EHEHEHEHEHEHEHEHEHEHEHEHEHEHEHEHE

HANDBOOK OF PUBLIC ECONOMICS

VOLUME II

Edited by

ALAN J. AUERBACH University of Pennsylvania

and

MARTIN FELDSTEIN

Harvard University





NORTH-HOLLAND AMSTERDAM · NEW YORK · OXFORD · TOKYO

CONTENTS OF THE HANDBOOK

VOLUME I

Editors' Introduction

Chapter J

A Brief History of Fiscal Doctrine R.A. MUSGRAVE

Chapter 2

The Theory of Excess Burden and Optimal Taxation ALAN J. AUERBACH

Chapter 3

Public Sector Pricing DIETER BÖS

Chapter 4

Taxes and Labor Supply JERRY A. HAUSMAN

Chapter 5

The Effects of Taxation on Savings and Risk Taking AGNAR SANDMO

Chapter 6

Tax Policy in Open Economies AVINASH DIXIT

Chapter 7

Housing Subsidies: Effects on Housing Decisions, Efficiency, and Equity HARVEY S. ROSEN

Chapter 8

The Taxation of Natural Resources TERRY HEAPS and JOHN F. HELLIWELL

VOLUME II

Chapter 9

Theory of Public Goods WILLIAM H. OAKLAND

Chapter 10

Incentives and the Allocation of Public Goods JEAN-JACQUES LAFFONT

Chapter 11

The Economics of the Local Public Sector DANIEL RUBINFELD

Chapter 12

Markets, Government, and the "New" Political Economy ROBERT INMAN

Chapter 13

Income Maintenance and Social Insurance ANTHONY B. ATKINSON

Chapter 14

The Theory of Cost-Benefit Analysis JEAN DREZE and NICHOLAS STERN

Chapter 15

Pareto Efficient and Optimal Taxation and the New New Welfare Economics JOSEPH STIGLITZ

Chapter 16

Tax Incidence LAURENCE KOTLIKOFF and LAWRENCE SUMMERS



CONTENTS OF VOLUME II

Introdu	action to the Series	v
Conter	ats of the Handbook	vii
Editors	"Introduction	xv
Chapter Theory	of Public Goods	
WILLIA	M H. OAKLAND	485
1.	Introduction	485
2.	Pure public goods	486
3.	Generalizations	491
	3.1. Negative benefits	492
	3.2. Public intermediate goods	493
	3.3. Distortionary taxation	495
	3.4. Externalities	496
	3.5. Congestion	499
	3.6. Club goods and local public goods	502
4.	Private provision of public goods	509
	4.1. No exclusion, small number of participants	509
	4.2. No exclusion, large number of participants	514
	4.3. Exclusion possible, large number of participants	515
	4.4. Exclusion possible, single seller	518
5.	Public sector provision of public goods	522
	5.1. Pigouvian taxes and subsidies	522
	5.2. Information	524
	5.3. Behavior of public officials	530
6.	Directions for further research	533
Re	ferences	533
Chapter		
	ves and the Allocation of Public Goods	
JEAN-J	ACQUES LAFFONT	537
1.	Introduction	537
2.	Implementation	538
	2.1. Dominant equilibrium: $c = d$	540
	2.2. Bayesian-Nash equilibrium	540
	2.3. Maximin equilibrium: $c = m$	541

Contents	of	Vol	ume	I.
----------	----	-----	-----	----

x	Con	tents of Volume I
	2.4. Nash equilibrium: $c \equiv n$	541
	2.5. Local dominant equilibrium	543
3.	The Gibbard-Satterthwaite theorem	545
4.	Public goods only; positional dictators	550
5.	The differential approach	551
6.	The Clarke-Groves-Vickrey mechanisms	554
7.	Weakening incentives requirements	559
8.	Planning procedures	561
,	8.1. Local dominant equilibrium	561
	8.2. Local maximin equilibrium	566
9.	Conclusion	567
Re	ferences	567
Chapter	11	
	conomics of the Local Public Sector	
DANIE	L L. RUBINFELD	571
1.	Introduction	571
2.	Community formation and group choice	574
۷.		57 6
	5.	580
3.	2.2. Optimum club size with congestion The Tiebout model	581
٥.		581
	3	583
	3.2. The property tax3.3. Production inefficiencies in the Tiebout model	585
	3.4. Will an equilibrium exist?	587
	3.4. Will all equitional exist?3.5. Capitalization of public spending and taxes in a Tiebout framework	591
	3.6. The efficiency of the Tiebout model with gapitalization	597
	3.7. Testing the Tiebout model	598
4.	Empirical determination of the demand for local public goo	
٦.	4.1. Introduction	601
	4.2. Empirical issues	606
	4.3. Some additional empirical issues	609
	4.4. Estimating demand functions in a Tiebout world	612
5.	Applications of the demand approach	614
٦.	5.1. Alternative methods for estimating the demand for local public good	
	5.2. Will the median level of services provided be efficient?	622
6.	Fiscal federalism	625
0.	6.1. The responsibilities of local government	625
	6.2. The role of grants in a federalist system	634
7.	Conclusions	637
	ferences	639
Ve	iciciecs	035

