



## Department of Economics Course Outline

		<b>Term:</b>	Winter 2007
<b>Course:</b>	Economics 611.13 [Public Finance]	<b>Section:</b>	[91]
<b>Time:</b>	M 18:30 ? 21:20	<b>Place:</b>	SS 423 (subject to change)
<b>Instructor:</b>	Dr. Jean François Wen		
<b>Office:</b>	SS 416	<b>Telephone:</b>	220-2478
<b>Office Hours:</b>	TR 14:00 ? 16:00	<b>E-Mail:</b>	wen@ucalgary.ca

### Textbook(s):

n/a

### Book(s) on Reserve:

n/a

### Course Outline:

This is a course on normative theory of Public Economics, with a particular focus on ideas and methods relevant for understanding the economics of 'welfare state' programs, such as unemployment insurance, pensions, health care, subsidized housing, education, and income redistribution. Welfare state programs comprise a very substantial part of government activities. Understanding the efficiency and equity rationales for the welfare state is therefore fundamental to understanding the economic role of government in the modern economy.

The theoretical concepts to be covered include the conditions for Pareto optimality, the welfare theorems, externalities and public goods, social welfare functions, interdependent utility functions, insurance market failures, optimal income taxation, negative income taxes, in-kind transfers, and unfunded public pensions. We will discuss how these topics relate to actual welfare states programs.

The following list articles will be covered; many are regarded as seminal contributions. (An asterisk means that reading the full paper is indispensable. Where there is no asterisk, the paper may contain considerably more material than will be discussed in class; in those cases, my lecture notes are sufficient and reading the paper, though recommended, is regarded as optional.)

## Topics and Reading List

### A. Economic Efficiency and the Fundamental Theorems of Welfare Economics

#### 1. Pareto Efficiency (1/2 lecture)

Reading:

- Bator, F.M. (1957) The Simple Analytics of Welfare Maximization, *American Economic Review* 47: 22-59.

#### 2. Competitive Equilibrium (1/2 lecture)

#### 3. Classic Market Failures (1 lecture)

Reading:

- Bowen, H.R. (1943) The Interpretation of Voting in the Allocation of Economic Resources, *Quarterly Journal of Economics* 58: 27-48.
- Meade, J. (1952) External Economies and Diseconomies in a Competitive Situation, *Economic Journal* 62: 54-76.
- Samuelson, P. (1955) Diagrammatic Exposition of a Theory of Public Expenditures, *Review of Economics and Statistics* 37: 350-6. (\*)
- Samuelson, P. (1954) The Pure Theory of Public Expenditures, *Review of Economics and Statistics* 36: 387-9.

#### 4. Incentives and Excess Burden (1 lecture)

Reading:

- Aaron, H. and G. von Furstenberg (1971) The Inefficiency of Transfers in Kind: The Case of Housing Assistance, *Western Economic Journal* 9, 184-191.
- Lindbeck, A. (1993) Tax Effects versus Budget Effects on Labor Supply, in *The Welfare State: the Selected Papers of Asser Lindbeck, Volume II* (Adelshot: Edward Elgar).

#### 5. Pareto Optimal Transfers (1 lecture)

Reading:

- Hochman, H. and J. Rodgers (1969) Pareto Optimal Distribution, *American Economic Review* 59: 542-57. (\*)
- Olson, E.O. (1971) Subsidized Housing in a Competitive Market: Reply, *American Economic Review* 61: 220-224.
- Thurow, L. (1971) Income Distribution as a Pure Public Good, *Quarterly Journal of Economics* 85: 327-36.

## B. Social Welfare Functions

### 6. Social Welfare Functions (1 lecture)

Reading:

- Jorgenson, D. (1990) Aggregate Consumer Behavior and the Measurement of Social Welfare, *Econometrica*, September.
- Samuelson, P. (1956) Reaffirming the Existence of Reasonable Bergson-Samuelson Social Welfare Functions, *Economica* 44: 81-8. (\*)
- Atkinson, A. (1970) On the Measurement of Inequality, *Journal of Economic Theory* 55: 749-64.
- Shorrocks, A.F. (1983) Ranking Income Distributions, *Economica* 50: 3-17.

