

BOSTON COLLEGE  
Department of Economics

EC 865.01  
Fall 2001/02

Richard Tresch

Public Sector Economics I

Course Requirements: Final examination (50%) and a short paper on one of the topics from Part II of the syllabus (50%). I encourage you to present your paper to the class, although the presentation is optional and I will only grade your paper, not your presentation. The final exam is scheduled for Thursday, December 13, at 12:30. The papers are also due on December 13.

Textbook: Richard Tresch, Public Finance: A Normative Theory, revised edition, typescript (hereafter, Tresch)

Two other frequently cited reference texts are:

A.B. Atkinson and J. Stiglitz, Lectures on Public Economics (hereafter, Atkinson, Stiglitz)

A.J. Auerbach and M. Feldstein, Handbook of Public Economics, Vols. I and II (hereafter, Handbook)

The syllabus contains two parts. Part I covers the theoretical foundations of classical, first-best public sector analysis. Part II contains a number of topics of recent professional interest. The topics are mostly empirical and are not always discussed in my text. We will consider a selection of them, approximately in the order listed below.

Readings to support the material covered in my text are listed in the References at the end of each chapter. The readings on this syllabus are, for the most part, additional references of interest that are not mentioned in the text, including very recent material.

I. The First-Best Theory of the Public Sector

A. Background and Overview-- Issues and Methods

Tresch, Chs. 1-3.

Also: Atkinson, Stiglitz, Ch. 11

R. Musgrave, "A Brief History of Fiscal Doctrine," in Handbook, Vol. I, (pp. 1-25 relate to the material of EC 865).

R. Inman, "Markets, Government, and the 'New' Political Economy," Ch. 12 in Handbook, Vol. II (This excellent, wide-ranging survey will make more sense after a year's study. You might try pp. 647-674 and 753-765 early on).

B. The Social Welfare Function

1. Arrow's Impossibility Theorem and Majority Voting Difficulties

Tresch, Ch. 3.

Also for reference:

R. Boadway and D. Wildasin, Public Sector Economics, Ch. 6, pp. 138-154; Ch. 10, pp. 269-277.

## 2. Recent contributions

U. Segal, "Let's Agree That All Dictatorships are Equally Bad," Journal of Political Economy, June, 2000. (Segal's attempt to rescue a simple weighted social welfare function, which I find convincing and important.)

L. Kaplow, "Any Non-Welfarist Method of Policy Assessment Violates the Pareto Principle," Journal of Political Economy, April 2001.

### C. Public Expenditure Theory

#### 1. Externalities and Public Goods

Tresch, Chs. 5-8.

Also: W. Baumol and W. Oates, The Theory of Environmental Policy, 2<sup>nd</sup> ed., 1988, Ch. 8.

Additional reference: W. Oakland, "Theory of Public Goods," Ch. 9 in Handbook, Vol. II.

#### 2. Decreasing Cost Production

Tresch, Ch. 9.

### D. First-best Tax Theory--Equity in Taxation

#### 1. Underlying Theory

Tresch, Ch. 10.

Also: Atkinson, Stiglitz, Ch. 11, pp. 333-343.

W. Hettich and S. Winer, "Blueprints and Pathways: The Shifting Foundations of Tax Reform," National Tax Journal, December, 1985.

#### 2. The Public Choice Perspective--Self-interested Redistribution

##### a. Overview

J. Rodgers, "Explaining Income Redistribution," in H. Hochman and G. Peterson (eds.), Redistribution Through Public Choice.

##### b. Pareto-optimal redistribution

Tresch, Ch. 10.

##### c. Public insurance

L. Friedman, Microeconomic Policy Analysis, Ch. 6.

R. Boadway and D. Wildasin, Public Sector Economics, Ch. 14 on Social Insurance.

##### d. Voting for transfers to oneself

A. Feldman, Welfare Economics and Social Choice Theory, Ch. 9 ( especially pp. 162-164, 171-175).

### 3. Towards Application--Horizontal and Vertical Equity

Tresch, Ch. 11.

Also:

Atkinson, Stiglitz, Ch. 11, pp. 350-356.

R. Musgrave, "A Brief History of Fiscal Doctrine," pp. 15-25, in Handbook, Vol. I.

S. Sheffrin, "What Does the Public Believe About Tax Fairness?" National Tax Journal, September 1993, pp. 301-303

E. Plug, B. van Praag, J. Hartog, "If We Knew Ability, How Would We Tax Individuals?", Journal of Public Economics, May, 1999. (Does this give one hope that lump-sum taxation is practicable?)

