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NEW YORK UNIVERSITY
SCHOOL OF LAW

"Democratic Law and Economics"
Zachary Liscow
Yale Law School

October 15, 2019
Vanderbilt Hall – 202
Time: 4:00 – 5:50 p.m.
Week 7

SCHEDULE FOR FALL 2019 NYU TAX POLICY COLLOQUIUM
(All sessions meet from 4:00-5:50 pm in Vanderbilt 202, NYU Law School)

1. <u>Tuesday, September 3</u> – Lily Batchelder, NYU Law School.

2. <u>Tuesday, September 10</u> – Eric Zwick, University of Chicago Booth School of Business.

3. <u>Tuesday, September 17</u> – Diane Schanzenbach, Northwestern University School of Education and Social Policy.

4. <u>Tuesday, September 24</u> – Li Liu, International Monetary Fund.

5. <u>Tuesday, October 1</u> – Daniel Shaviro, NYU Law School.

6. <u>Tuesday, October 8</u> – Katherine Pratt, Loyola Law School Los Angeles.

7. <u>Tuesday, October 15</u> – Zachary Liscow, Yale Law School.

8. <u>Tuesday, October 22</u> – Diane Ring, Boston College Law School.

9. <u>Tuesday, October 29</u> – John Friedman, Brown University Economics Department.

10. <u>Tuesday, November 5</u> – Marc Fleurbaey, Princeton University, Woodrow Wilson School.

11. <u>Tuesday, November 12</u> – Stacie LaPlante, University of Wisconsin School of Business.

12. <u>Tuesday, November 19</u> – Joseph Bankman, Stanford Law School.

13. <u>Tuesday, November 26</u> – Deborah Paul, Wachtell, Lipton, Rosen, and Katz.

14. <u>Tuesday, December 3</u> – Joshua Blank, University of California at Irvine Law School.

Democratic Law and Economics

Zachary Liscow[*]
Yale Law School

October 2019

ABSTRACT: Law and economics typically analyzes ideal policies, ignoring real-world institutions and constraints. It is helpful for real-world political actors, though, to have guidance for the real world, which this Article provides for policymakers setting policy with distributional impacts. Current guidance not considering real-world constraints may significantly hamper policymakers' effectiveness at addressing today's crisis of inequality. Critique of law and economics is widespread, but, to provide an alternative framework for policymaking, one needs to start with an account of its failures that can provide such an alternative framework. This Article provides such an account of the failures and an alternative framework.

This Article explores a major dissonance between expert and lay policy views: the set of *tax* prescriptions required by law and economics is sharply at odds with ordinary citizens' psychology about taxes. While standard economic reasoning views taxes solely as a system of incentives and redistribution, many ordinary people also think of taxes as rewarding *desert*—as recent rigorous survey experiments, advances in the economics of taxation, and decades of experience show. Desert-based tax views limit redistribution, since the poor are deemed to not deserve free cash and the rich are deemed to deserve some of their income. A democracy where Congress is attentive to such tax views will need to look elsewhere to achieve distributive justice.

Turning to the arcane, but essential, details of the economic theory of taxation reveals that acknowledging an idea as simple and intuitive as "views on desert likely impact our tax policy" turns law and economics prescriptions on their heads: rather than never redistributing, as standard law and economics prescribes, legal rules typically *should* redistribute. The Article takes citizen psychology seriously and develops policy prescriptions based on it to reveal *how* to redistribute, given the tradeoffs presented by standard efficiency concerns. The Article describes the issues and points the way forward for policymakers who care about addressing inequality and minimizing inefficiency, using an illustration of federal regulatory cost-benefit analysis and also describing implications in other areas.

Table of Contents

Introduction

The federal Department of Transportation's longstanding practice for distributing grant funds across projects is to conduct cost-benefit analysis to determine where money is best spent and then spend it there. The most important factor in the analysis is the value of time saved. Currently, saving the time of relatively poor people on buses counts for $25 per hour.[1] Saving the time of richer people at airports counts for well over twice as much: $63 per hour. This practice tends to push transportation spending toward the rich instead of the poor, despite the essential need of the poor to get to work to achieve economic mobility. How could it possibly be

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[1] The Value of Travel Time Savings: Departmental Guidance for Conducting Economic Evaluations Revision 2 (2016 Update) 17 (US Department of Transportation, Sept 27, 2016) (providing recommended hourly values of time travel savings for intercity business travel).

that baked into our policies is a method that spends on the well-to-do instead of the needy at a time of such great concern over inequality,[2] especially in light of evidence on the importance of transportation for economic mobility?[3]

This practice is actually the logical prescription of our dominant paradigm for economic policy because it is "efficient."[4] The basic logic is that the economic pie grows more when rich people work more than when poor people work more because the rich have higher wages. By saving an hour of time of the rich instead of the poor, we maximize the size of the economic pie. The gains can then be partly redistributed through cash "taxes and transfers" to make everyone better off than they would have been had we saved an hour of the poor's time instead. Yes, assuming the poor can get to work at all, they will work less because they must spend another hour in transit. But, because the rich get more transportation spending, they work and earn more, and can thus give larger cash transfers to the poor. Everyone is better off.

This Article argues that this standard efficiency logic is incomplete and problematic because it erroneously acts as if addressing distribution through cash and through transportation funding are interchangeable. It is inattentive to the *means* of achieving a just distribution and instead attentive only to the desired *outcome*. It acts as if there is only one economic pie to be distributed, while in fact—as the Article will explain—there are many separate economic pies in the eyes of much of the population. As a result, this logic may often yield bad policy. Instead, in examples like this, we should fund transportation for the poor considerably more than this example suggests. And we should do so based not on an external critique of law and economics[5] but rather based on the ultimate goal typically underlying economics: maximizing aggregate well-being.

The problem described here with the standard efficiency approach for achieving this goal of maximizing well-being is that it ignores how our real-world institutions and politics function due to voters' political and social psychology. It has been noted by critics of economics that the cash taxes and transfers needed to compensate for getting less transportation spending, for example, often never arrive.[6] But, why not? And what should we do about it? This Article gives

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[2] *See, e.g.*, PEW RESEARCH CENTER, THE GENERATIONAL GAP IN AMERICAN POLITICS 18 (2018), http://www.people-press.org/wp-content/uploads/sites/4/2018/03/03-01-18-Generations-release.pdf (noting that 62% of survey respondents felt that the U.S. economic system unfairly favors powerful interests, and 82% felt that income inequality in the U.S. was either a very big or moderately big problem). Republicans, too, have increasingly expressed concern about rising inequality, even before President Trump's populist rhetoric during the 2016 campaign. For example, Mitt Romney, Jeb Bush, and Rand Paul all complained about the continuing rise in inequality during the Obama presidency. *See* Catherine Rampell, *Republicans Have Started to Care About Income Inequality*, WASH. POST (Jan. 22, 2015), https://www.washingtonpost.com/opinions/catherine-rampell-republicans-have-started-to-care-about-income-inequality/2015/01/22/f1ee7686-a276-11e4-903f-9f2faf7cd9fe_story.html?utm_term=.92d3a15e5c57.

[3] Mikayla Bouchard, *Transportation Emerges as Crucial to Escaping Poverty,* N.Y. TIMES, May 7, 2015 (describing work by Raj Chetty and co-authors in which "commuting time has emerged as the single strongest factor in the odds of escaping poverty").

[4] Louis Kaplow & Steven Shavell, *Why the Legal System Is Less Efficient Than the Income Tax in Redistributing Income*, 23 J. LEGAL STUD. 667 (1994) [hereinafter *Redistributing Income*]; KAPLOW & SHAVELL, FAIRNESS VERSUS WELFARE (2009).

[5] For these, *see, e.g.*, ROBERTO UNGER, WHAT SHOULD LEGAL ANALYSIS BECOME? 9 (1996); C. Edwin Baker, *The Ideology of the Economic Analysis of Law*, 5 PHIL. & PUB. AFF. 3 (1975); Ronald Dworkin, *Is Wealth a Value?,* 9 J. LEGAL STUD. 191 (1980); Richard S. Markovits, *Why Kaplow and Shavell's "Double-Distortion Argument" Articles Are Wrong*, 13 GEO. MASON L. REV. 511 (2005).

[6] Lee Anne Fennell & Richard H. McAdams, *The Distributive Deficit in Law and Economics*, 100 MINN. L. REV. 1051 (2015); Markovits, *supra*.

a specific account based on widespread lay views about taxation, providing foundations for such political considerations in policy design.

The account first requires some understanding of the esoteric underbelly of standard law and economics: "optimal tax theory" on how those taxes and transfers upon which we should solely rely to have a fair distribution of income should look. The key point is that taxes are assumed to dissolve all individuals into producers of one pool of resources to be redistributed. There is no sense of "desert," or people being entitled to a larger or smaller share of resources based on what they themselves earn, beyond the incentives to increase the size of the pie. The Article develops a maintained hypothesis about commonplace social and political psychology: Contrary to the assumptions underlying economics, but consistent with common social psychology, a belief in desert is commonplace. That is, those who earn or save money deserve to keep some of it, and those who do not earn or save money deserve less income. Such views may reflect a kind of "everyday libertarianism," tapping into people's notions of reciprocity: recipients have to give to get.[7] They have to work to get the economic benefits. And, since Congresspeople who are selected by voters—and not a benevolent dictator—sets tax rates, taxes do not redistribute as much as is needed to achieve distributive fairness.

The Article hypothesizes that many ordinary citizens have this view about taxation because they have compartmentalized policy-specific views about distribution that the Article calls "mental policy accounts" in reference to the large literature in economics documenting how individuals have "mental accounts," especially in the area of savings. That is, although economics assumes that funds are fully fungible across different sources of income—regular paychecks, dividends, windfalls increases in the value of stocks, etc.—individuals treat them in very different ways. For both savings and policy views on redistribution, people follow prudent rules of thumb for each account, because time is limited and they are not supercomputers. As a result, resisting redistribution through taxation is completely consistent with supporting it through other means, such in-kind necessities like housing, healthcare, and education.[8] People could think this way for many reasons, including it being the normal way they think about issues that have considerably larger personal stakes for them, like their own finances. Whatever the reason, emerging evidence from carefully-designed survey experiments in economics,[9] as well as decades of experience,[10] suggest that voters are more willing to give in-kind transfers (like bus service) that improve equality of opportunity—the ability to get to work—than to give out cash. Taxes will not redistribute enough.

To be as conventional as possible, this Article takes the perspective that these views impose political constraints, but that normatively the standard approach in economics is right.[11]

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[7] SHEFFRIN, *supra* notes __.

[8] This policy-specific view is often called "specific egalitarianism." *See* James Tobin, *On Limiting the Domain of Inequality*, 13 J.L. & Econ. 263 (1970).

[9] STEVEN M. SHEFFRIN, TAX FAIRNESS AND FOLK JUSTICE (2013); Jimmy Charite, Raymond Fisman & Ilyana Kuziemko, *Reference Points and Redistributive Preferences: Experiment Evidence* (Nat'l Bureau of Econ. Research, Working Paper No. 21009, 2016); Raymond Fisman et al., *Do Americans Want to Tax Capital? Evidence from Online Surveys*, (Wash. Ctr. Equitable Growth Working Paper, 2017); Matthew C. Weinzierl, *A Welfarist Role for Nonwelfarist Rules: An Example with Envy* (Harv. Bus. Sch., Working Paper No. 17-021, 2017); Matthew C. Weinzierl, *The Promise of Positive Optimal Taxation: Normative Diversity and a Role for Equal Sacrifice*, 118 J. PUB. ECON. 128 (2014); Matthew C. Weinzierl, *Popular Acceptance of Inequality Due to Innate Brute Luck and Support for Classical Benefit-based Taxation,* 155 J. PUB. ECON. 54 (2017).

[10] *See infra* notes __.

[11] This Article thus represents a "second-best" approach. Richard G. Lipsey & Kelvin Lancaster, *The General Theory of Second Best*, 24 REV. ECON. STUD. 11 (1956).

Of course, there have been many critiques of law and economics. But to be constructive in a law and economics that takes real-world institutions into consideration, we need an account of politics that says that there is something special about taxation—that it is still socially desirable to reduce economic inequality, but that there's something peculiar about economists' chosen tool for addressing it. The maintained hypothesis provides such an account.

The Article illustrates its argument with an extended example on the Department of Transportation's allocation of transportation spending between the rich and the poor with which the Article began.[12] The Article suggests that current policy is wrong because of constraints on Congress's redistributionary taxation. The illustration shows four things. First, it shows how a regulator (or other party) could consider political constraints. By considering views on taxes as views on *just one means* of redistribution, rather than on views of redistribution writ large, as is typically done, the illustration shows how regulators can calibrate the appropriate distributive response to taxation. Second, the welfare losses from regulators being inattentive to political constraints can be large. Although the transportation example is just illustrative, it is supported by cutting-edge research in economics that shows just how little taxation redistributes relative to sensible baselines.[13] Third, the regulator does not need to take a stand on whether the views about taxes are normatively correct or not. One can remain agnostic on that question; all that matters is that, in fact, despite a desire to have more equal economic outcomes, taxes do not achieve the redistribution needed. Fourth, regulators do not need to be certain that redistribution is inadequate to act. All they need is a belief that there is *some probability* that redistribution is uncertain.

A key point of the Article is that ordinary people have policy-specific views that differ dramatically from the thinking reflected both in standard economics and in policies like that of the Department of Transportation. Many ordinary people do not view the government as one big allocational mechanism with perfect fungibility between policies. Department of Transportation policymakers should think carefully before acting like they do. Such a critique is especially important at the moment given the widespread populist anger at elites.

The Article reassesses economic policymaking in light of the combination of desert-based views about taxation, mental policy accounts, and real-world institutions. The policy implications are far-reaching. Indeed, they flip law and economics on its head: from a claim that nontax policies should *never* redistribute to a claim that, where politically feasible, they should *typically* redistribute. If the tax policy needed to achieve just distributive results conflicts with desert-based views about the process of taxation, then it is worth redistributing in the panoply of *nontax* policies that could be used to address redistribution: healthcare spending, childcare provision, regulatory cost-benefit analysis, and so on. In other words, if tax policy durably reflects desert-based views, then policymakers should use other legal rules to pick up the redistributive slack. Given widespread views about fairness in nontax policy, there should be many politically feasible areas. The Article also discusses several other considerations that surface when economic policy is viewed in these terms, which affect the desirability and feasibility of such redistribution.

Before moving on, several things should be made clear. First, this Article adopts the standard "utilitarian" or "welfarist" perspective of economics. Second, the Article does not claim that it is easy to discern common views about taxation or other policies. Rather the claim is that there is a strong case that common views about taxation are at odds with standard assumptions in

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[12] *See* Liscow, *Is Efficiency Biased?*, *supra*.
[13] Nathaniel Hendren, *Efficient Welfare Weights* (March 2019).

law and economics, using a host of evidence, including survey experiments and existing institutions. Third, the goal here is not to supplant politicians but rather to improve the policy advice given to them.

The Article relates to several literatures. One is the political science literature on "predistribution," which argues for using the government to equalize pre-tax resources rather than tax-based "redistribution."[14] This Article describes an account of why predistribution is good policy and works out the policy implications in an economics framework. Second, the Article contributes to the literature on optimal economic policy under political constraints.[15] This Article works out the implications of a specific explanation of political constraints in the context of the choice between taxes and legal rules across different institutions of the state. A third related literature is on legitimacy, or governing in a way accepted as right and proper.[16] Though working from the standard frame of economics, the Article can also be understood to describe how to redistribute in a legitimate way, given the commonplace views of citizens. Fourth, the Article relates to a movement among liberal economists to argue for more government intervention largely on efficiency grounds.[17] While that literature attempts to identify win-win policy reforms that simultaneously improve efficiency and reduce inequality, this Article provides a framework rooted in commonplace psychology that identifies policies to increase redistribution. Fifth, the Article relates to work on building support for redistribution through, for example, advertising program benefits or universalist designs of programs, notwithstanding potential efficiency costs.[18] This Article does not offer guidance on how to build support for redistribution, but instead takes voters' views as given and describes how policymakers should respond to them.

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[14] Jacob S. Hacker, *The Institutional Foundations of Middle Class Democracy*, POLICY NETWORK (May 6, 2011), http://www.policy network.net/pno_detail.aspx?ID=3998&title=The+institutional+foundations+of+middle-class+democracy (coining the term); Ed Miliband, Leader of the Labour Party and Leader of the Opposition, Speech at the Stock Exchange (co-hosted by the Policy Network) (Sept. 6, 2012) (transcript available at http://www.politics.co.uk/comment-analysis/2012/09/06/ed-miliband-s-redistribution-speech-in-full) (using the term); Jacob Hacker & Paula Dwyer, *Q&A: Clinton and the Politics of Predistribution*, BLOOMBERG OPINION (June 6, 2016), https://www.bloomberg.com/opinion/articles/2016-06-06/clinton-and-the-politics-of-predistribution; Martin O'Neill & Thad Williamson, *The Promise of Pre-Distribution*, THE POLICY NETWORK (Sept. 28, 2012); Martin O'Neill & Thad Williamson, *Philosophical Foundations for Good Capitalism*, 20 RENEWAL 20, 29 (2012).

[15] Conor Clarke & Edward Fox, *Perceptions of Taxing and Spending: A Survey Experiment*, 124 YALE L. J. 1252 (2015) (describing the apparent ease of providing tax breaks instead of economically equivalent direct transfers); Jake Haselswerdt & Brandon L. Bartels, *Public Opinion, Policy Tools, and the Status Quo: Evidence from a Survey Experiment*, 68 POL. RESEARCH Q. 607 (2015) (same); Alberto Bisin, Alessandro Lizzeri & Lefeat Yariv, *Government Policy with Time Inconsistent Voters,* 105 AM. ECON. REV. 1711 (2015) (developing a model that suggests that balanced budget rules could constrain government over-responsiveness to citizen caprice); Marina Halac & Pierre Yared, *Fiscal Rules and Discretion under Persistent Shocks*, 82 ECONOMETRICA 1557 (2014) (studying optimal policymaker discretion in light of time-inconsistent preferences and persistent shocks).

[16] TOM TYLER, WHY PEOPLE OBEY THE LAW (2006).__

[17] DEAN BAKER, THE END OF LOSER LIBERALISM: MAKING MARKETS PROGRESSIVE (2011); JOSEPH E. STIGLITZ, THE PRICE OF INEQUALITY: HOW TODAY'S DIVIDED SOCIETY ENDANGERS OUR FUTURE (2012); Economists for Inclusive Prosperity.

