

**Microeconomic Analysis of Government Activity
WWS 525**

Class: **Office:**
Telephone:
Office Hours:

WWS: The Course

Analysis of government involvement in the economy (a) to correct for 'market failures' and (b) to obtain a more acceptable income distribution. How can economic theory contribute to major policy issues such as the reduction of congestion and environmental pollution and the supply of 'public goods', such as health and education? How to regulate 'natural monopolies' in the infrastructure industries (e.g. telecommunications and electricity). The desirable structure of Social Security and saving for old age. Optimal progressivity and efficiency aspects of income and excise taxation, including capital gains taxes.

Prerequisite

The course will assume that students had a course in microeconomics.

Reading

Books on the Reading List will be on reserve in the WWS library. Lectures can be accessed on the Princeton University Blackboard website. Problem sets and lecture notes will be provided.

Books

1. Arnold, D., M. Graetz, E. Munnell (eds.) (1998), *Framing the Social Security Debate* (National Academy of Social Insurance).
2. Atkinson, A. and J. Stiglitz, (1980), *Lectures in Public Economics* (McGraw-Hill)
3. Atkinson, A. (1999), *The Economic Consequences of Rolling Back the Welfare State* (M.I.T)
4. Atkinson, A. (1995), *Public Economics in Action* (Oxford)
5. *Averting the old Age Crisis*, (1994), The World Bank
6. Barr, N. (2001), *The Welfare State As Piggy Bank* (Oxford)
7. Bateman H., G. Kingston, and J. Piggott, (2002), *Forced Saving: Mandating Private Retirement Incomes* (Cambridge)
8. Baumol, W. and W. Oates (1988), *Theory of Environmental Policy*
9. Diamond, P. (2002), *Social Security Reform*, (Oxford)
10. Diamond P. and P. Orszag, (2004), *Saving Social Security: A Balanced Approach*, (The Brookings Institution)
11. Evans, D., F. Fisher, D. Rubinfeld and R. Schmalensee (2000), *Did Microsoft Harm Consumers* (AEI-Brookings)
12. Gruber, J. and D. Wise (1999) *Social Security and Retirement Around the World* (Chicago)
13. Hindricks, J. and G. Myles, (2006) *Intermediate Public Economics*, (MIT Press)
14. Motta, M. (2004), *Competition Policy: Theory and Practice*, (Cambridge).
15. Rosen, H. (1992), *Public Finance* (Irwin)
16. Stiglitz, J. (1986), *Economics of the Public Sector* (Norton)
17. Stiglitz, J. (2002), *Globalization and Its Discontents* (Norton)
18. Train, K. (1991), *Optimal Regulation* (M.I.T)
19. Tuomala, M. (1991), *Optimal Income Tax and Redistribution* (M.I.T)
20. Viscusi, K. et-al (1995), *Economics of Regulation and Antitrust* (M.I.T)

A. Externalities and Corrective Taxation

Can road tolls and pollution taxes yield a "first-best" resource allocation?

Hindricks, Myles (2006), ch. 7

Baumol and Oates, ch. 3

Rosen (1992), ch. 6

Stiglitz (1986), ch. 8

2nd. Public Goods and Collective Decisions

What are 'Public Goods' and how can the government arrange for their supply?
Informational issues and the effects of distortive taxes.

Hindricks, Myles (2006), ch. 5,6

Rosen (1992), chs. 5,7

Stiglitz (1986), chs. 5,6,7

3rd. Natural Monopolies: Pricing, Regulation, Concessions and Public Enterprise

Economies of scale and 'fair rate of return' regulation, price caps, peak-load pricing, 'competition for the market', privatization of State Owned Enterprises.

Hindricks, Myles (2006), ch. 8
Train (1991), introduction, chs. 1,2,3,4,7,10
Viscusi *et-al* (1995), chs. 10,11,12,14
Evans *et-al* (2000)
Stiglitz (2002), chs. 1,5,7

4th. Taxation: Commodity Taxation, Tax Evasion

The deadweight Burden of taxes, optimal commodity taxes, distributional considerations, incentives for tax evasion.

Hindricks, Myles (2006), ch. 14

Rosen (1992), chs. 13,14,15
Atkinson-Stiglitz (1980), chs. 12

5th. Capital and Corporate Taxes

What are the welfare effects of interest income taxes? Should capital-gains be taxed at a lower rate than earnings?

Hindricks, Myles (2006), ch. 16
Stiglitz (1986), chs. 21,22

6th. Income Taxation: Base and Progressively

How progressive should the income tax be? Effects on labor supply, education and 'income maintenance' programs.

Atkinson (1999).
Hindricks, Myles (2006), ch. 10,12,13,15
Tuomoala (1990)
Atkinson (1995)

7th. Long-Term Savings: 'Ricardian Equivalence': Social Security and Pension Systems, Pay-As-You-Go vs. Funding.

Why is there a global crisis in government-run Social Security systems?
Defined Contribution vs. Defined Benefits: savings and labor supply effects;
reform proposals in the U.S. and elsewhere.

Aaron, H. (1997) "A Bad Idea Whose Time will Never Come," *Brookings Review*, 16-23

Arnold et-al (1998), chs. 2,4 and 7.

Barr, N. (2001) Parts 2,3

Bateman, Kingston, and Piggott (2002)

Gruber and Wise (1999)

Diamond, P. (1996), "Proposals to Restructure Social Security," *Journal of Economic Perspectives*, 66-68

Diamond, P. (1999), "Issues in Privatizing of Social Security," *National Academy of Social Insurance* (MIT)

Diamond P. and P. Orszag, (2004).

Kotlikoff and Sachs (1997), "Privatization of Social Security," *Brookings Review*