#### E. Fiscal Federalism

##### 1. The Sorting of Functions: Which Governments Do What?

Tresch, Ch. 29.

D. Rubinfeld, "The Economics of the Local Public Sector," Ch. 11 in Handbook, Vol. II, pp. 625-634.

D. Wildasin, "Theoretical Analysis of Local Public Economics," Ch. 29. in E. Mills (ed.), Handbook of Regional and Urban Economics, Vol. 2 (especially sections 2, 3, 4).

##### 2. The Sorting of People: Jurisdiction Formation and Mobility With Public Goods Supply

Tresch, Ch. 30.

D. Rubinfeld, "The Economics of the Local Public Sector," in Handbook, Vol. II, pp. 574-601.

For reference: Another sophisticated model of the location decision, and an empirical study based on location theory. Very difficult, but worth careful study if you become interested in these types of models.

J. Henderson, "Community Choice of Revenue Instruments," Regional Science and Urban Economics, April 1994.

D. Epple, H. Sieg, "Estimating Equilibrium Models of Local Jurisdictions," Journal of Political Economy, August, 1999.

Additional wrinkles, for reference:

S. Rose-Ackerman, "Beyond Tiebout: Modelling the Political Economy of Local Government," and B. Hamilton, "A Review: Is the Property Tax a Benefit Tax?," both in G. Zodrow (ed.), Local Provision of Public Services: The Tiebout Model After 25 Years.

J.V. Henderson, "The Tiebout Model: Bring Back the Entrepreneurs," Journal of Political Economy, April, 1985.

W. Fischel, "Homevoters, Municipal Corporate Governance, and the Benefit View of the Property Tax," National Tax Journal, March 2001.

Finally, the following three papers use a modelling approach that incorporates a broad spectrum of the federalism literature. The first considers efficiency, the second adds equity, and the third is an empirical exercise that supports the approach:

E. Berglas, "Distribution of Tastes and Skills and the Provision of Local Public Goods," Journal of Public Economics, 1976.

R. Tresch, "Optimal Fiscal Federalism in a First-best Environment with Dynastic Social Welfare," B.C. Working Paper.

J.V. Henderson, "Population Composition of Cities: Restructuring the Tiebout Model," Journal of Public Economics, July, 1985.

a. The distribution function and mobility

W. Johnson, "Income Redistribution in a Federal System," AER, June, 1988, along with his empirical study:

W. Johnson, "Decentralized Income Redistribution Reconsidered," Economic Inquiry, January, 1991.

D. Epple, et. al., "Equilibrium Among Local Jurisdictions: Toward an Integrated Treatment of Voting and Residential Choice," Journal of Public Economics, August, 1984. Note: not an easy paper--for reference).

J. Persky, "Suburban Income Inequality: Three Theories and a Few Facts," Regional Science and Urban Economics, June, 1990.

D. Wildasin, "Income Redistribution With a Common Labor Market," AER, September, 1991 (relevant to the European Union). Also, D. Wildasin, "Income Redistribution and Migration," Canadian Journal of Economics, August 1994. (For reference: A companion piece to his EU article).

3. The Role of Grants-in-Aid in a Federalist System

Tresch, Ch. 31.

J. Alm, "The Optimal Structure of Intergovernmental Grants," Public Finance Quarterly, October, 1983, or

J. Alm, "Intergovernmental Grants and Social Welfare," Public Finance, 1983, No. 3.

T. Downs, T. Pogue, "Adjusting School Age Formulas for the Higher Cost of Educating Disadvantaged Students," plus the "Symposium on Fiscal Equalization," National Tax Journal, March 1994.

M. Bordignon, P. Manasse, G. Tabellini, "Optimal Redistribution Under Asymmetric Information," American Economic Review, June 2001.

4. Centralized vs. decentralized governments

W. Oates, "An Essay on Fiscal Federalism," Journal of Economic Literature, September, 1999. (A wide-ranging essay on current issues in the centralized/decentralized debate, including tax policy, grants-in-aid, public goods provision, and political considerations.)

J. Wilson, "Theories of Tax Competition," National Tax Journal, June, 1999. (An excellent survey and starting point on this topic, which relates specifically to potential problems with local taxation)

#### F. Postscript on First-best Theory

How useful is first-best theory? Not very, according to Peter Hammonds. See: P. Hammonds, "Theoretical Progress in Public Economics: A Provocative Assessment," Oxford Economic Papers, January, 1990 (Special Issue on Public Economics--incidentally, OEP runs occasional special issues on a variety of topics and fields).

