

The war between taxis and chauffeur-driven private cars: everyone has their reasons

By [Guillaume Allègre](#)

Editor's note: This post was first published on the OFCE blog on 21 October 2013, when the issue of car with driver services was a subject of intense debate. Given the recent events in France, it seemed appropriate to republish this text by Guillaume Allègre.

"What's worse is that everyone has their reasons"

Jean Renoir, *La Règle du jeu*

In the war between taxis and chauffeur-driven private cars (*voitures de tourisme avec chauffeur* – VTCs), everyone has their reasons. We noted in [a previous post](#) that the discourse on innovation masked a classic conflict over distribution between producers, who want to defend their incomes, and consumers, who want an inexpensive quick-response taxi service including at peak times. This conflict is coupled with another no less classic one between holders of licenses with a scarcity value and new entrants, who support opening up the market.

In this conflict the current regulatory system is absurd. Limiting the number of taxi licenses was intended to support the income of independent taxis and prevent them from working too many hours per day to achieve a decent income. However, the authorities have committed two errors. First, by allowing the transfer of licenses, they transferred the benefit of quotas on taxi drivers to the license owners: a taxi driver

now must either rent their license or buy it at a price reflecting its scarcity value (230,000 euros in Paris in 2012!). The current situation is even more absurd given that new licenses are [allocated free of charge](#) (to a waiting list): if the *préfet* allocates 1000 new licenses for free, then a value of 230 million euros at market prices will be transferred to the fortunate winners (who may subsequently rent out the licenses)!

The second error is that the government has allowed the taxi license bubble to expand. The high price of licenses clearly reflects that supply is too low relative to demand. But it would now be unfair to penalize those who have just spent a fortune acquiring a license by, for example, massively increasing their number: why should recent purchasers pay for the shilly-shallying of the regulatory authorities?

What's the solution?

It would be preferable to put an end to a system that generates constant worry about the value of licenses issued for free. But redeeming all the licenses at their market price would be costly and would result in the unjust enrichment of those who received a license for free.

One solution, which was proposed in the [previous post](#), is to buy the current licenses over time (as taxi drivers retire), not at their market value but at their acquisition value plus interest, and to assign new licenses that are free but not transferable. This system would compensate recent purchasers, without contributing to the unjust enrichment of those who have obtained a license for free or at a very low price. It would allow a transition from a system of transferable licenses to a system of non-transferable licenses in which the number of licenses in circulation and the division of the market between chauffeured cars and taxis would depend on the demand for services and not on the nuisance power of one or the other party. This system is of course complex, but it

would help to overcome past mistakes in the fairest way possible.

For further information: [Chauffeur-driven private cars: Victory of the anti-innovation lobby?](#)

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How can a basic income be defended?

By [Guillaume Allègre](#)

Following the submission of 125,000 signatures collected by organizations supporting the introduction of a basic income, Swiss citizens will vote in a referendum on a popular initiative on the inclusion of the principle of an unconditional basic income in the Swiss Federal Constitution.

An [OFCE Note \(no. 39 of 19 December 2013\)](#) analyses the grounds for supporting the institution of a basic income.

While a basic income can take many forms, its principle is that it is paid (1) on a universal basis, in an equal amount to all, without testing for means or needs, (2) on an individual basis and not to households, and (3) unconditionally, without requirement of any counterpart. A progressive version would add a fourth characteristic: it must be (4) in an amount sufficient to cover basic needs and enable participation in social life.

While this looks attractive, it is not easy to find grounds in

terms of distributive justice that are consistent with these four characteristics of a guaranteed basic income. So long as there exist economies of scale and a political trade-off between conditionality and the level of minimum income, then in a Rawlsian perspective a system of guaranteed minimum income like the French RMI / RSA programme (family-based with weak conditionality) seems preferable to a pure basic income. In addition, the generalized reduction of working time seems more sustainable than a guaranteed basic income for achieving the ecological and emancipatory goals that are often attributed to a guaranteed basic income.

It seems that the main advantage of a guaranteed basic income is that its universality means that it does not cause any undue use or non-use and so does not stigmatize the net beneficiaries of the system. From this perspective, minimum income support could be turned into a universal benefit, which would be less stigmatizing. This allocation needs to take into account family composition and set conditions on social participation. It would involve checks on black market work and include incentives to work. It would be supplemented by specific policies to provide support for children, the elderly and disabled people, *i.e.* people who do not respond to incentives, and it would complement the insurance system (unemployment, retirement, illness). The social protection system would thus not really be simplified but transformed in such a way as to avoid stigmatization and the lack of take-up.

While a guaranteed basic income is not a stupid idea, nor is it the miracle reform pictured by its advocates, *i.e.* a veritable Swiss Army knife for reforming social welfare, a social and environmental emancipator.

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Towards a major fiscal reform – at last!

By [Guillaume Allègre](#), [@g_allegre](#)

At the start of the week, Jean-Marc Ayrault announced an overhaul of the French tax system that would involve, among other things, a reconciliation between income tax and the CSG wealth tax. The OFCE will definitely take part in this debate, one that it has already tried to shed light on many times, in particular on the occasion of a [special “Tax Reform” issue of the Revue de l’OFCE](#), edited by Mathieu Plane and myself, and published in April 2012.

Several contributions [all in French] can be mentioned: Jacques Le Cacheux’s article in the *Revue* discusses the purposes and methods of tax reform (“[Sustainability and economic justice](#)”), while reviewing what the fundamentals of fiscal policy actually are. Nicolas Delalande conducts a historical analysis of resistance to tax reform and assesses the constraints on the development and implementation of reform (“[The political economy of tax reform](#)”), all of which seem to be topical subjects today. He stresses that: “Indeed, it may be more difficult to bring together positive support for a measure than to temporarily rally disparate opponents with sometimes conflicting motivations, especially if this involves creating new taxes or affecting established situations.” Mathieu Plane raises the question of the consequences of a tax increase (which did indeed occur in 2012-2013): “In a context of rising unemployment, will it be possible to generate a new large-scale fiscal shock without plunging France into a new crisis? The determination to reduce public deficits solely through structural adjustment is

hurting growth and unemployment” ([“Public finances: towards a new tax increase?”](#)). While the government is now announcing it wants a reform that does not change the tax burden, the question of the impact of fiscal adjustments (this time through cuts in public spending) on growth and, ultimately, the social acceptability of a structural reform of the tax system is still posed for the period 2014-2017. Will the government be able to implement a structural reform in a context where unemployment is high and not falling?

The merger of the CSG tax and income tax raises a number of questions that were already discussed in an article in the *Revue de l’OFCE* in 2007 ([“Towards the merging of income tax and the CSG?”](#)). The legislature needs to decide the issue of either joint taxation of spouses or individualisation for the merged tax as well as how to take children into account ([“Should the family quotient be defended?”](#)). This is a particularly sensitive topic, as it affects the representation of the family and the relationship between the State and the family. It has been the subject of controversy even within the OFCE ([“Reforming the marital quotient”](#), [“In defence of the family quotient”](#)).

