Feedback on Optimal Taxation

1 Questions from Presentation

1. Why are prices type-specific?

   - Really, this comes from the fact that the final good producer has a downward-sloping demand function for each variety θ:

     $$y(\theta) = \frac{Y}{p(\theta)^{\varepsilon}}$$

     At the planner's optimum, $k(\theta)$ will be strictly increasing in θ, so $y(\theta)$ (and thus $p(\theta)$) will be unique. We should emphasize this.[1]

2 Ariel

1. What facts about heterogeneity in asset returns are we trying to capture?

   - Is it heterogeneity in *entrepreneurial outputs*, e.g. Zuckerberg and Gates?
     - I.e. real output
     - If so, elasticity argument makes sense
     - As does persistence in infinite horizon case
   - Or, is it heterogeneity in *asset returns/financial income*, e.g. David Tepper and other fund managers?
     - In this case, the idea of imperfect substitutability between output is perhaps less believable
   - My thought: the former is more what we have in mind
     - The households who are "heterogeneous" are producing capital goods, not generating income based on the outputs of other firms
     - It might be helpful to go to something like the SCF, to get some stylized facts on the degree of heterogeneity in asset returns/entrepreneurial income.

2. How do we rationalize our assumption that $p(\theta)$ is observable to the market, but not the government?

   - This will be important when we consider implementation, as it asks on which observables the government is able to condition capital taxes

[1] In the competitive equilibrium, prices will be such that $\theta p(\theta) = R$ for all θ, so prices in this case will be unique as well, as we will have $p(\theta) = R/\theta$.

3. In reality, we have differential taxation. What does our paper have to say about the existing tax code?
    - Is the existing degree of differentiation optimal?
4. Related to (3): other papers (mentioned in literature review) have generated differential rates. What do we *add* to this?
    - Similarly, is the main contribution here the theory, or the empirical implications?
5. A subtler discussion of the inefficiencies generated by price-taking is needed.
    - In most macro models, it is the case that individual agents do not internalize the effect of their decisions on prices. This is not inefficient!
    - To be more clear: when a type θ scales up, this affects prices for *everyone* who produces an intermediate good, which creates an externality.
    - In Dixit-Stiglitz notation, if I scale up, I change not only p_i, but also the price index P, which affects the demand function for *every* variety.