The Optimal Asymptotic Income Tax Rate\textsuperscript{1}

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Abstract

This paper shows that a policy maker needs only two types of information to set the optimal income tax rate at the top: a measure of labor supply elasticity and the shape of skills distribution. We find that the asymptotic tax rate is not affected by the degree of inequality aversion as long as the marginal utility of consumption converges to zero. By using empirically plausible estimates for the compensated labor supply elasticity and the shape of skills distribution, we find that the optimal marginal tax rate at the top should be between 33 and 60 percent, which is in line with the existing rates in the real world.

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