By intermingling private interests (what charges for which households?) and social interests (what instruments for what purpose?), the tax issue has always been at the centre of democratic debate. The role of the OFCE is to contribute to this debate with solid arguments backed by data. OFCE researchers will continue to offer their own vision of a “good” tax reform, while discussing its objectives, impact and sustainability in a transparent and rigorous fashion.

How can one defend the 1%?

By [Guillaume Allègre](#)

In a [forthcoming article](#) in the *Journal of Economic Perspectives* [\[1\]](#), Harvard Professor and bestselling textbook author Greg Mankiw defends the income earned by the richest 1% and denounces the idea of taxing them at a marginal rate of 75%. For Mankiw, people should receive compensation in proportion to their contributions. If the economy were described by a classical competitive equilibrium, then every individual would earn the value of his or her own marginal productivity, and it would be neither necessary nor desirable for the government to redistribute income. The government would limit itself to correcting market distortions (externalities, rent-seeking).

In a [OFCE's Note \(no. 4, 19 July 2013\)](#), we show that the economy in which the 1% live is very different from a classic competitive equilibrium in ways that Mankiw does not discuss, which seems to us to be a significant limitation in his argument. It is *because* the 1% do not live in a world of perfect competition that they are able to secure astronomical incomes. The incomes received on the market by the 1% do not therefore correspond to their marginal social contribution. This does not mean that their social contribution is null, but rather that the market is unable to measure this contribution. These astronomical incomes cannot therefore be defended on the basis of “merit measured by marginal contribution”, as proposed by Mankiw.

See the following OFCE blogs on the same subject: “[Superstars and equity: Let the sky fall](#)” and “[Pigeons: how to tax capital gains](#)”.

[1] G. Mankiw, 2013, "Defending the one percent", forthcoming *Journal of Economic Perspectives*. http://scholar.harvard.edu/files/mankiw/files/defending_the_one_percent_0.pdf

Reforming the conjugal quotient

By [Guillaume Allègre](#) and [Hélène Périvier](#)

As part of a review of family benefit programmes ([the motivations for which are in any case debatable](#)), the government has announced plans to reduce the cap on the family quotient benefit in the calculation of income tax (IR) from 2014. The tax benefit associated with the presence of dependent children in the household will be reduced from 2000 to 1500 euros per half share. Opening discussion on the family quotient should provide an opportunity for a more general review of how the family is taken into account in the calculation of income tax, and in particular the taxation of couples.

How are couples taxed today?

In France, joint taxation is mandatory for married couples and civil partners (and their children), who thus form part of one and the same household. It is assumed that members of a household pool their resources fully, regardless of who actually contributes them. By assigning two tax shares to these couples, the progressive tax scale is applied to the couple's average revenue $[(R1 + R2) / 2]$. When the two spouses

earn similar incomes, the marital quotient does not provide any particular advantage. In contrast, when the two incomes are very unequal, joint taxation provides a tax advantage over separate taxation.

In some configurations, separate taxation is more advantageous than joint taxation; this is due partly to the particular way that the employment bonus and tax reduction [1] operates, and to the fact that separate taxation can be used to optimize the allocation of the children between the two tax households, which by construction does not permit joint taxation. Tax optimization is complex, because it is relatively opaque to the average taxpayer. Nevertheless, in most cases, marriage (or a "PACS" civil partnership) provides a tax benefit: 60% of married couples and civil partners pay less tax than if they were taxed separately, with an average annual gain of 1840 euros, while 21% would benefit from separate taxation, which would save them an average of 370 euros ([Eidelman, 2013](#)).

Why grant this benefit just to married couples and civil partners?

The marital quotient is based on the principle that resources are fully pooled by the couple. The private contract agreed between two people through marriage or a PACS constitutes a "guarantee" of this sharing. In addition, the marriage contract is subject to a maintenance obligation between spouses, which binds them beyond the wedding to share part of their resources. However, the Civil Code does not link "marriage" to the "full pooling" of resources between spouses. Article 214 of the Civil Code provides that spouses shall contribute towards the expenses of the marriage "in proportion to their respective abilities", which amounts to recognizing that the spouses' abilities to contribute may be unequal. Since 1985, Article 223 has established the principle of the free enjoyment of earned income, which reinforces the idea that marriage does not mean that the spouses share the same standard of living: "each spouse is free to practice a

profession, to collect earnings and wages and to spend them after paying the costs of the marriage". The professional autonomy of the spouses and the right to dispose of their wages and salaries are fully recognized in the Civil Code, whereas the Tax Code is limited to an overview of the couple's income and expenditures.

In addition, there is some dissonance between the social and the tax treatment of couples. The amount of the RSA benefit [income support] paid to a couple is the same whether they are married or common-law partners. As for the increased RSA paid to single mothers with children, being single means living without a spouse, including a common law partner. Cohabitation is a situation recognized by the social system as involving the pooling of resources, but not by the tax system.

Do couples actually pool their resources?

Empirical studies show that while married couples tend to actually pool all their income more than do common-law partners, this is not the case of everyone: in 2010, 74% of married couples reported that they pooled all their resources, but only 30% of PACS partners and 37% of common-law couples. Actual practice depends greatly on what there is to share: while 72% of couples in the lowest income quartile report pooling their resources fully, this is the case for only 58% of couples in the highest quartile ([Ponthieux, 2012](#)). The higher the level of resources, the less the couple pools them. Complete pooling is thus not as widespread as assumed: spouses do not necessarily share exactly the same standard of living.

Capacity to contribute and number of tax shares allocated

The tax system recognizes that resources are pooled among married couples and civil partners, and assigns them two tax shares. The allocation of these tax shares is based on the principle of ability to pay, which must be taken into account to be consistent with the principle of equality before

taxation: in other words, the objective is to tax the standard of living rather than income *per se*. For a single person and a couple with the same incomes, the singleton has a higher standard of living than the couple, but due to the benefits of married life it is not twice as high. To compare the living standards of households of different sizes, equivalence scales have been estimated ([Hourriez and Olier, 1997](#)). The INSEE allocates a 1.5 share (or consumption unit) to couples and a 1 share to single people: so according to this scale, a couple with a disposable income of 3000 euros has the same standard of living as a single person with an income of 2000 euros. However, the marital quotient assigns two shares to married couples but one to the single person. It underestimates by 33% the standard of living of couples relative to single people, and therefore they are not taxed on their actual ability to contribute.

