

Econ 652: Public Finance I
Government Expenditure and Social Insurance
Mark Duggan, Autumn 2008

Meetings: The course will meet Mondays and Wednesdays from 9:30 – 10:45AM.

Course requirements: In addition to participating in class and reading the assigned papers (approximately two per week), there are four sets of requirements for this course. The first is to complete 2-3 problem sets. The second will be a mock referee report that will be due midway through the semester. The third will be to give a 15 minute presentation on one paper during the semester. The last requirement is the final exam that will take place at the end of the semester. The point allocation across these is roughly 20%, 15%, 15%, and 40%, respectively, with class participation accounting for the final 10%.

Useful texts

A. Auerbach and M. Feldstein, *Handbook of Public Economics: Volumes 3 and 4* (Amsterdam: North-Holland, 2003).

Committee on Ways and Means, *Overview of Entitlement Programs* (“Green Book”) – 2004 edition available at <http://waysandmeans.house.gov/Documents.asp?section=813>

1. Social Insurance Theory – required readings are bolded

George Akerlof, “The Market for Lemons,” *Quarterly Journal of Economics* 85 (1970), 488-500.

A.B. Atkinson, “Income Maintenance and Social Insurance,” in A. Auerbach and M. Feldstein, eds., *Handbook of Public Economics* Volume 2 (Amsterdam: North Holland, 1987), 779-908.

Michael Rothschild and Joseph Stiglitz, “Equilibrium in Competitive Insurance Markets,” *Quarterly Journal of Economics* 91 (1976), 629-649.

Charles Wilson, “The Nature of Equilibrium in Markets with Adverse Selection,” *Bell Journal of Economics* (Spring 1980), 108-130.

2. Social Security

2.1 Theoretical Models and Motivation

John Cawley and Tomas Philipson, “An Empirical Examination of Information Barriers to Trade in Insurance,” *American Economic Review* 89 (1999), 827-846.

Peter Diamond, “A Framework for Social Security Analysis,” *Journal of Public Economics* 8 (1977), 275-298.

Peter Diamond and James Mirrlees, “A Model of Social Insurance with Variable Retirement,” *Journal of Public Economics* 10 (1978), 295-336.

Peter Diamond and James Mirrlees, "Payroll-Tax Financed Social Security with Variable Retirement," *Scandinavian Journal of Economics* 88 (1986), 25-50.

Martin Feldstein, "The Optimal Level of Social Security Benefits," *Quarterly Journal of Economics* 100 (May 1985), 300-320.

Martin Feldstein, "Should Social Security Be Means Tested?" *Journal of Political Economy* 95 (1987), 468-484.

Amy Finkelstein and James Poterba, "Adverse Selection in Insurance Markets: Policyholder Evidence from the U.K. Annuity Market," *Journal of Political Economy*. 112 (2004), 183-208.

Alan Gustman and Thomas Steinmeier, "How Effective is Redistribution Under the Social Security Benefit Formula?" *Journal of Public Economics* (2001), 1-28.

Glenn Hubbard and Kenneth Judd, "Social Security and Individual Welfare: Precautionary Saving, Borrowing Constraints, and the Payroll Tax," *American Economic Review*, (September 1987), 630-646.

2.2 Social Security and Private Saving

Orazio Attanasio and Agar Brugiavini, "Social Security and Households' Saving" *Quarterly Journal of Economics* 118 (2003), 1075-1119.

Doug Bernheim, Jon Skinner, and S. Weinberg, "What Accounts for the Variation in Retirement Wealth Among U.S. Households?" *American Economic Review* 91 (2001), 832-857.

Doug Bernheim, "The Economic Effects of Social Security: Toward a Reconciliation of Theory and Measurement," *Journal of Public Economics* 33 (1987), 273-304.

Peter Diamond and Jerry Hausman, "Individual Retirement and Savings Behavior," *Journal of Public Economics* 23 (1984), 81-114.

Martin Feldstein, "Social Security, Induced Retirement, and Aggregate Capital Accumulation," *Journal of Political Economy* 82 (1974), 905-926.

