



College of Commerce
Division of Economic and Financial Studies

UNIT OUTLINE

ECON211: TAXATION ECONOMICS AND POLICY

Semester 2, 2005

**Glenn Jones
Unit convenor**

ECON211 TAXATION ECONOMICS AND POLICY

1. ABOUT THIS UNIT

This is a course in applied public economics. It uses microeconomics to analyse features of tax and social security systems, as well as proposed directions for reform.

The course will integrate the analysis of efficiency costs of taxes and benefits with the assessment of both vertical and horizontal equity. It will examine methods of interpersonal welfare comparison. A feature of the course will be an emphasis on data and measurement.

Topics covered include: an introduction to the tax and social security systems of Australia and other countries; basic theory of incidence; general equilibrium effects of taxes; tax equivalence; the impact of tax and social security on labour supply and savings; optimal income and commodity taxation; optimal mix of taxation; the importance of the unit for the design of taxes and means testing benefits; capital taxation; the effect of taxes on risk taking; tax evasion; company taxation; fiscal federalism.

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. It does not however require detailed econometrics nor high level mathematics.

Unit goals

After completing the unit students should:

- be familiar with the range of tax and social security instruments used in Australia and other countries.
- be able to describe the main methods by which tax policy is administered at the federal, state and local levels.
- be familiar with the empirical magnitudes of important issues in the literature
- be able to assess the efficiency impacts of policy changes.
- be able to assess the equity impacts of policy changes.
- be familiar with the policy implications of tax theory.
- be familiar with the major sources of data on taxation.

Generic skills

The unit will aim to develop generic skills including:

- literacy, numeracy
- team work and efficient collaboration
- effective presentation of knowledge and thought
- critical analysis involving evaluation, synthesis and judgement
- problem-solving skills
- identification of incentives and constraints as a common framework for apparently unrelated problems.

All of these skills will be enhanced by the lecture and tutorials, which deal specifically with public economics and which present material central to a contemporary understanding of the socio-economic environment.

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 E5A118

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

Copies of the lecture overheads will be available on the unit web page on the Monday before the Wednesday lecture

4. TUTORIALS

Two tutorial times have been scheduled:

Wednesday 12.00 E5A116
Wednesday 14.00 W5C302

Expected enrolment in this unit suggests that only 1 tutorial will be necessary and this will be held at 12.00 immediately following the lecture.

The tutorials will not be held every week. There will be eight tutorials in the semester. Tutorials will count towards 20% of the total grade 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.

5. ASSESSMENT

The components of assessment in this course are as follows:

	%
Mid-semester Test 1	10
Mid-semester Test 2	10
Tutorials	20
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.

The tutorial component will be comprised of two marks. 10% will be awarded for tutorial exercises and 10% for class participation. Tutorial exercises will not be marked unless the student attends the tutorial or has submitted a valid claim for special consideration.

The final examination will be of two hours duration and will require students to answer a choice of four essay style questions from a total of eight questions.

Examples of past mid-semester tests and final examination papers can be found on the unit web page.

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 unit convenor, 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>

Students are encouraged to use the discussion facilities available through the web page and to contact the unit convenor in person, by email or phone.

While all matters affecting the unit will be posted on the web page, direct email contact is a convenient way for the convenor to contact students concerning unforeseen changes to lectures or tutorials at short notice. To facilitate this contact students are requested to email the convenor during the first week of lectures so that the often incomplete record of student contact emails may be verified.

7. COURSE DIARY 2005

WEEK	DATE	LECTURE TOPIC	TUTORIAL
1	August 3	Introduction	
2	August 10	Tax incidence	Tutorial 1
3	August 17	Labour supply & saving with taxation	Tutorial 2
4	August 24	Measuring welfare effects of taxation	Test 1
5	August 31	Normative analysis and social welfare	Tutorial 3
6	September 7	Inequality and poverty	Tutorial 4
7	September 14	Taxation and welfare programs	Tutorial 5
MID SEMESTER BREAK			
8	October 5	Optimal income taxation	Tutorial 6
9	October 12	Optimal commodity taxation	Test 2
10	October 19	Taxation of income or expenditure: saving and social insurance	
11	October 26	Income tax extensions : capital taxation, risk and tax evasion	Tutorial 7
12	November 2	Corporation tax	
13	November 9	Fiscal federalism	Tutorial 8

7. TEXT AND REFERENCES

The recommended text, ordered at the bookshop is:

Abelson, P.W. (2002) Lectures in Public Economics, (3rd 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*, (3rd Ed) New York, Norton.

Rosen, H.S., (2002) *Public Finance*, (6th 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*, (2nd 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 2005 is from 16/11/2005 to 2/12/2005.

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>.