[18] *See* Gillian Lester, *Can Joe the Plumber Support Redistribution? Law, Social Preferences, and Sustainable Policy Design*, 64 TAX L. REV. 313, 318 (2011) (describing "how policies can shape political preferences about redistribution"); Suzanne Mettler, *Reconstituting the Submerged State: The Challenges of Social Policy Reform in the Obama Era,* 8 PERSP. ON POL. 803 (2010) (advocating for advertising or otherwise making known to taxpayers the programs they pay into and benefit from to increase public support for them); Yair Listokin & David M. Schizer, *I Like to Pay Taxes: Taxpayer Support for Government Spending and the Efficiency of the Tax System,* 66 TAX L. REV. 179 (2012) (similar).

The Article's contribution—combining behavioral economics, the reality of politics and institutions, basic law and economics tenets, and distributive questions—is thus threefold. First, it makes the *empirical* case that commonplace views about taxes are deeply at odds with standard assumptions in law and economics for a somewhat obscure, but key reason: desert in taxation can have no place under standard assumptions, but we have many reasons to think that such reasoning is pervasive. As a result, Congress will tend to redistribute less through taxes. Second, the Article illustrates how another institution—federal administrators allocating funding between the rich and the poor—should respond to this constraint. Thus, the Article carefully *applies* the implications of these views to a key question in law and economics: how the various pieces of economic policy—tax versus nontax government programs in particular—should fit together. Third, the Article points the way toward a more complete—perhaps democratic— version of the analysis in law and economics by taking into account real-world institutions and nonexpert views.

The Article proceeds as follows. Section I describes the standard view of the way to address distribution in law and economics: "optimally" redistributive taxes and efficient nontax legal rules. Section II develops the maintained hypothesis on commonplace social and political psychology: many people have mental policy accounts, with desert-based views about taxes and often views about nontax policies involving distributions that are more equal than is efficient. Section III adopts the perspective that these commonplace views cause political constraints and applies standard economic analysis to a particular illustrative institution: regulatory cost-benefit analysis of transportation spending. Section IV considers other factors in the analysis and discusses general policy implications. Section V addresses critiques. Section VI suggests other applications.

I.   The Standard View in Law and Economics: "One-Pieism"

The Article takes the standard economic perspective that the ultimate aim is maximizing welfare. In taking a "welfarist" or "utilitarian" perspective, I mean measuring societal well-being with reference to individuals' subjective well-being.[19] The method estimates each individual's well-being and aggregates those well-beings.[20] The goal is then to recommend a set of welfare-maximizing policies that is best for society among all possible combinations of policies.[21] This Article describes how to better accomplish this goal. This Section describes how a welfare-maximization analysis is typically conducted in law and economics now.

The standard approach to the analysis in economics, especially law and economics, is what I call "one-pieism"—the idea that there is one economic pie to be maximized consisting of perfectly commensurable stuff, rather than separate pies for cash transfers, healthcare, treatment by tort law, and the panoply of other "in-kind" (i.e., non-cash) government provisions and regulations. The goal of government policy is to find the most "efficient" way—across all

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[19] Ronald Dworkin draws a distinction between "psychological" and "preference" utilitarianism, the first (advanced by Bentham) based on subjective well-being and the second (advanced by many modern economists) based on satisfaction of preferences. RONALD DWORKIN, TAKING RIGHTS SERIOUSLY 233 (1977). I take the standard modern approach of focusing on preference satisfaction.

[20] *See* ANDREU MAS-COLELL ET AL., MICROECONOMIC THEORY 117-22, 817-50 (1995).

[21] N. GREGORY MANKIW, PRINCIPLES OF ECONOMICS 145 (7th ed. 2015); *see also* Marion Fourcade et al., *The Superiority of Economists*, 29 J. ECON. PERSP. 89, 107-08 (suggesting that economists tend to "mak[e] it their mission to maximize the welfare of ordinary people," with a "fix it" culture and "an orientation toward policy adjudication and advice, and a distinctive willingness, even eagerness to serve and intervene").

possible means—to arrive at a just distributive end. In other words, all that matters are the size and distribution of the slices, not what's in the pie, since all of the pie's policy ingredients are perfectly commensurable. In this framework, the standard argument is that taxes and transfers are typically the most efficient means of redistributing.[22] All other policies should be efficient.

The one-pieist argument proceeds in two steps—first, efficient nontax policies, and second, "optimal" taxes. Efficient nontax policies are those that maximize individuals' willingness to pay given the existing distribution of wealth.[23] When measuring efficiency, all that matters is each individual's atomistic willingness to pay to avoid harm and bring benefits to herself, and then the appropriate amount of public good is provided or penalty is enacted. The analysis typically embeds the idea that notions of "fairness" in means do not matter.[24] This two-step analysis has a more common lay description: In other words, it's best to maximize the size of the pie and then divide it up equitably. One sees such reasoning, for example, in the context of international trade: we should have free trade, maximize the size of the pie, and then divide up the pie to achieve a fair distribution.[25]

Deviating from this logic in the name of "fairness" of means would lead to Pareto failures, so the argument goes.[26] Suppose people are deemed to have a "right" to healthcare or a clean environment. If recipients value healthcare or a better environment at less than the equivalent cash transfer, the government can make everyone better off by taking the money allocated to healthcare benefits or environmental improvement and providing it as cash instead.[27] The essential logic behind using taxes and transfers, rather than in-kind benefits, regulation, or other nontax policies, is that, if rational people are willing to pay for something (and markets are working well), then they can buy it themselves with cash. Individuals can buy health insurance or rent an apartment in an area with good environmental quality if they want to. To help the poor through in-kind benefits is inefficient because they might value the cash more, since they might prefer to spend it on other things. Instead, nontax policies should be efficient, and cash taxes and transfers should bear the full redistributive burden. Thus, cost-benefit analysis should allocate more pollution to poorer people because they are willing to pay less for environmental health.

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[22] Kaplow & Shavell, *Redistributing Income*, *supra* note __. Even more stringently, the taxes need to be on labor income. Alan J. Auerbach & James R. Hines Jr., *Taxation and Economic Efficiency*, *in* 3 HANDBOOK OF PUBLIC ECONOMICS 1347 (Alan J. Auerbach & Martin Feldstein eds., 2002) (describing the Atkinson-Stiglitz result that, under a certain set of assumptions, there should be no taxes on capital).

[23] *See* Liscow, *Is Efficiency Biased?*, *supra* note __, at 1652.

[24] Of course, there are exceptions. *See, e.g.*, A. Mitchell Polinsky & Steven Shavell, *The Fairness of Sanctions: Some Implications for Optimal Enforcement Policy*, 2 AM. L. & ECON. REV. 223 (2000).

[25] *See, e.g.*, N. Gregory Mankiw et al., *An Open Letter*, GREG MANKIW'S BLOG (Mar. 5, 2015), http://gregmankiw.blogspot.com/2015/03/an-open-letter.html (open letter from more than a dozen prominent economists to congressional leaders arguing that "[t]rade is beneficial for our society as a whole, but the benefits are unevenly distributed" yet "economy-wide benefits resulting from increased trade provide resources[,]" which can be used to "help[] those who are adversely affected"); Robert Whaples, *The Policy Views of American Economic Association Members: The Results of a New Survey*, 6 ECON. J. WATCH 337, 340 (2009) (finding support among economists for the position that the U.S. should continue to liberalize trade and increase support for affected workers).

[26] KAPLOW & SHAVELL, FAIRNESS VERSUS WELFARE, *supra* note __; Louis Kaplow & Steven Shavell, *Any Non-Welfarist Method of Policy Assessment Violates the Pareto Principle*, 109 J. POL. ECON. 281 (2001).

[27] Though this is the dominant view, there have been a variety of internal critiques to this view as well. *See* Zachary Liscow, Note, *Reducing Inequality on the Cheap: When Legal Rule Design Should Incorporate Equity as Well as Efficiency*, 123 YALE L.J. 2478, 2481 & n.7 (2013) (collecting citations); Chris Sanchirico, *Taxes Versus Legal Rules as Instruments for Equity: A More Equitable View*, 29 J. LEGAL STUD. 797, 805-06 (2000); *see also* Chris Sanchirico, *Deconstructing the New Efficiency Rationale*, 86 CORNELL L. REV. 1003 (2001).

There should be no social spending (e.g. on healthcare) or regulations aimed at helping out poor people for non-efficiency reasons. And so on. In short, one-pieism leaves little room for law to address inequality—unless it's just an incident to increasing efficiency.

The standard story thus boils down policy into one pie made up of the willingness to pay of each individual for the slice of harms, public goods, and income that she receives. The views of the general population about what is in the slices (healthcare and environmental health versus bananas and automobiles) play no role. And the process by which the final arrangement comes about—whether people, say, have income because they worked for it or because they received it from the government[28]—also plays no role.

After those efficient nontax policies, the second step is then to take the economic pie and divide it up equitably through taxes and transfers. This *overall distribution* of the economic pie is the one place where lay views are sometimes taken to matter.[29] "Optimal" taxes use a social welfare function that aggregates individuals' utilities to determine the taxes that each person pays. The goal is to raise a given amount of money for public goods while also "redistributing" income from the rich to the poor. The prescriptive element of "efficient nontax policies" depends upon these taxes and transfers happening.[30] The standard story thus requires "one pie" in that the political process in fact treats distribution through various means the same way. Whether the pie consists of government-provided child care or taxes and transfers or guaranteed environmental quality, policy will ultimately arrive at the same distributional outcome, so that it makes sense to maximize the size of the pie before dividing it up.

The theory of optimal taxation dates to the 1970s.[31] It has played an important role in the development of modern law and economics.[32] But, though the basic logic is old, it was not until more recently—in the 2000s—that optimal tax economists started producing specific, empirically-based estimates of what amount of redistribution would be necessary in order to maximize welfare.[33] Economists have now extensively studied the tax rates required to achieve a utility-maximizing distribution of income, given the behavioral response to taxation,[34] though this optimal taxation literature has received little notice in the legal literature outside of tax scholars themselves.[35] This Article is the first to carefully juxtapose that high level of predicted redistribution with the substantially more modest redistribution we see in reality, and draw out implications for law and economics.

Redistribution is driven by the poor's higher marginal utility of consumption. But optimal redistribution does not fully equalize income because, under such a scheme, incentives to work would be so dulled that welfare would actually decrease because there is less to redistribute to the poor. A key aspect of the "optimal" tax is that only two factors determine it: people care

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[28] Of course, the fact that working for money involves costly labor would be factored into the analysis. But the income itself would be treated the same.

[29] KAPLOW & SHAVELL, FAIRNESS VERSUS WELFARE, *supra* note __ at 24-27.

[30] Liscow, *Is Efficiency Biased?*, *supra* note __, at 1664; Fennell & McAdams, *supra* note _.

[31] James A. Mirrlees, *The Theory of Optimal Taxation*, *in* 3 HANDBOOK OF MATHEMATICAL ECONOMICS 1197 (Kenneth J. Arrow & Michael D. Intriligator eds., 1986) (describing the classic treatment).

[32] Kaplow & Shavell, *Redistributing Income, supra* note __

[33] Emmanuel Saez, *Using Elasticities to Derive Optimal Income Tax Rates,* 68 REV. ECON. STUD. 205 (2001).

[34] N. Gregory Mankiw, Matthew Weinzierl & Danny Yagan, *Optimal Taxation in Theory and Practice*, 23 J. ECON. PERSP. 147 (2009) (summarizing the literature); Peter Diamond & Emmanuel Saez, *The Case for a Progressive Tax: From Basic Research to Policy Recommendations*, 25 J. ECON PERSP. 165 (2011) (disagreeing with some aspects of Mankiw, Weinzierl & Yagan, but establishing many points of consensus).

[35] For an example of tax scholars' discussion of optimal taxation, see Joseph Bankman & Thomas Griffith, *Social Welfare and the Rate Structure: A New Look at Progressive Taxation*, 75 CALIF. L. REV. 1905 (1987).

about their own income, and society values redistributing income toward the poor. Of course, there is no exact agreement on what an "optimal" utilitarian income tax would look like.[36] However, there is broad agreement on several features.[37]

First, optimal tax theory typically prescribes a large cash "demogrant" (essentially, a universal basic income) of several thousand dollars, though the exact size is unclear.[38] This demogrant goes by many names, but receives support from some on the left and the right. For example, Milton Friedman long advocated for such a "negative income tax," essentially a universal basic income by a different name.[39] Most recently, a sophisticated estimation by economist Emmanuel Saez recommends a demogrant of $11,900 (in 2018 dollars).[40]

Second, the demogrant is taxed away at fairly high marginal tax rates for moderate income-earners (very roughly those earning beneath the median income). The reason is that lots of taxpayers earn *at least* small amounts of income, so taxing this portion of the income of most taxpayers will raise a lot of money while distorting the behavior of few taxpayers, since most taxpayers will earn well beyond that amount in any case.[41] Nevertheless, this creates a large disincentive to work for low-income taxpayers—indeed, Saez estimates a resulting nonemployment rate of 13.8% because of the large demogrant and high taxes on the poor. The disincentive to work for lower-income earners is worth incurring because of the taxes collected on higher-income earners. In some models, marginal tax rates even go down somewhat for higher income-earners because high marginal taxes on the rich are a double-edged sword.[42] On the one hand, the rich have a lower marginal utility of consumption, so redistributing more money from the rich (who get less utility from their last dollar) to the poor (who get more utility from that dollar) will increase net societal utility. On the other hand, few people earn high incomes, so taxes on high incomes distort behavior while raising relatively little money, suggesting lower marginal tax rates will more efficiently raise revenue.[43] Other models do not

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[36] See, for example, the debate between Mankiw, Weinzierl, and Yagan on one side and Diamond and Saez on the other. Mankiw, Weinzierl, & Yagan, *supra* note ___ at 155-59; Diamond & Saez, *supra* note ___ at 175-77.

[37] *Id.* Important, the features here are on taxes on labor, but not capital, income. The traditional view has been to have low, possibly even zero, tax rates on capital income. Mankiw, Weinzierl, & Yagan, *supra* note __. But that view is under some flux. Diamond & Saez, *supra* note ___. For the purpose of this Article, view capital income as in the same category as "nontax" legal rules, as it is not a tax on labor income.

[38] Emmanuel Saez, *Optimal Income Transfer Programs: Intensive Versus Extensive Labor Supply Responses,* 117 Q.J. ECON. 1039, 1059-66 (2002).

[39] MILTON FRIEDMAN, CAPITALISM AND FREEDOM (1962), http://circuloliberal.org/livros/capitalismo-e-liberdade.pdf; Robert Moffitt, *Welfare Work Requirements with Paternalistic Government Preferences*, 116 ECON. J. F441, F441 (2006).

[40] Saez, *supra* note ___ at 1060 tbl. 1 pnl. B (showing a guaranteed income of $7,300 in 1996 dollars). If anything, this demogrant estimate is small, given recent estimates. *See* Raj Chetty, *Bounds on Elasticities with Optimization Frictions: A Synthesis of Micro and Macro Evidence on Labor Supply*, 80 ECONOMETRICA 969, 1008 (2012) (showing that the average estimate of the extensive margin elasticity is 0.25, which would imply an even larger demogrant than the one described in the text above). Importantly, this analysis does not include "tagging," allowing larger transfers to those, like the disabled, who have lower earnings abilities; incorporating tagging would lower the size of the demogrant. Nor does it include the possibility of provision of services like healthcare, which would also presumably lower the size of the optimal demogrant.

[41] In technical terms, the best way to raise money from middle and high-income earners is to have high tax rates on their "inframarginal" earnings, the dollars that they earn that are far from their decision-making margin. For example, if a worker makes $40,000 per year and the government places high taxes on any earnings below $25,000, the worker is unlikely to cut back their hours in order to get under the $25,000 threshold.

[42] Mankiw, Weinzierl & Yagan, *supra* note ___.

[43] Saez, *supra* note ___, at 1061; Mankiw, Weinzierl, & Yagan, *supra* note ___ .

imply that taxes go down with income, but those models still have high taxes on lower-income workers; for example, Saez's model has 37% marginal tax rates on the poor.[44]

Third, optimal tax theory says that, as inequality increases, taxes should become more redistributive.[45] That is, as the share of income earned by those with the highest incomes goes up, their tax rates should go up.[46] This makes sense: as the rich get richer, their marginal utility of consumption declines yet more, making it worth taxing them more.

And, fourth, fixed attributes of people should be "tagged"[47] to observable characteristics correlated with earnings ability.[48] That is, for two taxpayers earning the same income, the one with the characteristics that are correlated with having the higher earnings potential, like height, should be taxed more.[49] While taxing income incentivizes people to work less, taxing based on *fixed* characteristics that are correlated with earnings ability still partially taxes those who can earn more but provides no disincentive to work—fixed characteristics cannot be changed. In the extreme, if the government were omniscient, it could tax based on knowledge of an individual's earnings ability and not cause any distortion at all, since people would not be able to reduce their tax burden by changing their behavior.

The result of this two-step is what I call "one-pieism:" the idea that there is one economic pie to be maximized, and the goal of distributive government policy is to find the most "efficient" way to achieve a given distributive end. The goal is merely to have an efficient level of harm to individuals while achieving a fair ex post distribution of dollars among those individuals. In other words, it is the idea that tax and nontax policies with the same distributive impact perfectly substitute for each other in solving the distributive problem because all that matters is the size of the slice of pie that each person has. The next Section shows how such a view seems to conflict with commonly-held lay views.

II.   Common Views About Distributive Problems

This Section develops a maintained hypothesis about the commonplace social and political psychology of voters. By "maintained hypothesis," I mean that there is considerable evidence to believe that this is a good description of the world, but the case is hardly airtight. This maintained hypothesis is that, in contrast to the standard economic model, many ordinary people care about desert in taxation based on pretax income. That is, if people earn money, they deserve to keep some of it, and, if they work less, they—in some ways—deserve less money, all for reasons unrelated to incentives to work and save. This commonplace view is inconsistent with the standard economic model for reasons relating to the hoary details of optimal tax theory, and the standard model's prescriptions are deeply undermined in the presence of desert-based views. To explain why people think this way about taxes but still support redistribution elsewhere, the Article develops the idea of "mental policy accounts." That is, across policies, many ordinary people do not think like economistic social planners, trading off one policy against another to find the most efficient way to redistribute. Rather, to a large extent, they have

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[44] Saez, *supra* note ___, at 1061.

[45] Mankiw, Weinzierl & Yagan, *supra* note ___ , at 159-61; Diamond & Saez, *supra* note ___, at 189.

[46] SHEFFRIN, *supra* note ___ , at 130-31 (2013).

[47] The idea originally comes from George A. Akerlof, *The Economics of "Tagging" as Applied to the Optimal Income Tax, Welfare Programs and Manpower Planning*, 68 AM. ECON. REV. 8 (1978).

[48] Mankiw, Weinzierl & Yagan, *supra* note ___ at 161-64; Diamond & Saez, *supra* note ___ , at 166.