Martin Feldstein, "Social Security and Private Saving: Reply," *Journal of Political Economy* 90 (1982), 630-642.

D. Leimer and S. Lesnoy, "Social Security and Private Saving: New Time-Series Evidence," *Journal of Political Economy* 90 (1982), 606-629.

K. Scholz, A. Seshadri, and S. Khitatrakun, "Are Americans Saving Optimally for Retirement?" *Journal of Political Economy*, 2007.

2.3 Social Security and Labor Supply

Gary Burtless, "Social Security, Unanticipated Benefit Increases, and the Timing of Retirement," *Review of Economic Studies* (1986), 781-805.

Jon Gruber and David Wise, “Social Security Programs and Retirement Around the World,” *NBER Working Paper 6134*.

Alan Gustman and Thomas Steinmeier, “The Social Security Early Entitlement Age in a Structural Model of Retirement and Wealth,” forthcoming in the *Journal of Public Economics*.

Alan Krueger and Jorn-Steffen Pischke, “The Effect of Social Security on Labor Supply: A Cohort Analysis of the Notch Generation,” *Journal of Labor Economics* 10 (1992), 412-437.

John Rust and Christopher Phelan, “How Social Security and Medicare Affect Retirement Behavior in a World of Incomplete Markets,” *Econometrica* 65 (July 1997), 781-832.

Andrew Samwick, “New Evidence on Pensions, Social Security, and the Timing of Retirement,” *Journal of Public Economics* (1998) 207-236.

James Stock and David Wise, “Pensions, the Option Value of Work, and Retirement,” *Econometrica* 58 (1990), 1151-1180.

2.4 Social Security Reform

Andrew Abel, “The Effects of Investing Social Security Funds in the Stock Market when Fixed Costs Prevent Some Households from Holding Stocks,” *American Economic Review*, March, 2001, 128-148.

Peter Diamond, “Privatization of Social Security: Lessons from Chile,” *Revista de Analisis Economico* 9 (1994), 21-33.

Martin Feldstein, ed., *Privatizing Social Security*. Chicago: University of Chicago Press, 1998.

Martin Feldstein, “The Missing Piece in Policy Analysis: Social Security Reform,” *American Economic Review* (May 1996), 1-14.

Martin Feldstein, “Social Security Reform in China,” *NBER Working Paper 6794*. Also in *China Economic Review* 10 (1999).

Kent Smetters, “Is the Social Security Trust Fund Worth Anything?” *American Economic Review Papers and Proceedings*, May, 2004.

3. Unemployment Insurance

Daron Acemoglu and Robert Shimer, “Efficient Unemployment Insurance,” *Journal of Political Economy* 107 (1999), 893-928.

Patricia Anderson and Bruce Meyer, “Unemployment Insurance Takeup Rates and the After-Tax Value of Benefits,” *Quarterly Journal of Economics* 112 (1997), 913-938.

David Card, Raj Chetty, and Andrea Weber, “The Spike at Benefit Exhaustion: Leaving the Unemployment System or Starting a New Job?” *AEA Papers and Proceedings* 97 (2007), 113-118.

Raj Chetty, "A General Formula for the Optimal Level of Social Insurance," *Journal of Public Economics* 90 (2006), 1879-1901.

Raj Chetty, "Moral Hazard versus Liquidity and Optimal Unemployment Insurance," *Journal of Political Economy* 116 (2008), 173-234.

Martin Feldstein and James Poterba, "Unemployment Insurance and Reservation Wages," *Journal of Public Economics* 23 (1984), 141-167.

Martin Feldstein, "The Effect of Unemployment Insurance on Temporary Layoff Unemployment," *American Economic Review* 65 (December, 1978), 834-846.

Martin Feldstein, "Temporary Layoffs in the Theory of Unemployment," *Journal of Political Economy* 84 (October 1976), 937-958.

Larry Katz and Bruce Meyer, "The Impact of the Potential Duration of Unemployment Benefits on the Duration of Unemployment," *Journal of Public Economics* 41 (1990), 45-72.

