Optimal Dynamic Nonlinear Income Taxes: 
Facing an Uncertain Future with a Sluggish 
Government*

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Abstract

We consider the optimal nonlinear income taxation problem in a 
dynamic, stochastic environment when the government is sluggish in 
the sense that it cannot change the tax rule as uncertainty resolves. We 
argue that the zero top marginal tax rate result in static models is of 
little practical importance because it actually holds only when the top 
earner in the initial period receives the highest shock in every period.

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