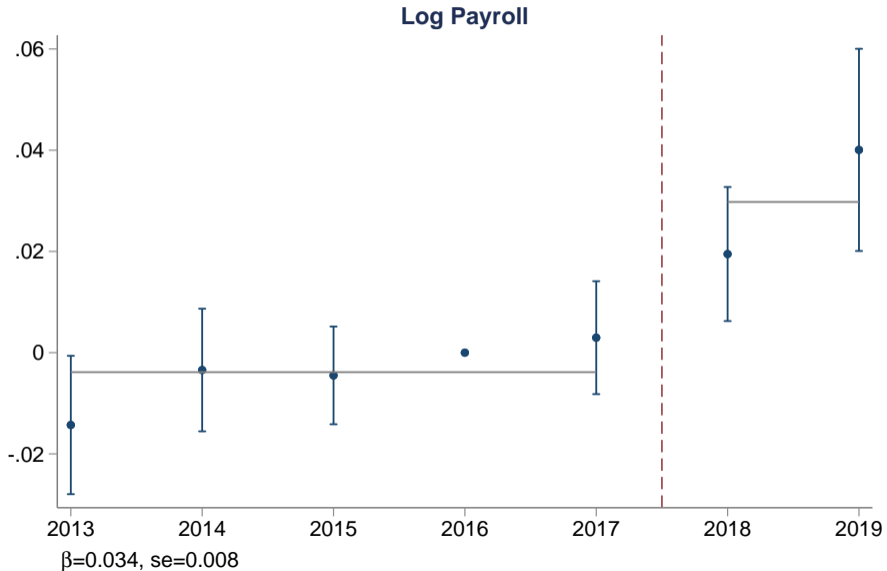
Shareholder Payouts



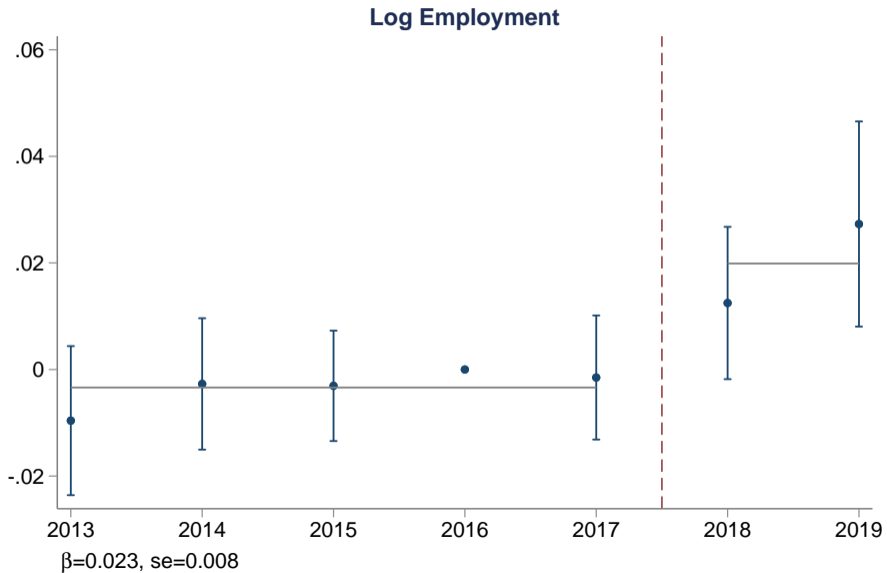
Net Investment / Lagged Capital



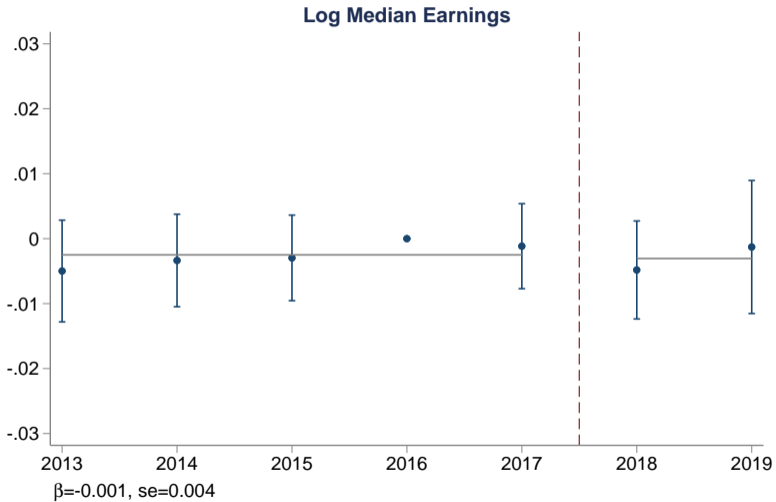
Labor Markets: Total Payroll



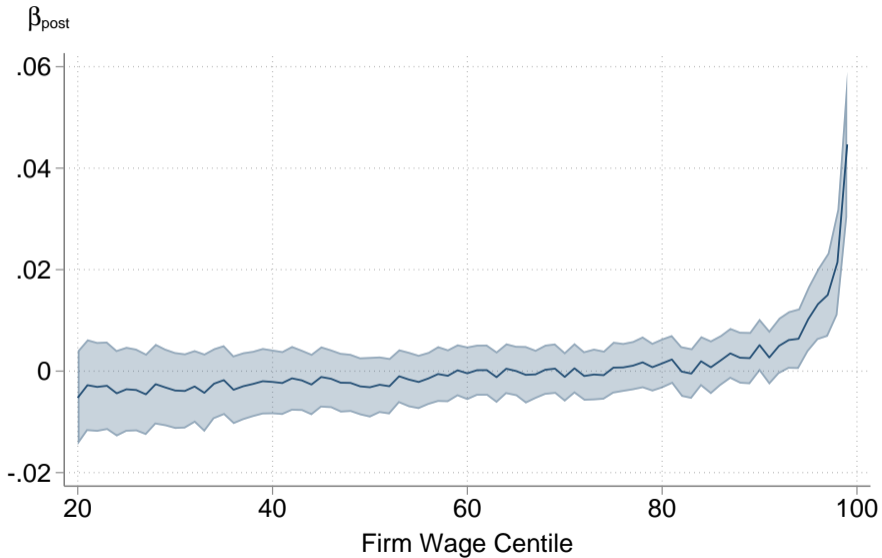
Employment



No Change in Median Earnings



Impacts on the Firm Wage Distribution



Elasticities

	(1)	(2)	(3)	(4)	(5)	(6)	(7)
	$\ln(1 - \tau_f^{MTR})$	Pre-tax π	Post-tax π	I_t/K_{t-1}	w_{p50}	w_{p95}	Executives
C \times Post	0.066*** (0.002)	0.030*** (0.007)	0.040*** (0.007)	0.029*** (0.004)	-0.001 (0.004)	0.013*** (0.004)	0.049*** (0.010)
2016 Outcome Mean	-0.31	0.47	0.41	0.06	47,724	175,757	4,851,366
ε^{NTR}		0.46	0.61	0.45	-0.01	0.20	0.69
s.e.		0.11	0.11	0.07	0.06	0.06	0.14
Firm FE	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Industry-Size-Year FE	Yes	Yes	Yes	Yes	Yes	Yes	Yes
R2	0.73	0.61	0.63	0.21	0.94	0.93	0.92
N	108,430	108,430	108,430	108,430	108,430	108,430	95,685
N Firms	15,490	15,490	15,490	15,490	15,490	15,490	14,140

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Leverage other elasticities to estimate incidence

Incidence

	USD	% Incidence
Panel A: Factors		
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Executives	13	10
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Bottom 90%	25	20

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- $\approx 80\%$ of benefits flow to top 10% of earners

More in the Paper

Additional results:

- Mechanism and robustness tests
- Shifting and evasion
- Firm and worker heterogeneity
- Market-level elasticities and GE effects
- Welfare estimates

Conclusion

Clear evidence that corporate tax cuts have significant effects on real outcomes

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Efficiency-equity tradeoff:

- **Efficiency:** Tax cuts increase aggregate output
- **Equity:** Short-run gains disproportionately flow to high earners

Thank you!