Bruce Meyer, "Unemployment Insurance and Unemployment Spells," *Econometrica* 58 (July 1990), 757-782.

Steven Shavell and Laurence Weiss, "The Optimal Payment of Unemployment Insurance Benefits Over Time," *Journal of Political Economy* 87 (1979), 1347-1362.

Robert Topel, "On Layoffs and Unemployment Insurance," *American Economic Review* 73 (1983), 541-559.

4. Disability Insurance and Workers' Compensation

David Autor and Mark Duggan, "The Rise in the Disability Rolls and the Decline in Unemployment," *Quarterly Journal of Economics* February 2003.

John Bound, "The Health and Earnings of Rejected Disability Insurance Applicants," *American Economic Review* 79 (1989), 482-503.

John Bound, "The Health and Earnings of Rejected Disability Insurance Applicants: Reply," *American Economic Review* 81 (1991), 1427-1434.

Peter Diamond and E. Sheshinski, "Economic Aspects of Optimal Disability Benefits," *Journal of Public Economics* 57 (1995), 1-24.

Mark Duggan, Perry Singleton, and Jae Song, "Aching to Retire? The Rise in the Full Retirement Age and its Impact on the Disability Rolls," *Journal of Public Economics*, (2007).

P. Fishback and S. Kantor, "Did Workers Pay for the Passage of Workers Compensation Laws?" *Quarterly Journal of Economics* 110 (1995), 713-742.

Jon Gruber, "Disability Insurance Benefits and Labor Supply," *Journal of Political Economy* 108 (2000), 1162-1183.

Janice Halpern and Jerry Hausman, "Choice under Uncertainty: A Model of Applications for the Social Security Disability Program," *Journal of Public Economics* 31 (1986), 131-162.

Bruce Meyer, Kip Viscusi, and D. Durbin, "Workers' Compensation and Injury Duration: Evidence from a Natural Experiment," *American Economic Review* 85 (June 1995), 322-340.

Don Parsons, "The Health and Earnings of Rejected Disability Insurance Applicants: Comment," *American Economic Review* 81 (1991), 1419-1426.

Don Parsons, "The Decline of Male Labor Force Participation," *Journal of Political Economy* 88 (February 1980), 117-134.

5. Government Intervention in Health Insurance Markets

5.1 Overview

Ken Arrow, "Uncertainty and the Welfare Economics of Medical Care," *American Economic Review* 53 (1963), 941-973.

David Cutler, "Health Care and the Public Sector," in A. Auerbach and M. Feldstein, eds., *Handbook of Public Economics* Volume 4 (Elsevier, 2002), 2143-2243.

Peter Diamond, "Organizing the Health Insurance Market," *Econometrica* 60 (1992), 1233-1254.

Joseph Newhouse, "Medical Care Costs: How Much Welfare Loss?" *Journal of Economic Perspectives*, 6 (1992), 3-21.

5.2 Health Insurance and Moral Hazard

Martin Feldstein, "The Welfare Loss of Excess Health Insurance," *Journal of Political Economy* 81 (1973), 251-280.

R. Feldman and B. Dowd, "A New Estimate of the Welfare Loss of Excess Health Insurance," *American Economic Review* 81 (1991), 297-301.

Jon Gruber and Jim Poterba, "Taxation and the Demand for Health Insurance: The Case of the Self-Employed," *Quarterly Journal of Economics* 109 (1994), 701-733.

Will Manning, et al, "Health Insurance and the Demand for Medical Care: Evidence from a Randomized Experiment," *American Economic Review* 77 (1987), 251-277.

Mark Pauly, "The Rational Non-Purchase of Long-Term Care Insurance," *Journal of Political Economy* 98 (1990): 153-168.

Mark Pauly, "Taxation, Health Insurance, and Market Failure in the Medical Economy," *Journal of Economic Literature* 24 (1986), 629-675.

5.3 Health Insurance and the Labor Market

Jon Gruber, “The Incidence of Mandated Maternity Benefits,” *American Economic Review* 84 (1994), 622-641.

Brigitte Madrian, “Employment-Based Health Insurance and Job Mobility: Is There Evidence of Job Lock?” *Quarterly Journal of Economics* 109 (1994), 27-54.

