



College of Commerce  
Division of Economic and Financial Studies

**UNIT OUTLINE**

**ECON211: TAXATION ECONOMICS AND POLICY**

**Semester 2, 2004**

**Glenn Jones  
Unit convenor**

# **ECON211 TAXATION ECONOMICS AND POLICY**

## **1. ABOUT THIS UNIT**

The course ECON211 Taxation Economics and Policy is a course in theoretical and applied public economics focusing on the analysis of taxation.

The economic foundation for taxation policy is closely related to that underlying expenditure policy but the scale of the literature is such that it is appropriate to treat the two sections of Public Economics in two separate units. The companion unit to ECON211 is ECON210 Public Economics. Both of these units have ECON200 Microeconomic Analysis as a prerequisite.

The course places strong emphasis on developing analytical and theoretical skills as a means of encouraging rigorous and logical thinking about the analysis and design of tax systems.

## **2. TEACHING STAFF**

Glenn Jones (unit convenor)  
Consultation hours: Wednesday 2.00 – 6.00  
Room: C5C 391  
Phone: 9850 8500  
Email: glenn.jones@mq.edu.au

## **3. LECTURES**

The lectures will be given:

Wednesday 10.00 – 12.00      C5A301

During the semester, any changes will be announced as far as possible in advance.

## **4. TUTORIALS**

Two tutorial times have been scheduled:

Wednesday 12.00      E5A116  
Wednesday 14.00      C5A226

The number of tutorials offered each week will depend on enrolment in the unit.

The tutorial program in ECON211 aims to explain and extend some of the material covered in lectures and to allow an opportunity for an in depth discussion of a particular aspect of the course.

The tutorials will not be held every week. There will be eight tutorials in the semester. Tutorials will count towards 10% of the total grade in the unit.

## 5. ASSESSMENT

The components of assessment in this course are as follows:

	%
Mid-semester Test 1	15
Mid-semester Test 2	15
Tutorials	10
Exam	60
Total	100

The two mid-semester tests will be of short answer format. They will each be of one hour's duration and will take place in the tutorial time and room in the weeks indicated in the course diary. The tests will examine the subject matter of the first three lectures and second five lectures respectively

It is a requirement that to pass the unit, students must pass the final examination.

Students are reminded of University rules governing requests for special consideration when illness, misadventure or other cause prevents attendance at tutorials, affects the submission of work or impairs performance in examinations.

Please submit requests for special consideration for within semester assessment directly to the lecturer, not to the Registrar. Requests for special consideration for the final examination must be submitted to the Registrar.

## 6. UNIT WEB PAGE:

*<http://www.econ.mq.edu.au/courses/econ211/index.htm>*

## 7. COURSE DIARY 2004

<b>WEEK</b>	<b>DATE</b>	<b>LECTURE TOPIC</b>	<b>TUTORIAL</b>
1	August 4	Introduction	
2	August 11	Tax incidence	<b>Tutorial 1</b>
3	August 18	Labour supply & saving with taxation	<b>Tutorial 2</b>
4	August 25	Measuring welfare effects of taxation	<b>Test 1</b>
5	September 1	Normative analysis and social welfare	<b>Tutorial 3</b>
6	September 8	Inequality and poverty	<b>Tutorial 4</b>
7	September 15	Taxation and welfare programs	<b>Tutorial 5</b>
<b>MID SEMESTER BREAK</b>			
8	October 6	Optimal income taxation	
9	October 13	Optimal commodity taxation	<b>Test 2</b>
10	October 20	Taxation of income or expenditure: saving and social insurance	<b>Tutorial 6</b>
11	October 27	Income tax extensions : capital taxation, risk and tax evasion	<b>Tutorial 7</b>
12	November 3	Corporation tax	<b>Tutorial 8</b>
13	November 10	Fiscal federalism	

## 7. TEXT AND REFERENCES

The recommended text, ordered at the bookshop is:

**Abelson, P.W. (2002) *Lectures in Public Economics*, (3<sup>rd</sup> Ed) Sydney, Applied Economics**

However there are other texts covering similar material and references to these texts will be given where appropriate:

**Stiglitz, J.E. (2000) *Economics of the Public Sector*, (3<sup>rd</sup> Ed) New York, Norton.**

**Rosen, H.S., (2002) *Public Finance*, (6<sup>th</sup> Ed) New York, McGraw-Hill**

Texts dealing with the subject at a greater level of detail are:

Atkinson, A.B. and J.E. Stiglitz (1980) *Lectures in Public Economics*, New York, McGraw-Hill

Brown, C.V. and P.M. Jackson (1986) *Public Sector Economics*, Oxford, Basil Blackwell.