I think Hammonds' viewpoint is too limited. If you agree with Hammonds, though, Richard Arnott will take you down some of Hammonds' preferred second-best roadways next term. (Note: Hammonds also has a fine overview of cost-benefit analysis.)

## II. Selected Topics (in approximate order of presentation)

### A. The Social Welfare Function in Empirical Analysis

Tresch, Ch. 4.

A related paper of interest on consumption and social welfare that I did not reference in the text is:

S. Yitzhaki, J. Slemrod, "Welfare Dominance: An Application to Commodity Taxation," AER, June, 1991.

### B. Policy Issues in the Control of Pollution

Tresch, Ch. 8

Other studies of interest not referenced in Ch. 8, by topic:

#### 1. Current U.S. Policy

J. Henderson, "Effects of Air Quality Regulation," AER, September 1996.

M. Kahn, "Particulate Pollution Trends in the United States," Regional Science and Urban Economics, February 1997.

#### 2. Direct Controls, Taxes, and Marketable Permits

P. Joskow, et. al., "The Market for Sulfur Dioxide Emissions," AER, September 1998.

P. Cramton, "A Review of Markets for Clean Air: The U.S. Acid Rain Program, by A. Ellerman, P. Joskow, R. Schmalensee, J-P Montero, and E. Bailey," Journal of Economic Literature, September 2000. (This review is so comprehensive that you might begin here rather than with the book, which Cramton characterizes as the definitive source on the SO<sub>2</sub> marketable emissions program).

T. Barthold, "Issues in the Design of Environmental Excise Taxes," Journal of Economic Perspectives, Winter 1994. (A detailed account of U.S. tax policies that have an impact on the environment).

#### 3. On the Benefits of Reducing Pollution

Another instance of how little we know about environmental damage relates to the current concern about global warming. See the Symposium on "Global Climate Change" in the Journal of Economic Perspectives, Fall 1993, particularly the articles by W. Nordhaus and J. Poterba.

#### 4. What the Future Holds

P. Portney, "Environmental Problems and Policy: 2000-2050," Journal of Economic Perspectives, Winter 2000.

### C. The Free Rider Problem

#### Tresch, Ch. 6.

Free riding behavior has been the subject of much experimental testing, often with economics students as subjects. Two well-known original experiments are: P. Bohm, "Estimating Demand for Public Goods: An Experiment," European Economic Review, Vol. 3, No. 2, 1972 (something of a classic); and F. Schneider and W. Pommerhene, "Free Riding and Collective Action: An Experiment in Public Microeconomics," Quarterly Journal of Economics, November, 1981. An interesting recent study not referenced in Ch. 6 is:

J. Falkinger, E. Fehr, S. Gächter, and R. Winter-Ebmer, "A Simple Mechanism for the Efficient Provision of Public Goods: Experimental Evidence," American Economic Review, March 2000.

#### 1. On the Coase Theorem and Externalities

##### Tresch, Chs. 7 and 20

G.W. Harrison, et. al., "Coasian Solutions to the Externality Problem in Experimental Markets," Economic Journal, June, 1987.

V. Aivazian, et. al., "The Coase Theorem and Coalitional Stability," Economica, November, 1987.

J. Farrell, "Information and the Coase Theorem," Journal of Economic Perspectives, Fall, 1987.

E. Masken, "The Invisible Hand and Externalities," AEA Papers and Proceedings, (American Economic Review), May 1994.

A. Dixit, M. Olson, "Does Voluntary Participation Undermine the Coase Theorem?" Journal of Public Economics, June 2000.

### D. Tax Reform

#### 1. Overview

Tax Reform for Fairness, Simplicity, and Economic Growth, Vol. I, U.S. Department of the Treasury, November, 1984 (hereafter, Treasury D), Overview, pp. vii-xix; Ch. 2; Appendix 4A, pp. 57-61.

Recent thinking on fundamental tax reform is discussed in the set of articles in "Applied Economics in Action: Discussing Fundamental Tax Reform," and "Prospects for Fundamental Tax Reform," American Economic Review, May 1997, pp. 114-155.

## 2. Tax Income or Expenditures?: Equity and Administrative Issues

Treasury I, Ch. 9.