[49] N. Gregory Mankiw & Matthew Weinzierl, *The Optimal Taxation of Height: A Case Study of Utilitarian Income Redistribution*, 2 AM. ECON. J.: ECON. POL'Y 155 (2010).

category-by-category views about what is just for a given policy, despite the potential gains from trading off across policies. Thus, distributive views can be different between taxation and other means of redistribution, as well as different between taxation and overall distribution.

A. Taxation Should Reflect Desert

The previous Section described the standard approach in "optimal" taxation—the welfare-maximizing distribution through taxes under a set of one-pieist assumptions that then allows nontax legal rules to be "efficient." This subsection describes the major ways in which the standard optimal tax model differs from common views about just taxation.

Many people think that people "deserve" to keep part of their income. The seminal statement of such desert comes in Liam Murphy and Thomas Nagel's *The Myth of Ownership: Taxes and Justice*, in which they argue that it is a myth that an individual could be an "owner" of her pretax income, since that pretax income is determined by legal structures for which she has little direct responsibility. They nevertheless describe the "enormous appeal" of what they call "everyday libertarianism" in taxation.[50] They root the commonplace view in two ideas: property rights to pretax income and "desert in market rewards." By the term "everyday libertarianism," they mean not the literal Nozickian libertarian idea that people have an absolute property right to their pretax income, but rather the ideas that result because it is difficult "banishing [the ideas of property rights in pretax income and "desert in market rewards"] from our everyday thinking."[51] Just because such thinking "may not survive cursory critical reflection"—since our pretax incomes are themselves products of the legal regime created by the state—does not stop those views from being widely held.[52] Regarding property rights, they note that "people [may] intuitively feel that they are in an absolute sense morally entitled to their net incomes," generating a sense of property rights to those incomes that hinder progressive taxation.[53] Regarding desert, they argue that "the unreflective ideas that we may have unqualified moral entitlement to what we earn in the market and that higher market returns are in some sense deserved as a reward arise naturally within the everyday outlook of participants in a capitalist economy."[54] It is commonplace to think that people deserve to be rewarded for hard work and thrift, and the market does, to some extent, reward those virtues with higher incomes. However, "[t]he natural idea that people deserve to be rewarded for thrift and industry slides into the much broader notion that all of pretax income can be regarded as a reward for those virtues."[55]

Notwithstanding their insistence that everyday libertarianism is not just morally wrong but illogical, Murphy and Nagel acknowledge that a change in mindset would require a "shift to a purely conventional conception of property," which they "acknowledge [is] counterintuitive," as "[t]axes are naturally perceived by most people as expropriations of their property."[56] Put differently,

> We recognize that it is a lot to hope that this philosophical point [that property is conventional] should become psychologically real to most people. Pretax economic transactions are so salient in our lives that the governmental framework that determines

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[50] *Id.* at 34.
[51] *Id.*
[52] *Id.*
[53] *Id.* at 35.
[54] *Id.* at 36.
[55] *Id.* at 36.
[56] *Id.* at 175.

their consequences and gives them real meaning recedes into the background of consciousness. What is left is the robust and compelling fantasy that we earn our income and the government takes some of it away from us, or in some cases supplements it with what it has taken from others.[57]

They suggest that "[c]hanging this habit of thought would require a kind of gestalt shift, and it may be unrealistic to hope that such a shift in perception could easily become widespread."[58] The claim is not that taxation is impossible; that claim is, of course, false. Rather, the claim is that everyday libertarian views lead to a kind of drag on the ability of the state to redistribute through taxes.

The normative starting point of Murphy and Nagel is perfectly consistent with optimal tax theory, and the commonplace "everyday libertarianism" that they describe is not consistent with it. Optimal tax theory imagines all resources combined into one pie and then reallocated to maximize welfare based on ultimate outcomes. It does not matter who has what to begin with. Of course, allowing people to keep part of their income is important to encourage work. But desert-based views are saying something different. With such views, pretax income generates desert, so that more unequal pretax income will tend to increase the desired inequality in post-tax incomes, even if incentives do not play a role. In contrast, for the optimal tax theory used in law and economics, each individual's income is just used to achieve the ultimate social income; there are no rights and there is no desert based on pretax income.

Recent evidence from Matthew Weinzierl, Steve Sheffrin,[59] and others reinforce the view that a lot of people don't view taxes in exclusively welfarist terms. Based on an extensive reading of the literature on taxation and original research on redistributive views, Sheffrin writes in *Tax Fairness and Folk Justice*,

[o]ne clue to ordinary ideas of justice is that in their day-to-day lives, individuals [are] often much more concerned about *process and procedure* than they are about *purely distributional issues*, or "who gets what." Expert theories of justice inevitably focus on distribution. Folk justice may include distributional concerns, but also includes procedural concerns.[60]

In particular, behavior consistent with "equity theory"[61] in psychology may be helpful in understanding part of the typical American's views around taxation. The theory holds that "fair" outcomes are characterized by a rough proportionality between input and output.[62] In the case of taxes, that means a rough proportionality between the amount one pays in taxes and the benefits one receives from the government. Of course, defining exactly what proportionality means is challenging. The key point for the present purposes though is that *desert matters*: people have some entitlement to the money that they earn, and those who do not earn lack some entitlement.

Our political discourse reflects such concerns. For example, President George W. Bush often described tax cuts as letting Americans "keep more of their hard-earned dollars," an apparent appeal to hard work generating desert.[63] While Bush mentioned incentives too, the issue of distributive justice—setting tax rates based on need, a key factor in optimal taxation—was

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[57] *Id.* at 176.

[58] *Id.* at 175.

[59] SHEFFRIN, *supra* note __.

[60] *Id.* at 3.

[61] *Id.* at 35.

[62] WALSTER, WALSTER & BERSCHEID, *supra* note ___, at 10.

[63] President George W. Bush, President's Weekly Radio Address, (Apr. 15, 2006) https://georgewbush-whitehouse.archives.gov/news/releases/2006/04/text/20060415.html.

often entirely absent. Even today's liberal crop of Democratic presidential candidates seem to at least partially agree: with the exception of Andrew Yang (who polls in the low single digits),[64] even the most liberal candidates do not propose providing large unrestricted cash transfers to the poor. And Democrats commonly use similar language about desert.[65]

While there have now been several survey experiments done on the topic,[66] this Article will focus on one illustrative survey experiment. Weinzierl developed a compelling survey that showed the importance of desert based in pretax income.[67] He gives survey respondents a hypothetical in which two people have different pretax incomes, one richer (with an income of $60,000) and one poorer (with an income of $30,000). But the parties only get these incomes if they agree to jointly pay $18,000 for a public good. This setup removes any possible incentive effects of taxation, since the parties are just given the money irrespective of behavior. Respondents are then asked how a tax and subsidy burden should be divided between the two individuals.[68] A typical social welfare function would suggest equalizing the incomes of the two people, since there is a declining marginal utility of income. That is, Person A should pay for the entire public good and also transfer $6,000 to person B, so that both end up with $36,000. However, a large majority of respondents—75%—stop short of full equalization, and many stop well short of equalization.[69] Put differently, the entirely arbitrary "pretax income" appeared to have moral weight. Pretax incomes appear to generate desert.

Of course, though Weinzierl produces a variety of robustness checks, the evidence can be interpreted in a variety of ways. And nothing in the experiment suggests that people are not also motivated in part by standard utilitarian concerns; there is some redistribution after all. Nevertheless, this evidence suggests that people have some views quite distinct from the utilitarian redistributionist ones that economists typically focus on. Pretax income—even if entirely arbitrary, like natural ability over which people have no control—appears to drive many people's views of fair taxation.

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[64] *2020 Democratic Presidential Nomination*, REAL CLEAR POLITICS, https://www.realclearpolitics.com/epolls/2020/president/us/2020_democratic_presidential_nomination-6730.html (Accessed September 16, 2019) (showing no poll higher than 5% between April and early September of 2019).
[65] For example, in response to the question, "Does anyone deserve to have $1 billion?" Senator Kamala Harris responded, "If they earn it and work hard for it, sure." Alexander Burns Sydney Ember Jonah M. Kessel, & Haeyoun Park, *Meet the Candidates: Does Anyone Deserve to Have a Billion Dollars?*, N.Y. Times (2019), https://www.nytimes.com/interactive/2019/us/politics/billionaires-democratic-candidates.html. President Barack Obama said, "Understand we've never begrudged success in America. We aspire to it. We admire folks who start new businesses, create jobs, and invent the products that enrich our lives. And we expect them to be rewarded handsomely for it." *President Obama on Inequality (transcript)*, Politico (Dec. 4, 2013, 1:54 PM EST), https://www.politico.com/story/2013/12/obama-income-inequality-100662. Indeed, Daniel Markovits argues that an ethos of "meritocracy" pervades our age, including the idea that, because success is meritocratic, the earnings from career success are thus deserved. DANIEL MARKOVITS, THE MERITOCRACY TRAP (2019).
[66] For other recent work, see Jimmy Charite, Ray Fisman, and Ilyana Kuziemko. *Reference Points and Redistributive Preferences: Experiment Evidence* (Nat'l Bureau of Econ. Research, Working Paper No. 21009, 2016); Ray Fisman, et al. *Do Americans Want to Tax Capital? Evidence from Online Surveys*. (Working paper) (2016); Weinzierl, *A Welfarist Role for Nonwelfarist Rules, supra* note _; Weinzierl, The Promise of Positive Optimal Taxation, *supra* note __; Ilyana Kuziemko, et al. *How elastic are preferences for redistribution? Evidence from randomized survey experiments*, 105. AM. ECON. REV. 1478 (2015); Alberto Alesina, Stefanie Stantcheva & Edoardo Teso, *Intergenerational mobility and preferences for redistribution*, 108 AM. ECON. REV 521 (2018).
[67] Weinzierl, *Popular Acceptance, supra* note ___.
[68] The interface clearly showed how much money each party ended up with given a proposed allocation, making outcomes salient. *Id.* at 58.
[69] *Id.* at 56.

Building on similar reasoning, N. Gregory Mankiw makes a normative case that a "just deserts" perspective on taxation, in which "people should receive compensation congruent with their contributions," is the correct goal of taxation.[70] He argues that such a view "is more consistent with our innate moral intuitions" than the standard optimal tax model.[71] For example, he suggests that many people would still think that higher-skilled people should be paid more, even if there were no incentive reason for paying them more.[72] Yet the optimal tax model would say that, absent incentive effects, everyone should have the same after-tax income. And, to boot, since the highly-skilled are so much more productive, they should be forced to work harder to provide more resources to be redistributed. That is, since the costs of work are the same for everyone but the benefits for society of work are so much higher for the high-skilled, the high-skilled should work much more. That is an intuition that may be shared by few.

Perhaps it is unsurprising then that real-world policy does not reflect the optimal tax ideal. Existing institutions provide additional evidence of the dissonance between the standard economic story with optimal taxes and commonplace views about taxation, assuming that the real-world evolution of political institutions reflects those commitments to some extent. Indeed, no tax system even closely approximates the implications of one-pieist methodology.[73]

Recall the typical implications of optimal tax theory. The first two implications of optimal tax theory are that there should be a large demogrant that everyone receives that is then taxed away at fairly high marginal tax rates for those at low incomes. No developed country in the world gives out large demogrants.[74] This outcome is consistent with the importance of desert and a resulting distaste for unrestricted cash transfers: the state does not give out money to those who do not work for it, without some strings attached. And to those who do work at low incomes, it would be unfair to have high tax rates because they would not be getting a fair share of output of their labor. Indeed, as suggested above, those high tax rates would discourage large numbers of people from working at all, eliminating their workplace contribution to the state altogether.

The third prediction of optimal tax theory is that, as inequality goes up, taxes become more redistributive. Yet, despite the well-documented rise in income inequality,[75] nothing of the

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[70] N. Gregory Mankiw, *Defending the One Percent*, 27 J. ECON. PERSP. 21, 32 (2013); N. Gregory Mankiw, *Spreading the Wealth Around: Reflections Inspired by Joe the Plumber*, 36 E. ECON. J. 285 (2010).

[71] Mankiw, *One Percent, supra* at 33.

[72] *Id.* at 29.

[73] Mankiw, Weinzierl & Yagan, *supra* note ___, at 159-61.

[74] Note that some Gulf States have an "implicit government job guarantee" for nationals, but that is different from a demogrant because it involves work. Steffen Hertog, *The GCC's National Employment Challenge*, WASH. POST (July 31, 2014), https://www.washingtonpost.com/news/monkey-cage/wp/2014/07/31/the-gccs-national-employment-challenge/?utm_term=.01a5916a1fd3. As well, some Scandinavian countries have generous unemployment programs. For example, unemployment insurance in Denmark allows beneficiaries to receive up to 90% of their previous salary. However, receipt of unemployment benefits requires previous work experience (with exceptions for those who have just finished education or training) and active job searching, and a person is only entitled to benefits for 2 years within a 3-year period. *Denmark–Unemployment Benefit*, EUR. COMMISSION: EMP., SOC. AFFAIRS & INCLUSION, http://ec.europa.eu/social/main.jsp?catId=1107&langId=en&intPageId=4496. Again, this policy is not a demogrant because it is tied to work. Finally, the UK passed a small Child Trust Fund, in which children were given modest savings accounts, but these are far smaller than the sum of annual demogrants and in any case only go to children.

[75] Thomas Piketty & Emmanuel Saez, *Income Inequality in the United States, 1913 – 1998*, 118 Q.J. ECON. 1 (2003). The extent of the rise is disputed. *E.g.* Richard Burkhauser et al., *Recent Trends in Top Income Shares in the United States: Reconciling Estimates from March CPS and IRS Tax Return Data*, 94 REV. ECON. & STAT. 371 (2012); Alan

sort has happened. A striking piece of evidence consists of the relatively low support for high taxes on the rich: recent surveys show only roughly half of Americans want high taxes on the rich.[76] The large numbers of relatively poor people who do not want higher taxes on the rich is especially striking, with 26% earning less than $25,000 opposing higher taxes on the rich and an additional 17% neutral.[77] This result is also consistent with the importance of desert: people get what they deserve. And, if inequality goes up, that does not necessarily mean that they should pay more because their benefit from the state may not have increased.

A fourth implication of optimal tax theory is that people's features should be "tagged." There should be a tax on height, for example, because it is correlated with higher earnings. In practice, we do not see taxation based on "tags" like height. Nor does a tax based on height seem like a plausible thing to do. To many, it would seem unfair to tax two people differently if they earn the same income, but one is taller than the other. And, indeed, evidence from survey experiments confirms that very few people believe that tagging is appropriate in tax policy.[78] This result is also consistent generally with an aversion to setting taxes on the basis of only incentives and redistribution, rather than also internal norms like desert. If two people produce the same amount, they should be treated the same by the state, even if one is tall and one is short.

Recent advances in the empirics of taxation have allowed economists to quantify the redistributive views implicit in the tax code that we have versus what we would see given alternative redistributive views. The method, used by Nathan Hendren and others,[79] first considers the incentive effects of taxation: if people's incomes are taxed, they will tend to work and save less. And then it asks, given those incentive effects, how much people implicitly would weight, or value, a dollar in the hands of a rich versus poor person. Hendren shows that our current tax code implicitly values a dollar in the hands of someone at the 10th percentile of income 1.9 times as much as someone at the 90th percentile of income.[80]

By contrast, consider what individuals' own personal behavior regarding risk implies.[81] For themselves, they value an extra dollar about *thirteen*[82] times more highly if they had an income of 14,000 (the 10th percentile of income) than if they had an income of $179,000 (the 90th percentile of income).[83] The reason is that people value the things (often necessities) they would

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J. Auerbach, Laurence J. Kotlikoff & Darryl R. Koehler, *U.S. Inequality, Fiscal Progressivity, and Work Disincentives: An Intragenerational Accounting* (Nat'l Bureau of Econ. Research, Working Paper No. 22032, 2016).

[76] Emmanuel Saez & Stefanie Stantcheva, *Generalized Social Marginal Welfare Weights for Optimal Tax Theory*, 106 AM. ECON. REV. 24 App. 14-20 (2016) (presenting survey evidence suggesting that virtually no one supports tagging in a particular context); Karlyn Bowman & Andrew Rugg, *Public Opinion on Taxes: 1937 to Today,* AM. ENTERPRISE INST. 25 (Apr. 2012), http://www.aei.org/wp-content/uploads/2012/04/-aei-public-opinion-study-on-taxes-2012_082833686158.pdf; SHEFFRIN, *supra* note ___ at 119-20.

[77] Rebecca Reed-Arthurs & Steve Sheffrin, *Windows into Public Attitudes Towards Redistribution*, 102 PROC. OF THE NAT'L TAX ASS'N 165 (2009).

[78] Emmanuel Saez & Stefanie Stantcheva, *supra* note _ at 33.

[79] Hendren, *Efficient Welfare Weights*, *supra* note _; Benjamin B. Lockwood & Matthew Weinzierl, *Positive and Normative Judgments Implicit in US Tax Policy, and the Costs of Unequal Growth and Recessions*, 77 J. MONETARY ECON. 30 (2016).

[80] Hendren, *Efficient Welfare Weights*, *supra* note _, Figure 6, p. 24.

[81] These results are conservatively, and roughly, approximated by the "logarithm" function.

[82] For incomes, *see Average, Median, Top 1%, and Income Percentiles in 2018 in the United States*, DQYDJ.COM, https://dqydj.com/united-states-household-income-brackets-percentiles/ (last visited Sept. 24, 2019).

[83] See, for example, Raj Chetty, *A New Method of Estimating Risk Aversion*, 96 AM. EC. REV. 1821 (2006) (finding a "coefficient of relative risk aversion" of 1 approximately, which has this implication). The "logarithmic" utility function implied by this analysis is also suggested by cross-country studies measuring stated happiness. Nestor Gandelman & Rubén Hernández-Murillo, *Risk Aversion at the Country Level,* (2015): 53-66. Note that, as Chetty (p.

be buying at low incomes more than the things (often luxuries) they would be buying at high incomes. The results come from looking at, for example, how much people are willing to pay for insurance, which essentially redistributes money to times when the individual is poorer because of loss of an asset like a house burning down.

So our current tax code redistributes across people nowhere remotely close to the amount that individuals do internally for themselves, given the implicit ratio of values between the 10th and 90th percentile income-earners of 1.9 in the tax code versus 13 internal to individuals. Thus, the tax code implicitly only gives poor individuals 15% of the weight implied by people's own behavior. Of course, there are major issues of interpersonal comparability in going from within-person to between-person comparisons. And it is difficult to know what the appropriate social welfare weights are. Nevertheless, this vast divergence is at least suggestive.