Moreover, once again there is an inconsistency between the treatment of couples by social policy and by fiscal policy: social security minima take into account the economies of scale associated with married life in accordance with the equivalence scales. The base RSA (*RSA socle*) received by a couple (725 euros) is 1.5 times greater than that received by a single person (483 euros). There is an asymmetry in the treatment of spouses depending on whether they belong to the top of the income scale and are subject to income tax, or to the bottom of the income scale and receive means-tested social benefits.

What family norms are encapsulated in the marital quotient?

The marital quotient was designed in 1945 in accordance with a certain family norm, that of Monsieur Gagnepain and Madame Aufoyer ["Mr Breadwinner and Ms Housewife"]. It contributed together with other family programmes to encouraging this type of family organization, *i.e.* the one deemed desirable. Until 1982, tax was based solely on the head of the family, namely the man, with the woman viewed as the man's

responsibility. But far from being a burden on her husband, the wife produced a free service through the domestic work she performed. This home production (the care and education of children, cleaning, cooking, etc.) has an economic value that is not taxed. Single earner couples are thus the big winners in this system, which gives them an advantage over dual earner couples, who must pay for outsourcing part of the household and family work.

In summary, the current joint taxation system leads to penalizing single persons and common-law couples compared to married couples and civil partners, and to penalizing dual-earner couples compared to single-earner couples. The very foundations of the system are unfavourable to the economic liberation of women.

What is to be done?

The real situation of families today is multiple (marriage, cohabitation, etc.) and in motion (divorce, remarriage or new partnerships, blended families); women's activity has profoundly changed the situation in the field. While all couples do not pool their resources, some do, totally or partially, whether married or in common law unions. Should we take this into account? If yes, how should this be done in light of the multiplicity of forms of union and the way they constantly change? This is the challenge we face [in reforming the family norms and principles that underpin the welfare state](#). Meanwhile, some changes and rebalancing could be achieved.

Currently, the benefit from joint taxation is not capped by law. It can go up to 19,000 euros per year (for incomes above 300,000 euros, an income level subject to the highest tax bracket) and even to almost 32,000 euros (for incomes above 1,000,000 euros) if you include the benefit of joint taxation for the exceptional contribution on very high incomes. For comparison, we note that the maximum amount of the increase in

the RSA for a couple compared to a person living alone is 2900 euros per year. The ceiling on the family quotient (QF), which is clear, is 1500 euros per half share. A cap on the marital quotient of 3000 euros (twice the cap on the QF) would affect only the wealthiest 20% of households (income of over 55,000 euros per year for a single-earner couple with two children). At this income level, it is likely that the benefit from joint taxation is related to an inequality in income that is the result of specialization (full or not) between the spouses in market and non-market production or that resources are not fully shared between the partners.

Another complementary solution would be to leave it up to every couple to choose between a joint declaration and separate declarations, and in accordance with the consumption scales commonly used to accord the joint declaration only 1.5 shares instead of 2 as today. The tax authorities could calculate the most advantageous solution, as households do not always choose the right option for them.

A genuine reform requires starting a broader debate about taking family solidarity into account in the tax-benefit system. In the meantime, these solutions would rebalance the system and turn away from a norm that is contrary to gender equality. At a time when the government is looking for room for fiscal maneuvering, why prohibit changing the taxation of couples?

[\[1\]](#) A tax reduction [*décote*] is applied to the tax on households with a low gross tax (less than 960 euros). As the reduction is calculated per household and does not depend on the number of persons included in the household, it is relatively more favourable for singles than for couples. It helps ensure that single people working full time for the minimum wage are not taxable. For low-income earners, the reduction thus compensates the fact that single persons are

penalized by the marital quotient. No similar mechanism is provided for high-income earners.

France, Germany: The nonworking poor

By [Guillaume Allègre](#)

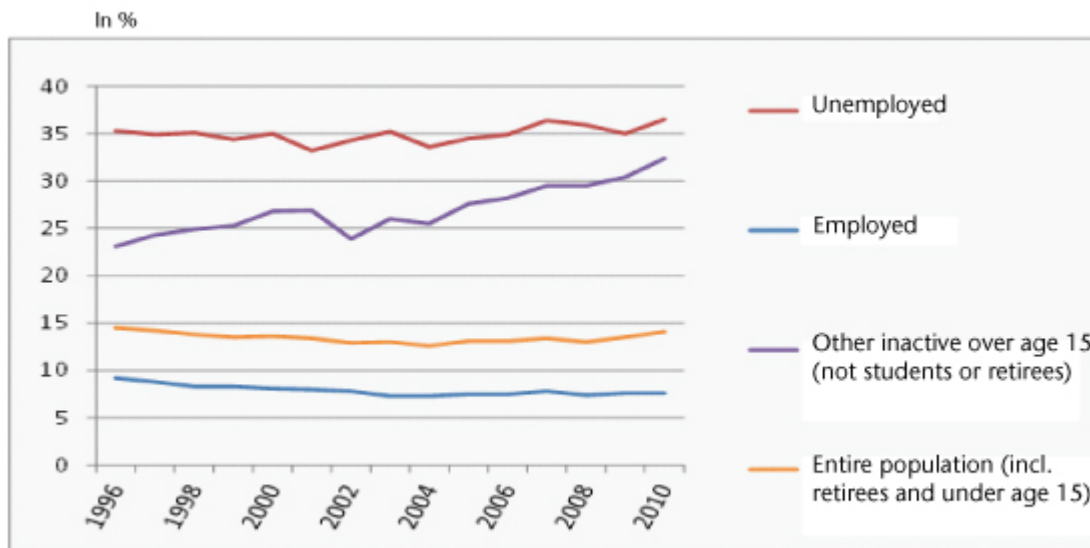
“The ways of thinking society, managing it and quantifying it are indissolubly linked”

[Alain Desrosières](#), 1940-2013

The subject of working poverty emerged in Europe in public debate and academic discussion in the early 2000s, in parallel with the implementation of policies to “make work pay”. European guidelines on employment have explicitly mentioned the need to reduce working poverty since 2003, and Eurostat set up an indicator on the working poor in 2005 ([Bardone and Guio](#)). In France, policies to make work pay have taken the particular form of earned income supplements ([PPE](#), then [RSA](#)). In Germany, a series of reforms of the labour market and social welfare (the Hartz Laws) were introduced in the early 2000s with the aim of activating the unemployed. Critics of the German reforms often highlight the proliferation of atypical forms of employment ([Alber and Heisig, 2011](#)): the recourse to part-time, low-wage work and mini-jobs without social protection. In France as in Germany, this focus on workers has masked a less well-known aspect of the changing face of poverty: among working-age people, it is poverty among the unemployed (the “inactive” in France, the “unemployed” in Germany) that has been on the rise since the late 1990s.