Blueprints for Basic Tax Reform, U.S. Department of the Treasury, January 17, 1977. (written by David Bradford, a call for a consumption/expenditures tax)

D. Bradford, "The Possibilities for an Expenditure Tax," National Tax Journal, September, 1982.

Articles by Goode, Bradford, and Graetz in J. Pechman (ed.), What Should Be Taxed: Income or Expenditures?

Economists remain divided on the issue of taxing income or consumption. See the National Tax Association Symposium on "New Directions in Tax Policy," National Tax Journal, September, 1993, especially the articles by T. Barthold, C. McLure, and J. Sabelhaus for some of the issues surrounding tax reform that have been influential in Washington.

## 3. Integrating the Corporation and Personal Income Taxes

G. Hubbard, "Corporate Tax Integration: A View From the Treasury Department," Journal of Economic Perspectives, Winter 1993 (Not scintillating, but a good discussion of the issues related to integration along with some mention of the Treasury's 1992 proposals. Good sources).

## 4. Simplicity, Compliance Costs, and Tax Evasion

Tresch, Ch. 15 (The sections on Tax Evasion and Tax Amnesties)

Also:

M. Blumenthal, J. Slemrod, "The Compliance Cost of the U.S. Individual Income Tax System: A Second Look," National Tax Journal, June 1992.

M. Pitt, J. Slemrod, "The Compliance Cost of Itemizing Deductions: Evidence from Individual Tax Returns," AER, December, 1989.

## E. Income Taxes and Economic Behavior

### 1. Taxation, labor supply, saving, and investment--overview

A. Auerbach, J. Slemrod, "The Economic Effects of the Tax Reform Act of 1986," Journal of Economic Literature, June 1997. (A discussion of TRA86 is perhaps dated, but the article offers a good overview of the issues in this section, along with a superb bibliography of the best related journal articles. And TRA86 was the biggest federal tax reform ever enacted.)

### 2. Taxation and labor supply

Tresch, Ch. 13

Further textbook Coverage: R. Boadway, D. Wildasin, Public Sector Economics, Ch. 11, pp. 287-301.

Atkinson, Stiglitz, Ch. 2.



### 3. Taxation and saving

Textbook Coverage: R. Boadway, D. Wildasin, Public Sector Economics, Ch. 11, pp. 301-314.  
Atkinson, Stiglitz, Ch. 3.

For interesting analyses in the life-cycle tradition, see:

L. Kotlikoff, "Taxation and Savings: A Neoclassical Perspective," Journal of Economic Literature, December 1984. (The OLG framework classic.)

Also, for reference: A. Auerbach, L. Kotlikoff, Dynamic Fiscal Policy, a monograph published in 1987 that applies their OLG model to all kinds of public expenditure and tax policies.

A more recent empirical study that emphasizes the interaction between the personal and corporate income taxes is: M. Feldstein, "The Effects of Tax-based Savings Incentives on Government Revenue and National Saving," Quarterly Journal of Economics, May 1995.

A. Imrohorglu, et. al., "The Effect of Tax Favored Retirement Accounts on Capital Accumulation," AER, September 1998. (One of the latest in a large literature on IRA's and saving, with a good beginning summary of the results to date).

### 4. Taxation and investment

Textbook coverage: R. Roadway, D. Wildasin, Public Sector Economics, Ch. 11, pp. 321-337.  
Atkinson, Stiglitz, Ch. 5.

#### a. Taxation and the cost of capital

A. Auerbach, "The Tax Reform Act of 1986 and the Cost of Capital," Journal of Economic Perspectives, Summer, 1987.

B. Bernheim, J. Shoven, "Taxation and the Cost of Capital: An International Comparison," in C. Walker, M. Bloomfield (eds.), The Consumption Tax.

#### b. Inflation, tax rules, and the cost of capital

Articles by Bradford, Hall, Hulten and Wycoff in C. Hulten (ed.), Depreciation, Inflation, and the Taxation of Income From Capital.

L. Rose, "A Respecified Tax-Adjusted Fisher Relation," Economic Inquiry, April, 1986 (Good review of the empirical literature).

I. Hansson and C. Stuart, "The Fisher Hypothesis and International Capital Markets," Journal of Political Economy, December, 1986.

## c. What determines investment demand?

R. Chirinko, "Business Fixed Investment Spending," Journal of Economic Literature, December 1993. (An excellent survey covering what has been done and why, and offering an agenda for future research).