Inferring commonplace views from existing policies while trying to offer recommendations to improve policy leads to an obvious circularity problem.[84] Policies could look the way they do for many reasons, including political capture.[85] Nevertheless, the difference between what taxes would need to do under optimal tax theory and what they in fact do is remarkably gaping. This is especially so because there are no technological barriers to any of the implications of optimal taxes: a demogrant, high marginal tax rates for low-income earners, or taxation based on tags. We have just chosen not to do those things, along with the rest of the developed world. And, in any case, as the next subsection will explain, another account would need to explain the great deal of redistribution through nontax means. Maybe asking the tax code to provide the redistribution necessary for a just society is simply asking ordinary people to accept something inconsistent with their moral intuitions.

More broadly, we are left with a major puzzle: One of the two foundations for the law and economics two-step is imposing an "optimal" tax. Yet, people appear to hold views at odds with the implications of optimal taxation, and current policy is far off from those implications. Later Sections will return to potential policy implications of this dissonance. The writers described here disagree about the extent to which notions of right and desert to pretax income should be considered normatively. Weinzierl writes down normative models in which nonstandard views are at least partly normatively correct. Mankiw holds an even stronger view that a "just deserts" theory of taxation is the correct one. Murphy and Nagel find any normative view of taxation based on desert illogical. Sheffrin is inclined to at least partly consider these views on the basis of "consonance."[86] But all agree that these views are commonplace, which is the only claim this Article makes. What has been missed in the debate thus far—which has focused on the implications of these views *for taxation*—is the implication of the commonplace

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1821) points out, many other estimates imply even higher risk aversion, which suggest an even larger divergence in distributional weights between the rich and the poor.

[84] *See, e.g.*, RAYMOND GUESS, PHILOSOPHY AND REAL POLITICS 49-50 (2008) (describing how conceptual instruments used to analyze social reality are often inextricable from social reality itself: "Often, you can't see the original problem clearly until you have the conceptual instrument, but having the instrument can then change the 'real' situation with which one is confronted so that other, unforeseen problems emerge.").

[85] *See, e.g.*, Philip Bump, *Who Actually Wants Congressional Republicans to Pass Trump's Tax Bill?*, WASH. POST (Nov. 2, 2017), https://www.washingtonpost.com/news/politics/wp/2017/11/02/who-actually-wants-congressional-republicans-to-pass-trumps-tax-bill; Marissa Schultz, *GOP's Big Donors Threaten to Close Wallets if Tax Reform Isn't Passed*, N.Y. POST (Nov. 6, 2017), https://nypost.com/2017/11/06/gops-big-donors-threaten-to-close-wallets-if-tax-reform-isnt-passed; Dylan Scott, *House Republican: My Donors Told Me to Pass the Tax Bill or "Don't Ever Call Me Again"*, VOX (Nov. 7, 2017), https://www.vox.com/policy-and-politics/2017/11/7/16618038/house-republicans-tax-bill-donors-chris-collins.

[86] SHEFFRIN, *supra* note __ at 8-9 (2013) (describing "consonance" with existing policies).

views for vast array of *nontax policies*, given that tax policy is set by Congresspeople who are at least partly answerable to voters.

   B. Why? Mental Policy Accounts

   One explanation for why people have nonstandard views about policy is that they are normatively correct. This Article, for the most part, puts that explanation to the side. To be as conventional as possible within economics, this Article assumes that the standard normative goals of maximizing societal welfare without regard to the means of redistribution are the right ones. Instead, the Article introduces a novel explanation of commonplace redistributive views: "mental policy accounts," or partially compartmentalized category-specific views about good policy that do not reflect a holistic vision of tradeoffs across policies. Importantly, with partially compartmentalized policy views, it is completely consistent to be resistant to redistribution through the *specific process* of taxes, while at the same time supporting either more equal outcomes overall or more egalitarian provisions through specific goods (like healthcare) or processes (like regulatory cost-benefit analysis).

   The explanation builds on work in economics on "mental accounts." The example typically given for mental accounting is savings behavior.[87] As Richard Thaler puts it, in standard economics, a "key assumption is *fungibility*:" people should treat a dollar the same way regardless of how they receive it.[88] But people do not act that way. For example, even though a dollar is basically the same whether it is earned through one's wages, appreciation in stock, a dividend, or one of many other means, people often have very different likelihoods of increasing consumption as wealth increases in the different "mental accounts." Thaler's explanation is that people adopt prudent rules-of-thumb in their financial decision-making. For example, believing that they should "live within your means," people consume out of their current wage income or dividends much more than increases in the value of their stock.[89]

   The maintained hypothesis of this Article is that, in many ways, individuals view policy in the same way that they view their personal mental accounts: with prudent rules of thumb that apply to each account. Economists tend to view welfare maximization as beginning with one big pie, containing taxes, environmental health,[90] healthcare, education, transportation spending,[91] minimum wage laws, etc., that can be distributed with perfect commensurability across policies as the social planner sees fit. This Article hypothesizes that many people, instead, view distributional issues on a category-by-category basis, like they view their personal finances. In the words of Michael Walzer, different goods are in different "spheres of justice," each with its own notion of the proper role of the state in adjudicating distributive issues.[92] For example, as

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[87] Richard H. Thaler, *Anomalies: Saving, Fungibility, and Mental Accounts*, 4 J. ECON. PERSP. 193 (1990) (arguing mental accounts prevent people from thinking about money as fungible across types of wealth); Richard H. Thaler, *Mental Accounting Matters*, 12 J. BEHAVIORAL DECISION MAKING 183 (1999) (same).

[88] Thaler, *Anomalies*, *supra* at. 194.

[89] *Id.* at 195.

[90] Maureen Cropper, Alan Krupnick & William Raich, *Preferences for Equality in Environmental Outcomes* (Nat'l Bureau of Econ. Res., Working Paper 22644, 2016).

[91] *See, e.g.*, Todd Litman, *Evaluating Transportation Equity*, VICTORIA POL'Y INSTIT. 2 (July 24, 2018), http://www.vtpi.org/equity.pdf (calling "[t]ransportation equity analysis" both "important and unavoidable" because "transport planning decisions often have significant equity impacts, and equity concerns often influence planning debates").

[92] MICHAEL WALZER, SPHERES OF JUSTICE: A DEFENSE OF PLURALISM AND EQUALITY 7-11 (1984).

just described, people have policy views on taxes, which are often not just about proper incentives and redistributing from the rich to the poor, but rather are often partly about desert to pretax incomes.

This Article focuses on the tax mental policy account. A description of all potential policies is, of course, beyond the scope of the Article. But to illustrate distributional views in a different mental policy account, consider those for in-kind "necessities," for which there appears to be widespread support for provision more egalitarian than the efficient prescription. Thomas Scanlon describes how, when making moral judgments about government policy, "it seems clear that the criteria of well-being that we actually employ . . . are objective" rather than based totally upon the subjective views of individuals, as in the optimal tax model.[93] And, in particular, people commonly consider the "urgency" of the desire, such that, for example, "health is more important than amusement," making government support for healthcare more justified than support for amusement.[94]

There are various indications of the mental policy account for necessities. For one, our rhetoric surrounding necessities is often about rights. For example, in-kind rights "including food, clothing, housing and medical care" are delineated in the UN Declaration of Human Rights;[95] it does not say that people should get cash to spend as they wish. Even in the U.S. many seem to believe in a "right" to healthcare based on polls.[96] And across countries there is widespread in-kind redistribution in areas considered necessities, such as healthcare, education, housing, food, and childcare.[97] Some of that spending can be justified on standard efficiency grounds, such as high returns to education for children who cannot pay for it themselves.[98] But not all spending can be justified that way. For example, there is lots of redistribution through housing even to the elderly, who could presumably choose whether to spend cash on housing or other things absent a behavioral failing. And the U.S. likely provides healthcare to people that costs far in excess of what poor people would be willing to pay for it.[99] This policy is so notwithstanding the traditional efficiency analysis suggesting a possible Pareto improvement:

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[93] Scanlon, *Preference and Urgency*, 72 J. Phil. 655, 658 (1975). For a related normative account, see also John Rawls, Justice as Fairness: A Restatement 42 (Erin I. Kelly ed., 2001) (arguing for the provision of "primary goods" like health care "to meet the needs and requirements of citizens as free and equal").

[94] Scanlon, *supra* note __ at 660.

[95] United Nations, Universal Declaration of Human Rights, Article 25 (1948), https://www.un.org/en/universal-declaration-human-rights/.

[96] Larry Bye & Alyssa Ghirardeli, *American Health Values Survey*, Robert Wood Johnson Found. 5 (2016), https://www.rwjf.org/content/dam/farm/reports/reports/2016/rwjf437263 (finding that an overwhelming majority of Americans believe that "[e]nsuring that low income Americans have the same chance to get good quality health care as those who are better off financially" should be a "top" or "high" priority); *Healthcare System*, Gallup (last visited Feb. 22, 2019), https://news.gallup.com/poll/4708/healthcare-system.aspx (showing that since the beginning of the poll in the late 1990s, large numbers of Americans—up to 69%, but never less than 42%—thought Stern & Grossman, *supra* note_; Scott, *supra* note_.

[97] Janet Currie & Firouz Gahvari, *Transfers in Cash and In-Kind: Theory Meets Data,* 46 J. Econ. Literature 333, 335-337 (2008) (describing the in-kind programs across countries).

[98] Jonathan Gruber, Public Finance and Public Policy (2005).

[99] Consider someone in her 50s who earns $20,000 per year. Based on average expenditures, healthcare costs about $8,000 to provide to this person. Bradley Sawyer & Gary Claxton, *How do health expenditures vary across the population?*, Peterson-Kaiser Health System Tracker (Jan. 16, 2019), https://www.healthsystemtracker.org/chart-collection/health-expenditures-vary-across-population/#item-start; *2019 Health Insurance Plans and Prices*, Healthcare.gov (Accessed Sept. 18, 2019), https://www.healthcare.gov/see-plans/#/plan/results. It seems likely that someone so poor would prefer the cash to the full $8,000 in healthcare.

everyone would be better off if people unwilling to pay for a full complement of healthcare instead received money through the tax system.

One could consider many other mental policy accounts as well. For example, people seem unwilling to tolerate valuing the lives of the rich more highly than the lives of the poor for the purpose of regulatory cost-benefit analysis—which would be required in any efficient regime, since the rich are "willing to pay" more for their lives owing to their greater ability to pay.[100] For now, though, it is, at minimum, arguable that people hold category-specific views. They have views about rights in healthcare that are more egalitarian than the efficient prescription. They have views about desert after being harmed by trade deals.[101] And just because a person gets more in one category does not mean that people think that the person should get less in another category: that's how economists think, but often not how non-experts think. These category-specific views about fairness could have major implications for the right policy to adopt in a given real-world situation. Section III addresses those implications.

But why do people have these policy mental accounts? In some sense, it should not be surprising that people think this way. We have such imperfect fungibility in our everyday lives. For example, in our family lives, while there may be some trading off between partners ("you do the cleaning, I'll pick up the kids"), there are limits ("if you do all the childcare, you can spend more money on videogames").

And, as explained earlier, even in one's own personal financial decision-making, with huge individual stakes, people tend to think in these terms. So perhaps it is unsurprising that in their thinking about policy issues, where the personal stakes of one's actions like voting are trivial by comparison, they would similarly develop rules of thumb policy by policy. Just as it could be efficient for individuals to respond the same way to a one-dollar increase in stock holdings as to a one-dollar increase in take-home salary, it may be efficient for government to redistribute a dollar by looking across all policies and using the policy that best maximizes aggregate welfare. But those are really hard optimization problems, even for experts. For example, notwithstanding the broad tendency among economists to agree that the government should redistribute with taxes and transfers and make other policies "efficient," there is huge disagreement over what "efficient" policy is: Until fairly recently, economics experts tended to argue that less regulation was generally more efficient. However, in light of failures of competition, behavioral failures, and other market failures like information asymmetries, more economists now argue that government "intervention" is efficient.[102] The optimization problem

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[100] *Income Elasticity and Income Growth Estimates: Technical Memorandum* *2 (Environmental Protection Agency, Feb 5, 2016), archived at http://perma.cc/BW2Q-PFEZ (showing that willingness to pay to avoid mortality increases by between 70 percent and 110 percent in response to income doubling). Despite the clear efficiency-based logic to value the lives of the rich more, federal agencies never do, apparently due to political opposition. *See* U.S. Dep't of Transp., Revised Departmental Guidance 2016: Treatment of the Value of Preventing Fatalities and Injuries in Preparing Economic Analyses 1, 3 (2014), https://www.transportation.gov/sites/dot.gov/files/docs/2016%20Revised%20Value%20of%20a%20Statistical%20Life%20Guidance.pdf (saying that lives are not valued differently "for policy reasons"). See Exec. Order No. 12,866, 3 C.F.R. § 638 (1994) (requiring cost-benefit analysis based on efficiency in federal agencies); *see also* Michael A. Livermore & Richard L. Revesz, RETAKING RATIONALITY: HOW COST-BENEFIT ANALYSIS CAN BETTER PROTECT THE ENVIRONMENT AND OUR HEALTH 83-84 (2008) (arguing that "a cost-benefit analysis using an average value of a statistical life is unmoored from its economic justification").

[101] Dani Rodrik, *Populism and the Economics of Globalization*, 1 J. INT'L BUS. & SOC. 12 (2018), https://link.springer.com/article/10.1057/s42214-018-0001-4 (arguing that a political backlash to advanced stages of globalization was predictable).

[102] See, for example, the Economists for Inclusive Prosperity for a group of economists making this argument.

that is hard for people who spend their whole lives on the task is certainly hard for laypeople as well. And a resort to policy-specific rules of thumb about fairness—some form of desert for taxation and some form of equality or basic provision for necessities—seems a reasonable response to the vast epistemic and analytical uncertainties.

A related reason that people may have these mental accounts is difficulty monitoring politicians. People's lived experiences may have a positive correlation to the broader reality on this matter[103]—for example, people may observe how little the distributional consequences of trade deals have been offset.[104] So, people may use proxies, like fairness within each policy, to evaluate how fair policy is overall even at the cost of losing out on between-policy tradeoffs.[105]

Even Louis Kaplow and Steven Shavell, the strongest proponents of what this Article calls one-pieism, acknowledge that social norms of fairness may be important, rooting them in adaptive norms of fairness that evolved in small-group settings. Such norms play a useful role in promoting cooperation in everyday behavior. They argue that such norms ought not to have independent weight in evaluating social policy,[106] as such norms developed by the evolution of hunter-gatherers may often be irrelevant for policymaking in modern states.[107] But even they acknowledge their existence. This Article makes no claims about their normative weight, but only says that they are important social phenomena.

Overall then, the Article operates from a maintained hypothesis about the social and political psychology of voters: Many have, in significant part, desert-based views about taxes, such as thinking the well-off deserve to keep part of their earnings, and the poor deserve less unless they work for it. This thinking directly contradicts the logic underlying optimal tax theory and, in turn, the efficiency-minded stance of law and economics. They think this way because they have "policy mental accounts" for taxation and other policies, each with its own rules-of-thumb policy views. As a result, there is imperfect fungibility across the mental accounts. And distributive views about taxation—just one of many policies—do not necessarily reflect distributive views about other means or about distribution overall.

The key takeaway is that there will not be enough redistribution through taxes, economists' chosen tool. Murphy and Nagel may have perfect logic about the "myth of ownership" of one's earnings, but word has not gotten out. Nor has word gotten out on optimal income tax theory or the standard two-step prescription of law and economics. Rather, people have an aversion to both redistributionary taxation and inequality. Under the standard economic

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[103] Hayek's analysis on local and tacit knowledge are particularly instructive. *See generally* FRIEDRICH HAYEK, THE CONSTITUTION OF LIBERTY (Ronald Hamowy ed., 2011). For a lucid summary of Hayek's views on these subjects, see Fuat Oguz, *Hayek on Tacit Knowledge*, 6 J. INST. ECON. 145, 159 (2010).

[104] David H. Autor et. al., *The China Syndrome: Local Labor Market Effects of Import Competition in the United States*, 103 AM. ECON. REV. 2121, 2151 (examining the distributional effects of import competition from China and finding that "rising transfer income offsets only a small part of the decline in household earnings.").

[105] There are two components to monitoring: information-gathering about each policy and use of that information to compare policy platforms. Citizens neither gather an equal amount of information about every policy nor consider each policy dimension of a platform when comparing platforms. People are more likely to access information for issues that they care about. Shanto Iyengar, Kyu S. Hahn, Jon A. Krosnick, and John Walker, *Selective Exposure to Campaign Communication: The Role of Anticipated Agreement and Issue Public Membership,* 70 J. POL. 186 (2008). And when facing a difficult decision among party platforms, citizens often use "noncompensatory" strategies, "where either some alternatives are given little consideration or some attributes are more or less ignored," and therefore ignore many relevant between-policy tradeoffs. RICHARD R. LAU & DAVID P. REDLAWSK. HOW VOTERS DECIDE: INFORMATION PROCESSING IN ELECTION CAMPAIGNS, 257 (2006).

[106] KAPLOW & SHAVELL, FAIRNESS VERSUS WELFARE, *supra* note _, at 69-81.

[107] *Id.* at 70.

logic, these should be the same thing because taxes should do the work of redistribution. But it need not be the case that taxes redistribute. And we have good reason to think that taxes are in a separate mental account from other goods, such that many ordinary people do not expect them to be solely a tool of redistribution.

III.   What to Do? An Illustration of Democratic Cost-Benefit Analysis

In response to the maintained hypothesis, one could adopt a variety of interpretations. For example, one could question whether the normative goals of economics are the correct ones. Economists have proposed a variety of possibilities, like Mankiw's "just deserts" theory of taxation. With an eye toward being as conventional as possible according to the standard economics logic, this Article takes a different approach: as a baseline matter, the Article stipulates that the right social welfare function is the one that is standard in economics: add up the utilities of people with declining marginal utilities of consumption—that is, with nothing nonstandard. Of course, that could be the wrong social welfare function. If so, then one could let in a panoply of other concerns, including those on equality of opportunity or process values; the government would clearly be doing the wrong thing by being efficient in the standard way. So, to be most favorable toward the standard economic model, I merely follow the economics convention here. Note as well that you do not need to be convinced that the maintained hypothesis is correct—only that there is a decent chance that it is correct—for this reasoning to matter to you.

Instead, this Article interprets the maintained hypothesis as leading to a kind of political constraint. In other words, there is not just one economic pie because not all means of distribution fare equally in the political process. Since voters have mental policy accounts—and, in particular, believe that desert based on pretax income is important in the tax mental policy account—Congress will redistribute less through the tax code than is welfare-maximizing.

