

Swarthmore College

## Works

---

Economics Faculty Works

Economics

---

12-1-1994

### Review Of "The Political Economy Of Tax Reform" By T. Ito and A. O. Krueger

Larry E. Westphal

*Swarthmore College*, lwestph1@swarthmore.edu

Follow this and additional works at: <https://works.swarthmore.edu/fac-economics>



Part of the [Economics Commons](#)

[Let us know how access to these works benefits you](#)

---

#### Recommended Citation

Larry E. Westphal. (1994). "Review Of "The Political Economy Of Tax Reform" By T. Ito and A. O. Krueger". *Journal Of Economic Literature*. Volume 32, Issue 4. 1894-1895.  
<https://works.swarthmore.edu/fac-economics/315>

This work is brought to you for free and open access by . It has been accepted for inclusion in Economics Faculty Works by an authorized administrator of Works. For more information, please contact [myworks@swarthmore.edu](mailto:myworks@swarthmore.edu).

Review

Reviewed Work(s): *The Political Economy of Tax Reform*. by Takatoshi Ito and Anne O. Krueger

Review by: Larry E. Westphal

Source: *Journal of Economic Literature*, Vol. 32, No. 4 (Dec., 1994), pp. 1894-1895

Published by: American Economic Association

Stable URL: <http://www.jstor.org/stable/2728823>

Accessed: 21-09-2017 15:47 UTC

---

JSTOR is a not-for-profit service that helps scholars, researchers, and students discover, use, and build upon a wide range of content in a trusted digital archive. We use information technology and tools to increase productivity and facilitate new forms of scholarship. For more information about JSTOR, please contact [support@jstor.org](mailto:support@jstor.org).

Your use of the JSTOR archive indicates your acceptance of the Terms & Conditions of Use, available at <http://about.jstor.org/terms>



JSTOR

*American Economic Association* is collaborating with JSTOR to digitize, preserve and extend access to *Journal of Economic Literature*

delivery point relative to the general flow of the commodity.

The authors then go on to discuss possible solutions to manipulation, including *ex ante* enforcement, in which the exchange forces traders to reduce large positions prior to delivery, and otherwise attempts to influence potentially manipulative trading strategies as they develop; *ex post* enforcement, in which manipulators are sanctioned, and contract design, in which the exchange attempts to adjust contract provisions to make manipulation difficult. They argue for a mixture of approaches, but express doubt that a complete solution can be found, because all enforcement efforts run the risk of deterring economically beneficial activity, and because contract designs that deter long manipulation tend to facilitate short manipulation.

Despite its coherent and detailed analysis, the manipulation section fails to draw on the resources of the Exchange to present concrete examples of manipulation, or to examine data on manipulation attempts. By confining themselves to a theoretical discussion, the authors pass up the opportunity to enliven their somewhat dry presentation, and to break some new and potentially very useful ground.

Finally, the book concludes with an analysis of potential changes in the delivery mechanism that might compensate for some of the problems identified in earlier chapters. In particular, the authors argue that the evolution of the grain market has reduced Chicago to a delivery role of secondary importance, and that a change in contract provisions to encourage deliveries at other points would improve the contract as a hedge for mainstream users. They support these conclusions with a simulation analysis of potential delivery points.

Overall, Pirrong, Haddock, and Kormendi have created a detailed and tightly reasoned, but rather specialized and dry analysis of the grain futures delivery mechanism. This work will be useful to serious students of commodities futures, but will probably find its most attentive audience at the CBOT.

KENNETH CONE

*Lexecon Inc.*

## H Public Economics

*The political economy of tax reform.* Edited by TAKATOSHI ITO AND ANNE O. KRUEGER. NBER East Asia Seminar on Economics, vol. 1. Chicago and London: University of Chicago Press, 1992. Pp. x, 348. \$60.00. ISBN 0-226-38667-8. *JEL* 93-0140

This worthwhile volume is the result of a conference—held in Seoul, Korea in June 1990—jointly sponsored by the Korea Development Institute and the National Bureau of Economic Research. Each chapter will be of considerable value to readers interested in its subject matter.

Ito and Krueger's introduction emphasizes two themes: growing international economic interdependence and increasing concern with tax policy consequences. As they state, only the latter pervades the volume. International repercussions remain of secondary importance relative to domestic interests in the contemplation and design of tax reforms. Nonetheless, several chapters pay more than passing attention to international interactions.