R. Chirinko, S. Fazzari, A. Meyer, "How Responsive is Business Capital Formation to its User Cost? An Exploration With Micro Data," Journal of Public Economics, October, 1999 (The answer is "not much"--recommended by Fabio Schiantarelli as the latest word.)

A. Goolsbee, "Investment Tax Incentives, Prices, and the Supply of Capital Goods," Quarterly Journal of Economics, February 1998 (Suggests that much of investment tax breaks are captured by capital goods suppliers in the form of higher prices, which he thinks explains the low investment response to tax policy.)

Also: M. Feldstein, "Inflation, Tax Rates, and Investment: Some Econometric Evidence," Econometrica, July, 1982.

T. Wisley, S. Johnson, "An Evaluation of Alternative Investment Hypotheses Using Non-Nested Tests," Southern Economic Journal, October, 1985.

B. Bernanke, et. al., "Alternative Non-nested Specification Tests of Time-series Investment Models," Journal of Econometrics, March 1988 (econometric reference only).

## d. On measuring effective tax rates:

D. Fullerton, "Which Effective Tax Rate," National Tax Journal, March, 1984.

D. Bradford, C. Stuart, "Issues in the Measurement and Interpretation of Effective Tax Rates," National Tax Journal, September, 1986.

M. Daly, et. al., "The Sensitivity of Effective Marginal Tax Rate Calculations to Alternative Arbitrage Assumptions," Economic Letters, Vol. 21, No. 2, 1986.

## 5. Taxation and investment in human capital

P. Trostel, "The Effect of Taxation on Human Capital," Journal of Political Economy, April 1993.

M. Nerlove, et. al., "Comprehensive Income Taxation, Investments in Physical and Human Capital, and Productivity," Journal of Public Economics, March 1993.

## F. Transfer Payments

Tresch, Ch. 19.

Interesting articles not referenced in Ch. 19, by topic:

### 1. Universal vs. Means-tested Transfers

G. Burtless, "The Economist's Lament: Public Assistance in America," Journal of Economic Perspectives, Winter, 1990.

J. Creedy, "Comparing Tax and Transfer Systems: Poverty, Inequality, and Target Efficiency," Economica, 1996 Supplement. (Tough analytics, but the approach is clear enough and the basic premise is interesting in comparing the two types of transfer schemes.)

R. Moffitt, "A Problem with the Negative Income Tax," Economic Letters, 17/3, 1985.

### 2. Cash vs. In-kind Transfers

E. Browning, "Valuation of In-Kind Transfers and the Measurement of Poverty," Public Finance Quarterly, April, 1991.

Three short articles on the deadweight loss from Christmas in the American Economic Review, December 1998, pp. 1350-1359.

F. Gahvari, "In-Kind vs. Cash Transfers in the Presence of Distorting Taxes," Economic Inquiry, January 1995.

Also, for reference only:

B. DeBorger, "Estimating the Welfare Implications of In-Kind Government Programs: A General Numerical Approach," Journal of Public Economics, March, 1989.

### 3. Workfare

D. Friedlander, et. al., "Evaluating Government Training Programs for the Economically Disadvantaged," Journal of Economic Literature, December 1997; and

J. Geron, "Work and Welfare: Lessons on Employment Programs," Journal of Economic Perspectives, Winter, 1990.

C. Colburn, "Work Requirements and Income Transfers," Public Finance Quarterly, April 1993.

### 4. The Earned Income Tax Credit

Tresch, Ch. 19.

## 5. The Incentive Effects of the U.S. Welfare System on Labor Supply, Family Structure, and Other Issues

R. Moffitt, "Incentive Effects of the U.S. Welfare System: A Review," Journal of Economic Literature, March 1992.

M. Keane, R. Moffitt, "A Structural Model of Multiple Welfare Program Participation and Labor Supply," International Economic Review, August 1998. (For reference: Heavy econometrics, but considers the combined effect of the welfare programs on labor supply.)

B. Meyer, D. Rosenbaum, "Making Single Mothers Work: Recent Tax and Welfare Policy and its Effects," National Tax Journal, December 2000, part 2.

D. Ellwood, "Anti-Poverty Policy for Families in the Next Century: From Welfare to Work--and Worries," Journal of Economic Perspectives, Winter 2000. (A surprisingly balanced assessment given that Ellwood resigned his position at Health and Human Services when President Clinton signed the TANF bill in 1996, which ended the entitlement to welfare for poor single parents and their families).