There are multiple concerns to the approach. I sketch responses here. First, and most basically, the relationship between voters' policy views and actual policymaking is unclear. For example, some argue that the policy preferences of none but the richest drive policy.[108] Nevertheless, it seems reasonable to argue that widespread voters' views—especially among the well-off, who are likely most inclined to value desert—have an important impact on those that they elect. A second concern is that politics can change rapidly. As the Article discusses below, this factor should be considered, including by changing policies if those views do change. The features of the maintained hypothesis, though, seem like durable features of industrialized democracies, and it also seems reasonable to predict that the psychology underlying the policies will continue into the future. A third concern is that this Article is only considering a subset of political constraints—those generated by voters' psychology. If followed broadly, political constraints could lead many places, such as placing additional weight on the views of people of Wyoming because of the existence of the U.S. Senate. But being helpful to policymakers by considering a subset of political constraints should not require consideration of *all* political

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[108] *See generally* MARTIN GILENS, AFFLUENCE AND INFLUENCE (2014) (showing that lay views correlate with policymaking—but that, controlling for the views of the well-off, the views of the poor show no relationship with actual policy); *see also* Omar S. Bashir, *Testing Inferences About American Politics: A Review of the "Oligarchy" Result*, 2 RES. & POL. 1 (2015) (criticizing the conclusion that politics is dominated by the preferences of the wealthy); J. Alexander Branham et al., *When Do the Rich Win?*, 132 POL. SCI. Q. 43 (2017) (making the same argument); Peter K. Enns, *Relative Policy Support and Coincidental Representation*, 13 PERSP. ON POL. 1053 (2015) (finding that the preferences of the middle class exert influence over policy).

constraints at once, in the same way that standard economic analyses commonly consider only one behavioral failing or other market failure.

Furthermore, the obvious response to misunderstandings leading to political constraints is to educate people: explain that property is a product of laws so that pretax income is a poor indicator of entitlement, explain that taxes are an efficient way to redistribute and that giving people choices over how to spend resources tends to maximizes welfare, and explain that heuristics that work well in small group settings may not be best for setting government policy. The project of economics—especially law and economics—the past several decades has been one of education partly along these lines, at least with respect to an emphasis on *tradeoffs*.[109] Without denying that education can have an impact—indeed, evidence suggests that people are swayed by economics educations[110]—there is strong reason to think that attitudes about taxes inconsistent with the standard optimal tax model are likely durable. Indeed, while some of the specific implications of optimal tax theory have only more recently come into focus, arguments on similar grounds about the value of cash date at least to Milton Friedman in the 1960s[111] and optimal tax theory itself dates to the 1970s. These are old ideas that may cut against significant aspects of social psychology or just commonplace intuitions. Taxing institutions have not appeared to change to incorporate them across the developed world. So this Article assumes that these ideas are, at least over the medium term, to some extent fixed, and that legislative inertia and interest group politics are not the only causes. This Article returns in Section IV to the extent to which these commonplace intuitions are fixed.

Finally, before continuing to the illustration, it is important to make a clarification about the question on politics at stake here. In law and economics, it is typical to frame the issue as being one of needing taxes and transfers to "compensate" for distributional changes. My own work has portrayed the issue that way.[112] However, such thinking sometimes reflects a basic confusion: compensation is neither necessary nor sufficient to maximize welfare. Compensation is necessary for a policy change to lead to a Pareto improvement. But, while all Pareto improvements improve welfare, there are many welfare gains that are not Pareto improvements, and not all Pareto improvements are the best way to improve welfare. In particular, consider an efficient policy that benefits the poor and harms the rich in the context of a society that is not distributionally just such that the poor have few resources. A Pareto improvement would transfer from the poor to the rich so that everyone is better off. But, since the poor do not have sufficient resources, a policy that improves welfare yet more is for the poor to keep all of their gains.

So considering policy responses one-by-one does not ask the most important question if society is not distributionally just to begin with. There can be compensation policy-by-policy, but welfare could still be far from maximized. This Article's maintained hypothesis is that redistribution through taxes alone will lead to insufficient redistribution. Thus, the standard policy-by-policy tax-and-transfer logic is not the one that applies here.

A key point of this Article is that the *reason* for the failure of taxes and transfers to appear matters for the policy response. For example, if political inertia were the reason for the absence of taxes and transfers, then it would be harder to justify why taxes versus nontax policies

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[109] N. GREGORY MANKIW, PRINCIPLES OF ECONOMICS, 7TH ED. (2014).

[110] Robert H. Frank et al., *Does Studying Economics Inhibit Cooperation?*, 7 J. ECON. PERSP. 159 (1993).

[111] MILTON FRIEDMAN, CAPITALISM AND FREEDOM (1962), http://circuloliberal.org/livros/capitalismo-e-liberdade.pdf.

[112] Liscow, *Is Efficiency Biased?*, *supra* note __ ; Zachary Liscow, *Are Court Orders Sticky? Evidence on Distributional Impacts from School Finance Litigation*, 15 J. EMPIRICAL LEGAL STUD. 4 (2018).

or why progressive versus regressive policies are particularly implicated. Similarly, if the story is about a capture of the political process by the rich, then again it is unclear why taxes versus nontax tools would be differentially implicated. This Article provides a novel account, explaining that voter psychology treats taxes differently as a means of redistribution, which yields a specific set of policy recommendations, to which the Article turns now.

A. An Illustration with Political Constraints

To talk about political constraints, we need to discuss a particular institution and have a theory of government underlying our analysis. This Article takes as its primary example that of federal regulators conducting cost-benefit analysis. There is a voluminous literature on distribution in regulatory cost-benefit analysis. As suggested earlier, the standard view in economics is that distribution should not be considered and that, instead, regulatory cost-benefit analysis should be efficient—for example, the lives of the rich valued for CBA purposes at more than the lives of the poor, etc. Typically, these arguments delve into little detail of real-world political institutions. David Weisbach does consider political institutions and still comes to the view that distribution should not be considered in regulatory cost-benefit analysis.[113] He points to "a version of a political Coase theorem" in which the legislature undoes the distributional choices of the administrative agency.[114] He says that, "at a minimum a claim that an agency can change that [distributive] outcome needs a story explaining why and how." This Article provides that explanation: Since, under the maintained hypothesis, many ordinary people view issues of distribution through taxes and other means differently, the legislature is unlikely to respond to a change in distribution from an administrative agency with tax policy changes that fully offset the administrative agency's actions. This significantly constricts the political Coase theorem. And, in any case, as described earlier, even if all the distributional impacts of regulation were undone by Congress, that does not imply that society would be distributionally just.

There are dissenting views as well. For example, Adler and Posner prominently argue that cost-benefit analysis should be based on well-being, not efficiency.[115] They note that policymakers could "launder" preferences—that is, treat everyone as if they have the same income.[116] They do not describe the factors that would go into setting appropriate distributional weights under political constraints. Richard Revesz argues for the establishment of a body to consider the distributional consequences of regulations on a case-by-case basis and address those consequences when they become severely negative enough.[117] However, he explicitly would not consider general distributional consequences.[118]

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[113] David A. Weisbach, *Distributionally Weighted Cost–Benefit Analysis: Welfare Economics Meets Organizational Design*, 7 J. L. ANALYSIS 151, 178 (2014). Weisbach does allow the possibility that an agency should consider distribution "based on the particular circumstances."

[114] *Id*. 177.

[115] Matthew D. Adler & Eric A. Posner, *Rethinking Cost-Benefit Analysis*, 109 YALE L. J. 165 (1999); MATTHEW D. ADLER & ERIC A. POSNER, NEW FOUNDATIONS OF COST-BENEFIT ANALYSIS (2006).

[116] *See id*. at 130–31, 142–46, 152 (2006) (discussing adjustments to willingness to pay to compensate for parties' different incomes and potential objections to such an approach). See also Matthew D. Adler, *Benefit–Cost Analysis and Distributional Weights: An Overview*, 10 REV. OF ENVIR. EC. & POL. 264, 269-73 (2016) (cited in __) (same). What the "distributional weights" should be is a difficult question for policymakers to answer.

[117] Richard L. Revesz, *Regulation and Distribution,* 93 N.Y.U. L. REV. 1489 (2018).

[118] *Id*. at 1578 (noting that "[s]keptics would say that only Congress can effectively and constitutionally undertake social policy of that magnitude").

Under the maintained hypothesis that taxes are unlikely to redistribute enough due to ordinary people's views, this Article analyzes a specific example: Department of Transportation regulators deciding how to conduct cost-benefit analysis to allocate expenditures for spending on transportation public goods between rich and poor people.[119] As discussed in the Introduction, current practice is to value commuting times of the rich more than commuting times of the poor because the rich are willing to pay more owing to their higher wages.[120] As a result, transportation spending will tend to follow to the rich. This Section asks: is valuing the time of the rich more than the time of the poor in allocating transportation spending a good idea?

Four main insights come from the illustration, paralleling the next four subsections. First, the model shows a concrete framework for how policymakers can *think conceptually and practically* about distributive questions given the reality of political constraints. Second, under the maintained hypothesis, the Department of Transportation's current policy is mistaken. Desert-based views about taxes lower redistribution through that means, but people still care about inequality. The Department of Transportation errs in not equalizing its transportation spending to help achieve less inequality. And the welfare impacts of erroneously spending only the "efficient" amount on the poor can be large. Third, one can actually remain agnostic on whether considering desert in taxation is normatively correct. The transportation planner's right choice is unaffected. And fourth, even in the face of normative uncertainty, regulators should often still act to help the poor.

B. Model Setup

This Section describes the broad details of the model, the specifics of which are in the Appendix. Consider two representative individuals, one rich (with wages of $5 per hour) and one poor (with wages of $2 per hour). I use a standard public finance model in which people work less as taxes go up because their incentives to earn are dulled.[121] Everyone faces a flat tax as a share of income to produce government revenue. That revenue can be used for three things: a cash transfer to the poor, transportation spending for the rich (e.g., runways at airports), or transportation spending for the poor (e.g., buses). Transportation spending reduces each party's commuting time, allowing more time working. As transportation spending increases, the rich and poor face the same declining marginal reduction in commuting time. There is a declining marginal utility of consumption, so a dollar generates more utility in the hands of a poor person than in the hands of a rich person, but raising taxes to redistribute shrinks the amount of income available by discouraging work.

I begin by comparing the policy outcomes under two models. The first, "standard" setup I call Model 0, such that:

Utility = standard utility

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[119] Much cost-benefit analysis may have distributional consequences different from those described here. In particular, in many cases, regulated parties themselves may pay the costs of the regulations themselves—for example, needing to pay more for housing after building regulations or receiving lower wages because of workplace regulations. Cass Sunstein calls these the "easy cases." CASS SUNSTEIN, THE COST-BENEFIT REVOLUTION (2018). In contrast, in the case here, the parties affected by regulators do not pay for the spending allocated to them, so they benefit fully from it. Sunstein calls these "hard cases."

[120] Liscow, *Is Efficiency Biased?*, *supra* note_.

[121] *See, e.g.,* Emmanuel Saez, *Using Elasticities*, *supra* note _.

where "*standard utility*" is a commonly-used function of utility that increases with more after-tax income and decreases with more work.[122] This model is the standard one-pieist utility function. Social welfare equals the sum of the utility for the rich person and the utility for the poor person.

To this model, I make one nonstandard addition: to account for the desert-based commitment against cash transfers not tied to work, the model directly adds to individuals' utility functions a dispreference for cash transfers to the poor. Thus, the larger the cash transfer not tied to work, the more utility goes down. This yields the following utility function for both the rich and poor, which I call Model A:

*Utility = standard utility – disutility of cash transfers to the poor * size of transfer*

So Model A is the same as Model 0, with just one change: there is disutility from redistributing through cash because people dislike such cash transfers on principle. Note that this model does not require any particular view about equality of opportunity or equality in the process of allocating transportation dollars. All that is motivating the model are a desire for more equal outcomes and a distaste for cash handouts.

At this point, think of this utility function as a representation of *how Congress acts*—that is, not necessarily as a reflection of well-being, but rather as a political constraint. So, *social welfare* is still calculated the same way as in Model 0—as just the sum of the standard utilities. A politically attuned regulator continues to believe that this is how to calculate social welfare even if cash transfers are reduced because of views about desert in taxation.

Policymaking occurs sequentially in two steps. First, Congress appropriates funds for the cash transfer and total funds for transportation maximizing the utilities set forth above. Details are in the Appendix, but roughly Congress sets these budgets anticipating that the Department of Transportation will set policy that maximizes well-being. Second, the Department of Transportation allocates the transportation funds separately to the rich and the poor to maximize well-being taking Congress's actions as fixed. As is common, although Congress precisely specifies the distributional impacts of tax policy, it leaves considerable discretion to the executive branch for the distributional impacts of regulatory and expenditure policy.

The model shows concretely, for a particular illustrative example (the specifics of which would change in any given circumstance), how one can incorporate both a concern for distributional outcomes as well as a distaste for addressing the issue through the particular *means* of cash taxes and transfers. In other words, rather than treating income net of taxes and transfers as the same thing as the outcome, taxes should be treated as one among many possible means of redistribution. This is a way of reconciling a distaste for using taxes and transfers to redistribute because of desert-based beliefs with widespread concern about economic inequality.[123] At the same time, the model allows for *tradeoffs* among the various factors: the declining marginal utility of income driving redistribution to the poor, the distortion from taxation, and the desert-based distaste for unearned transfers to the poor.

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[122] The *standard utility* function is: $\log\left(wL(1-\tau) - \frac{1}{k+1}(L+H)^{k+1}\right)$, where w is wages, L is labor supply, τ is the tax rate funding transportation and transfers to the poor, H is commuting time (reduced by transportation spending), and $1/k$ is the labor supply elasticity. The poor also receive a cash transfer. The rich and poor have different wages and receive separate amounts of transportation funding. See, for example, Saez, *Estimating Optimal Taxes*, supra note __.

[123] *See supra* Section_.

C. Results

1. Model 0: Standard view on transfers

Start with a baseline for comparison: the optimal policy for transportation administrators assuming that Congress redistributes optimally. This baseline result is shown in the top row of Table 1: spend only $0.50 on transportation per poor person, but spend $1.48 on transportation per rich person. (Recall that the model considers one rich person earning $5 per hour and one poor person earning $2 per hour. So think about this as an annual government appropriation per person.) The flip side is that there is a large transfer to the poor: $2.57. Thus, with standard views on taxes, the optimal answer is current policy: based on the standard efficiency analysis, spend substantially more to save an hour of time for the rich than to save an hour of time for the poor. The poor are willing to pay only their relatively small hourly wage to save an hour, while the rich are willing to pay their relatively large hourly wage. As a result, starting from a point where the rich and poor received equal transportation funding and only small transfers to the poor, it would be a Pareto improvement to spend less on transportation for the poor and then give larger cash transfers from the rich to the poor, saving money on transportation not justified on efficiency grounds and giving cash instead.

One way to understand the outcome is by considering the "distributive weights," or the relative contribution to social welfare of a dollar in the hands of a given person. The question that matters for the transportation spender is not the distributive weight in the abstract—that is, not for an omniscient social planner pulling all levers of policy. Rather, what matters for the Department of Transportation is the distributive weight after Congress has redistributed through cash transfers. Model 0 suggests that, after the large transfer to the poor, a dollar in the hands of the poor should effectively be worth the same as a dollar in the hands of the rich, so that the ratio of the distributive weights is 1:1. Importantly, for the transportation planner, a dollar is valued equally when used for the rich and the poor, even though post-tax and post-spending incomes are not equalized: the post-tax incomes of the rich and poor are $10.58 and $3.54, respectively. Of course, all else equal, a dollar continues to be worth more in the hands of the rich. But all is not equal: there is an efficiency cost to transportation spending on the poor instead of the rich, and this efficiency cost perfectly balances the redistributive benefit, leading to the 1:1 ratio of distributive weights. Other scholars, looking at the overall social weight, continue to place a greater weight on a dollar for the poor because of their lower incomes for those conducting cost-benefit analysis.[124] But the approach here would not do so because of the existing redistribution through cash and inefficiency of redistributing through transportation spending.

2. Model A: Desert-based view on cash transfers

We turn now to what transportation administrators should do if they are considering the insufficient redistribution through taxes by Congress. Under Model A, voters—and thus their Congresspeople—have desert-based views about taxes, resulting in transfers that are less redistributive than in the standard case. In particular, the distaste for cash transfers leads Congress to spend only $0.85 on cash transfers, rather than the $2.57 in the standard model.

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[124] Matthew D. Adler, *Benefit–Cost Analysis and Distributional Weights: An Overview*, 10 REV. ENVTL. ECON. POL'Y 264 (2016).

But the flip side of these desert-based views is that, with the cash transfer dramatically cut, optimal transportation spending by the Department of Transportation will be more redistributive: transportation spending on the rich drops to $1.19, while the spending on the poor increases to $1.59. The implicit distributive weight that the transportation planner uses then is a weight of 3.3 for the poor versus 1 for the rich, which offsets the higher wages of the rich. This spending depends on the trade-off between the standard efficiency cost and the redistributive gain. Spending on transportation is one possible means through which the fiscal system could achieve distributive goals by redistributing, even in the face of some efficiency loss. While welfare is not as high as under Model 0, where the most efficient means of redistributing are used, the transportation spending on the poor helps pick up some of the redistributive slack.

Congress could help remedy this situation on its own: If the desert-based view is a mistake, then approaches other than increased transportation spending on the poor may be available: For example, as already mentioned, de-biasing or exerting political will could alleviate the constraint on taxation. Another is reframing. For example, if the optimal tax policy is to give everyone a demogrant, then a refundable transportation tax credit through the tax code would functionally contribute to a demogrant while being framed as spending "for transportation" (at least for those who use transportation). Private spending on transportation is different from public spending, of course, but this private spending could be a partial substitute. Alternatively, if it were important that the funding go to public goods, the transportation tax credit could be received for a contribution to local public goods.[125]

This is actually a live political issue.[126] There is significant ongoing debate—including during the debate concerning the 2017 Tax Act—about the extent to which transportation expenditures should be tax deductible. Under the logic in this Article, it is welfare-maximizing to provide the cash. Much of what tax subsidies for transportation spending do is provide some relief for funds that people were *already going to spend*—thus, effectively providing a cash transfer. The logic of the Article thus suggests providing some deductibility or credits for spending on transportation, which then phases out at higher incomes, to target the benefits to lower income earners. Of course, there are a host of other concerns—on administrability, transactions costs, treatment of those who use versus don't use transportation, to list only a few issues beyond the scope of the Article—but the logic here suggests at least unappreciated benefits of the transportation spending deduction, and an account that leads to particular design features, like a phaseout.

