ECO401H1S: TOPICS IN ECONOMIC POLICY

Course Information

Instructor: Kory Kroft
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Syllabus, lecture slides, and problem sets, are all posted online at: portal.utoronto.ca.

Course Goals

This course covers material on (I) Welfare Economics and Incidence and Efficiency Cost of Government Policies, (II) Taxation and Redistribution, (III) Social Insurance, (IV) Economics of Mandates. The emphasis will be on the theoretical and empirical evaluation of public policy. The course will be a project-oriented capstone course, designed to give students a background in the economic analysis of public policy, with a focus on empirical (evidence-based) analysis.

Class meetings

Tuesday, 2pm-4pm, SS1088.
Friday, 1pm-2pm, SS1088.

Prerequisites

One course from A, B and C:

A) Microeconomic Theory: (ECO200Y1/ECO204Y1/ECO206Y1)
B) Macroeconomic Theory: (ECO202Y1/ECO208Y1/ECO209Y1)
C) Quantitative Methods in Economics: (ECO220Y1/ECO227Y1)
Statistics: (STA247H1,STA248H1)/(STA250H1,STA255H1)/(STA257H1,STA261H1))

At least one FCE in ECO at the 300 level or higher.

Requirements

There will be three problem sets (40%), a class presentation (20%), class participation (10%), and a midterm test (30%).

Important Dates

February 3 – Problem Set #1 Due
February 24 – Midterm Test
March 3 – Problem Set #2 Due
March 10 – Presentation Slides Due
March 17/March 24/March 31 – Class Presentations
March 31 – Problem Set #3 Due

Software

The course involves a significant amount of computing, and students must learn and use a sophisticated statistical software package. STATA is highly recommended, and is the ***only*** package that will be supported by the instructor and TA.

Students should purchase **STATA/IC 12**, available online at:
http://www.stata.com/order/new/edu/gradplans/cgpcampus-order.html

Unless you are planning to use STATA in the future, a six month license will be sufficient. "Small STATA" is unlikely to suffice.

After orders are placed online, you will pick up your software at the Software Licensing Office in the Information Commons at Robarts Library:
http://www.utoronto.ca/ic/software/detail/stata.html

Familiarity with EXCEL is also useful.

COURSE POLICIES

1) Midterm Test

The midterm test will be held on Tuesday, February 24 during class time (2:10pm – 4:00pm) in SS1088.

Questions will be in a similar format to the questions on the problem sets.

If you miss the midterm, you will be given a grade of 0 unless you present me with a medical note **within one week of the midterm**, and I accept the note.

- The note must be provided using the University of Toronto Student Medical Certificate. No other documentation will be accepted. You can find a copy of the form here:
- http://www.healthservice.utoronto.ca/pdfs/medcert.htm
- The form must be completed by a Medical Doctor, including her/his OHIP registration number.
- Only **original** notes will be accepted. I will not accept photocopies or emailed certificates.
- The note must clearly state that **on the date of the midterm**, the student was too sick to write the test. Illness before the test is not sufficient grounds for missing the test. Nor will I accept notes that indicate that the student would have performed "sub-optimally".
- To comply with these requirements, it is expected that the student will have met with the doctor on the date of the test.
- **The student must email me the day of the test to indicate that they will not be able to write the test.**
- I will review each sick note to determine whether there are sufficient grounds for a student to be excused from a test. Part of this review process may include meeting with the student, and/or following up with the physician.
- It is an academic offence to feign illness to avoid a test.

If a student has been excused from the mid-term on medical grounds, he or she will be permitted to write the make-up test. The make-up midterm will be given **on Friday, March 6, 2:10pm-4:00pm**. The test will also be 2 hours.

- It may not be the exact same format as the midterm test itself.
- Consistent with university policy, there is no "make-up" test for the make-up test. No medical excuses will be accepted, and a grade of zero will be applied if a student fails to write the make-up test.

2) Problem Sets

The problem sets are due at the beginning of class on the assigned dates (February 3, March 3 and March 31). Late problem sets will receive a grade of zero. All students must hand in their own problem sets, but are welcome to help each other out. This means writing your own code and running your own output for empirical problem sets. Any evidence of copying/cutting/pasting from each other will be treated as plagiarism.