Figure 1 shows the change in the poverty rate for individuals between 1996 and 2010, calculated at the threshold of 60% of the median living standard, according to their employment status. Two points stand out. First, poverty primarily affects the unemployed: their poverty rate was about 35% over this period. Second, economically inactive people over age 15, who are neither students nor retired (called “other inactive”), *i.e.* the “discouraged unemployed” and men and women (especially women!) in the home, are the group most affected by the rise in poverty. Their poverty rate was 23% in 1996, but hit 32% in 2010. At the same time, poverty among people in work fell from 9% to 8%. As a result, while the economically active with jobs accounted for 25% of the poor in 1996 and “other inactive” 12%, the latter’s share of the poor rose to 17% in 2010 while the share of the active declined to 22%. The weight of the working poor among all poor people is tending to decrease, while the weight of the inactive is rising.

Figure 1 : Poverty rates according to activity status, France



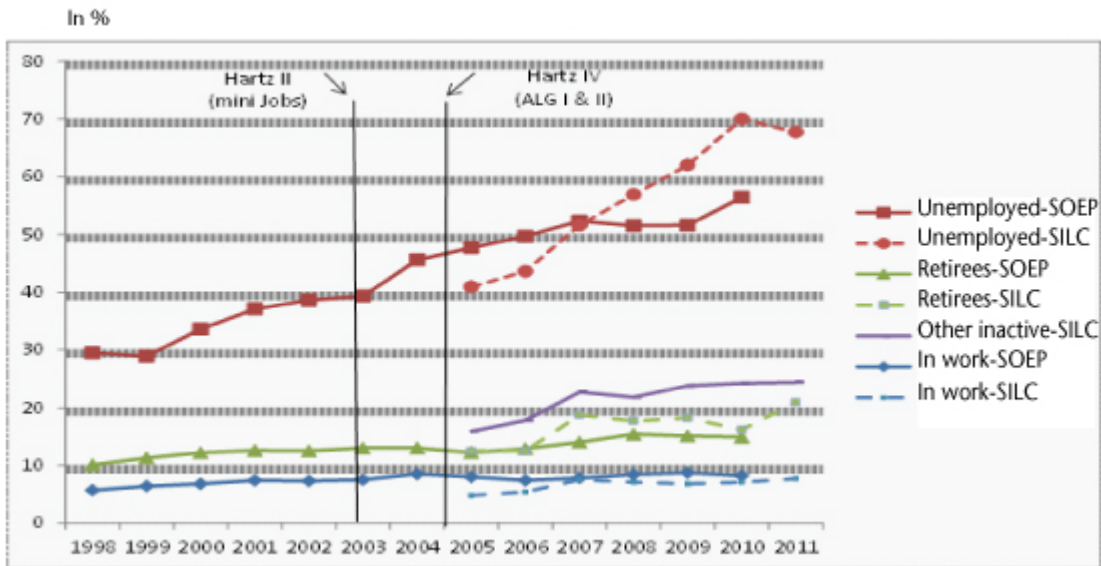
Source : Insee-DGI, Enquêtes Revenus fiscaux et sociaux rétrospectives 1996 à 2004 ; Insee-DGFiP-Cnaf-Cnav-CCMSA, Enquêtes Revenus fiscaux et sociaux 2005 à 2010.

As for Germany, the analysis of poverty rates by employment status is fraught with discrepancies attributable to the sources, in particular with regard to changes in the poverty level among the unemployed, which according to Eurostat (EU-SILC survey) is much higher than in the national SOEP survey (see Figure 2). Despite the statistical uncertainties, it is

still clear that poverty affects the unemployed above all, and that their poverty rate has risen substantially: from 30% to 56% between 1998 and 2010, according to the SOEP survey, which is generally considered more reliable than the SILC ([Hauser, 2008](#)). While poverty is increasing for all categories of the population ([see Heyer, 2012](#)), it is among the unemployed that it is most pronounced.

The increase in poverty among the jobless is the result of certain provisions of the Hartz IV laws, which are less well known than those establishing mini-jobs (Hartz II). Prior to this legislation, the jobless could receive unemployment benefits for a maximum period of 32 months, after which they could receive means-tested unemployment assistance for an indefinite period ([Ochel, 2005](#)). But unlike the ASS benefit [i] in France, the amount of this assistance depended on the net income at the last job and provided a relatively generous replacement rate (53% of net income for people without children). This system was replaced starting in 2005 by a much less generous compensation, based on the goal of employment activation. Unemployment benefit (*Arbeitslosengeld I* – ALG I) was limited to 12 months for unemployed people under age 55, and the grounds for penalties were expanded. Following this period, unemployment assistance (*Arbeitslosengeld II* – ALG II) is greatly reduced and essentially serves only as an ultimate safety net: the amount for a single person is limited to 345 euros per month, while the penalties have also been expanded and toughened [ii]. Germany's strategy to promote employment hence uses two levers: reducing income support for the unemployed, and penalties. While this policy may have contributed to lowering unemployment (see [Chagny, 2008](#), for a discussion of the controversial impact of this reform), by its very design it has had a significant impact with regard to poverty among the unemployed.

Figure 2 : Poverty rates according to employment status and source, Germany



Source : Eurostat (SILC) ; DIW (SOEP).

One paradox that needs to be examined is the only small change since the early 2000s (at least according to the SOEP survey) of the poverty rate among people in work. Indeed, during this period, the proportion of low-wage workers rose and the recourse to part-time work increased sharply, without a substantial rise in the poverty rate for people in work. In 2010, 4.9 million people (12% of people in work) held a mini-job for which they cannot receive more than 400 euros per month in earned income ([Alber and Heisig, 2011](#)). There has also been the growth of part-time work with social protection (from 3.9 million jobs in 2000 to 5.3 million in 2010). We would expect therefore to see an increase in working poverty. But this is being countered by two factors: the development of opportunities for cumulation with unemployment benefits (the third lever of the employment activation policy), and family solidarity. Indeed, part-time and low-wage jobs are predominantly held by women, who account for two-thirds of workers on low annual incomes [iii]. The income of their spouse, when they have one, often enables them to avoid poverty, as the income of all household members is aggregated to determine the standard of living and poverty. In this respect, to paraphrase [Meulders and O'Dorchai](#), the household is a fig-leaf concealing women's low incomes. Lone mothers, on the other hand, are especially affected by poverty: the

poverty rate is about 40% among single-parent families.

From the perspective of the indicators, the use of the category “working poor” thus poses several problems. First, the category hides the role of unemployment and inactivity as determinants of poverty; by its very name, it highlights one important determinant of working poverty (“work doesn’t pay”) in relation to other determinants (“small number of hours worked” or “heavy family responsibilities”). Public policies based on this approach thus run the risk of limiting the population targeted by the fight against poverty (in France, people on unemployment benefit are excluded from the RSA-activité [income supplement for the working poor]) and of focusing on strengthening financial incentives for returning to work in order to stimulate the supply of labour, even though the high level of unemployment is related to the demand-side rationing of labour. Second, the category is blind to gender inequality: women are more often poor and constitute the majority of low-wage workers, but they are less likely to be working poor! ([Ponthieux, 2004](#)) If all that we manage well is what we measure, it is necessary that the measure be easily interpreted by policy makers. Reducing inequalities in living standards (between households) and in earned income (between individuals) are two legitimate public policy goals (as explained [here](#) [in French]), which need to be measured separately, just as these two goals require the use of specific instruments.