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[125] This would resemble the state and local tax deduction.
[126] I.R.C. §§ 132(f)(8) (suspending the qualified bicycle commuting reimbursement exclusion), 274(a)(4) (disallowing businesses from deducting qualified transportation fringe benefits), 512(a)(7) (same) (2018); Tax Cuts and Jobs Act, Pub. L. No. 115- 97, §§ 11047, 13304, 13703, 131 Stat. 2054, 2088, 2123, 2169 (2017); I.R.S. Notice 2018-99 (Dec. 10, 2018), https://www.regulations.gov/document?D=IRS-2018-0038-0001 (offering guidance for implementing TCJA transportation benefits taxation changes); Daniel Di Martino, *Tax Treatment of Transportation Fringe Benefits*, TAX FOUND. (July 22, 2019), https://taxfoundation.org/transportation-fringe-benefits/ (advocating for treating transportation benefits like wages); *Unrelated Business Income Taxes (UBIT) | Nonprofit Transportation Benefits*, NAT'L COUNCIL OF NONPROFITS (Accessed Sept. 9, 2019), https://www.councilofnonprofits.org/trends-policy-issues/unrelated-business-income-taxes-ubit-nonprofit-transportation-benefits (discussing the impact on nonprofits and advocating for reform).

Table 1: Optimal Transportation Spending and Transfers Under Standard and Politically Attentive Models

	Optimal transportation spending	Cash transfer to the poor	Distributive weight to transportation planner, poor : rich	Welfare cost of adopting standard model's spending pattern (i.e., efficient transportation spending)
Model 0: Standard model	Poor: $0.50 Rich: $1.48	$2.57	1:1	n/a
Model A: Politically attentive model with distaste for cash transfers	Poor: $1.45 Rich: $1.19	$0.85	3.3:1	6.7% of income

3. Political Constraints with Naïve "Efficient" Regulator

The third case is the one that follows current government policy: under the maintained hypothesis, there are political constraints reducing redistribution through taxes but regulators continue to allocate transpiration spending in an "efficient" manner, weighting a dollar in the hands of the rich and poor equally. That is, transportation planners are naïve and allocate spending as if there were optimal cash transfers, even though they are not optimal—the transfer is only the amount from Model A. In particular, suppose that regulators allocate spending between the rich and the poor in the same ratio as they did in Model 0,[127] even though in fact there is not enough redistribution through cash.

Table 2 shows these welfare costs as a percent of income. Welfare is reduced by a large amount for just one policy: 6.7%. (As detailed in the Appendix, welfare impacts are measured as the amount of money that would be needed to compensate the parties for the loss in welfare versus the optimal policy.) The welfare loss arises because there is not enough spending on the poor when cash transfers are not redistributing very much. Multiplying the impact across even a handful of policies would quickly yield very large shares of welfare. Thus, under the maintained hypothesis, current Department of Transportation policy is erroneous because it is inattentive to Congress's actions on cash transfers. The Department of Transportation spends too little on the poor relative to the rich, reducing social welfare because of the high social value of the income the poor earn from being able to commute to work more quickly.

D. If Desert in Taxation Is Normatively Correct, Prescription Is Unchanged

The Article has thus far assumed that nonstandard views about taxation operate merely as a constraint and that they do not constitute preferences deserving moral weight. Some might disagree and argue that desert-based views on taxes do deserve moral weight and wonder how the results change if the desert-based views about taxation are normatively the correct ones.[128] Remarkably, even if desert-based views about cash redistribution through taxes do constitute the

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[127] We cannot assume that the exact same *amounts* (versus ratios) are allocated to the rich and the poor because Congress optimally allocates more total funds to transportation when it allocates less to cash transfers.

[128] See, for example, Weinzierl, *supra* note _ (showing how optimal policy changes when this is the normative goal).

normatively correct values (at least as understood here), then the main results remain unchanged. In particular, regulators should still "redistribute" through transportation spending—and in the exact same amount. The reason is that redistribution through transportation spending is totally consistent with having a distaste for redistribution *through the particular means of cash transfers through the tax system*, while also caring about inequality in general. Taxes are just one particular tool. From the perspective of the Department of Transportation regulator, the size of the cash transfer to the poor is fixed in both cases: Congress can vote for lower transfers out of a mistaken desert-based view or to reflect the true normative goal, and the amount of cash redistribution will be the same in the two cases. How cash transfers affect social welfare does not affect the Transportation planner's decision. Therefore, since the parties value transportation spending the same in both cases and since the overall distributive goal is the same in both cases, the optimal transportation spending is the same.

Thus, transportation policymakers can, to a large extent, remain agnostic about the normative consequence of desert in taxation. This deeper normative question of whether desert-based views on taxation have any normative force does not need to be answered to conclude that transportation regulators should spend more than the efficient amount on the poor, so that they can earn more money by getting to work more quickly. Other major normative questions remain, such as the appropriate distribution of income, but—if one agrees that there is at least a moderate chance that Congress acts as if desert matters for the *particular means* of redistribution through taxes, correctly or incorrectly—the policy prescription for Transportation spenders remains.

For other actors, the normative force of desert in taxation does matter. For example, earlier the Article briefly discussed implications for economic experts and Congress of desert-based views about taxes. For economic experts, if desert-based views on taxes are normatively correct, then of course the prescription to educate people to consider cross-policy tradeoffs and break down the mental policy accounts no longer holds, since those mental accounts would have normative force. And for Congress, which could help address mental policy accounts by allowing tax deductions or credits for spending on transportation for lower-income households, if desert-based views are normatively correct, then a policy that largely repackages cash as spending "on transportation" may no longer be wise policy, depending on whether this policy is normatively disfavored as well.

E. Error Costs and Normative Uncertainty

Thus far, the Article has largely assumed that we know the right normative model. A separate question considers which policies to adopt under uncertainty about the appropriate normative model. This question leads to reasoning resembling "error cost" analysis in antitrust, which compares the cost of, say, erroneously allowing and erroneously preventing a merger.[129] I follow a similar analysis here.

In particular, suppose for simplicity that there are two possibly correct normative models. As described above, in Model A, Congress does not redistribute as much through taxes because of a distaste for redistributing through cash in particular. In contrast, Model B has no distaste for cash in particular; rather, Congress has enacted the normatively correct amount of redistribution.

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[129] *See, e.g.*, Paul L. Joskow & Alvin K. Klevorick, *A Framework for Analyzing Predatory Pricing Policy*, 89 Yale L.J. 213, 222–25 (1979); Frank H. Easterbrook, *The Limits of Antitrust*, 63 Tex. L. Rev. 1 (1984); Alan Devlin & Michael Jacobs, *Antitrust Error*, 52 Wm. & Mary L. Rev. 75, 97 (2010).

That is, it is normatively correct to care about the welfare of the poor less than the Article has thus far been assuming. More precisely, for Model B,

Utility of the rich = standard utility

Utility of the poor = F · standard utility

The rich and poor have the same utility function (which increases in income and decreases in work), except that the utility of the poor is multiplied by some amount $F < 1$, which rationalizes why relatively little cash is redistributed to the poor.

Thus, seeing a low amount of cash transfers, leaders at the Department can believe one of two narratives (or a combination of the two):

Narrative A is: *Congress reflects the will of the people. In setting cash transfers to the poor, it redistributes in line with the social value of redistribution <u>through cash transfers specifically</u>. There is a specific distaste for "giving out cash," even as redistribution (including through transportation spending, which allows people to earn money) continues to be valued. As regulators, we should reflect those same normative commitments.*

Narrative B is: *Congress reflects the will of the people. In setting cash transfers to the poor, it redistributes in line with the social value of redistribution. As regulators, we should reflect those same normative commitments.*

Table 2 shows the optimal spending patterns and welfare costs under normative uncertainty.[130] The first row repeats the outcome in Table 1 for Model A. The second row shows the optimal spending under Model B. The spending ratio is even more tilted toward the rich than under the standard model baseline (with optimal spending of $0.67 on the poor and $1.97 on the rich), even with lower cash transfers to the poor, because now redistribution to the poor is less valuable.

There are potential error costs under both normative models. If Model A is normatively right but the Department of Transportation adopts Model B's prescription, transportation spending is insufficiently redistributive and there is a welfare loss of 6.8%. (This is the case whether the dispreference for cash transfers is either normatively correct or merely a political constraint, as described in the previous subsection.) If Model B is normatively right (i.e., there is just a weak preference for redistributing), but regulators adopt the more redistributionary transportation spending of Model A, then there is also a welfare loss, though a smaller one: of 3.7%.

In principle, regulators could compare the error costs in any given situation to help with their decision-making: the larger the welfare cost of adopting the wrong policy, the more consideration that normative framework should get. Suppose, for example, that there is a 50 percent chance of each possibility being correct. The resulting optimal spending is $1.10 on the poor and $1.44 on the rich. This resulting ratio of spending on the rich and poor is between the

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[130] As explained in the Appendix, so that the cash transfers and transportation budget are the same under Models A and B, this subsection sets as Congressional appropriations the average of these amounts that Model A and Model B would produce in isolation.

two extremes, though closer to the Model A outcome because the welfare costs of deviating from it are smaller than the welfare costs of deviating from Model B.

This illustration reflects the rule in economics that the marginal cost of deviating from the optimal policy increases in the size of the deviation.[131] That is, being a little off from the optimal outcome for either Model A or Model B is not very costly: the transportation planner is close to indifferent for the marginal transportation cent. It is only when spending deviates further from the optimal amount that the marginal costs get large. Thus, given uncertainty about the right normative model, it makes sense to adopt a policy close to the middle of the two possibilities, so that there are not large deviations from either.

Table 2: Error Costs Analysis

	Optimal transportation spending	Cash transfer to the poor	Error cost of adopting alternative model's policy
Model A: Politically attentive model with distaste for cash transfers	Poor: $1.45 Rich: $1.19	$0.85	6.8% of income
Model B: Less redistributive model	Poor: $0.67 Rich: $1.97	$0.85	3.7% of income

F.   Summary

Overall, the illustration reveals four main things. First, it shows concretely a framework for how policymakers can *think conceptually and practically* about distributive questions given reality of political constraints. Congress acts like its voters think about taxes: there is something bad about violating notions of desert with cash transfers. At the same time, this view does not contradict the notion that voters also care about helping the poor. Rather, the view is about the *particular means* of taxation. Taxation is *just one tool* for addressing inequality and views about that do not necessarily reflect overall redistributive views. People continue to care about having more equal outcomes. Implicitly, people are more comfortable when money is earned by going to work, which is enabled by more transportation spending.

Second, the welfare impacts in the illustrative example can be large. This illustration has shown how regulators' adoption of efficient policy prescriptions risks considerably reducing welfare when Congress does not use economists' chosen tool of taxes to redistribute, owing to voters' social psychology about desert in taxation. The welfare impacts show the cost of adopting the standard prescription of efficient in-kind benefits, like transportation spending, when taxes are inadequate. And, recall, the cutting-edge research in economics suggests that the amount by which the US tax code implicitly weights rich versus poor is only a small fraction of sensible (though by no means obvious) understandings of the declining utility of money from poor to rich. There is a lot of redistributive space for nontax policy to productively fill.

Third, the regulator's right behavior does not depend upon whether the desert-based views driving reduced redistribution through cash transfers are normatively correct or not. In

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[131] GRUBER, *supra* note __.

either case, so long as more redistribution than taxes provide is still good, regulators should respond with more equitable transportation spending.

And fourth, regulators need not be certain that mental policy accounts are at play to act. If they are uncertain about whether the tax and transfer system that they see is due to a general dispreference for redistribution, on the one hand, or desert-based views about taxation in particular, on the other hand, they should still adjust their transportation allocation to the poor in proportion to the likelihood that desert-based views about taxation are at play.

IV.   Other Considerations and General Policy Implications

The basic illustration shows how a regulator could respond in the case of transportation spending given a view that Congress is not redistributing enough through taxes. Essentially, various policymakers should take some understanding of a fair distribution of income, consider how much is already being redistributed through the tax code, and then use a suitable distributive weight. Various others have discussed using distributive weights.[132] Such analyses typically end without giving guidance on what such weights should be. And I am unaware of any that considers distributive weights *for a particular institution*, given the existing behavior of tax policy. The framework here—along with recent advancements at the cutting-edge of economics—allows us to actually suggest what those distributional weights should be.

How redistributionary the government policy should be is, of course, a difficult normative question. But, as discussed earlier, for the 10th versus the 90th percentile, one sensible (but of course contestable) approach would be to adopt a ratio of 13 *for overall government policy*.[133] Transportation regulators *for their own institution* then need to adjust their redistribution downward for the amount of redistribution that already takes place through taxes: recall that the tax code currently implicitly redistributes with a distributive weight ratio of 1.9 for the 10th versus 90th income percentiles.

This weighting could still mean spending less on transportation for the poor than for the rich—or it could mean spending more on the poor by actually weighting their time more highly than that of the rich. In any case, under the maintained hypothesis, it means spending more than the efficient amount on the poor. Regulators would want to do the same thing across all cost-benefit analyses, as well as for any other policy analyses. That is, as long as the efficiency costs are not too high, legal rules typically *should* redistribute—and should continue redistributing up to the point that efficiency costs become too high.

And, recall from the previous section that, for modest deviations from the efficient form of redistribution, the welfare costs are small because policymakers are close to the margin anyways in their decision-making. The same reasoning applies here: the costs of adopting modest amounts of inefficient forms of redistribution are small because policymakers are close to the margin between choosing tax and nontax means of redistribution. For the same reason, it is better to redistribute a modest amount more through many legal rules rather than a lot more through few legal rules.

The Article here first describes four factors that should affect how much policymakers operating in the shadow of insufficiently redistributive taxation should act, under the understanding that mental policy accounts with desert-based taxation drive the phenomenon. In other words, when evaluating tradeoffs between equity and efficiency in setting policy, what

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[132] Adler, *supra* note __ at 264-285 (providing an overview).
[133] See supra section II.A; Hendren, *Efficient Welfare Weights*, *supra* note __.

factors should politically attuned policymakers consider? Second, the Section speculates about what precise decision rule policymakers should use given that political constraints exist for in-kind redistribution, as well as for taxes.

A. Other Factors Determining Optimal Nontax Redistribution

1. Other Nontax Policies Currently Redistribute

The maintained hypothesis of this Article is that, because of commonplace desert-based views, taxes do not and are unlikely to redistribute enough to achieve distributive justice. But, as described earlier, nontax policies like those in housing and healthcare arguably already do redistribute beyond the efficient amount.[134] The current presence of in-kind redistribution affects the optimal amount of redistribution through policies like transportation. The more existing in-kind redistribution there is, the less distributive weight there should be on the poor and the less the transportation spenders should redistribute.

This Article analyzes redistribution through nontax legal rules versus an efficient baseline. A separate, but related, question is whether nontax policy should redistribute more than *current policy* does, not just more than is efficient. This Article cannot decisively answer that question, as it is fundamentally a normative one, depending on what distribution is just. Nevertheless, it is worth noting that polling and our political discourse continue to suggest widespread concern about inequality. For example, a recent Pew Research Center poll found that 82% of respondents thought that income inequality in the U.S. was a big or moderately big problem.[135] And across the political spectrum, there is discussion of the problem of inequality. For example, Mitt Romney, Jeb Bush, and Rand Paul all complained about the continuing rise in inequality during the Obama presidency.[136] Our discourse, in particular, suggests widespread unease about inequality of opportunity, rather than outcomes, which is consistent with the idea that people care about the means of addressing inequality; taxes that address after-the-fact inequality do not fully address those concerns.[137]

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[134] Note __ supra describes how the optimal income tax results described in the Article are for labor, but not capital, income taxation. Sizable taxes on capital income also decrease the desirability of redistribution through other nontax means.

[135] *See, e.g.*, PEW RESEARCH CENTER, THE GENERATIONAL GAP IN AMERICAN POLITICS 18 (2018), http://www.people-press.org/wp-content/uploads/sites/4/2018/03/03-01-18-Generations-release.pdf. Republicans, too, have increasingly expressed concern about rising inequality, even before President Trump's populist rhetoric during the 2016 campaign.

[136] *See* Catherine Rampell, *Republicans Have Started to Care About Income Inequality*, WASH. POST (Jan. 22, 2015), https://www.washingtonpost.com/opinions/catherine-rampell-republicans-have-started-to-care-about-income-inequality/2015/01/22/f1ee7686-a276-11e4-903f-9f2faf7cd9fe_story.html?utm_term=.92d3a15e5c57.

[137] Jackie Calmes, *In Talk of Economy, Obama Turns to 'Opportunity' Over 'Inequality,'* N.Y. TIMES (Feb. 3, 2014), https://www.nytimes.com/2014/02/04/us/politics/obama-moves-to-the-right-in-a-partisan-war-of-words.html (discussing then President Barack Obama's shift in rhetoric away from income inequality and towards equality of opportunity); Mike Pence, *Remembering Jack Kemp*, HILL (May 4, 2009), https://thehill.com/blogs/congress-blog/politics/25577-remembering-jack-kemp-rep-mike-pence ("His devotion to ensuring equality of opportunity for every American regardless of race, creed or color helped ground the Republican Party in the true ideals of Lincoln."); Representative Paul Ryan, Chairman, House Budget Committee, Speech to the Heritage Foundation: Saving the American Idea (Nov. 15, 2011), https://www.heritage.org/political-process/report/saving-the-american-idea-rejecting-fear-envy-and-the-politics-division ("These actions starkly highlight the difference between the two parties that lies at the heart of the matter: whether we are a nation that still believes in equality of opportunity, or whether we are moving away from that and toward an insistence on equality of outcome."); Benjy Sarlin, *Racial Wealth Gap is Vast: 2020 Democrats Have Plans to Close It*, NBC NEWS (May 20, 2019),

2. More Nontax Redistribution Causes Less Efficient Redistribution

The weight on the poor should be reduced to the extent that the legislature itself will respond by reducing its redistribution through taxes. Part of the reason that there may not be more redistribution through taxes is that there is widespread "inefficient" in-kind redistribution. If cash is the first-best means of redistributing, then this effect would be perverse. In other words, political institutions could end up at a bad equilibrium of inefficient redistribution this way—in a kind of "kludgocracy."[138] One mechanism by which such a bad equilibrium could arise is that people are educated through policy and, the less of one type of redistribution we have, the less they learn about it. Or alternatively, voters come to expect less efficient in-kind redistribution. Finally and most basically, Congress may simply see more redistribution elsewhere and redistribute less through taxes.

Inertia in policymaking would compound this factor. If it would be harder in the future for the legislature to adopt more efficient redistribution if regulators enact more in-kind redistribution today, then more in-kind redistribution is less desirable. However, given standard discount rates, redistribution today matters a lot relative to hypothetical future redistribution.[139] And, if in the future decreasing excessive redistribution is easier than increasing insufficient redistribution, then redistributing today becomes more valuable. So, if it is harder to reduce redistribution that is excessive than it is to increase redistribution that is insufficient, then there should be less redistribution today. If the reverse is true, there should be more redistribution.