3) Academic misconduct

I have a zero-tolerance policy for any form of academic misconduct. Academic offenses, such as plagiarism or cheating during exams are serious academic offenses and could result in punishments ranging from failing the course to suspension or expulsion from the university. Please review the University's Code of Behavior on Academic Matters regarding what constitutes academic misconduct (http://www.governingcouncil.utoronto.ca/policies/behaveac.htm)

4) Appealing an exam

Appeals regarding the grading of a test must be submitted to me or the TA in writing, within one week of your receipt of the graded work. You must include the test with your written appeal. I shall re-grade the **entire exam** and this might result in a lower grade than the original.

5) Accessibility needs

The University of Toronto is committed to accessibility. If you require accomodations for a disability, or have any accessibility concerns about the course, the classroom or course materials, please contact Accessibility Services as soon as possible: disability.services@utoronto.ca or http://studentlife.utoronto.ca/accessibility.

6) Class rules

All students must arrive on time and be prepared to participate in class discussion. The use of computers, iPhones, iPods, iPads, Blackberries and all other computer devices are prohibited.

7) Presentations

You will be required to choose an empirical academic paper and present the paper in class. The length of the presentation will be around 10-15 minutes, including time for questions and discussion. You should be prepared to discuss the following:

(i) What is the main question of the paper?
(ii) How does the paper contribute to the academic literature?
(iii) What is the research design and empirical strategy?
(iv) What are the main results of the paper?
(v) What are some of the drawbacks of the research design?
(vi) Are there alternative explanations for the empirical results?

Presentation Slides are due one week before the class presentations on March 10. **No medical notes will be accepted for the slides**.

Should you miss your presentation, you will be given a grade of 0 unless you present me with a medical note and I accept the note. The medical note should conform to the same restrictions alluded to above for the Midterm policy (#1). A very high standard will be applied to any medical accommodation.

If a student has been excused from his/her presentation on medical grounds, with appropriate notice (same day), the student will be required to make his/her presentation in the next available slot, unless they are medically unable – which will require a new medical note. More details will be provided later.

8) Class Participation

Students will be evaluated on class participation. The performance will largely be based on students having read required articles **prior to class** and being prepared to engage in a meaningful discussion on these articles during class time. Evaluation will also partly be based on whether students adhere to the class rules in 6) above.

LECTURE SCHEDULE – WINTER 2015

Section I: Welfare economics, incidence and efficiency cost of government policies

1	January 6	Introduction and roadmap
2	January 13	Welfare economics
3	January 20	Incidence and efficiency cost of government policies **Problem Set 1 Distributed**

Section II: Labour Income Taxation and Redistribution

IIA. Theoretical Aspects: Optimal Income Taxation and Redistribution

4	January 27	Optimal income taxation and transfer programs

IIB. Empirical Aspects: Behavioral Responses to Taxes and Transfers

5	February 3	Labor supply responses to taxation and transfers **Problem Set 1 Due** **Problem Set 2 Distributed**
6	February 10	Responses of Taxable Income to Tax Rates, In-kind transfers
7	February 24	**Midterm**

Section III: Social Insurance

8	March 3	Asymmetric information: adverse selection and moral hazard **Problem Set 2 Due** **Problem Set 3 Distributed**
9	March 10	Overview of social insurance and unemployment insurance **Presentation Slides Due**

Class Presentations

10	March 17	
11	March 24	
12	March 31	**Problem Set 3 Due**

READING MATERIAL

Most of the course material will consist of detailed lecture notes which will be posted on BlackBoard before the start of each class.
There will also be some required readings. Students should aim to complete the readings for each week before the start of lecture.
Bold: required reading.
***: reading emphasized in class.**
Students can access most readings using JSTOR through the U of T library.

0. GENERAL REFERENCES

Background Reading: The most popular undergraduate textbooks

J. Gruber, Public Finance and Public Policies, 3rd edition, Worth Publishers, 2009.
H. Rosen, Public Finance, 7th edition, McGraw Hill, 2005.
H. Rosen, J. Wen, T. Snoddon, B. Dahlby, R. Smith, Public Finance in Canada, 3rd edition, McGraw-Hill, 2008.
J. Stiglitz, Economics of the Public Sector, 3rd edition, Norton, 1999.

References on Empirical Methods:

Angrist, J.D. and A. B. Krueger (2001), "Instrumental Variables and the Search for Identification: From Supply and Demand to Natural Experiments," Journal of Economic Perspectives, 15(4): 69-85.