From the standpoint of public policy, the change in poverty based on employment status in France and Germany emphasizes that an effective fight against poverty requires addressing all forms of poverty. For the working-age population, in economies where dual-earner couples have become the norm, this means putting in place policies on full-time work and full employment policies that do not foster atypical forms of work. This requires, from a macroeconomic point of view, growth or job-sharing (and the associated income-sharing) and, from a

microeconomic point of view, meeting needs with respect in particular to childcare, training and transport. While these policies are costly, more economical measures, such as strengthening financial incentives, have failed to demonstrate that they can actually reduce overall poverty.

[i] The *Allocation de solidarité spécifique* (ASS), means-tested benefits paid to unemployed persons whose right to unemployment benefits has expired.

[ii] In total, 1.5 million penalties were applied in 2009, for 2.8 million on jobless benefits, compared with 360,000 in 2004, for 4 million on jobless benefits (according to [Alber and Heisig, 2011](#), Tables 6-8, pp. 24-30).

[iii] Set at the threshold of two-thirds of median salary.

Superstars and fairness: Let the sky fall

By [Guillaume Allègre](#)

Are actors overpaid? A column by [Vincent Maraval](#) has launched a debate that is in essence ideological ... in a good way. Indeed, it seems proper that high incomes need to be justified based on arguments that can convince the largest number of people. Pay levels cannot be fair unless they are publicly defensible. In this spirit, by drawing on an analysis of the economics of superstars, this post supports the idea that a small number of actors, and of artists in general, receive collectively constructed income, which justifies an

intervention that is designed to reduce income inequalities.

How do you explain the huge revenues of a handful of singers or actors while most artists struggle to make a living from their work? The superstar effect has been analyzed by economists based on a seminal paper by Rosen ([The Economics of Superstars](#)). It is related to the structure of demand (by nature gregarious), technology (which allows broadcasting productions at a low cost) and the legal environment (which can be used to exclude stowaways or freeriders). To this we must add that the special position of entertainment stars allows them to capture a large share of the collectively constructed income. These characteristics justify a high level of income redistribution. It does not seem that this matter can be resolved satisfactorily just through the tax system: a tax rate of 75%, [which is already viewed as confiscation](#), is not enough in an economy where superstars can earn 100 times as much as the average income – not to mention the risk of tax exile. Intervening directly in the institutional environment and on pay, especially for projects that receive public funds or assistance thus seems legitimate.

Is it fair that artists who are successful are subject, for example, to a tax rate of 75% for incomes of over a million euros, or is this just confiscatory? If this question can be raised for all activities, entertainment (artistic or sports) can be considered as a case study, because there is little doubt about spectators' willingness to pay, and there is no information asymmetry or principal-agent problems. The issue of the compensation of artists does not arise in the same way as, for example, business leaders who are engaged in activities whose contribution is difficult to estimate (*i.e.* their marginal productivity), and who can exercise control over the committees that set their pay: are the company's good results due to chance, to the work of the CEO, to the entire management team or to the effort of all the employees? Does the CEO's salary depend on their contribution or on their

ability to convince the remunerations committee of their value? [In a recent note](#), Galbraith makes a distinction between the case of Depardieu and that of business leaders [i]. In his book *Anarchy, State and Utopia*, Robert Nozick uses the transparency of the entertainment industry and takes the example of a superstar of the time, the basketball player Wilt Chamberlain (the book was published in 1974), to justify very high incomes. His argument is famous: if a million people are willing to pay 25 cents extra to see Wilt Chamberlain play, and he signs a contract with a basketball team offering to pay him 25 cents per ticket, giving him an income of \$250,000, which is well above the median or average income at the time, is fair and legitimate. Redistributing this income would be immoral; freely consented inequalities must be respected.

But how do we explain the fact that many individuals are willing to pay so much for a particular artist, and nothing for most of the others? Where does this winner-take-all characteristic come from? In other markets, if a service is perceived as having a slightly lower quality, many buyers are willing to buy it for a bit less than the high-quality service, so that a range of quality levels co-exist. In contrast, in the world of entertainment, a relative handful earn astronomical sums. In a seminal article, *The Economics of Superstars* (1981), Rosen explains this phenomenon by the structure of demand and production technology. What matters is that lesser talents cannot easily replace the greater talents (people would rather watch one top show than ten mediocre shows) and that the cost of production does not increase in proportion to the quantity supplied (the effort is the same whether 10 or 1000 people are in the audience or buy the book). In fact, according to Rosen, it is technology (especially television) which explains the sharp increase in the income of superstars. He concludes his article with these words: "What changes in the future will be wrought by cable, videocassettes, and home computers?"

The high incomes of superstars are not simply the result of a slightly superior talent (as in the model proposed by Rosen). The studios are not simply paying for the incomparable talent of the actors in *Friends* or of Depardieu in *Astérix and Obélix at the Olympic Games*. Some actors actually manage to capture an income that is built in part by them but also by chance and by the behind-the-scenes work of many other contributors to the entertainment economy. The actors in *Friends* were able to negotiate significant wage increases as the series was renewed again and again. While under the season 1 contract each actor was paid 22,500 dollars per episode, they received \$75,000 per episode in season 3, \$100,000 in the fifth, \$125,000 in the sixth, \$750,000 in seasons seven and eight and one million dollars for the last two seasons, more than 40 times higher than in the first season, whereas the audience only doubled between the first and last season (source: [Wikipédia](#)). In season 2, the pay rates were negotiated individually, but the actors, including Jennifer Anniston and David Schwimmer, whose wages were well above those of the rest of the group, quickly realized the importance of collective bargaining: while the studio might manage to dispense with any individual actor (by replacing them or killing off their character), they could not replace the entire cast. Clearly, the 40-fold increase in income is not due to any exponential increase in the actors' talents, but to the fact that they have benefited from the commitment of the spectators to the series, a commitment that was forged by the actors but also by the work of the scriptwriters, designers, and directors in the early seasons. Because they embody the series and bargained collectively, the actors in *Friends* managed to capture for themselves an economic rent that was collectively constructed.