Two chapters provide a general background. In a theoretical chapter, Assaf Razin and Efraim Sadka contend that arbitrage conditions imply that tax competition among countries may lead to taxation only of immobile factors. In turn, Vito Tanzi and Parthasarathi Shome provide an extremely informative overview of tax structures and their effects in Hong Kong, Indonesia, Korea, Malaysia, the Philippines, Singapore, Taiwan, and Thailand. By discussing structural characteristics and distinguishing features in each case, they highlight many specific issues covered at greater depth in other chapters, placing them in a richer comparative context.

Four chapters provide general perspectives on past tax reforms. The introduction of consumption-related value added taxes (VAT) in Japan and Taiwan are respectively discussed by Masaaki Homma and Chuan Lin. The Japanese sought simplification and rationalization as well as greater horizontal and vertical equity in the tax structure. It was not until the second round of reform, in 1987, that opposition to the VAT was overcome, in part because the original intention of revenue

neutrality was abandoned in favor of overall tax reduction. Homma's examination of distributional effects suggests that the great majority of households benefited to some degree from its introduction.

Less ambitious objectives were sought in Taiwan's case. The VAT introduced in 1986 was intended as a revenue neutral replacement of the existing turnover tax. Lin judges that it improved the progressivity of the overall tax system. Lin, and Homma to a lesser degree, give fascinating accounts of administrative difficulties, indicating that a devil is in the details. But not for this reason alone do both authors view the VAT's introduction as but the first in a sequence of changes leading to a more comprehensive VAT system.

Charles McLure's chapter on American tax reform provides a rich account of how serendipitous interaction of circumstances and personalities enabled a technocratically inspired simplification of the federal tax structure in 1986. He observes that international ramifications were not considered adequately in the prior tax reform of 1981, which increased incentives for investment far more than for savings, leading to an increased foreign capital inflow. The balance was somewhat redressed by the 1986 act, but McLure concludes that discussions preceding this reform did not reflect a complete understanding of international effects.

Taewon Kwack and Kye-Sik Lee present a well-balanced overview of the history of Korean tax reform since 1948, emphasizing the continuous iteration between fine-tuning adjustments and more fundamental structural reforms. Important reforms took place in the mid-1970s with the introduction of a global income tax and replacement of various indirect taxes by a VAT coupled with other changes to offset possible adverse effects and mitigate political controversy. Korea's establishment of the VAT, which now yields more than one-fifth of total tax revenue, appears to have been less problematic and more successful than either Japan's or Taiwan's. Unlike Taiwan, Korea has lacked an effective means of taxing capital gains from investments in land and structures. The search for an appropriate means is a central issue of tax reform in the 1990s, focused on equity.

The remaining six chapters are more narrowly focused. Using a neoclassical dynasty model, Tatsuo Hatta and Hideki Nishioka investigate efficiency gains from distortion reducing changes in Japanese capital income taxes, finding them to be quite small. Irene Trela and John Whalley, using a small computable equilibrium model, conclude that Korea's export-oriented tax policies accounted for no more than ten percent of its growth over the 1962–82 period. Krueger's comments on this result usefully emphasize that the contribution is not so small as it might appear when considered in light of mutually reinforcing reforms across many policy domains.

Yokio Noguchi's chapter provides a careful analysis of revenue requirements under alternative tax policies to maintain the existing social security system in the face of Japan's rapidly aging population. He argues that the VAT has an important future role to play in spreading the increased tax burden equitably among generations. Thomas Barthold and Takatoshi Ito give a detailed comparative description of American and Japanese gift, estate, and inheritance taxes. In a seminal exercise using tax return data, they also estimate the share of intergenerational transfers in total household assets. The American share is determined to be at least one quarter; the Japanese share is somewhat greater, disproportionately so for land bequests which are effectively given preferential treatment.

The final two chapters focus on direct foreign investment. Kun-Young Yun carefully estimates effective tax rates on such investments made in Korea, finding that most rates are well below ten percent, with many being negative. In turn, in the course of providing a more comprehensive overview of direct investment in Taiwan, Ching-huei Chang and Peter Cheng demonstrate that it also provides an attractive tax climate for direct investment.

I trust that the foregoing sketch of the volume's complete contents will suffice to entice the many readers who can benefit from one or more of its chapters.

LARRY E. WESTPHAL

*Swarthmore College*