Hillman, A.L., (2003), *Public Finance and Public Policy*. Cambridge, Cambridge University Press.

Jha, R. (1998) *Modern Public Economics*. London, Routledge.

Myles, G. D. (1995) *Public Economics*, Cambridge, Cambridge University Press.

Tresch, R. W. (2002) *Public Finance: a normative theory*, (2<sup>nd</sup> Ed), San Diego, Elsevier, Academic Press

A useful but difficult to find text is:

Boadway, R.W. and D.E. Wildasin (1984) *Public Sector Economics*, Toronto, Little, Brown.

## **8. LECTURE OUTLINE**

### **Lecture 1 Introduction**

Scope and framework of public economics  
Institutional description of the Australian tax system  
Revision of assumed microeconomics  
    Optimisation with taxes  
    Income and substitution effects  
    Extension: Slutsky equation

*Abelson: Chapter 1*  
*Stiglitz: Chapter 17*  
*Stiglitz: Chapter 19, pp 518 - 521*  
*Rosen: appendix p 507*  
*Brown and Jackson: Chapter 1*

### **Lecture 2 Tax incidence**

Basic competitive tax incidence  
    Unit and ad valorem taxes  
Shifting taxes to factors  
    Marshall's rules  
Non- competitive tax incidence

*Abelson: Chapter 19*  
*Stiglitz: Chapter 18*  
*Rosen: Chapter 12*  
*Brown: and Jackson Chapters 10 and 11*

### **Lecture 3 Labour supply and savings with taxes**

Labour supply  
    Budget constraint with income taxes  
    Laffer curve and revenue  
Inter-temporal consumption  
Tax equivalence  
    Consumption taxes  
    Labour income taxes  
    Expenditure taxes  
    Income taxes

*Abelson: Chapter 19*  
*Stiglitz: Chapter 19, pp 535 - 547*  
*Stiglitz: Chapter 25, p 699*  
*Stiglitz: Chapter 19, pp 532 - 534*  
*Stiglitz: Chapter 18 pp 502 - 505*  
*Rosen: Chapter 16*  
*Brown and Jackson: Chapter 10*  
*Atkinson & Stiglitz: Chapters 2 and 3 pp 62 - 85*

## **Lecture 4 Measuring welfare effects of taxation**

Compensated demand functions  
Measures of Welfare Change  
    Laspeyres  
    Equivalent gain  
    Weighted or Unweighted Aggregation  
Efficiency  
    Excess Burden (Dead Weight Loss or Efficiency Cost)  
    Revenue neutrality  
    Lump sum comparisons  
Extension :Duality  
    Indirect utility function  
    Expenditure function  
    Marginal utility of income

*Abelson: Chapters 6 and 20*

*Stiglitz: Chapter 5, pp 107 - 112*

*Stiglitz: Chapter 19, pp 521 - 532*

*Rosen: Chapter 13*

*Moffit, R (1992), Incentive effects of the US welfare system: a review. Journal of Economic Literature, 31, 1-61*

## **Lecture 5 Normative analysis and social welfare**

Interpersonal welfare comparisons  
Measures of Welfare Level  
    Preferences and utility functions  
    Measured money income  
    Endowments: full and potential income  
    Equivalent Income  
Data and Measurement problems  
Efficiency  
Pareto Improvements and Potential Pareto Improvements  
First Theorem of Welfare Economics  
Social welfare functions  
Second Theorem of Welfare Economics  
Theory of Second Best  
Fallacy of counting distortions

*Abelson: Chapters 3, 6 and 23*

*Stiglitz: Chapter 3*

*Stiglitz: Chapter 5*

*Stiglitz: Chapter 17, pp 468 - 479*

*Rosen: Chapter 3*

*Atkinson and Stiglitz: Chapter. 11*

*Brown and Jackson: Chapters 1, 12 and 13, pp 297 – 299*

King, M. A., (1983) *Welfare Analysis of Tax Reforms Using Household Data*,  
*Journal of Public Economics*, 21, 183 - 214.