The extent that more in-kind redistribution causes less efficient redistribution is very difficult to judge and is ultimately an empirical question. If the median voter theorem[140] is operative, and there's an amount of redistribution that is socially desired and is enacted through Congress, then any distributive change enacted through parties other than Congress should be undone. I am unaware of any evidence on the response by Congress to the distributional implications of regulatory policies.[141]

One striking piece of evidence of more nontax redistribution *not* impacting taxes comes from court orders on education spending.[142] In half of the states, state supreme courts have mandated that legislatures spend more money on education in poor areas, leading to huge changes in spending priorities. If legislatures act as law and economics assumes, they would enact the population's desired amount of redistribution and, if that is disrupted, reequilibrate to the desired level. That is, if courts mandate that more resources go to the poor, then the legislature should enact other changes that disadvantage the poor. This does not happen, even 25

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https://www.nbcnews.com/politics/2020-election/racial-wealth-gap-vast-2020-democrats-have-plans-close-it-n1007051 ("'We've got to find ways to balance the economic scales and have true equality of opportunity in our country,' Booker told NBC News in an interview.").

[138] Steven M. Teles, *Kludgeocracy in America*, NAT'L AFF. (2013) https://www.nationalaffairs.com/publications/detail/kludgeocracy-in-america.

[139] Liscow, *Is Efficiency Biased?*, *supra* note __.

[140] ANTHONY DOWNS, AN ECONOMIC THEORY OF DEMOCRACY (1957).

[141] While the repeal of several Obama Administration regulations, such as those limiting mandatory arbitration clauses, could be construed as a reaction to the distributional consequences of those regulations, I have not found any articles analyzing the issue from that perspective. Pub. L. No. 115-74, 131 Stat. 1243 (Nov. 1, 2017) (repealing Abitration Agreements, 82 Fed. Reg. 137 (July 19, 2017)); *see also* Paul Larkin, Jr., *The Trump Administration and the Congressional Review Act*, 16 Geo. J. L. & Pub. Pol'y 505, 508-09 (2018).

[142] Liscow, *Court Orders*, *supra* note _. *But see* Richard T. Boylan & Naci Mocan, *Intended and Unintended Consequences of Prison Reform*, 30 J. L. ECON. & ORG. 558 (2014) (showing evidence from a much smaller change—mandating more spending on prisoners—suggesting that social welfare spending was cut to pay for it).

years after the court order. Taxes do not go up on the poor more than the rich. No social programs that benefit the poor are discernably cut. Though there are a variety of possible interpretations of this phenomenon, one is that voters do not view taxes and education spending as fully fungible. Each has its own distributive pie. Of course, this is just one example, and the empirical question is an open one.

In any case, under the reasoning described before, for small or modest amounts of redistribution through legal rules instead of taxes, the cost will be relatively small. Even under the standard view, policymakers are right on the margin between the efficient amount of in-kind provision and a little more, so a little more in-kind redistribution (instead of taxes) is not very costly to welfare. Of course, large deviations could lead to large costs.

3. Other, Non-Standard Normative Goals

This Article has thus far assumed that the standard welfare function is correct: no concerns with fairness count beyond overall redistributive preferences. Especially in light of what is arguably the large failure to enact the recommendations of the standard model, it is worth considering the impact of a richer set of values—including rights or fairness in either process or outcomes—on desirable redistributive policy. Consider the transportation spending example, and suppose that (unlike in the illustration) the analysis with standard normative values still suggests valuing the time of the rich more than that of the poor, spending more on the rich, and leaving the poor with considerably worse transportation options. One possible value would be a process norm of treating a minute of the poor's time like a minute of the rich's time, which would suggest more equal treatment in the regulatory procedures.[143] If equality of opportunity in getting to work is important, then more equal spending would be valuable. In either case, a welfare function that gave weight to these equality norms would further reinforce a movement toward treating the rich and the poor equally in regulatory cost-benefit analysis. Of course, these same equality norms could undermine a recommendation that values the poor more highly or spends more on them. And, of course, the myriad other possible values—equality-oriented or otherwise—could have myriad impacts on desirable redistribution.

4. Endogenous Political Changes: Political Power and Legitimacy

Another factor is endogenous political changes. For example, it is plausible that poorer people with better transportation access may be more active politically—and perhaps vote more.[144] Whether having more politically active poorer people is a good thing depends in part on

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[143] See Adam M. Samaha, *Death and Paperwork Reduction*, 65 DUKE L. J. 279 (2015).

[144] Local officials and transit providers have raised and sought to mitigate concerns about transportation accessibility limiting voter turnout. *See, e.g.*, Luz Lazo, *Need a Ride to the Polls Tuesday? Here's Some Help*, WASH. POST: GRIDLOCK (Nov. 5, 2018), https://www.washingtonpost.com/nation/2018/11/05/need-ride-polls-tuesday-heres-some-help/ ("Transit services across the country are trying an unprecedented experiment to boost turnout Tuesday, waiving bus and rail fares and offering free and discounted bike, scooter and car trips."). However, while research supports the connection between income and voting, there do not appear to be many studies examining the connection between transportation, income, and voting. *See, e.g.*, Moshe Haspel & H. Gibbs Knotts, *Location, Location, Location: Precinct Placement and the Costs of Voting*, 67 J. POL. 560, 567 (2005) https://www.journals.uchicago.edu/doi/abs/10.1111/j.1468-2508.2005.00329.x ("When automobiles are universally available . . . , voters are much less sensitive to changes in distance"); Rosie Romano, *Increasing Voter Turnout: Can Mass Transit Help?*, 1 CLOCKS & CLOUDS 1 (2012), http://www.inquiriesjournal.com/articles/1618/increasing-voter-turnout-can-mass-transit-help (finding no connection between voter turnout and distance to Metro stations in an undergraduate research journal); Jeannine Stover, *Comparing Voter Turnout to Public Transit Access Using 2012 General Election Data* 17, BOS. UNIV. (Dec. 5, 2016),

one's account of the political failing. For example, if poorer people were more politically active, perhaps tax policy would be more redistributive—and Congressional behavior would move closer to the first-best. But such an outcome is not obvious. Second, beyond standard economics goals, more politically active poorer populations may be intrinsically good.

Finally, redistributing in ways that are seen as legitimate, given how ordinary people think, could be itself good for a variety of reasons. One reason is that doing so could increase compliance with the law.[145] Another is potentially reducing the likelihood of a destructive populist backlash to elites inattentive to "ordinary people" that may interfere with the good functioning of the political system; among other problems, such a backlash could reduce investment in things like education that make larger numbers of people better off.[146] To the extent that this mechanism is operative, under the maintained hypothesis that people have mental policy accounts supportive of in-kind redistribution, more weight should be put on redistributing to the poor through in-kind means. This factor would mitigate the impact of the second factor—on the possibility that more in-kind redistribution reduces more "efficient" redistribution—because the improved legibility of redistribution through in-kind means would have their own salutary effects, partially offsetting the "efficiency" costs measured in standard ways.

B. Redistribution Through Legal Rules, Politics, and an Equal Treatment Heuristic

The Article has emphasized the political feasibility of redistributing through taxes, but a symmetric question also matters: the political feasibility of redistributing through nontax in-kind goods or legal rules. An implication of the preceding analysis is: Wherever politically feasible, redistribute more than the standard "efficient" amount up to the point that the efficiency costs become too large. A full analysis of what is politically feasible is beyond the scope of the Article, but it is important in an analysis on political feasibility to at least suggest that the proposed alternative to taxation is politically feasible.

Presumably, sometimes the nontax alternative is feasible, and sometimes it is not. Section II.B described how people seem to view some goods—like healthcare, housing, education, and food—as necessities, making redistribution through those means more feasible. As to the Article's specific example, unfortunately we know little about commonplace views on regulatory cost-benefit analysis or on transportation spending.[147] Indeed, we do not know if people pay

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https://www.bu.edu/cityplanning/files/2017/02/UA654FinalJeannineStover1.pdf. See also Sam Sturgis, *Could Free Public Transit Get Americans to Voting Booths*?, CITYLAB (Nov. 3, 2014) https://www.citylab.com/transportation/2014/11/will-free-public-transit-get-americans-to-voting-booths/382199/.

[145] TYLER, *supra* note __

[146] JAN-WERNER MULLER, WHAT IS POPULISM? (2016); J. Eric Oliver & Wendy M. Rahn, *Rise of the* Trumpenvolk*: Populism in the 2016 Election*, 667 ANNALS AM. ACADEMY POLITICAL & SOC. SCIENCE 189 (discussing President Trump as a populist); Dani Rodrik, *Populism and the Economics of Globalization*, *supra* note _; Ronald F. Inglehart & Pippa Norris, *Trump, Brexit, and the Rise of Populism: Economic Have-Nots and Cultural Backlash* (Harvard Kennedy School Working Paper No. RWP16-026, 2016), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2818659 (arguing that cultural backlash explains populism more than economic insecurity); Ana Swanson, *The Rise of Populism Shouldn't Have Surprised Anyone*, WASH. POST (Aug. 10, 2017), https://www.washingtonpost.com/news/wonk/wp/2017/08/10/the-rise-of-populism-shouldnt-have-surprised-anyone/ ("Countries, including the United States, have seen the rise of a populist backlash against more liberalized trade and international integration that could result in globalization playing out in reverse").

[147] But see Rena Steinzor, *The Unpopularity of Cost-Benefit Analysis*, HUFF. POST (Sept. 17, 2012), https://www.huffpost.com/entry/the-unpopularity-of-costb_b_1884369 (asserting by implication, but not citing any hard empirical evidence, that cost-benefit analysis is unpopular among the American public).

much attention to such regulatory and spending processes at all. That said, the equal "value of a statistical life" given to the rich and the poor, in contradiction to the efficiency-oriented regulatory practices of the Federal government, suggests that people do pay attention to that rule, and that they would not like unequal treatment.[148] And presumably people pay a fair amount of attention to the transportation options they have, though perhaps not their options versus those of others.

I speculate that, as a matter of process, valuing the time of the poor closer to (but not more than) the time of the rich would seem fair. And, I speculate that, as a matter of spending outcomes, improving peoples' ability to get to work resonates in equality-of-opportunity terms that are likely politically appealing, as encouraging work seems to be a widely-held value.[149] On the other hand, those primarily concerned with economic development may want to spend considerably more on the rich, owing to their greater wages and output per marginal hour worked—but that is an objection to any redistribution to the poor beyond the efficient baseline. So I speculate that valuing the time of the rich and poor similarly in transportation is a fairly politically feasible form of redistribution.

Other times, redistribution beyond the efficient amount may not be politically feasible. Consider the following redistributive example. Suppose that an agency is analyzing two regulations, both of which will increase the profits of harmed parties by $1 million through pollution reduction. The first regulation benefits owners of small businesses who tend to be relatively poor (say, owners of laundromats), while the second regulation benefits large corporations by $1 million, whose owners tend to be rich. Both rules cost $1 million to two different polluters, both of whom are owned by those with average incomes. The logic of distributional weights means that we should adopt the first regulation but not the second one, since benefitting the poor is more valuable than benefitting the rich. I do not know how people would react to that, but one could imagine resistance. For the same reason that there may be resistance to valuing two lives differently, there may be resistance to explicitly valuing $1 in the hands of rich more than $1 in the hands of the poor. Or, switch the example from a regulatory context to a tort: a rich person and a poor person have their cars rear-ended by the same middle-income person, and each incurs $5,000 in costs to their cars. The Article's logic is that the damages paid to the poor person should be larger than those to the rich person. One wonders though whether process norms in the context of torts would make unpalatable different treatment of two people who suffered the same financial damages. In other words, the same process norms of equal treatment that support treating the poor more like the rich may work against actually

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[148] *See* Cass R. Sunstein, *Are Poor People Worth Less than Rich People? Disaggregating the Value of Statistical Lives* 5-6 (John M. Olin Law & Economics Working Paper No. 207, 2004), http://citeseerx.ist.psu.edu/viewdoc/download?doi=10.1.1.826.7725&rep=rep1&type=pdf ("When risks are faced disproportionately by wealthy people, VSL, based on actual WTP, should be higher than $6.1 million—just as it should be lower when it is faced disproportionately by poor people."); *see also* Cass Sunstein, *Cost-Benefit Analysis and the Environment*, 115 ETHICS 351, 371 (2005), https://www.jstor.org/stable/pdf/10.1086/426308.pdf ("[G]overnment does people no favors by forcing them to pay the amount that they would pay if they had more money."); Cass R. Sunstein, *The Value of a Statistical Life: Some Clarifications and Puzzles*, 4 J. BENEFIT-COST ANALYSIS 237, 243 (2013), https://www.cambridge.org/core/services/aop-cambridge-core/content/view/7C9C27FAB00A11D4EA5268D1F7653DC7/S2194588800000609a.pdf/value_of_a_statistical_life_some_clarifications_and_puzzles.pdf (arguing that government should respect willingness to pay, even if limited by ability to pay);

[149] *See* Robert A. Moffitt, *From Welfare to Work: What the Evidence Shows,* Policy Brief 13 (Brookings Inst., Wash. D.C.) Jan. 2, 2002, at 1 ("The American public has made clear that work by welfare recipients is a defining goal of state and federal welfare laws….").

valuing the time of the poor more highly than the time of the rich in the transportation case or giving larger damages to the poor in the torts case.

An "equal treatment" heuristic—of equally valuing the time of the rich and the poor and engaging in similar treatment across other legal rules—is one alternative. As Murphy and Nagel argue, "[t]he moral ideas that do the work of legitimation have to be graspable and intuitively appealing, not just correct."[150] Equal treatment is graspable, is intuitively appealing, and would move in the right direction distributionally. This method resembles the conclusions reached by some liberals[151] and some welfarists,[152] but does so on different grounds: the reasoning is neither liberal nor a modified version of welfarism that ignores the Pareto gains that can come from redistributing cash rather than other goods. Rather, the normative reasoning is purely conventional: there's a standard welfarist goal, but various government actors face constraints of using methods of redistribution that are feasible.

An equal treatment heuristic has welfare costs compared to using distributive weights because in some cases it redistributes too little and in other cases it redistributes too much. Consider the distinction I drew elsewhere between "neutral rules" and "rich-biased rules."[153] Neutral rules provide the same efficient legal entitlement to the rich and poor. The examples of poor versus rich owners of businesses that are polluted on and poor versus rich car owners who are rear-ended are examples of neutral rules: since rich and poor people value a dollar the same, the efficient rule is to treat the rich and poor equally. Thus, under an equal treatment heuristic, neutral rules are insufficiently redistributive: since the efficient rule is equal treatment, failing to redistribute more than that misses out on low-cost opportunities for redistributing.

Rich-biased rules, in contrast, allocate more of a legal entitlement to the rich than the poor because of the rich's greater willingness to pay. The transportation example is rich-biased: the rich are willing to pay more for transportation spending, so the government allocates more to them than to the poor. An equal treatment heuristic thus may redistribute too much or too little to the poor for rich-biased rules. In Section III's illustration, an equal treatment heuristic would redistribute too little to the poor, since redistributing through transportation was not very inefficient and so little was redistributed to the poor through taxes. But, in other cases, where redistributing is costlier or where we believe that taxes are not as extraordinarily insufficient at redistributing, equal treatment will lead to an insufficiently high amount of redistribution.

Importantly, averaging out neutral legal rules with insufficient redistribution and rich-biased legal rules with excessive redistribution would not maximize welfare for two reasons. First, doing so might redistribute the wrong amount—too little if neutral legal rules predominate or possibly too much if rich-biased legal rules predominate. Second, the heuristic would miss efficient opportunities to redistribute through neutral rules in exchange for excessive inefficient redistribution through rich-biased rules. The welfare cost of adopting the equal treatment heuristic versus distributional weights thus depends on two factors: first, how far overall redistribution is off from the optimal amount and, second, how heterogeneous the costs of redistribution are across different legal rules, thereby driving up efficiency costs. But, so long as cash redistribution is very insufficient, so that equal treatment rarely "overshoots" in redistribution for rich-biased rules, an equal treatment heuristic is still an improvement on always having efficient legal rules.

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[150] MURPHY & NAGEL, *supra* note __ at 188.
[151] Samaha, *supra* note __.
[152] *See* Adler, *supra* note _ (describing cleaning preferences).
[153] Liscow, *Is Efficiency Biased?*, *supra* note __.

Whatever the particularities of political feasibility in any given case, though, the policy advice remains: If standard notions of welfare are the goal and desert matters in taxation, then redistribute more through other means up to the point where the increased distributive benefits no longer outweigh the efficiency costs.

V.   Addressing Critiques

The Article briefly addresses three critiques not already considered as factors to include in deciding how much to redistribute to the poor.

Impossible to know the right distribution of resources
One objection is the difficulty of knowing what the "right" distribution of resources is. I fully acknowledge this critique; it is beyond the scope of the Article to define such a distribution. Any given set of assumptions could over- or under-state the optimal distribution of resources. However, uncertainty about the right distribution does not necessarily imply a default to the standard economic prescription of efficient economic policymaking that is inattentive to equity. Given the multi-step, multi-institution nature of representative democracies, we need a theory of politics to explain how redistribution happens. The median voter theorem, applied such that money is fungible across different forms of redistribution, is the view implicit in standard law and economics. It suggests that the distribution we see is roughly the right distribution. Given widespread concern about inequality and the evidence in favor of mental policy accounts, this view may be naïve.[154] At minimum, it is not obviously correct.
One way to view this Article is that it describes how to address redistribution within legal rules, *given a certain desire for redistribution*. If one is certain that the current distribution is a fair one, then the Article has little to contribute. If, on the other hand, one believes that the distribution is not currently fair, this Article gives guidance on how to maximize welfare given the maintained hypothesis about mental policy accounts on tax and nontax policies.
Another way to understand the Article is that, if one is uncertain about what the right distribution of resources is, the maintained hypothesis gives a strong reason to think that the political system will not yield enough redistribution if it only redistributes through taxes and makes other policies efficient. Under the maintained hypothesis, for which there is considerable (if not incontrovertible) evidence, we cannot depend on taxes to address the full amount of needed redistribution. Thus, we ought to redistribute at least some through nontax means, given the likelihood that taxes are inadequately redistributive.

Illegitimate to redistribute through administrative means
One may also argue that it is illegitimate to redistribute in ways that voters themselves do not appear to want. There are several responses. First, the normative frame here is the standard welfarist goal, so this non-welfarist "legitimacy" critique is not responsive to and gets no weight on welfarist grounds—at least not without a more complex story. Nevertheless, taking on the critique directly: This critique misunderstands the maintained hypothesis. The maintained hypothesis is that a large number of ordinary people do not think of the appropriate amount of "redistribution" across all policies. That is how economic policy wonks think about the issue,

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[154] Of course, there are many other views of politics as well, such as James Buchanan's "leviathan" view of government that it seeks to maximize revenue. GEOFFREY BRENNAN & JAMES M. BUCHANAN, THE POWER TO TAX: ANALYTICAL FOUNDATION OF A FISCAL CONSTITUTION (1980).

but not large numbers of ordinary people. Rather, they care about a variety of means—like transportation that can lead to equality of opportunity—and processes—like taxes, where people "deserve" to keep some of their income. The fact that Congress does not redistribute enough to achieve distributive justice through taxes alone does not imply that people are opposed to, say, valuing the rich and the poor equally in transportation cost-benefit analysis and, thus, spending more on the poor *relative to the efficient baseline*. These are different means. Congress has not dictated to the Department of Transportation how to allocate the funds between the rich and the poor.[155] It is not at all clear that voters or Congresspeople want to value the time of the rich more than the time of the poor. Especially in the absence of such guidance, if regulators at the Department of Transportation are welfarists, it is up to them to do what they can to maximize welfare.

