COMMENTS

"DO AMERICANS MOVE FOR LOWER TAXES? THE TAX REFORM ACT OF 1986 AS A NATURAL EXPERIMENT" BY MING-FENG HSIEH AND HUI-CHEN WANG

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WANG AND HSIEH EXAMINE HOW CHANGES in state-specific tax burdens resulting from the Tax Reform Act of 1986 affected interstate migration in the late 1980s. They consider two key channels by which the effects of TRA86 varied in magnitude according to state of residence. First, the legislation made sweeping changes to individuals' federal income tax base and federal income tax liability, concepts that are used in establishing state income tax liabilities. Because TRA86 broadened the federal income tax base while generally reducing federal tax liabilities, the reform caused increases in state income tax liabilities for the residents of some states and decreases for others. Second, TRA86 removed state sales taxes from the list of items that individuals could itemize in determining their taxable income. The resulting change in federal income tax liabilities was zero for residents of states that did not impose a sales tax, but positive for itemizers living in states with high sales taxes.

The paper examines the extent to which these state- and taxpayer-specific tax changes contributed to interstate moves between 1985 and 1990, controlling for other influences. An important basis for the study is that TRA86 was exogenous from the perspective of the individual states. The Wang-Hsieh paper represents sound econometric practice that should be emulated by other researchers. This attention to endogeneity issues is perhaps the most important contribution of their research.

The authors find that greater TRA86-induced tax increases by state of origin induced out-migration, while greater TRA86-induced tax increases by destination reduced immigration. The effects were especially strong for single householders and low-income householders. The conditional logit regressions include appropriate controls for other fiscal parameters, economic conditions, demographics, and amenities, as well as for individual circumstances (such as income and number of dependents) that affect their tax liability.

Although the direction of the results is in line with expectations, the magnitudes are too large to be plausible. Wang and Hsieh cite the estimates in Marshall (1991) of per capita TRA86-induced windfalls by state ranging from -$32 to +$64. These magnitudes—a maximum gain of under $100 per year from making the optimal move from a tax standpoint—seem much too small to justify incurring the pecuniary and non-pecuniary costs of a major move. (If Wang and Hsieh are picking up larger tax effects in their Census microdata, their paper would be strengthened substantially if they provided such statistics.) I conclude that the coefficient estimates are likely picking up the effects of some correlated, unobserved variables that influence interstate migration.

As a test of this hypothesis, I encourage the authors to examine the degree to which their results are driven by college-graduation-related and retirement-related moves that were unlikely to have been influenced much if at all by TRA86. Moves on the part of these demographic groups are included in the Wang-Hsieh study because their data encompasses individuals who were aged 25 to 65 in 1990 (and therefore aged 20 to 60 in the base period).

Young adults move much more frequently than middle-aged adults. Examining a sample representing the college graduation classes of 1979 to 1991, I found that 34 percent were living in a state different from their high school location and 29 percent were living in a state different from their college location five years after graduating from college (Kodrzycki, 2001). Most students who were in college during the pre-TRA86 base period in the Wang-Hsieh study would not have had high enough earnings for them to have paid federal income tax. At most, then, their moves might have been influenced by tax liabilities in alternative destination states. This argument is consistent with the Wang-Hsieh finding that the effects of taxes in the destination states are stronger than those of the origin states. However, my regression study found that the migration patterns of young college graduates were not influenced by housing costs (controlling for economic factors, amenities, and the like). Differences in apartment rents and imputed rents on owner-occupied housing across states are substantially larger in dollar terms than the tax liabilities that Wang and Hsieh consider.

Retirement is another point at which many individuals move across state lines. The Gurley and Harper paper presented in the same session found that cross-state variation in the tax treatment of pension income was one determinant of the location of individual moves. I would be willing to bet that estate taxes—not considered in the Wang-Hsieh study—constitute another big-ticket factor that older individuals take into account when deciding where to retire.

References

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