REMARKS

ABOUT HENRY AARON

John B. Shoven

Congratulations to Henry Aaron for receiving the 2010 Daniel M. Holland Medal for outstanding contributions to the study and practice of public finance from the National Tax Association. Perhaps I should congratulate the National Tax Association for making such a superb choice. I cannot think of a more deserving winner. Henry Aaron has addressed all of the major public finance issues of the past 45 years. He graduated from UCLA in 1958 and received his PhD from Harvard in 1963, where he also served as an instructor until 1966. He joined the Johnson Administration as a senior staff economist of the Council of Economic Advisors in 1966, when the Council was chaired by Gardner Ackley and the other members were Jim Duesenberry and Arthur Okun. He moved to the Brookings Institution in 1968, where he has been continuously since, except for his service as Assistant Secretary of Health, Education and Welfare in 1977 and 1978. While at Brookings, he also was a Professor of Economics at Maryland for the 22 years, 1967-89.

Let us go back to the theme that Henry worked on all of the important public finance issues of the last almost half century. He evaluated the great society programs of the Johnson Administration and the accompanying war on poverty. He is an expert on welfare reform, on health reform, on Social Security, and on tax policy. He has written on government policies towards housing, on inflation and the income tax, on adjusting institutions for dramatically longer lifetimes, on the impossibility and the inevitability of rationing healthcare, and on the choice between income taxation and consumption taxation. You would be hard pressed to name an important public finance debate that Henry has not engaged in. In fact, that is one of the traits I admire the most about Henry Aaron – he works on important issues. He does not choose topics because they are hard or easy, but because they are topical and important.

It is really pretty difficult to summarize Henry's career to date. I looked at his CV, but it is 22 pages long, mostly listing a vast list of publications. I know I felt a little reassured when I read somewhere, I can not remember where, that there is no evidence that Henry Aaron took performance enhancing drugs.

In order to keep my task manageable, I have decided to talk about the times that our paths have crossed, which will lead to a very partial and selective survey of Henry's prodigious contributions. I think that the first article of Henry Aaron's that I read was in the 1970 *American Economic Review*. It was not Henry's first article, but it being the first I read probably reflects that I was a second year graduate student at Yale in 1970-71, taking a public finance class taught by the 2009 winner of the Daniel Holland Medal, Peter Mieskowski. I read Henry's paper, "Income Taxes and Housing." My recollection is that it was the lead article in the *AER* and I found it incredibly clear and straightforward. I think its lessons are still applicable today. I hear so many people assert that the tax expenditure with respect to owner-occupied housing is the deductibility of property taxes and mortgage interest. In fact, Henry lays out very clearly that if we are trying to institute an income tax that does not discriminate between owner-occupants and renters, the big tax expenditure involved not including the imputed rental income of the owner-occupants. If you did that, then the deductibility of mortgage interest and property taxes is completely appropriate. In fact, you would want to add to the list of deductions amounts for maintenance and depreciation. Simply disallowing mortgage interest deductions would create a new distortion between cash buyers and those who need to borrow to buy a house. Anyway, I learned a lot from that article and included it on my public finance reading list. It belongs on such reading lists today. Henry went on to produce a book on government programs towards housing, titled *Shelter and Subsidies* that looked at a wider range of government programs for with a particular emphasis on distributional impacts.

Speaking of public finance, I started teaching at Stanford in 1973. One of my first courses was undergraduate public finance and I assigned what was Henry's new book at the time, *Why is Welfare So Hard to Reform?* It was a great analysis of the implicit tax rates faced by people on income support programs such as AFDC, Medicaid, Food Stamps, public housing and school lunch programs. Henry showed with laser like clarity that the marginal tax rates faced by people who were on multiple programs were in the vicinity of 100 percent. People whose average tax rates were negative had the highest marginal tax rates in the economy. The answer to the title question is that it is difficult to the point of being nearly impossible to be both generous to the poorest of the poor and to preserve work incentives for low-wage individuals. A balance has to be struck, but it is hard to believe that the proper balance involves 100 percent marginal taxation. The welfare reform of the 1990s made some progress on this tradeoff, but it is still true that some of the lowest income households have the highest effective marginal tax rates. I recently wrote a paper with Gopi Shah Goda of Stanford and Sita Slavov of Occidental College on Medicare as a secondary payer. One of the lessons of that article, that targeted assistance programs inevitably involve high implicit marginal tax rates, was taken right from Henry Aaron's 1973 book.

Aw, the 1970s. The topic of the decade was inflation or stagflation and Henry edited the book on inflation and the income tax. In some ways it was a technical matter of how to accurately record and tax real incomes, but it was not simple and Henry has a comprehensive knowledge of the subject and put together a first rate conference volume. Again, this was a topic that I was interested in, having co-authored a couple of papers in the *Brookings Papers on Economic Activity* with Jeremy Bulow concerning inflation and the measurement and taxation of corporate income, so our paths crossed on this one.

Henry Aaron, along with Joe Pechman, Harvey Galper and former Holland Medal winners Charles McLure, Marty Feldstein and a number of others, was a major player in the debate about fundamental tax reform in the 1980s. There were debates about the issue of whether the tax base should be income or consumption, whether the U.S. should adopt a value added tax, whether the corporate and individual income taxes should be integrated and Henry was involved with all of them. I am not going to emphasize that part of Henry's work, because we did not work together so much on these topics, but he was an important player on these issues which led, in part, to the landmark 1986 tax reform.

