Report on Seisser: Perfecting Imperfect Competition

The paper by Seisser analyzes an output tax scheme to induce a monopolist to choose the welfare maximizing output and not the (lower) monopolistic output. The output tax is equal to Lerner's (1934) index of market power. So the higher the market power, the higher the tax, leading in effect to a trade off between market power and profits.

Unfortunately, the paper does not present an overview of the IO and regulation literature and thus it is difficult to assess the novelty of the paper. The Handbook of IO offers a good starting point on monopoly and regulation. It would be interesting to know which papers have considered an output tax before and how the author's result contributes to this literature.

The author formulates his model for a specific demand and cost function but the results are then shown, as far as I can see, for more general demand and cost functions. It is shown that under the proposed setting, the output tax induces the monopolist to increase output beyond Q_m, but under realistic assumption it will not reach the first best output Q_c.

But later on and in the interpretation, it is also not clear if the author has in mind a general monopoly situation or the more specific natural monopoly situation with economies of scale due to the fixed cost F. In such a case, the efficient output $p = MC$ will invariably lead to negative profits F. So either the government offers a subsidy (which has to be financed by taxes) or a Ramsey second best price solution is implemented. The author should relate his results to such a second best Ramsey result.

The author is a bit too enthusiastic about the applicability and feasibility of his results. If the aim is to achieve a first best competitive, then other solutions may be easier, e. g. a per unit subsidy (which requires a great deal of information) with a lump sum tax or (requiring less information from the regulator) a two-part tariff following Feldstein (1972) with the monopolist choosing the first best output Q_m and extracting all the rents which can be recovered if the monopoly franchise is auctioned ex ante. Having said this, it is not clear in a natural monopoly situation that the first best $p = MC$ is per se the desired outcome. This is reflected in the literature, which mostly focus on the second best Ramsey outcome.

Small typo in equation (11): it should be p in the denominator and not p^2. This does not alter any of the results.