Lawrence Summers, “Some Simple Economics of Mandated Benefits,” *AEA Papers and Proceedings* 79 (1989), 177-183.

Aaron Yelowitz, “The Medicaid Notch, Labor Supply, and Welfare Participation: Evidence from Eligibility Expansions,” *Quarterly Journal of Economics* 105 (1995), 909-940.

5.4 Medicaid and the Uninsured

Janet Currie and Jon Gruber, “Saving Babies: The Efficacy and Cost of Recent Changes in the Medicaid Eligibility of Pregnant Women,” *Journal of Political Economy* 104 (1996), 1263-1296.

David Cutler and Jon Gruber, “Does Public Insurance Crowd Out Private Insurance?” *Quarterly Journal of Economics* 111 (1996), 391-430.

Joseph Doyle, “Does Health Insurance Affect Treatment Decisions and Patient Outcomes? Using Automobile Accidents as Unexpected Health Shocks,” *Review of Economics and Statistics*, 2007.

Mark Duggan, “Does Contracting Out Increase the Efficiency of Government Programs? Evidence from Medicaid HMOs,” *Journal of Public Economics* 88 (December, 2004) 2549-2572.

John Ham and Lara Shore-Sheppard, “The Effect of Medicaid Expansions for Low-Income Children on Medicaid Participation and Private Insurance Coverage: Evidence from the SIPP.” *Journal of Public Economics* 89 (2005), 57-83.

5.5 Medicare, Medicaid, and Supplier Issues

David Cutler, “The Incidence of Adverse Medical Outcomes Under Prospective Payment,” *Econometrica* 63 (1995), 29-50.

Leemore Dafny, “How Do Hospitals Respond to Price Changes?” *American Economic Review*, 2006.

David Dranove, Daniel Kessler, Mark McClellan, and Mark Satterthwaite, “Is More Information Better? The Effects of ‘Report Cards’ on Health Care Providers,” *Journal of Political Economy* 111 (2003) 555-588.

Mark Duggan, “Hospital Ownership and Public Medical Spending,” *Quarterly Journal of Economics* 115 (2000), 1343-1374.

Mark Duggan and Fiona Scott-Morton, “The Effect of Health Insurance on Pharmaceutical Pricing: Evidence for the Medicaid Program,” *Quarterly Journal of Economics*. (February 2006), 1-31.

Amy Finkelstein, "Minimum Standards and Insurance Regulation: Evidence from the Medigap Market," *Journal of Public Economics* 88 (December 2004).

Amy Finkelstein, "Static and Dynamic Effects of Health Policy: Evidence from the Vaccine Industry," *Quarterly Journal of Economics* 119 (May 2004) 527-564.

Amy Finkelstein, "The Aggregate Effects of Health Insurance: Evidence from the Introduction of Medicare," 122 (2007), 1-38.

Daniel Kessler and Mark McClellan, "Do Doctors Practice Defensive Medicine?" *Quarterly Journal of Economics* May, 1996.

Albert Ma and Thomas McGuire, "Optimal Health Insurance and Provider Payment," *American Economic Review* 1997, 685-704.

5.6 The Impact of Health Care Treatments

David Cutler, Mark McClellan, Joe Newhouse, Dahlia Remler, "Are Medical Prices Declining?" *Quarterly Journal of Economics* 113 (1998), 991-1024.

Joseph Doyle, "Returns to Local Area Health Care Spending: Using Health Shocks to Patients Far from Home," MIT Sloan School of Management mimeo, 2008.

Mark Duggan, "Does Medicaid Pay Too Much for Prescription Drugs? The Case of Second-Generation Antipsychotics" *Journal of Health Economics* 24:1 (2005), 1-31.

Mark McClellan, Barbara McNeil, and Joseph Newhouse, "Does More Intensive Treatment of Acute Myocardial Infarction Reduce Mortality?" *Journal of the American Medical Association* 859-866, September 1994.