### **Lecture 6 Inequality and poverty.**

Welfare measurement

Vertical equity

Inequality

Decile analysis

Lorenz curve

Gini coefficient

Atkinson/Kolm measure

Poverty

Absolute/relative

Poverty line

Headcount ratio

Horizontal equity

Spearman rank correlation

King measure

Equivalence scales

*Abelson: Chapters 23*

*Stiglitz: Chapter 20, pp 550 - 562*

*Rosen: Chapter 9, Chapter 17 and 16, pp 363 – 366.*

*Brown and Jackson: Chapters 14, 15, pp 318 - 319*

*Australian Bureau of Statistics, (2001), Income Distribution Australia, 1999 – 2000, Cat No 6523.0, AGPS Canberra*

### **Lecture 7 Income Taxation and welfare programs.**

Direct and indirect taxes

Progressive, proportional and regressive taxes

Taxation and labour supply

Participation

Means testing benefits

Tax unit Individual or Household

Effective marginal tax rates

*Abelson: Chapters 24 and 26*

*Stiglitz: Chapter 15*

*Rosen Chapters 8 and 15*

*Whiteford, P. and G. Angenent, (2002), The Australian system of social protection – an overview, Occasional Paper NO 6, Dept Family and Community Services Canberra.*



## **Lecture 8 Optimal income taxation.**

Simple linear income tax  
Non-linear possibilities  
Empirical estimates

*Abelson: Chapter 21*  
*Stiglitz: Chapter 20, pp 550 – 562.*  
*Rosen: Chapter 14*  
*Brown and Jackson: Chapter 20.*  
*Atkinson and Stiglitz: Chapters 13 and 14.*

*Dixit, A.K and A. Sandmo, 1977, Some Simplified Formulae for Optimal Income Taxation, Scandinavian Journal of Economics, 79, 417-423*

*Stern, N H., 1976, On the Specification of Models of Optimal Income Taxation, Journal of Public Economics, 6, 123 – 162*

*Stern, N.H. (1987), The theory of optimal commodity and income taxation: an introduction, in D. Newbery, and N. Stern, eds, The theory of Taxation for Developing Countries, Oxford, Oxford University Press, 22 – 59.*

## **Lecture 9 Optimal Commodity Taxation**

Identical individuals: efficiency  
Ramsey Rule  
Corlette and Hague  
Different individuals: efficiency and equity  
User charges as commodity taxes  
Empirical estimates and policy implications

*Abelson: Chapter 21*  
*Stiglitz: Chapter 20, pp 562 - 576*  
*Rosen: Chapter 14*  
*Atkinson and Stiglitz: Chapter 12*

*Sandmo, A., 1976, Optimal Taxation. an introduction to the literature, Journal of Public Economics, 6, 37-54*

*Deaton, A.S., 1977, Equity, Efficiency and the Structure of Indirect Taxation, Journal of Public Economics 87 299-312*

## **Lecture 10 Taxation of income or expenditure: saving and social insurance**

Direct-indirect tax mix  
Simple two period model  
Extensions to multi-period setting  
Savings and social insurance  
Empirical sensitivity

*Abelson: Chapter 26*  
*Stiglitz: Chapter 14*  
*Rosen: Chapter 9*

*King M A., 1980, Taxation and Savings, in Hughes. G.A. and G.M. Heal (eds),  
Public Policy and the Tax System, George Allen and Unwin.*