A. Angrist and J.S. Pischke, Mostly Harmless Econometrics. Princeton University Press, 2008.

I: WELFARE ECONOMICS, TAX INCIDENCE AND EFFICIENCY COST OF TAXATION

Week 1: Introduction and roadmap

Noah, T. (2010). "Introducing the Great Divergence", Slate Magazine.

Piketty, T. and E. Saez (2003). "Income Inequality in the United States, 1913-1998", Quarterly Journal of Economics, 118(1): 1-39.

Saez, E. and M. Veall (2005). "The Evolution of High Incomes in North-America: Lessons from the Canadian Evidence", American Economic Review, 95(3): 831-849.

Week 2: Traditional welfare economics and behavioral welfare economics

Congdon, W., Kling, J., and S. Mullainathan (2011). "Policy and Choice: Public Finance Through the Lens of Behavioral Economics", Brookings Institution Press, Washington, D.C.

Kroft, K. (2011). Book Review: "Policy and Choice: Public Finance Through the Lens of Behavioral Economics", Journal of Economic Literature, 49(4): 1241-1250.

Reinhardt, U. (2010). "Is `More Efficient' Always Better?", New York Times Economix Blog

Reinhardt, U. (2010). "When Value Judgments Masquerade as Science", New York Times Economix Blog

Week 3: Incidence and efficiency cost of government policies

Taxation

Auerbach, A. (1985). "The Theory of Excess Burden and Optimal Taxation," in A. Auerbach and M. Feldstein, Handbook of Public Economics, 1: 61-127. Amsterdam: North Holland. Sections 1, 2, 3.1, and 4.

Chetty, R. (2009). "Sufficient Statistics for Welfare Analysis: A Bridge Between Structural and Reduced-Form Methods", Annual Review of Economics, 1: 451-488.

*Chetty, R., Looney A. and K. Kroft. "Salience and Taxation: Theory and Evidence," American Economic Review, 99(4): 1145-1177.

Gruber, J. and B. Koszegi (2001). "Is Addiction Rational? Theory and Evidence", Quarterly Journal of Economics, 116(4): 1261-1305.

*Hendren, Nathaniel (2013). "The Policy Elasticity," Harvard University Working Paper.

Hines, J. R. (1999). "Three Sides of Harberger Triangles," Journal of Economic Perspectives, 13(2): 167-188.

*Marion, J. and E. Muehlegger (2008). "Measuring Illegal Activity and the Effects of Regulatory Innovation: Tax Evasion and the Dyeing of Untaxed Diesel", Journal of Political Economy, 116(4): 633-666.

O'Donoghue, T. and M. Rabin (2006). "Optimal Sin Taxes," Journal of Public Economics, 90: 1825-1849.

Willig, R. (1976). "Consumer's Surplus Without Apology", American Economic Review, 66(4): 589-597.

Price ceilings and price floors

Davis, L. and L. Kilian (2011). "The Allocative Cost of Price Ceilings in the U.S. Residential Market for Natural Gas", Journal of Political Economy, 119(2): 212-241.

Glaeser, E. and E. Luttmer (2003). "The Misallocation of Housing Under Rent Control", American Economic Review, 93(4): 1027-1046.

II: LABOUR INCOME TAXATION AND REDISTRIBUTION

Week 4: Optimal Income Taxation and the Design of Optimal Transfer Programs

Diamond, P. and E. Saez (2011). "The Case for a Progressive Tax: From Basic Research to Policy Recommendations," Journal of Economic Perspectives, 25(4): 165-90.

*Piketty, T. and E. Saez (2007). "How Progressive is the US Federal Tax System? A Historical and International Perspective", Journal of Economic Perspectives, 21(1): 3-24.

Heady, C. (1993). "Optimal Taxation as a Guide to Tax Policy: A Survey", Fiscal Studies, 14(1): 15-41.

*Saez, E. (2001). "Using Elasticities to Derive Optimal Income Tax Rates", Review of Economics Studies, 68: 205-229.

*Akerlof, G. (1978). "The Economics of Tagging as Applied to the Optimal Income Tax", American Economic Review, 68(1): 8-19.

Blank, R. (2002). "Evaluating Welfare Reform in the United States", Journal of Economic Literature, 40(4): 1105–1166.

*Nichols, A. and R. Zeckhauser (1982). "Targeting Transfers Through Restrictions on Recipients", American Economic Review, 72(2): 372-377.