## 6. What Determines the Willingness to Redistribute?

This recent and rapidly expanding literature tends to focus on the question of why the United States and Europe have such different attitudes towards redistribution despite their similar economies, with Europe being much more egalitarian. (The determinants emphasized by the articles are in parentheses.)

G. Corneo, H. Gruner, "Social Limits to Redistribution," American Economic Review, December 2000. (social status)

R. Benabou, "Unequal Societies: Income Distribution and the Social Contract," American Economic Review, March 2000. (imperfect capital markets and political participation) (very difficult)

R. Benabou, E. Ok, "Social Mobility and the Demand for Redistribution: the POUM Hypothesis" Quarterly Journal of Economics, May 2001 (social mobility vs. demand for income insurance)

E. Luttmer, "Group Loyalty and the Taste for Redistribution," Journal of Political Economy, June 2001 (heterogeneous vs. homogeneous populations) (empirical)

## G. The Incidence of Taxes and Government Expenditures Under First-Best Assumptions

### 1. Tax Incidence

Tresch, Chs. 16, 17.

#### a. The Harberger model

Tresch, Ch. 16.

Also:

T. Hatta, J. Haltwanger, "A Decomposition of the Harberger Expression for Tax Incidence," Journal of Public Economics, December, 1982.

L. Ebrill, D. Hartman, "On the Incidence and Excess Burden of the Corporation Income tax," Public Finance, 1982(1).

b. The sources and uses approach

Tresch, Ch. 17

Also:

J. Poterba, "Lifetime Incidence and the Distributional Burden of Excise Taxes," AEA Papers and Proceedings, May, 1989.

J. Gravelle, "Equity Effects of the Tax Reform Act of 1986," Journal of Economic Perspectives, Winter 1992.

A. Mitrusi, J. Poterba, "The Distribution of Payroll and Income Tax Burdens, 1979-99," National Tax Journal, September 2000, part 2. (a good account of the major changes in the tax laws over the past 20 years, and the shifting importance of the two taxes for the majority of taxpayers)

c. Summary and overview

L. Kotlikoff, "Tax Incidence," Handbook, Vol. II (especially for tax incidence in a dynamic setting).

2. Expenditure Incidence

Tresch, Ch. 17.

G. Brennan, "The Distributional Implications of Public Goods," Econometrica, March, 1976.

R. Musgrave, et. al., "The Distribution of Fiscal Burdens and Benefits," Public Finance Quarterly, 1974.

3. Incidence Measures in the Lorenz Tradition

Tresch, Ch. 17.

Also:

A. Atkinson, "Horizontal Equity and the Distribution of the Tax System," in H. Aaron, M. Boskin (eds.), The Economics of Taxation.

Some recent articles following Aronson and Lambert:

M. Kean, H. Papapanago, A. Shorrocks, "Tax Reform and Progressivity," Economic Journal, January, 2000.

J-Y Duclos, P. Lambert, "A Normative and Statistical Approach to Measuring Classical Horizontal Equity," Canadian Journal of Economics, February, 2000.

N. Kakwani, P. Lambert, "Measuring Income Tax Discrimination," Review of Economics and Statistics, February, 1999.

J. Creedy, J. Van de Ven, "Decomposing Redistributive Effects of Taxes and Transfers in Australia: Annual and Lifetime Measures," Australian Economic Papers, June 2001.

4. Economy-wide Dynamic Incidence Studies

Tresch, Ch. 17

D. Altig, A. Auerbach, L. Kotlikoff, K. Smetters, and J. Walliser, "Simulating Fundamental Tax Reform in the United States," American Economic Review, June 2001. (combines Auerback/Kotlikoff OLG and Fullerton/Rogers lifetime CGE approaches)

## H. The Empirical Analysis of Grants-in-Aid

### 1. Overview

Tresch, Ch. 31.

E. Gramlich surveys the early empirical literature in Ch. 12 of W. Oates (ed.), The Political Economy of Fiscal Federalism.

D. Rubinfeld, "The Economics of the Local Public Sector," Handbook, Vol. II, pp. 634-637.

### 2. The Flypaper Effect

B. Hamilton, "The Flypaper Effect and Other Anomalies," Journal of Public Economics, December, 1983.

W. Dougan and D. Kenyon, "Pressure Groups and Public Expenditures: The Flypaper Effect Reconsidered," Economic Inquiry, January, 1988.