6.1 Public Goods

James Andreoni, "Impure Altruism and Donations to Public Goods: A Theory of Warm-Glow Giving," *The Economic Journal*, 100, 1990, pp. 464-477.

James Andreoni, "An Experimental Test of the Public Goods Crowding Out Hypothesis," *American Economic Review*, December 1993.

James Andreoni, "Towards a Theory of Charitable Fundraising", *Journal of Political Economy*, Vol. 106, No. 6. (Dec., 1998), pp. 1186-1213.

James Andreoni and Abigail Payne, "Do Government Grants to Private Charities Crowd Out Giving or Fundraising?" *American Economic Review* 93(3), June 2003, 792-812.

Theodore Bergstrom, Laurence Blume and Hal Varian, "On the Private Provision of Public Goods," *Journal of Public Economics*, 1986, v 29, 25--49.

Steven T. Berry and Joel Waldfogel, "Public Radio in the United States: Does it Correct Market Failure or Cannibalize Commercial Stations?," *Journal of Public Economics*, v.71, February 1999, 189—211.

Jonathan Gruber and Daniel Hungerman, "Faith Based Charity and Crowdout," *Journal of Public Economics*, 2007.

Bruce Kingma, "An Accurate Measure of the Crowd-out Effect, Income Effect, and Price Effect for Charitable Contributions," *Journal of Political Economy*, October 1989.

Abigail Payne, "Does the Government Crowd-Out Private Donations? New Evidence from a Sample of Non-Profit Firms," *Journal of Public Economics*, v.69 (3), 1998, 323--345.

Paul A. Samuelson, "The Pure Theory of Public Expenditure," *Review of Economics and Statistics*, Nov. 1954, 387-389.

Paul A. Samuelson, "Diagrammatic Exposition of a Theory of Public Expenditures," *Review of Economics and Statistics*, 1955, 350--356.

6.2 Externalities

Daron Acemoglu and Joshua Angrist, "How Large are Human-Capital Externalities? Evidence from Compulsory Schooling Laws" *NBER Macroeconomics Annual* (2000).

Ian Ayres and Steven Levitt, "Measuring Positive Externalities From Unobservable Victim Precaution: An Empirical Analysis of LoJack" *The Quarterly Journal of Economics* (1998), pp. 43-77.

Kenneth Chay and Michael Greenstone, "The Impact of Air Pollution on Infant Mortality: Evidence from Geographic Variation in Pollution Shocks Induced by a Recession" *Quarterly Journal of Economics* 118 (2003), pp. 1121-1167.

Enrico Moretti, "Estimating the Social Return to Higher Education: Evidence from Longitudinal and Repeated Cross-Sectional Data" *Journal of Econometrics* 121 (2004).

Martin Weitzman, "Prices versus Quantities," *Review of Economic Studies* (1974), pp. 477-491.

Willard Manning, Emmett B. Keeler, Joseph P. Newhouse, Elizabeth M. Sloss, and Jeffrey Wasserman, "The Taxes of Sin: Do Smokers and Drinkers Pay Their Way?" *Journal of American Medical Association* 261 (1989), pp. 1604-9.

7. Fiscal Federalism -

Tim Besley and Stephen Coate, "Centralized versus Decentralized Provision of Local Public Goods: A Political Economy Analysis" *Journal of Public Economics* 87 (2003), pp. 2611-2637.

Truman Bewely, "A Critique of Tiebout's Pure Theory of Local Public Expenditures" *Econometrica* 1982, 713-737.

David Bradford and Wallace Oates, "Towards a Predictive Theory of Intergovernmental Grants" *American Economic Review* 6 (1971).

Dennis Epple and Holger Sieg, "Estimating Equilibrium Models of Local Jurisdictions" *Journal of Political Economy* 107 (1999) 645-681.

Nora Gordon, "Do Federal Grants Boost School Spending? Evidence from Title I" *Journal of Public Economics* 88 (2004), 1771-1792.

James Hines and Richard Thaler, "Anomalies: The Flypaper Effect" *Journal of Economic Perspectives* 1995.

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

Robert Moffitt, "The Effects of Grants in Aid on State and Local Expenditures: The Case of AFDC," *Journal of Public Economics* 23 (1984), 279-305.

