

## Economics 446: Economics of the Public Sector

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GE 268

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### Preliminaries

The aim of this course is to teach students to read and begin to conduct research in public policy and the economics of the public sector. The focus is on tools of theoretical and empirical analysis, and teaching will be through a mix of lectures, reading and discussing scholarly articles, and self-study assignments including quantitative analysis.

Evaluation of students will be based on a series of class presentations and take-home assignments. There are no exams.

Through the course of the semester, each student will be called on alternatively to *present* or *discuss* an assigned article. The *presenter* will prepare a written summary of the paper of about 2-3 pages, which is to be submitted at the start of class time, and will present this material orally during class time, speaking for about 15 to 20 minutes. The *discussant* then responds, speaking for 5-10 minutes to raise questions and problems about the paper, and leading a general class discussion. Each student should expect to serve as presenter and discussant 2 or 3 times during the semester.

The grading scheme for the course is:

Written paper summaries	15%
Class presentations/discussions	30%
Take-home assignments (3)	45%
General class participation	10%

There is no required textbook. For background on the microeconomic theory of welfare measurement, you may wish to consult *Microeconomics: Theory and Applications with Calculus*, 3rd Ed. by Jeffrey M. Perloff. Another, more technical treatment is in *Microeconomics: An Intuitive Approach with Calculus* by Thomas Nechyba. Both books are on course reserve at Robarts Library.

### Lectures

In the following list, lectures marked in boldface will be presented in the current year (those marked † may be substituted, depending on the interests of students). Papers marked \* should be read before class, and papers marked + will be discussed in class but advance reading is optional.

#### 1. **Week 1: Welfare measurement**

Perloff, chaps. 2-5.

#### 2. **Week 2: Deadweight loss and behavioural response to policy**

\*A. Auerbach and J. Hines, 2002, "Taxation and economic efficiency," secs. 1-2, in A. Auerbach and M. Feldstein, eds., *Handbook of Public Economics*, vol. 3, pp. 1347-1421. (Also NBER Working Paper 8181.)

Chetty, Raj. 2009. "Is the Taxable Income Elasticity Sufficient to Calculate Deadweight Loss? The Implications of Evasion and Avoidance" *American Economic Journal: Economic Policy* 2009, 1:2, 3152.

### 3. **Week 3: Optimal taxation**

\*A. Auerbach and J. Hines, 2002, "Taxation and economic efficiency," sec. 3, in A. Auerbach and M. Feldstein, eds., *Handbook of Public Economics*, vol. 3, 2002, 1347-1421.

+Sarah E. West and Roberton C. Williams III, 2007, "Optimal taxation and cross-price effects on labor supply: Estimates of the optimal gas tax," *Journal of Public Economics*, Volume 91, Issues 3-4, April 2007, Pages 593-617

### 4. **Week 4: Income support programs**

\*Eissa, N. and J.B. Liebman, 1996, Labour Supply response to the Earned Income Tax Credit. *Quarterly Journal of Economics* 111, 605-637.

\*T. Lemieux and K. Milligan, 2008, Incentive effects of social assistance: A regression discontinuity approach, *Journal of Econometrics* 142, 807828.

Emmanuel Saez, 2010, "Do taxpayers bunch at kink points?" *AEJ: EP* 2, 180212.

Chetty, Friedman and Saez, 2012, Using differences in knowledge across neighborhoods to uncover the impacts of the EITC on earnings, *NBER WP #18232*

### 5. **Week 5: Empirical analysis of tax avoidance**

\*Saez, E., J. Slemrod, and S. Giertz, 2012, "The Elasticity of Taxable Income with Respect to Marginal Tax Rates: A Critical Review," *Journal of Economic Literature* 50, 3-50.

+Feldstein, M., 1995, "The effects of tax rates on taxable income: A panel study of the 1986 Tax Reform Act," *Journal of Political Economy* 103, 551-572.

\*Austan Goolsbee, 1999, "Evidence on the High-Income Laffer Curve from Six Decades of Tax Reform," *Brookings Papers on Economic Activity*, Vol. 1999, No. 2 (1999), pp. 1-64.