*Saez, E. (2002). "Optimal Income Transfer Programs: Intensive Versus Extensive Labor Supply Responses", Quarterly Journal of Economics, 117: 1039-1073.

Week 5: Labor Supply Responses to Taxation and Transfer Programs

*Ashenfelter, O. and M. Plant (1990). "Non-Parametric Estimates of the Labor Supply Effects of Negative Income Tax Programs", Journal of Labor Economics, 8: 396-415.

Chetty, R. (2011). "Bounds on Elasticities with Optimization Frictions: A Synthesis of Micro and Macro Evidence on Labor Supply", forthcoming Econometrica.

Chetty, R., Friedman, J., Olsen, T. and L. Pistaferri (2011). "Adjustment Costs, Firm Responses, and Micro vs Macro Labor Supply Elasticities: Evidence from Danish Tax Records", Quarterly Journal of Economics, 126(2): 749-804.

Eissa, N. and J. Liebman (1996). "Labor Supply Response to the Earned Income Tax Credit", Quarterly Journal of Economics, 111: 605-637.

Goolsbee, A. (2000). "What Happens When You Tax the Rich? Evidence from Executive Compensation", Journal of Political Economy, 108: 352-378.

Heckman, J. (2000). "Causal Parameters and Policy Analysis in Economics: A Twentieth Century Retrospective", Quarterly Journal of Economics, 115(1): 45-97.

*Imbens, G., D. Rubin and B. Sacerdote (2001). "Estimating the Effect of Unearned Income on Labor Earnings, Savings, and Consumption: Evidence from a Survey of Lottery Players", American Economic Review, 91: 778-794.

Moffitt, R. (2003), "The Negative Income Tax and the Evolution of U.S. Welfare Policy," Journal of Economic Perspectives, 17(3): 119-140.

*Saez, E. (2010) "Do Taxpayers Bunch at Kink Points?" American Economic Journal: Economic Policy, 2(3): 180-212.

Week 6: Responses of Taxable Income to Tax Rates, In-kind transfers

*Feldstein, M. (1995). "The Effect of Marginal Tax Rates on Taxable Income: A Panel Study of the 1986 Tax Reform Act", Journal of Political Economy, 103: 551-572.

*Giertz, S., Saez, E. and J. Slemrod (2011). "The Elasticity of Taxable Income with Respect to Marginal Tax Rates: A Critical Review", Journal of Economic Literature.

Hoynes, H. and Schanzenbach, D. (2009). "Consumption Responses to In-Kind Transfers: Evidence from the Introduction of the Food Stamp Program", American Economic Journal – Applied Economics, 1(4): 109-139.

Schanzenbach, D. (2011). "What Are Food Stamps Worth?" Princeton University Industrial Relations Section Working Paper #468.

III. SOCIAL INSURANCE

Week 8: Asymmetric information: adverse selection and moral hazard

Einav, L. and A. Finkelstein (2011), "Selection in Insurance Markets: Theory and Empirics in Pictures," Journal of Economic Perspectives, 25(1): 115-38.

Cullen, M., Einav, L. and A. Finkelstein (2011). "Estimating Welfare in Insurance Markets Using Variation in Prices", Quarterly Journal of Economics, 123(3): 877-921**.**

Rothschild, M. and J. Stiglitz (1976). "Equilibrium in Competitive Insurance Markets: An Essay on the Economics of Imperfect Information", Quarterly Journal of Economics, 90(4): 629-650.*

Week 9: Social insurance: unemployment insurance

Chetty, R. (2009). "Sufficient Statistics for Welfare Analysis: A Bridge Between Structural and Reduced-Form Methods", Annual Review of Economics, 1: 451-488.

*Chetty, R. (2008). "Moral Hazard vs. Liquidity and Optimal Unemployment Insurance", Journal of Political Economy, 116(2): 173-234.

Feldstein, M. (1976), "Seven Principles of Social Insurance", Challenge, November/ December 1976, 6-11.

Gruber, Jon (1997). "The Consumption Smoothing Benefits of Unemployment Insurance", American Economic Review, 87(1): 192-205.

Krueger, A. B. and B. D. Meyer (2002). "Labor supply effects of social insurance", Handbook of Public Economics, chapter 33, pp: 2327-2392.

Nicholson, W. and K. Needels (2006). "Unemployment Insurance: Strengthening the Relationship between Theory and Policy", Journal of Economic Perspectives, 20(3): 47-70.