Similarly, if Depardieu has succeeded in establishing himself as a national figure, it is partly due to his talent but also due to the work of the many directors who have used him (and their scriptwriters, etc.). While it is difficult to explain the success of any particular cultural product, the element of

chance or luck should not be overlooked. This is related to one of the characteristics of cultural products: they are generally more appreciated when the experience is shared because, as [André Gunthert](#) emphasises, cultural consumption gains meaning through its socialization (conversation, judgment, citation, re-use). Success thus breeds success, which explains phenomena of the type seen with the films *Les Intouchables* and *Bienvenue chez les Chtis*, whose success cannot be explained solely by the quality of the films. If in Rosen's model, we replace talent by audience (people prefer to watch one show with a large audience rather than ten shows with small audiences), a small initial advantage, which may be due to chance, but not only to chance, can turn into a phenomenon due to a snowball effect ([Adler, 1985](#)). In addition, the fact that televisions require stars to get co-financing for films, [as Maraval explains](#), shows why celebrity is self-reinforcing and leads to a concentration of wealth in the hands of a few very well-known actors. The small initial advantage in terms of reputation is not necessarily due to pure chance, as can be seen by observing the number of sons and daughters in the profession, including the offspring of producers and directors. Stardom is also a status where you can enjoy a reputation that is "ill-gotten" and [where negative buzz also provides visibility](#).

For the superstar effect to be converted into a high income, artists need to be able to exercise their intellectual property rights and exclude freeriders. The artists need a legal environment that legally recognizes and enforces their intellectual property rights [ii]. The fact that actors can capture a significant share of the income is partly a consequence of incomplete contracts and asymmetries in legislation on intellectual property. For example, California law prohibits contracts with terms of over seven years, which explains the jump in the remuneration of actors for series with long runs. Actors can also always threaten to quit, which constitutes a credible threat if they have gained enough

reputation. The studios cannot contractually retain the anticipated benefits of this reputation. The actors also benefit from the fact that other people cannot or can no longer assert their right to intellectual property. Patents on television broadcasting technology have long been in the public domain: industrial property rights are much shorter (maximum 20 years) than artistic copyrights (70 years after the author's death in France and the United States). A certain number of ideas that contribute to the success of cultural products (films, series, etc.) are not copyrightable: we do not copyright a joke, a story, a way of filming or editing, or a concept or idea for a scenario. The fact that some players in the entertainment and cultural industry can capture an income is therefore not merely the natural consequence of differences in talent or an objective way of measuring the contribution of each, but flows largely from the specific provisions governing intellectual property rights that establish what is copyrightable or not, along with the duration of the protection. It is not at all clear, for example, that we should give celebrities the exclusive right to commercially use their public image (see [Madow, 1993](#)).

In addition to the protection of intellectual property rights, government intervention in the film industry can be considered to be massive (whether in the form of subsidies or regulations): investment quotas in the production and broadcasting of French-language cinematographic works for TV channels; the artist unemployment scheme, whose deficit is financed out of general taxation; tax incentives (SOFICA, tax credits); reduced VAT; aid from local authorities (regional, departmental and municipal) for filming, festivals and local cinemas ; and the financing of the CNC (mostly from industry revenues and already partly redistributive). Moreover, [Coq et al. \(2006\)](#) show that changes in regulations, which have favoured the goal of defending the market share of domestic films rather than pluralistic creation within the country, have led to a greater concentration of resources for expensive

films, while the requirements placed on television exacerbate the superstar effect, as the networks are fond of stars.

From an economic viewpoint, two arguments thus justify redistribution of income: the capture of an economic rent constructed by many individuals and the element of chance (to which should be added the weight of public intervention in the cinema). In the presence of chance or risk, redistribution plays the role of an insurance, which can increase both the equity and efficiency of the system. From the viewpoint of equity, before the winners are revealed, risk-averse individuals would be willing to socialize the risky gains. From the viewpoint of efficiency, too much risk leads to underinvestment on the part of very talented individuals who do not want to engage in an activity where there are too few chosen (and where they have too few connections). From the viewpoint of both equity and efficiency, the structure of the entertainment economy justifies a significant level of redistribution. This redistribution can take several forms: (1) universal taxation coupled with sector subsidies, (2) insurance, for example, based on the specific status of the entertainers, (3) minimum and / or maximum wages, in particular for projects receiving public funding or support (France Television, Regional Councils, etc. [iii]). Economists generally prefer the method of taxes or social insurance over direct interventions on wages, leaving the market to operate freely before redistributing income. The tax system also helps to avoid the arbitrary effects of thresholds when setting a maximum wage. However, in practice, fiscal redistribution faces a major limitation: once gross salaries are determined by the interaction between market forces and the institutional environment, they are generally considered legitimate; a high tax rate, e.g. 75%, may then be regarded as confiscatory, or as representing an “undue burden”, in the words of [a recent decision](#) of the Constitutional Council, even though such rates could clearly be insufficient to reduce the inequalities in a superstar economy where income differentials can reach ratios

of 1 to 100. Reducing inequalities then requires direct intervention both in the institutional environment – for example, by reducing the duration of intellectual property rights – and on the determination of remuneration, which is all the more justified in a highly regulated and subsidized sector.

[i] “In reality, the case of Depardieu is very different. He grew rich thanks to his talent. This is not the case of business leaders! Their revenue comes from companies that have earned money through a collective effort.” From our perspective, there is a capture of a collectively-constructed economic rent in both cases.

[ii] In this sense, we must understand the libertarianism of Nozick as the absolute respect for individual property rights (which have a natural character). This is a long way from the libertarian liberalism that seeks to minimize external constraints, since in this case it is necessary for authority to enforce property rights. This explains why a contradictory mix of appeals to freedom and to authoritarianism stems from this doctrine.

[iii] As well as private television channels with respect to their obligations, as they benefit in return from the free use of the broadcast spectrum, which is similar to a public subsidy.

Pigeons: how to tax

entrepreneurial income? (2/2)

By [Guillaume Allègre](#) and [Xavier Timbeau](#)

After having proposed in the [2013 Budget Bill](#) to tax gains from the sale of securities at the progressive scale used by France's income tax, and no longer at a proportional rate of 19%, the government has now promised to correct its course, under the pressure of a group of entrepreneurs who rallied on the social networks under the hashtag #geonpi ("pigeons", using French verlan slang, which inverts syllables). [An amendment proposed by the government](#) introduces an exemption from the income tax rate on the condition of a specified period of ownership (2 years), a percentage of ownership of the shares (10% of voting rights) and status as an employee or director. Entrepreneurs will thus remain subject to the proportional tax rate of 19%. [In a first post](#), we described how capital gains should be taxed in an equitable way with levies on income from work. In what conditions could entrepreneurs and people with a significant stake in a company justify special treatment of their gains from the sale of securities?

At first glance, the joint taxation of capital income and labour income is particularly relevant for entrepreneurs, who can choose to pay themselves either in the form of wages or in the deferred form of capital gains. In this context, the neutrality of the tax is fair and effective in so far as it does not distort the entrepreneur's choice.