\*Oates, Wallace E., and Robert M. Schwab. 2015. "The Window Tax: A Case Study in Excess Burden." *Journal of Economic Perspectives*, 29(1): 163-80.

Sillamaa, M. and M. Veall, 2001, "The effect of marginal tax rates on taxable income: A study of the 1988 tax flattening in Canada," *Journal of Public Economics* 80, 341-356.

### 6. **Week 8: Transfers in cash and in kind<sup>†</sup>**

\*Janet Currie and Firouz Gahvari, 2008, "Transfers in Cash and In-Kind: Theory Meets the Data," *Journal of Economic Literature* 46 #2, June 2008, 333-83.

Akerlof, George, "The Economics of Tagging as Applied to the Optimal Income Tax, Welfare Programs, and Manpower Planning," *American Economic Review*, 1978.

Besley, Timothy and Stephen Coate, "The Design of Income Maintenance Programmes," *Review of Economic Studies*, 1995.

+Blackorby, Charles and David Donaldson, "Cash versus Kind, Self Selection and Efficient Transfers," *American Economic Review*, 1988.

Besley, T. and S. Coate, 1992, "Workfare versus Welfare: Incentive Arguments for work requirements in Poverty Alleviation Programs", *American Economic Review* 82, 249-261.

\*B. Jacob and J. Ludwig, 2012, "The Effects of Housing Assistance on Labor Supply: Evidence from a Voucher Lottery," *American Economic Review* 102, 272-304

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

## 7. **Week 7: Income taxation**

\*Peter Diamond and Emmanuel Saez, 2011, "The case for a progressive tax: From basic research to policy recommendations," *Journal of Economic Perspectives* 25 (4), 165-190

\*Mankiw, N Gregory. 2013. "Defending the One Percent." *Journal of Economic Perspectives*, 27(3): 21-34.

A. Auerbach and J. Hines, 2002, "Taxation and economic efficiency," sec. 4.

Brewer, Mike, Emmanuel Saez, and Andrew Shephard, 2010, "Means-testing and Tax Rates on Earnings," in *Dimensions of Tax Design: the Mirrlees Review*, J. Mirrlees, et al. (eds), Oxford University Press.

K. Milligan and M. Smart, 2015, "Taxation and top incomes in Canada," *Canadian Journal of Economics* 48, 655-681.

## 8. Taxation of the family<sup>†</sup>

\*John Piggott and John Whalley, 1996, "The Tax Unit and Household Production," *Journal of Political Economy*, Vol. 104, No. 2 (Apr., 1996), pp. 398-418.

\*Alexander Gelber and Joshua Mitchell, 2012, "Taxes and Time Allocation: Evidence from Single Women and Men," *Review of Economic Studies* 79. 863-897

A. Gelber, 2014, "Taxation and the Earnings of Husbands and Wives: Evidence from Sweden," *Review of Economics and Statistics* 2014, 96(2), 287-305

Alesina, Alberto, Andrea Ichino, and Loukas Karabarbounis. "Gender-based taxation and the division of family chores." *American Economic Journal: Economic Policy* 3.2 (2011): 1-40.

H. Kleven, C. Kreiner and E. Saez, 2009, "The Optimal Income Taxation of Couples." *Econometrica* 77, pp. 537-560. An earlier version is available as NBER Working Paper 12685, November 2006.

Michael J. Boskin and Eytan Sheshinski, 1983, "Optimal tax treatment of the family: Married couples," *Journal of Public Economics*, Volume 20, Issue 3, April 1983, Pages 281-297.

## 9. Distribution of income and wealth<sup>†</sup>

\*Piketty, Thomas. 2015. "Putting Distribution Back at the Center of Economics: Reflections on Capital in the Twenty-First Century." *Journal of Economic Perspectives*, 29(1): 67-88.

Emmanuel Saez and Michael R. Veall, 2005, "The Evolution of High Incomes in Northern America: Lessons from Canadian Evidence," *American Economic Review*, Vol. 95, No. 3 (Jun., 2005), pp. 831-849.

Joseph Stiglitz, 2015a, "Of income and wealth among individuals: Part I. The wealth residual," NBER Working Paper 21189

Joseph Stiglitz, 2015b, "Of income and wealth among individuals: Part II. Equilibrium wealth distributions," NBER Working Paper 21190

\*Paul Krugman, 2014, "Why We're in a New Gilded Age," *New York Review of Books*, May 8, 2014.