## C. Limits to Redistribution

### 7. Progressive Income Taxation (1 and ½ lectures)

Reading:

- Atkinson, A. and J. Stiglitz (1980) The Structure of Income Taxation, chapter 13 in *Lectures on Public Economics*.
- Browning, M. and Johnson (1984) The Tradeoff Between Equality and Efficiency, *Journal of Political Economy* 92: 175-203. (\*)
- Slemrod, J., S. Yitzhaki, J. Mayshar, and M. Lundholm (1994) The Optimal Two-Bracket Linear Income Tax *Journal of Public Economics* 53: 269-290.
- Stern, H.N. (1976) On the Specification of Models of Optimum Income Taxation, *Journal of Public Economics* 6: 123-62. (\*)

### 8. In-Kind Transfers (1 and 1/2 lectures)

Reading:

- Blackorby, C. and D. Donaldson (1988) Cash versus Kind, Self-Selection, and Efficient Transfers, *American Economic Review* 78: 691-700. (\*)

- Hanushek, E., C.K.Y. Leung, and K. Yilmaz (2003) Redistribution Through Education and Other Transfer Mechanisms, *Journal of Monetary Economics* 50: 1719-1750. (\*)

## D. Insurance Market Failures

### 9. Insurance Against Illness and Unemployment (1 lecture)

Reading:

- Dahlby, B. (1981) Adverse Selection and Pareto Improvement through Compulsory Insurance, *Public Choice* 37: 547-558.
- Pauly, M.V. (1974) Overinsurance and Public Provision of Insurance: The Roles of Moral Hazard and Adverse Selection, *Quarterly Journal of Economics* 88: 44-62.
- Pauly, M.V. (1968) The Economics of Moral Hazard: Comment, *American Economic Review* 58: 531-537. (\*)
- Rothschild, M. and J.E. Stiglitz (1976) Equilibrium in Competitive Insurance Markets, *Quarterly Journal of Economics* 90: 629-650. (\*)

### 10. Social Insurance (1 lecture)

Reading:

- Atkinson, A.B. (1991) Social Insurance: The Fifteenth Annual Lecture of the Geneva Association Review 38: 883-889.
- Dworkin, R. (1993) Justice in the Distribution of Health Care, *McGill Law Review* 38: 883-898.
- Varian, H. (1980) Redistributive Taxation as Social Insurance, *Quarterly Journal of Economics* 14: 49-68. (\*)

### 11. Annuities and Public Pensions (1 lecture)

Reading:

- Feldstein, M. (1985) The Optimal Level of Social Security Benefits, *Quarterly Journal of Economics* 100: 303-320. (\*)
- Feldstein, M. (1974) Social Security, Induced Retirement and Aggregate Capital Accumulation, *Journal of Political Economy* 82: 905-926. (\*)
- Barr, N. (1979) Myths My Grandpa Taught Me, *Three Banks Review* 124: 27-55.

## E. Time Inconsistency

### 12. Time Consistent Transfers (1 lecture)

Reading:

- Bruce, N. and M. Waldman (1991) Transfers in Kind: Why They Can Be Efficient and Nonpaternalistic, American Economic Review 81: 1345-51.

### Grade Determination and Final Examination Details:

There will be four assignments, worth 10 percent each; a mid-term exam worth 20 percent; and a final exam worth 40 percent. The tentative date for the midterm exam is Monday, March 5 from 6:30-8:30 PM.

Tests and final exams are marked on a numerical (percentage) basis, then converted to letter grades. The course grade is then calculated using the weights indicated above. As a guide to determining standing, these letter grade equivalences will generally apply:

A+	90-100	B	70-74	C-	56-58
A	85-89	B-	65-69	D+	53-55
A-	80-84	C+	62-64	D	50-52
B+	75-79	C	59-61	F	0-49

If, for some reason, the distribution of grades determined using the aforementioned conversion chart appears to be abnormal the instructor reserves the right to change the grade conversion chart if the instructor, *at the instructor's discretion*, feels it is necessary to more fairly represent student achievement.

A passing grade on any particular component of the course is not required for a student to pass the course as a whole.

Non-programmable calculators will be allowed during the writing of tests or final examinations.

There will be a 3 hour final examination scheduled by the Department of Economics.

Tests and exams will not involve multiple choice questions.

### Notes:

- Students seeking reappraisal of a piece of graded term work (term paper, essay, etc.) should discuss their work with the Instructor *within fifteen days* of the work being returned to the class.
- It is the student's responsibility to request academic accommodations. If you are a student with a documented disability who may require academic accommodation and have not registered with the Disability Resource Centre, please contact their office at 220-8237. Students who have not registered with the Disability Resource Centre are not eligible for formal academic accommodation. You are also required to discuss your needs with your instructor no later than fourteen (14) days after the start of this course.

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JFW:mi

2006-12-18