### **Lecture 11 Income tax extensions: capital taxation, risk and evasion**

Capital taxation  
Risk taking  
Administration costs  
Tax evasion

*Stiglitz: Chapter 21*  
*Rosen Chapter 14*  
*Atkinson and Stiglitz: Chapter 4*  
*Brown and Jackson: Chapter 14, p 343*

### **Lecture 12 Corporation Tax**

Reasons for corporations tax  
Corporate profits  
Types of corporate tax  
Depreciation  
Cost of capital  
Incidence  
Harberger model  
Efficiency

*Stiglitz: Chapter 23*  
*Rosen: Chapter 17*  
*Brown and Jackson: Chapter 18*

### **Lecture 13 Fiscal federalism**

Local public goods  
Externalities  
Tiebout model  
Equity between regions  
Property taxes  
Capitalization  
Grants in aid

*Abelson: Chapter 27*  
*Stiglitz: Chapters 26 and 27*  
*Rosen: Chapter 20*  
*Brown and Jackson: Chapter 9*  
*Atkinson and Stiglitz: Chapter 5*

*Garnaut, R and V Fitzgerald, 2002, Review of Commonwealth-State Funding, Treasuries of NSW, Victoria and Western Australia*

## **EXAMINATIONS**

The University Examination period in Second Half Year 2004 is from 17/11/2004 to 1/12/2004.

You are expected to present yourself for examination at the time and place designated in the University Examination Timetable. The timetable will be available in Draft form approximately eight weeks before the commencement of the examinations and in Final form approximately four weeks before the commencement of the examinations.

<http://www.timetables.mq.edu.au/exam>

The only exception to not sitting an examination at the designated time is because of documented illness or unavoidable disruption. In these circumstances you may wish to consider applying for Special Consideration. Information about unavoidable disruption and the special consideration process is available at <http://www.reg.mq.edu.au/Forms/APSCon.pdf>

If a Supplementary Examination is granted as a result of the Special Consideration process the examination will be scheduled after the conclusion of the official examination period. (Individual Divisions may wish to signal when the Division's Supplementaries are normally scheduled.)

You are advised that it is Macquarie University policy not to set early examinations for individuals or groups of students. All students are expected to ensure that they are available until the end of the teaching semester, that is the final day of the official examination period.

## **PLAGIARISM**

The University defines plagiarism in its rules: "Plagiarism involves using the work of another person and presenting it as one's own." Plagiarism is a serious breach of the University's rules and carries significant penalties. You must read the University's practices and procedures on plagiarism. These can be found in the Handbook of Undergraduate Studies or on the web at: <http://www.student.mq.edu.au/plagiarism/>

The policies and procedures explain what plagiarism is, how to avoid it, the procedures that will be taken in cases of suspected plagiarism, and the penalties if you are found guilty. Penalties may include a deduction of marks, failure in the unit, and/or referral to the University Discipline Committee.

## **UNIVERSITY POLICY ON GRADING**

Academic Senate has a set of guidelines on the distribution of grades across the range from fail to high distinction. Your final result will include one of these grades plus a standardised numerical grade (SNG).

On occasion your raw mark for a unit (i.e., the total of your marks for each assessment item) may not be the same as the SNG which you receive. Under the Senate guidelines, results may be scaled to ensure that there is a degree of comparability across the university, so that units with the same past performances of their students should achieve similar results.

It is important that you realise that the policy does not require that a minimum number of students are to be failed in any unit. In fact it does something like the opposite, in requiring examiners to explain their actions if more than 20% of students fail in a unit.

The process of scaling does not change the order of marks among students. A student who receives a higher raw mark than another will also receive a higher final scaled mark. An exception to this rule may occur (though it is unlikely) in the grading of units with a requirement that students are required to pass a specific component of the unit, such as the final exam.

For an explanation of the policy see  
<http://www.mq.edu.au/senate/MQUonly/Issues/Guidelines2003.doc> or  
<http://www.mq.edu.au/senate/MQUonly/Issues/detailedguidelines.doc>.

## **STUDENT SUPPORT SERVICES**

Macquarie University provides a range of Academic Student Support Services. Details of these services can accessed at  
<http://www.student.mq.edu.au>.