Matthew Rognlie, MIT Dep, 2015, "Deciphering the fall and rise in the net capital share," *Brookings Papers on Economic Activity*, forthcoming.

Jones, Charles I. 2015. "Pareto and Piketty: The Macroeconomics of Top Income and Wealth Inequality." *Journal of Economic Perspectives*, 29(1): 29-46.

#### 10. **Week 8: Savings and Public Policy**

\*J. Mintz, 2009, *Summary Report of Retirement Income Adequacy*, Department of Finance, December 18, 2009, <http://www.fin.gc.ca/activity/pubs/pension/riar-narr-eng.asp>.

+D. Benjamin and M. Smart, 2012, "Savings trends in Canada," mimeo, University of Toronto.

E. Hurst, 2003, "Grasshoppers, Ants, and Pre-Retirement Wealth: A Test of Permanent Income," NBER Working Paper No. 10097

+G. Mastrobuoni and M. Weinberg, 2009, "Heterogeneity in intra-monthly consumption patterns, self-control, and savings at retirement," *AEJ: EP* 1, 163-189.

E. Saez, 2009, "Details matter: The impact of presentation and information on the take-up of financial incentives," *AEJ: EP* 1, 204-228.

+Bernheim, B. D., 2002, "Taxation and saving," *Handbook of public economics*, vol. 3, A. Auerbach and M. Feldstein, eds., (Amsterdam, North-Holland).

Chari, VV and Patrick Kehoe, "Optimal Fiscal and Monetary Policy," in *Handbook of Macroeconomics*, Volume 1C, John Taylor and Michael Woodford, Eds, North Holland, Amsterdam, 1999. (Also Minneapolis Fed Staff Report 251, 1998.), sec. 2.

Banks, James and Peter Diamond, 2010, "The Base for Direct Taxation," in *Dimensions of Tax Design: the Mirrlees Review*, J. Mirrlees, et al. (eds), Oxford University Press.

#### 11. **Week 9: Targeted savings programs<sup>†</sup>**

Gale, William G. and John Karl Scholz, 1994, "IRAs and Household Saving," *American Economic Review* 84, December 1994, 1233-1260.

Poterba, James M., Steven F. Venti and David A. Wise, 1995, "Do 401(k) Contributions Crowd Out Other Personal Saving?" *Journal of Public Economics* 58, 1995, 1-32.

\*Engen, E., W. Gale, and J.K. Scholz, 1996, "The Illusory Effects of Saving Incentives," *Journal of Economic Perspectives* 10, 113-138.

Poterba, J., S. Venti, and D. Wise, 1996, "How Retirement Saving Programs Increase Saving," *Journal of Economic Perspectives* 10, 91-112.

Alexander Gelber, 2009, "How Do 401(k)s Affect Saving? Evidence from Changes in 401(k) Eligibility," September 2009.

12. Behavioural public economics<sup>†</sup>

Becker, Gary and Kevin Murphy, "A Theory of Rational Addiction," *Journal of Political Economy*, 1988.

Bernheim, B. Douglas, 2009, "Behavioral Welfare Economics," *Journal of the European Economic Association*, Vol. 7, No. 2-3, Pages 267-319

Chetty, Raj, Adam Looney and Kory Kroft, "Salience and Taxation: Theory and Evidence," *American Economic Review*, vol. 99(4), pages 1145-77, September.

\*Finkelstein, Amy, 2009, "EZ-Tax: Tax Salience and Tax Rates," *Quarterly Journal of Economics*, Vol. 124, No. 3, Pages 969-1010.

Ted O'Donoghue and Matthew Rabin, 2003, "Studying Optimal Paternalism, Illustrated by a Model of Sin Taxes," *American Economic Review Papers and Proceedings*, 93(2), May 2003, 186-191.

13. **Week 10: Valuing public goods**<sup>†</sup>

M. Gunderson and D. Hyatt, 2001, "Workplace Risks and Wages: Canadian Evidence from Alternative Models," *Canadian Journal of Economics* 34(2), 377-395.