Advocates for the special treatment of entrepreneurship advance several arguments: (1) Entrepreneurship contributes a strong positive externality in terms of innovation, growth and employment. (2) Entrepreneurs are deserving (they work hard and take risks). (3) The risks taken by entrepreneurs cannot be diversified. They cannot offset their capital losses and gains, so the taxation of capital gains in itself reduces the

ex-ante yield from entrepreneurship, and therefore the number of entrepreneurs, growth and employment.

The counter-arguments to this are:

(1) Income tax is a poor instrument for taking into account externalities: from this perspective, researchers, teachers, social workers, doctors, and in general all occupations in activities that produce externalities (health, education, culture, etc.) could claim a tax benefit (journalists have already managed to hold their own), so what is to be feared, in this context, is that the tax benefit reflects the level of influence rather than the economic externality.

(2) From the point of view of equity, there is no reason to treat labour income and the risky income of entrepreneurs differently. Young people without connections who engage in long-term studies also take a risk: like entrepreneurs, they forego an immediate wage income for an uncertain future income (they may fail in their studies or choose a poorly paid career, etc.). The entrepreneur's income already takes into account the risk and the effort: it is because entrepreneurship is risky and demanding that it is potentially profitable. The government cannot – and should not – distinguish the share of income (labour or capital) that derives from risk, effort and talent from the share that is the fruit of chance, social networks and circumstance. Finally, taking risk into account by rewarding those who have the good fortune to emerge as winners (those with capital gains) reflects a peculiar vision of equity: in the presence of chance, equity advocates compensating the losers rather than adding to the rewards of the winners.

(3) In terms of efficiency, in the presence of a chance event, compensating the losers acts as insurance, which encourages risk-taking. Domar and Musgrave (1944) emphasized long ago that the proportional taxation of income from business encourages the taking of entrepreneurial risk. This

result is based on the assumption of a negative income tax in the presence of losses, so that the State acts as a supportive partner. While this assumption is justified for large corporations that can consolidate the gains and losses of their subsidiaries and / or carry forward certain losses, it is less legitimate for entrepreneurs who cannot diversify the risks they take. The limited liability company, the limitation on the goods that the entrepreneur can pledge, the possibility of being able to refuse an inheritance so that any eventual debts (including tax and social charges) of entrepreneurs facing failure can then be wiped clean (whereas any eventual assets, if successful, may be transmitted) are all devices that favour individual risk-taking. A more favourable tax treatment for the allocation and carrying-forward of shortfalls and capital losses for entrepreneurs and individuals who hold a significant proportion of a company could enhance these opportunities and increase the incentives for entrepreneurship.

Entrepreneurs need to have the benefit of a legal and administrative environment that is simple and accessible. The authorities can strengthen the entrepreneurial ecosystem by bringing together entrepreneurs, financiers (in particular France's Public Investment Bank), incubators and research laboratories.

Ex-post, from the point of view of equity as well as efficiency, it is the entrepreneurs who fail, and not those who succeed, that must be helped via personal bankruptcy laws, unemployment compensation, and favourable tax systems for deductibility and carrying forward losses. Implicit subsidies for those who succeed, through income tax, while the potential rewards are already extremely large, are instead a form of social Darwinism.

Pigeons: how to tax capital gains (1/2)

By [Guillaume Allègre](#) and [Xavier Timbeau](#)

After having proposed in the [2013 Budget Bill](#) to tax gains from the sale of securities at the progressive scale used by France's income tax, and no longer at a proportional rate of 19%, the government has now promised to correct its work under the pressure of a group of entrepreneurs who rallied on the social networks under the hashtag #geonpi ("pigeons", using French verlan slang, which inverts syllables). An [amendment to the Bill](#) was passed to this effect. Here we discuss the equitable taxation of capital gains on securities. In a second post, we will discuss the specificity of entrepreneurship.

The Budget Bill reflects François Hollande's commitment to enact a major tax reform to make the contribution of each fairer: "capital income will be taxed just like work income" (Commitment 14 of the 60 commitments for France). When the capital results from the saving of employment income that was paid at a "normal" rate, taxing it poses the problem of double taxation and may seem questionable. Note, however, that in a financialized economy income from capital is not simply the result of saving, but also the direct result of an activity (see issue 122 of the special *revue de l'OFCE* issue on tax reform, and in particular Allègre, Plane and Timbeau on "Réformer la fiscalité du patrimoine? "Reforming wealth taxation"). In this sense, capital income derives from households' ability to pay, just as does labour income. The progressive tax on income must apply to all income, whether it comes from capital or labour, in order to respect the principle of horizontal equity, *i.e.* "on equal income, equal

tax”.

With respect to gains on disposal, only the change in the real value of the capital can be considered as income: if the value of a good has increased at the same rate as inflation, the nominal gain, even if positive, does not cover the implicit cost of ownership. The Bill provided that gains on disposals are entitled to an allowance based on the length of holding, which was copied from that applicable to real estate gains. The amendment reduces the durations of holding relative to the original text:

– the capital gains taxable at the income tax rate are reduced by an allowance equal to:

a) 20% of their value when the shares, units, rights or securities have been held for at least two years and less than four years at the date of sale;

b) 30% of their value when the stocks, units, rights or securities have been held for at least four years and less than six years at the date of sale;

c) 40% of their value when the stocks, units, rights or securities have been held for at least six years.

This type of allowance on the nominal capital gain is a poor instrument for taking account of inflation: if the variation of the real value of the capital is zero, then the tax should be zero (there is no real income), whereas an allowance will only reduce it; and on the contrary, if the change in the real value of the capital is much higher than inflation, then the allowance will be too favourable; the allowance is a fixed amount based on increments, while price rises are a continuous phenomenon. At least the allowance does not reach 100%, which is still the case for most real estate capital gains, which are totally exempt from gains on property that has been held 30 years. A good system would not apply an allowance to the nominal gain, but would actualize the purchase price using an

index that reflects prices, which would make it possible to determine changes in the real value of the asset.

Examples: a good is purchased in January 2000 for 100. It is re-sold for 200 in January 2011. The nominal gain is 100. The allowance of 40% applies, and hence, in the system proposed by the government, the taxation would be on 60, and incorporated in the income tax. The variation in the real value of the capital is 79, which is the most reasonable basis for the taxation (we are not interested here in the rate of taxation, but the taxable base).

If, however, in January 2011 the property were re-sold for 120, the amount used by the allowance system would be 8, whereas the variation in the real value of the capital would be -1.

The following table shows the tax base according to the allowance system and the change in the real value of the capital (in parentheses) based on the re-sale value and on the date of acquisition for a good acquired for a value of 100 and re-sold in 2012.

