Some Background

How do financing methods affect the distributional analyses of tax cuts?

Q. How do financing methods affect the distributional analyses of tax cuts?

A. Tax cuts are financed through reductions in current outlays or higher government debt that will eventually have to be repaid. Distributional analyses omit this information as well as the effects of tax increases on current outlays and debt.

Distributional analyses omit the ways tax cuts and tax increases affect other government finances—through either lower (or higher) spending or higher (or lower) debt. These omissions implicitly assume that lost revenue from tax cuts is never paid and that additional revenue from tax increases simply disappears. No one believes these assumptions are realistic, but there is no generally accepted way to include these financing effects. Gale (2018) and Gale, Khitatrakun, and Krupkin (2017) show that the distributional effects of the 2017 Tax Cuts and Jobs Act tax cuts are significantly altered if alternative financing effects are considered.

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Further Reading

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