\*A. Ashenfelter and M. Greenstone, "Using Mandated Speed Limits to Measure the Value of a Statistical Life," *Journal of Political Economy*, 2004.

K. Chay and M. Greenstone, 2005, "Does air quality matter? Evidence from the housing market," *Journal of Political Economy* 2005.

14. **Week 11: Electoral accountability**<sup>†</sup>

\*Ashworth, Scott. "Electoral accountability: recent theoretical and empirical work." *Annual Review of Political Science* 15 (2012): 183-201.

\*Ferraz, Claudio, and Frederico Finan. "Electoral Accountability and Corruption: Evidence from the Audits of Local Governments." *The American Economic Review* 101.4 (2011): 1274.

Besley, Timothy, and Anne Case. "Political institutions and policy choices: evidence from the United States." *Journal of Economic Literature* (2003): 7-73.

Persson, Torsten, and Guido Enrico Tabellini. *Political economics: explaining economic policy*. MIT press, 2002, cjaps. 3-4.

Healy, Andrew, and Neil Malhotra. "Retrospective voting reconsidered." *Annual Review of Political Science* 16 (2013): 285-306.

15. International taxation<sup>†</sup>

\*R. Gordon and J. Hines, "International taxation," NBER Working Paper 8854.

\*Zucman, Gabriel. 2014. "Taxing across Borders: Tracking Personal Wealth and Corporate Profits." *Journal of Economic Perspectives*, 28(4): 121-48.

Roger H. Gordon, 1992, "Can Capital Income Taxes Survive in Open Economies?" *Journal of Finance* 47, No. 3, pp. 1159-1180

Hines, James R., 1996, "Altered states: Taxes and the location of foreign direct investment in America," *American Economic Review* 86(5), 1076-1094.

Hines, James R. Jr. 2010. "Treasure Islands." *Journal of Economic Perspectives*, 24(4): 103-26.

16. **Week 12: Fiscal federalism**<sup>†</sup>

Boadway, R. and F. Flatters, 1982, "Efficiency and equalization payments in a federal system of government," *Canadian Journal of Economics* 15, 613-633.

Smart, M., 1998, "Taxation and deadweight loss in a system of intergovernmental transfers," *Canadian Journal of Economics* 31, 189-206.

D. Albouy, 2010, "Evaluating the Efficiency and Equity of Federal Fiscal Equalization," NBER Working Paper 16144.

Fernandez, R. and R. Rogerson, 1996, "Income Distribution, Communities, and the Quality of Public Education," *Quarterly Journal of Economics*, Vol. 111, No. 1 (Feb., 1996), pp. 135-164.

\*J. Hines and R. Thaler. 1995. "Anomalies: The Flypaper Effect." *Journal of Economic Perspectives*, 9: 217-226.

Knight, B., 2002, "Endogenous Federal Grants and Crowd-Out of State Government Spending: Theory and Evidence from the Federal Highway Aid Program," *American Economic Review* 92, 71-92.

Per Pettersson-Lidbom, 2010, "Dynamic commitment and the soft budget constraint: An empirical test," *AEJ: EP* 2, 154-179.

\*M. Feldstein and M. Wrobel, 1998, "Can state taxes redistribute income?" *Journal of Public Economics* 68, 369-396.

17. Tax competition<sup>†</sup>

\*Kanbur, R. and M. Keen 1993, "Jeux sans frontieres: Tax competition and tax co-ordination when countries differ in size", *American Economic Review*, 83, 877-892.

J. Wilson, 1999, "Theories of tax competition", *National Tax Journal*, 52, 269-304.

J. Wilson and D. Wildasin, 2004, "Capital Tax Competition: Bane or Boon?" *Journal of Public Economics*, 1065-1091.

18. Taxation and development<sup>†</sup>

\*R. Gordon and W. Li, 2009, "Tax structures in developing countries: Many puzzles and a possible explanation," *Journal of Public Economics* 93, 855-866.

\*Besley, Timothy, and Torsten Persson. 2014. "Why Do Developing Countries Tax So Little?" *Journal of Economic Perspectives*, 28(4): 99-120.

R. Burgess and N. Stern, 1993, "Taxation and Development," *Journal of Economic Literature* 31, 762-830.