Year of purchase	1990	1995	2000	2005	2010	2012
Re-sale value						
110	6 (-36)	6 (-22)	6 (-14)	6 (-2)	8 (6)	10 (10)
150	30 (4)	30 (18)	30 (26)	30 (38)	40 (46)	50 (50)
200	60 (54)	60 (68)	60 (76)	60 (88)	80 (96)	100 (100)
250	90 (104)	90 (118)	90 (126)	90 (138)	120 (146)	150 (150)

Note on interpretation: For a good purchased at 100 in 1990 and resold at 110 in 2012, the tax base after deduction of 40% is 6 while the change in the real value of the capital is -36, given inflation. While the economic income is negative (there is a loss of purchasing power), with the allowance system the tax base increases. For a good purchased at 100 in 2005 and resold at 250 in 2012, the tax base after deduction is 90, while the change in the real value of the capital is 138: the allowance system is very favourable when the gain is large.

The tax base should be the capital gain after taking into account the inflation tax (variation in the real value of the capital). But this tax base should not be directly subject to a progressive tax scale. Gains on disposals are in fact deferred and should be subject to a charge equivalent to that on a regular income throughout the ownership period. Smoothing with a quotient that varies with the holding period deals with this point. This kind of system divides the income by the number of years held [1], applying the progressive scale to this "regular income equivalent", while adding the household's other income for the current year, then multiplying the increase in the tax related to the exceptional income by the number of years held [2]. An alternative is to tax the capital gains upon disposal at a constant rate equal to the principal marginal rate (30%, to which should be added the CSG wealth tax).

The following points need to be added to the comments above:

- General clearing systems between gains and losses over a long period (currently 10 years) make it possible to take into account risks and potential losses, at least for diversified investors;
- As income from employment can easily be converted into capital income (through various financial instruments and portage arrangements), aligning the two taxes could limit the temptations of tax optimization, which opens the door to tax avoidance;
- In this respect, an Exit Tax, based on the unrealized capital gains, could be used to minimize the interest of becoming a tax exile, which increases with accumulated gains and tax potential.

Donations, especially when they are made outside inheritance, should not be used to erase capital gains, as is currently the case. This provision, which was initially intended to avoid double taxation, can now be used to completely escape taxation.

[1] Based on the equivalence of tax treatment for a regular income and an exceptional income, it appears that the division is made using a coefficient that depends on the interest rate. In practice, for low interest rates, this coefficient is equal to the number of years of ownership.

[2] This calculation is equivalent to regular taxation over time if the household's current earnings are representative of its income (assuming regular income) for the duration of ownership and if the tax schedule is relatively stable.

Financing higher education: Should students have to pay?

By [Guillaume Allègre](#) and [Xavier Timbeau](#)

Is it necessary to ensure that a greater portion of the cost of higher education is borne by students in the form of higher tuition fees, which might or might not be coupled with loans? It is often argued that financing higher education through taxes is anti-redistributive. We show in a [working document](#) that from a life cycle perspective proportional taxation is not anti-redistributive.

While raising higher education fees is not on the political agenda in France, it is a subject of intense fighting, not only in Quebec, but also in Spain and Great Britain, where student protests erupted at the end of 2010. Reports in France

regularly propose raising tuition fees: recently (2011), in a note by the [Institut de l'Entreprise](#) [in French] on the role of business in financing higher education, Pierre-André Chiappori proposes “lifting the taboo on tuition fees”. In a [contribution to Terra Nova](#) [in French] published in 2011, Yves Lichtenberger and Alexandre Aïdara propose raising annual university tuition fees by about 1000 euros. Paradoxically, the authors also propose creating a study allowance that could be used anytime in a person’s life. The authors are attempting to deal with two contradictory economic dynamics. On the one hand, a study allowance would help raise the general level of education, a factor in innovation and growth, while simultaneously fighting against social self-selection in higher education:

In countries that have adopted it [the study allowance], disadvantaged social strata may have an opportunity to undertake lengthier studies even though their social origins have predestined them to short-term courses that provide quick entry into salaried employment. This is an important means of raising the general level of education and the qualifications of young people, which is a central concern of this report. (Lichtenberger and Aïdara, [p.82](#))

But on the other hand, education benefits better-off strata, and being free makes it anti-redistributive:

The fact that public higher education is virtually free leads, first, to a transfer of resources (the public cost of education) to young people who are in education the longest. This overwhelmingly means young people from better-off strata. This transfer is reflected ultimately in private returns to the beneficiaries: higher wages and then pensions, which benefit the most highly educated throughout their lives.... As things stand, higher education’s free character has no redistributive value and even aggravates inequalities. (Lichtenberger and Aïdara, [p.84](#))

Indeed, even if the anti-redistributive character of free higher education is not the only argument made by advocates of higher tuition, it is one of their main arguments. This

argument relies on a static and familialist vision of redistribution. We adopt a life cycle perspective instead.

As highlighted in the second excerpt above, on average the beneficiaries of education spending enjoy a significant private benefit: they will have higher wages and pensions throughout their lives. Even assuming that tax (on income) is proportional to income (which is not the case: in reality, it is progressive), they will pay much more tax, in absolute terms, than individuals who have completed shorter studies. Above all, tax allows for the financing of education by individuals who actually receive significant private benefits, and in proportion to this benefit. People who suffer discrimination in the labour market or who were oriented towards less profitable sectors and benefit from low returns to education reimburse society a lesser amount through their taxes than those who benefit more. Financing through income tax leads people with higher incomes to contribute even when they have not had a lengthy education. The injustice would therefore lie in the transfer between persons with high incomes who are not highly educated and those who are highly educated. But if education is characterized to a great extent by significant social returns, thanks to its impact on growth ([see Aghion and Cohen](#)), then people with high incomes are actually beneficiaries of spending on education, whether or not they are highly educated themselves (for instance, self-taught entrepreneurs benefit from the availability of skilled labour).

Adopting a life cycle perspective, we show in a [working document](#) that financing spending on non-compulsory education (beyond 16 years) by a proportional tax represents a net transfer from those with higher incomes during their careers to those with lower incomes during their careers. From a life cycle perspective, free non-compulsory education financed by taxes does not benefit individuals with more affluent parents (the transfer from individuals from better-off households to those from poorer households is not significantly different from zero). If individuals from the poorest households react

to the increase in tuition fees by reducing their investment in education, even when this is financed by loans, then there can be little doubt that they will be the first victims of this type of reform. Advocates of tuition increases generally argue for small increases in tuition fees and exemptions based on means-testing the parents. But recent developments in Australia, the United Kingdom and Canada show that, once the fees have been introduced, it is difficult to prevent governments that are seeking new funds from increasing the fees and reducing the exemption thresholds.

In higher education, the leading injustice is the lack of access to people from modest backgrounds. The surest way to ensure equity in education is still to fund it through income tax and to reform education so that it is targeted at academic success for all rather than at selection.