The Impact of the Tax Reform in 2004 on the Female Labour Supply in Japan*

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ABSTRACT

In 2003, the Japanese Diet passed legislation to abolish part of the special deduction for spouses (*Haigusha Tokubetsu Kojo*), with the abolition to take effect in the 2004 tax year. This paper investigates the impact of this tax reform on the female labour supply in Japan. A number of earlier studies have shown that married women are likely to adjust their labour supply so that their husbands will be eligible to take advantage of the spouse deduction. By using data from the first and second waves of the Keio Household Panel Survey (KHPS) collected in 2004 and 2005, this paper uses the difference-in-differences approach to examine whether there has been any change in the behaviour of female labour supply as a result of this tax reform. Our approach is unique in that we use information on the awareness of the policy change to find a control group and a treatment group. This method is effective to rule out the possibility of dynamic aspects of labour supply. The empirical evidence indicates that the tax reform in 2004 did not have any impact on the decision of female spouses to enter the labour market. However, there are some effects on the number of hours they worked conditional on their participation in the labour market. Due to the partial abolition of the special spouse deduction, it is estimated that part-time female workers increased their weekly hours of work by about 3.7 hours. It can be argued that the awareness of the partial abolition of the spouse allowance is crucial in accounting for the changes in married women's labour supply.

Keywords: Difference-in differences, female labour supply; policy reform; program evaluation; tax reform

JEL Codes: H24, J22, C21