I am going to pick up our interactions again in 1991. I had become Director of the Center for Economic Policy Research in 1989, and, as with a lot of situations, I had some influence on who was appointed to the organization's research advisory board. I wanted to add Henry Aaron. He is now coming up on twenty years on that board and he continues to make valuable contributions. For instance, at a conference we held in March 2011, which we modestly refer to as an "Economic Summit", had a session discussing the Bowles-Simpson Commission report and the general long-run fiscal situation of the country. Naturally, I asked Henry Aaron to anchor a panel discussion. Subsequently, Donald Marron agreed to share his perspective on the subject. I did peak at Henry's website and noticed that he had already written on the subject of the Bowles-Simpson proposals. I frequently turn to Henry at SIEPR for what I view as the liberal or progressive view on any topic. I know that he always bases his discussion on facts rather than politics – he always does a remarkable job.

Henry Aaron was a Guggenheim Fellow at the Center for Advanced Study in the Behavioral Sciences at Stanford in 1996-97. We got together several times during the year and what I remember most about that sabbatical for Henry is that he was studying psychology and behavioral economics. He was certain that there was something to this new behavioral economics stuff and he was going to become an expert in it. Of course, he was right, but what impressed me the most was here was a guy that was still adding to his human capital more than 30 years after the completion of his PhD. I thought that this was exactly what sabbaticals were supposed to be about, but seldom are.

The next time we crossed paths was when Ben Friedman asked us to debate or at least have two points of view about Social Security reform. This is the one place where I found Henry's CV to be inaccurate. It lists the title of our 1999 book as "*Should Social Security Be Abolished*?", whereas the correct title is "*Should the United States Privatize Social Security*?" In truth, neither title quite reflects our points of view as well as the titles of our individual chapters. Henry's Chapter was titled "Social Security: Tune it Up, Don't Trade it In" whereas mine had the handle "Social Security Reform: Two Tiers are Better than One." Maybe, the title in Henry's CV about whether

Social Security should be abolished or not reflects his opinion about what I proposed. But, I doubt that explanation. I favored plans which maintained a significant core defined benefit element of Social Security but which added a second tier defined contribution element. My favorite plan would have involved increased contributions and increased total benefits for almost everyone. As Henry's title suggests, he proposed tuning up the existing Social Security system with a combination of benefit cuts and tax increases. One element of our debate was whether mandatory contributions to the second tier defined contribution element of my proposal were equivalent to taxes or not. I said "no" since the money would ultimately be returned with return to the participant, but to Henry, mandatory meant a tax. Rather than follow the advice of either of us, we have done essentially nothing on Social Security reform in the intervening 13 years. My view is that the country would be in better shape if it had followed either path or something in between. Anyway, my point today is that we had a lively, high level debate that resulted in a book whose title Henry has trouble with and that our friendship and mutual respect came through completely unscathed.

I should add that Henry Aaron is clearly an expert on Social Security. His first paper on the topic was in 1966 and he has been writing a lot on it periodically ever since. He also was Chairman of the 1978-79 Advisory Council on Social Security.

The next subject where our interests overlapped is institutional adjustments to dramatically longer life expectancies. Henry Aaron has had a long standing interest in economic demography. Just one example of that is his 1988 book with Barry Bosworth and Gary Burtless, *Can America Afford to Grow Old?* In 1998 or so or perhaps earlier, he became convinced that there is great uncertainty in the future pace of mortality progress and there is at least a nontrivial chance that the rate of progress could be 2 percent per annum instead of the 0.68 percent per year of the base case for Social Security's forecasts. He thought and I tend to agree with him that Social Security had little to no facts on which to base its prediction that the rate of mortality progress would slow in the first half of this century relative to the rate of progress in the second half of the 20th century. I believe that Henry finds the work of William Schwartz, the former chairman of the Department of Medicine at Tufts and the author of *Life Without Disease*, stimulating and thought provoking. The difference between 2% per year improvement in age specific mortality and 0.68% per year widens out dramatically. For instance, with 2 percent improvement, life expectancy at birth in 2050 would be 107 for males and 111.5 for females instead of 83 and 87 under the Social Security base case. That is a lot of extra Social Security checks! This is not just anybody's projection; it is the calculation of Henry Aaron and Benjamin Harris. Think about the long-run fiscal outlook under that scenario! Well, in fact, that is what Henry Aaron and William Schwartz did in the book they edited with the title *Coping with Methuselah*. I had a piece in that volume and my own work on what I call "new age thinking" about new ways of measuring age clearly owes a lot to my interactions with Henry and his interest in this topic.

Over the past 20 years, the public finance field has moved significantly into health economics for reasons that Willie Sutton would understand – that is where the money is. At least that is true in terms of what drives the long-run fiscal deficit. For those of you not old enough to remember Willie Sutton, he was a prolific bank robber who allegedly answered the question of why he robbed banks with the reply, because that is where the money is. Henry once again was ahead of the field in focusing on health policy having added health economics to his portfolio of interests at least 30 years ago. While it was not his first foray into health economics, I would point out that his 1984 book with William Schwartz, *The Painful Prescription: Rationing Hospital Care* was way ahead of its time and won the Policy Studies Organization Outstanding Book Award for 1984 and even won recognition from the American College of Health Care Executives.

Let me close by summing up. Henry has worked on tax policy, social security policy, health policy, inflation, welfare reform, and institutional adjustments to changing demographics, all of the big public finance topics of the past 45 years. I used to think of Joe Pechman as Mr. Public Finance, but now I think it is time we give Henry Aaron that title as well as the recognition bestowed by the Daniel Holland Medal. Congratulations, Henry.