K. Strumpf, "A Predictive Index for the Flypaper Effect," Journal of Public Economics, September 1998.

### 3. Project Grants With Negotiable Matching Rates

H. Chernick, Ch. 7 in P. Mieszkowski and W. Oakland (eds.), Fiscal Federalism and Grants-in-Aid.

### 4. The Budget Constraint With Closed-ended Matching Grants

S. Megdal, "The Flypaper Effect Revisited: An Econometric Explanation," Review of Economics and Statistics, May, 1987.

R. Moffitt, "The Econometrics of Kinked Budget Constraints," Journal of Economic Perspectives, Spring, 1990.

### 5. Grants and the granting government

J. Yinger, H. Ladd, "The Determinants of State Assistance to Central Cities," National Tax Journal, December, 1989. (A companion piece is: H. Ladd, "State Assistance to Local Governments: Changes During the 1980's," AEA Papers and Proceedings, May, 1990).

D. Schwallie, "Measuring the Effects of Federal Grants-in-Aid on Total Public Sector Size," Public Finance Quarterly, April, 1989.

## I. Estimating the Demand for Public Goods

### 1. The Median Voter Model

Tresch, Ch. 31.

Atkinson, Stiglitz, Ch. 10, pp. 294-307, 321-330.

D. Rubinfeld, "The Economics of the Local Public Sector," Handbook, Vol. II, pp. 601-614, 622-625.

T. Borcharding and R. Deacon, "The Demand for the Services of Non-Federal Governments," AER, December, 1972.

T. Bergstrom and R. Goodman, "Private Demands for Public Goods," AER, June, 1973.

E. Gramlich and D. Rubinfeld, "Micro Estimates of Public Spending Demand Functions and Tests of the Tiebout and Median Voter Hypotheses," Journal of Political Economy, June, 1982.

a. Tiebout bias, to which researchers now routinely pay attention

D. Wildasin, "Demand Estimation for Public Goods," Review of Economic Studies, August, 1989, pp. 354-362 (good discussion of other issues, too, in estimating the demand for local public goods).

## 2. Capitalization and the Hedonic Price Technique

Tresch, Ch. 26.

D. Rubinfeld, "The Economics of the Local Public Sector," Handbook, Vol. II, pp. 619-622.

A.M. Freeman, III, The Benefits of Environmental Improvement, Ch. 4, pp. 78-83, Ch. 6, Appendix.

a. Econometric issues and difficulties (for reference only):

J. Follain and E. Jimenez, "Estimating the Demand for Housing Characteristics: A Survey and Critique," Regional Science and Urban Economics, February, 1985.

T. Bartik, "The Estimation of Demand Parameters in Hedonic Price Models," Journal of Political Economy, February, 1987.

Smith, Huang, "Can Markets Value Air Quality? A Meta Analysis of Hedonic Property Value Models," Journal of Political Economy, February 1995. (Contains a huge bibliography of hedonic price studies, which it surveys).

## 3. Survey Techniques

Tresch, Chs. 26 and 31.

D. Rubinfeld, "The Economics of the Local Public Sector," Handbook, Vol. II, pp. 614-619.

D. Brookshire, et. al., "Valuing Public Goods: A Comparison of Survey and Hedonic Approaches," American Economic Review, March, 1982.

J. Clinch, A. Murphy, "Modelling Winners and Losers in Contingent Valuation of Public Goods: Appropriate Welfare Measures and Econometric Analysis," Economic Journal, April 2001. (when the same external effects are viewed as positive by some, negative by others).

An interesting empirical paper that uses the survey technique to try to separate insurance and charity motives for transfers is:

T. Husted, "Micro-based Estimation of the Demand for Income-Redistribution Benefits," Public Finance Quarterly, April, 1990.

## J. The New Political Economy

This is an exploding area of public sector analysis that I do not cover in my text because it is strictly positive analysis and often macro oriented. If interested, you might begin with the following review article of two recent books:

G. Saint-Paul, "The 'New Political Economy': Recent Books by Allen Drazen and by Thorsten Persson and Guido Tabellini, Journal of Economic Literature, December 2000.

Two related and recent overview articles are:

C. Manski, "Economic Analysis of Social Interactions," and E. Ostrom, "Collective Action and the Evolution of Social Norms," both in the Journal of Economic Perspectives, Summer 2000.

Section F-6 above on the determinants of redistribution would be considered part of the new political economy analysis.