Institutional capacity

A related critique is that it is beyond the institutional capacity of regulators to decide distributional questions. Acknowledged, deciding on distributional weights is a normative decision that will of necessity involve some arbitrariness. However, it is not difficult to assemble a list of numbers. And, more basically, for those who—out of a combination of concerns about political constraints or possibly normative commitments—find the case-by-case equal treatment more compelling, it is not clear what is complicated about setting equal values for everyone. Indeed, treating everyone equally rather than having different values for different modes of transportation based on different incomes seems to make the job easier, not harder.

VI.   Other Applications

This Article has illustrated how policymakers should maximize welfare while responding to political constraints using the example of regulators conducting cost-benefit analysis for transportation spending. But the implications of the social psychology of voters about taxation can be applied elsewhere too.

Courts

The analysis for courts is in some ways similar to that for agencies. Like agencies, courts are governed by expert actors who are (at least arguably) less accountable to the voters than Congress is. It seems unlikely that many statutes and constitutions would permit explicit judicial imposition of distributional weights. But, at least on marginal cases, judges could err on the side of distribution toward lower-income people. Or statutes could give latitude to juries to conduct such redistribution, such as providing broad latitude for suffering, which some evidence suggests juries used to provide larger damages to poorer groups.[156]

Probably more so than agencies, court-driven redistribution would raise issues of expertise, such as understanding what the distributional impacts in a given instance are. And, as for agencies, there is a risk of violating norms that legitimate the courts, at least if such reasoning were explicitly stated, which could undermine the rule of law. On the standard welfare account

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[155] *See supra* note __.

[156] Lucinda Findley, *The Hidden Victims of Tort Reform: Women, Children, and the Elderly*, 53 EMORY L.J. 1263 (2004) (arguing that damages caps had a disproportionate impact on women, children, the elderly, the disabled, since juries had been implicitly using categories like pain and suffering to make up for the fact that actual damages awards for these categories—being based on lost income—often were disproportionately low).

though—where neither legitimacy nor political dynamics matter—courts should adopt implicit distributional weights and redistribute accordingly.

Voters, legislatures & in-kind provision

A theme of this Article is that institutions and politics matter when considering what policies should be. Thus, the Article considers policies in a particular institutional setting. Another important institutional setting is the legislature itself. For example, if I as a well-trained economic policy wonk have one-piest views, but know that other voters do not, should that change how I vote for my legislator? Suppose, for convenience, that I am voting for a pivotal member of Congress (or alternatively a Presidential candidate). Suppose further that my vote is pivotal. Finally suppose (as is the case for nearly all the current Democratic primary candidates, including the most liberal ones) that I do not have an option who will give large cash transfers to the poor. But I do have one option who will raise a flat tax to fund an in-kind transfer and a second option who will not do so. If I'm a welfarist, there is a case that I should vote for the first option as a second-best alternative to the unavailable policy plan with more efficient redistribution.

Take the particular case of healthcare. As discussed in Section II, the standard economic view is that someone in his 50's earning $20,000 would not be willing to pay the $8,000 that health insurance costs for people of that age and would instead prefer cash.[157] But, given mental policy accounts and desert-based views on taxation, the case for providing healthcare to low-income people is strengthened. At the same time, commonplace rights-based views on the provision of basic healthcare strengthen political feasibility. As to whether it is welfare-enhancing to provide healthcare, this Article suggests analyzing the situation as follows: Look at the willingness to pay of the poor for the healthcare—appropriately adjusted by the right distributive weight—and compare that to the cost. So, adjusting for the factors above in Section IV, one would want a number X such that a dollar in the hands of those earning $20,000 is worth X more in welfare terms than the average person. Suppose that X is 4. Then, if the poor person is willing to pay $3,000 (more than one quarter of $8,000), it would be worth providing healthcare. And, if the poor person is willing to pay only $2,000 (less than one quarter of $8,000) it would not be worth providing the healthcare.

Similarly, standard logic suggests that low-income parents would likely prefer to receive cash instead of either subsidies or directly provided childcare. Childcare is expensive, and low-income people need cash. Of course, there may be important standard efficiency reasons for childcare provision, such as increasing the children's lifetime earning capacity, for which parents may be unwilling or unable to pay. But, beyond the efficient provision, one could apply the Article's logic here. Even the most economics-oriented voter should support "inefficient" childcare if he accepts that desert-based taxation places considerable limits on how redistributive taxes will be and if the willingness to pay of the poor is close enough to the cost of provision to justify the expense.

Congress and tax policy

If the maintained hypothesis is right that desert matters and that the desert comes from *pretax* incomes, then Congress could modify tax policy in several ways that both redistribute more and are politically feasible. One way is to tax high-income employees on the *employer* side to subsidize low-income employees. We are accustomed to thinking of employees as earning a

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[157] See *supra* note __.

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salary and then paying taxes based on that salary. In fact, employers can and do pay taxes based on their employees' salaries, principally through payroll taxes that nominally fund Social Security and Medicare[158] but also for purposes like unemployment insurance.[159] And, for high-income executives, the tax code limits the amount of compensation that publicly-traded employers can count as business expenses.[160] If voters read such taxes partly as taxes on businesses, rather than as taxes on the earners themselves, then it may be tolerable to impose such taxes on employers (though, of course, there would be implementation difficulties, such as the incentive for a high-income employee to split his job for one company into two related companies to avoid the tax). Likewise, since there appears be an aversion to providing cash transfers or tax credits in excess of an individual's tax liability, perhaps a subsidy to employers for hiring low-income workers would be a feasible way to drive up wages for low-skilled workers, and thereby increase their desert. Finally, policymakers could aid low-income taxpayers through tax expenditures, the popularity[161] of which could in part be driven by desert to pretax income. Like the commuting subsidy that phases out with income discussed earlier,[162] a variety of tax expenditures could be targeted at lower-income households.

Pedagogy

It is common in law schools to describe the "law and economics" solution as being the standard efficient solution. If "law and economics" means welfare-maximizing, and if welfare-maximizing means "in the real world," and if one is convinced that desert is important in tax policy, then this result does not hold. It may be unproductive to train students in this way, as they may be unaware of the nature of the underlying assumptions required by optimal tax theory. Like the discussion on voters and in-kind provision (which includes much of the "law"), it may be more accurate to train future voters and policymakers to be more keenly aware of the welfare-maximizing policies that are politically achievable.

Conclusion

We live in a democracy, with voters electing politicians and many institutions operating together to yield the set of policies that produce distributive outcomes. Yet, in making policy recommendations law and economics analysis (like economics analysis), overwhelmingly acts like there is one benevolent dictator.[163] However, because the standard law and economics approach to distributive questions requires many actors across many institutions to act in particular ways, it essentially requires that these actors agree with the propositions for which standard law and economics and optimal income theory stand: taxes should redistribute and everything else should be efficient. The Article argues that the twin enterprises of law and economics and optimal income taxation have been unsuccessful in convincing the general

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[158] I.R.C. § 3111 (2018) (imposing taxes on employers based on employee wages for hospital and old age and disability insurance).

[159] I.R.C. §§ 3301-11 (2018) (imposing unemployment taxes on employers and setting out the approval process for state unemployment systems).

[160] I.R.C. § 162(m) (2018) (limiting the deductibility of salaries at publicly held corporations).

[161] Clarke & Fox, *supra* note _; Haselswerdt & Bartels, *supra* note _.

[162] *See* Section III.C.

[163] Mankiw, *supra* note _; STEVEN SHAVELL, FOUNDATIONS OF ECONOMIC ANALYSIS OF LAW (2009); A. MITCHELL POLINSKY, AN INTRODUCTION TO LAW AND ECONOMICS (2018); ROBERT COOTER & THOMAS ULEN, LAW AND ECONOMICS (2016).

population of their positions. Since we live in a democracy, and people vote for their representatives, even assuming that standard law and economics is completely right normatively, legal rules should adjust to the constraints that voters' views impose on policymaking. Describing the unconstrained optimal policy is helpful for policymakers. So is describing what should actually be done in the real world. This Article is thus unapologetically "second-best" in developing an alternative set of policy recommendations that turns law and economics on its head: Rather than never redistributing through legal rules, legal rules should typically redistribute where feasible.

Such a "democratic" law and economics analysis allows consideration of a hallmark value of economic reasoning: tradeoffs. Pointing not only to the extent that taxes fail to redistribute, but also to a host of other factors that policymakers should consider, the Article points the way forward in the analysis of legal rules given widespread policy views at odds with law and economics reasoning. In particular, the Article shows how policy should respond given "mental policy accounts," in which voters have policy-specific distributive views without fully considering the complex optimization problem trading off each policy against all other policies. They instead use rules of thumb, such as the idea that the tax code should reflect desert, which limits its redistributiveness in practice.

But, though this Article develops a framework for analysis, many questions remain for future scholars. One set of questions is empirical. How fixed are views of desert that reduce the political desirability of redistribution through giving out cash? How fungible in practice is redistribution across different means? Put differently, what is the right model of politics for setting distributive policies: to what extent do our politics operate as if there really is one big pie to be maximized[164] versus operating through policy-by-policy battles, each with its own, at least partially independent, distributive outcome?[165]

Another set of questions is conceptual. This Article emphasizes political constraints that commonplace citizen views place on policymaking. In calling such views reflective of "mental policy accounts" and discussing political constraints, it may suggest that there is not a moral logic behind such views. But that is only one possible approach. Another one—described briefly in this Article, but mostly beyond the scope of this paper—is incorporation of these views as normatively valuable themselves. Such an approach would raise a host of questions, including how to measure and quantify such views and how to address repugnant views (e.g., racist ones). Yet another approach allows the possibility that nonstandard views contain information embedded in them.[166] For example, perhaps from interacting with their friends and family, people have a sense for whether others irrationally work too much or too little, with implications for the extent to which work should be encouraged or discouraged.

A final set of questions is methodological. The approach here is fundamentally technocratic: An expert in a particular institution knows (or has educated guesses about) the right answer, but there are constraints elsewhere in the system; this Article offers guidance on how such an expert policymaker should act. A separate question is to what extent do the uncertainties opened up by this Article militate in favor of normative modesty and deference to nonexperts or "democratically-determined" outcomes? Alternatively, how much of the traditional approach of

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[164] This is consistent with at least a simplified reading of the "median voter theorem" in which all that matters are overall distributive outcomes. *See, e.g.*, DOWNS, *supra* note __ at 51-74.

[165] *See* Liscow, *School Finance*, *supra* note_, at 5 (offering example of school finance in which increased court-mandated funding for school finance for the poor does not result in less support for the poor elsewhere).

[166] *See*, for example, Weinzierl, *A Welfarist Role for Nonwelfarist Rules*, *supra* note _ (taking a such an approach).

attempting to "debias" people from their nonstandard lay moral commitments should be pursued? Presumably, educating people away from misconceptions and biases is typically desirable. And, if a widespread perception that experts have failed to produce good outcomes helps generate some of the desire for a law and economics that is more deferential to the views of nonexperts, should attention be paid to backlash as well?

Answers may become apparent as the implications of other forms of more realistic psychology are considered in other contexts, including those outside of questions about inequality. For now, though, the example of regulatory cost-benefit analysis of transportation spending for the rich versus the poor illustrates the stakes. Current policy tends to help the rich get to work more than the poor, who need it the most. It is striking that even administrations like President Obama's, that hoped to address issues of inequality, adopted this policy on the basis of narrow, blinkered preconceptions about politics. More generally, something has not worked very well with the standard expertise for the past few decades, yielding neither robust economic growth[167] nor greater economic equality[168] nor greater trust in government policy.[169] Populist revolts around the world put economic policy up for grabs. It may be time to try something a little different.

APPENDIX

A. Model 0: Standard Model

Two representative economic agents of the rich and poor are indexed by r and p. Each supplies L_i units (e.g., hours per year) of labor, paid at wage w_r for the rich and w_p for the poor. Each receives utility from income after taxes, but also experiences disutility from providing labor. The individuals spend H_i units of time (e.g., hours per year) commuting to work, an activity that also detracts from utility. Additionally, the poor can receive a cash transfer s ($s \geq 0$). These preferences are represented with log utility functions given by,

$$U_r = \log\left(w_r L_r (1 - \tau) - \frac{1}{k+1}(L_r + H_r)^{k+1}\right) \tag{1}$$

$$U_p = \log\left(w_p L_p (1 - \tau) + s - \frac{1}{k+1}\left(L_p + H_p\right)^{k+1}\right) \tag{2}$$

Here, k is exogenously given, τ represents the rate at which the individuals' income is taxed, and H_i is the length of individuals' commutes. The first term, $w_i L_i (1 - \tau)$, plus s for the poor, is post-tax-and-transfer income. The second term, $\frac{1}{k+1}(L_i + H_i)^{k+1}$, is the disutility from supplying

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[167] The causes of reduced growth are myriad, *see, e.g.*, Robert Gordon, THE RISE AND FALL OF AMERICAN GROWTH: THE U.S. STANDARD OF LIVING SINCE THE CIVIL WAR 7-8 (2016) (arguing that "the pace of innovation since 1970 has not been as broad or as deep as that spurred by the innovations" of the century before), and the contribution of economic policy is unclear.

[168] Piketty & Saez, *supra* note_. But *see* STEVEN PINKER, ENLIGHTENMENT NOW: THE CASE FOR REASON, SCIENCE, HUMANISM, AND PROGRESS (2018) (arguing that, in many ways, outcomes in the world are improving).

[169] Uri Friedman, *Trust is Collapsing in America*, ATLANTIC (Jan. 21, 2018), https://www.theatlantic.com/international/archive/2018/01/trust-trump-america-world/550964.

labor and commuting to work. The effect of taxes on labor supply is what generates the distortion to efficiency in the model. H_i is a convex function of the level of government spending T_i on transportation services for each group. Specifically,

$$H_i = \alpha \frac{T_i^2}{2} + T_i z + Q \tag{3}$$

where $z < 0, Q > 0$, which yields a linear marginal impact of T on H.

Finally, T_i and s are funded by revenues from the tax on the individuals' income and are, along with τ, chosen by a social planner to maximize a welfare function $W(U_r, U_p)$, which is the sum of the individuals' utilities. The revenue constraints binding the social planner are given by,

$$R = w_r L_r \tau + w_p L_p \tau$$

$$R \geq T_r + T_p + s$$

B. Model A: Desert-Based Views on Cash Transfers

To represent the possibility that many people may have a distaste for giving out cash transfers, I first add to equations (1) and (2) a preference that the poor not receive transfers without working for them. I express this change by putting a distaste parameter λ, shared by both the rich and poor, on the transfer s (with $\lambda > 0$).

This addition yields the following utility functions:

$$U_r = \log\left(w_r L_r (1 - \tau) - \frac{1}{k+1}(L_r + H_r)^{k+1}\right) - \lambda s \tag{4}$$

$$U_p = \log\left(w_p L_p (1 - \tau) + s - \frac{1}{k+1}(L_p + H_p)^{k+1}\right) - \lambda s \tag{5}$$

All other features of the model remain unchanged. I then solve for the values that maximize utility, subject to the revenue constraint explained in subpart D below.

The main body uses parameters $w_p = 2, w_r = 5, k = 1.075, \alpha = 0.2, z = -0.6, Q = 1$, and $\lambda = 0.15$.

C. Model B: Less Redistributive Goals Overall

Model B includes a new parameter, F, that represents some discounting of the utility of the poor, such that U_i become,

$$U_r = log\left(w_r L_r (1 - \tau) - \frac{1}{1 + k}(L_r + H_r)^{k+1}\right) \tag{6}$$

$$U_p = F \cdot log\left(w_p L_p (1 - \tau) + s - \frac{1}{1 + k}(L_p + H_p)^{k+1}\right) \tag{7}$$

where $0 < F < 1$.

Model B captures an alternate explanation for low cash transfers, relative to the "efficient scenario," other than a disutility of cash transfers (i.e. $\lambda > 0$): distaste for the utility of the poor itself. F is calibrated to generate the same s as Model A produces. As for Model A, I then solve for the values that maximize utility, subject to the revenue constraint explained in subpart D below.

D. Setting the Transportation Budget

To have the same budgets in Models A and B, the Article follows the following two-step procedure: First, using the revenue, R^m, and transfer, s^m, found in unconstrained Models (m) A and B, find the average total transportation spending, T, of the two models:

$$T = \frac{(R^A - s^A) + (R^B - s^B)}{2} \tag{8}$$

Second, for each of Models A and B—keeping fixed the F already found in the unconstrainted Model B—add a new revenue constraint restricting the social planner to this level of transportation spending:

$$T = T_p + T_r \tag{9}$$

As a result of this procedure, Models A and B have the same transportation spending available to the regulators, consistent with the real Congressional appropriations process. In the main text, Models A and B reflect this constraint.[170]

E. Measuring Welfare Impacts

Welfare impacts are measured through the following four-step process: First, calculate welfare under the normatively correct model with optimal policy; call that C (for "correct"). Second, calculate welfare under the normatively correct model, but with the rich and poor transportation spending ratio (T_p/T_r) from the alternate model; call that E (for "erroneous"). We know that $C \geq E$ because C has the optimal (i.e., welfare-maximizing) policies under that model, while E does not. Third, calculate the amount of money that one must take away from the rich under the normatively correct model to lower welfare from C to E.[171] Fourth, divide that money taken from the rich by the total income that parties earn when utility is maximized under the normatively correct model.

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[170] Note that, since spending on transportation for the rich increases tax revenues by more than spending on transportation for the poor, there is a slight decrease in tax rate when more is spent on the rich to achieve a consistent budget across scenarios.

[171] For example, suppose that society's true preferences are captured by $\lambda > 0$ but that policymakers erroneously allocate transportation spending between the rich and poor as if $\lambda = 0$ and $F > 0$. Starting from the optimal welfare level C, find the value A in

$$U_r = \log\left(w_r L_r(1-\tau) - A - \frac{1}{k+1}(L_r + H_r)^{k+1}\right) - \lambda s \tag{10}$$

$$U_p = \log\left(w_p L_p(1-\tau) + s - \frac{1}{k+1}(L_p + H_p)^{k+1}\right) - \lambda s \tag{11}$$

such that the maximized sum of the two utilities (10) and (11) equals welfare level E.