Thomas Nechyba, "Local Property and State Income Taxes: The Role of Interjurisdictional Competition and Collusion," *Journal of Political Economy* 105 (1997), 351-384.

Wallace Oates, "An Essay on Fiscal Federalism" *Journal of Economic Literature* 37 (1999).

Wallace Oates and Robert Schwab, "Economic Competition among Jurisdictions: Efficiency Enhancing or Distortion-Inducing?" *Journal of Public Economics* (1988), 333-354.

Koleman Strumpf and Felix Oberholzer-Gee, "Endogenous Policy Decentralization: Testing the Central Tenet of Economic Federalism" *Journal of Political Economy* 110 (2002), 1-31.

Charles Tiebout. "A Pure Theory of Local Public Expenditures," *Journal of Political Economy*, 1956, 416-424.

8. Publicly Provided Goods: Education

Eric Hanushek, "Publicly Provided Education," *Handbook of Public Economics* Vol 4 (2002) 2045-2141.

8.1 School Inputs and Educational Attainment

Josh Angrist and Alan Krueger, "Does Compulsory School Attendance Affect Schooling and Earnings?" *Quarterly Journal of Economics* 106 (1991), 979-1014.

David Card and Alan Krueger, "Does School Quality Matter? Returns to Education and the Characteristics of Public Schools in the United States," *Journal of Political Economy* 100 (1992), 1-40.

Esther Duflo, "Schooling and Labor Market Consequences of School Construction in Indonesia: Evidence from an Unusual Policy Experiment," *American Economic Review* 91 (2001), 795-813.

Caroline Hoxby, "How Teachers' Unions Affect Education Production," *Quarterly Journal of Economics* 111 (1996), 671-718.

Brian Jacob and Lars Lefgren, "Remedial Education and Student Achievement: A Regression-Discontinuity Analysis," *Review of Economics and Statistics* 86 (February 2004) 226-244.

8.2 Competition, School Choice, and Vouchers

Joshua Angrist, Eric Bettinger, Erik Bloom, Elizabeth King, Michael Kremer, "Vouchers for Private Schooling in Columbia: Evidence from a Randomized Natural Experiment," *American Economic Review*, December, 2002.

Julie Berry Cullen, Brian Jacob, and Steven Levitt, "The Impact of School Choice on Student Outcomes: An Analysis of the Chicago Public Schools," *Journal of Public Economics* 89 (2005), pp. 729-760.

Dennis Epple and Richard Romano, "Competition between Private and Public Schools, Vouchers, and Peer Group Effects," *American Economic Review* 88 (1998), 33-62.

Scott Imberman, "Achievement and Behavior in Charter Schools: Drawing a More Complete Picture," University of Houston mimeo, 2008.

Brian Jacob, "Public Housing, Housing Vouchers, and Student Achievement: Evidence from Public Housing Demolitions in Chicago," *American Economic Review* 94 (March 2004), 233-258.

8.3 Educational Subsidies

Sue Dynarski, "Does Aid Matter? Measuring the Effect of Student Aid on College Attendance and Completion," *American Economic Review*, (2003), 279-288.

Martin Feldstein, "College Scholarship Rules and Private Saving," *American Economic Review* 85 (1995), 552-566.

Philip Ganderton, "The Effect of Subsidies-in-Kind on the Choice of a College," *Journal of Public Economics* 48 (1992), 269-292.

Rod Garratt and John Marshall, "Public Finance of Private Goods: The Case of College Education," *Journal of Political Economy* 102 (1994), 566-582.

Michael McPherson and Morton Shapiro, "Does Student Aid Affect College Enrollment? New Evidence on a Persistent Controversy," *American Economic Review* 81 (1991), 309-318.

Sam Peltzman, "The Effect of Government Subsidies-in-Kind on Private Expenditures: The Case of Higher Education," *Journal of Political Economy* 81 (1973), 1-27.

Jon Sonstelie, "Welfare Costs of Free Public Schools," *Journal of Political Economy* 90 (1982), 794-808.