Contents of Volume II xi

Che	apter	12	
	•	ts, Governments, and the "New" Political Economy	
		T P. INMAN	647
	1.	Introduction	647
	2.	Market failures and the role of government	649
		2.1. The minimal role of government	650
		2.2. Beyond the minimal state: When markets fail	653
		2.3. Market failures as a Prisoner's Dilemma: The potential case for government	663
	-	2.4. Summary	672
	3.	The search for efficient government	672
		3.1. Collective action as voluntary exchange	674
		3.2. Coercive mechanisms of collective choice: Democracy vs. efficiency	681
		3.3. Dictatorial processes: The dictator as a benevolent planner	692
		3.4. Democratic processes	703
		3.5. Summary	738
	4.	Public policies for the public sector	739
		4.1. On designing policies for government reform	740
		4.2. An example: Constitutional limitations for government efficiency	743
		4.3. Summary	753
	5.	Conclusion: Drawing the borderline between markets	
		and governments	753
	Ad	ldendum	765
	Re	ferences	769
	apter		
lno	com	e Maintenance and Social Insurance	
A.F	3. AT	KINSON A	779
	1.	Introduction	779
	2.	Objectives	785
		2.1. Income support and the abolition of poverty	785
		2.2. Measurement of poverty	789
		2.3. Welfare economics and social welfare functions	791
		2.4. Concluding comment	795
+	3.	The design of state income maintenance	795
		3.1. A simple model	795
		3.2. Income support – individualistic preferences	799
		3.3. Ethical preferences	803
		3.4. Social insurance and intertemporal allocation	807
		3.5. The form of income support	811
		3.6. Concluding comment	815
		e e e e e e e e e e e e e e e e e e e	

xii Contents of Volume II

4.	The impact in practice	815
	4.1. Complex budget constraints	815
	4.2. Non-receipt of benefits	820
	4.3. Benefits, taxes, and poverty	822
	4.4. Overall redistributive effect	826
	4.5. Political economy of income support	829
	4.6. Concluding comment	833
5.	Effects on economic behaviour	833
	5.1. Income support and its effect on retirement decisions	834
	5.2. Disability benefits and participation	847
	5.3. Unemployment insurance and work decisions	851
	5.4. The take-up of welfare/public assistance	865
	5.5. Income support and family formation	868
	5.6. Pensions and savings	869
	5.7. Concluding comments	880
6.	Reforms and simulation of their implications	880
	6.1. Specification of effects of reforms and hypothetical examples	881
	6.2. Modelling using representative samples	883
	6.3. Incorporation of changes in behaviour	884
	6.4. General equilibrium effects	887
7.	Envoi	889
Re	ferences	889
Chapter	14	
-	heory of Cost-Benefit Analysis	
	DRÈZE AND NICHOLAS STERN	909
1.	Basic principles	909
	1.1. Introduction	909
	1.2. Project evaluation, cost-benefit analysis, and shadow prices	910
	1.3. The basic theory of shadow prices	912
	1.4. Shadow prices and optimal public production	916
_	1.5. Cost-benefit analysis and the theory of reform	918
2.	Lessons from second-best theory	920
	2.1. The model	921
	2.2. General properties of the model	926
	2.3. Some important second-best theorems	937
	2.4. Shadow prices in distorted economies	945
-	2.5. Conclusion	953
3.	Selected applications of the theory	954
	3.1. Introduction	954
	3.2. The distribution of welfare	955
	3.3. Traded and non-traded goods	961

Contents	of Volume II	xiii
	3.4. Shadow wages	964
	3.5. Numeraires, discount rates, and foreign exchange	967
	3.6. Private projects and Boiteux firms	976
	3.7. Uncertainty and time	977
	3.8. Some neglected issues	980
4.	Summary and conclusions	982
	ferences	985
Chapter		
	Efficient and Optimal Taxation and the New New Welfare Ec	
JOSEPH	E. STIGLITZ	991
1.	Introduction	991
	Part I: One-commodity neoclassical models	993
2.	The basic model	993
	2.1. Optimal lump-sum taxes	994
	2.2. Imperfect information	996
	2.3. Implementing the optimal allocations by means of a tax structure	1002
	2.4. The optimal tax structure with $\lambda_2 > 0$, $\lambda_1 = 0$	1003
	2.5. The optimal tax structure with $\lambda_1 > 0$, $\lambda_2 > 0$	1005
	2.6. Equity-efficiency trade-offs	1006
3.	Continuum of individuals	1006
4.	Some mathematical problems	1008
	4.1. Non-differentiability	1009
	4.2. Discontinuities	1011
5.	Generalizations: Random taxation	1011
6.	Limitations: Restricted taxation	1014
7.	Limitations: The push-pin versus poetry controversy	1017
8.	Limitations: General equilibrium effects of taxation	1019
9.	Other limitations on the general model	1021
10.	Numerical calculations	1022
	Part II: Pareto efficient taxation with many commodities and	
	many periods	1023
11.	Alternative tax bases	1023
	11.1. Formal analysis	1024
	11.2. Ramsey versus Atkinson-Stiglitz Pareto efficient taxation	1026
	11.3. Redistributive commodity taxes with optimal linear income taxes	1027
	11.4. Other forms of restricted taxation	1029
12.	Implications for capital taxation	1030
	12.1. Overlapping generations models	1031
	12.2. Infinitely lived individuals	1032
13.	Imperfect capital markets	1034
14.	Altruism and inheritance taxation	1034
15.	Commitment	1035

1095

16. 17. Re	- F	1036 1036 1037 1039
		1037
Chapte		
	ncidence	1040
LAUR	ENCE J. KOTLIKOFF AND LAWRENCE H. SUMMERS	1043
0.	Introduction	1043
1.	Preliminaries	1045
	1.1. The partial equilibrium analysis of tax incidence	1045
	1.2. Methodological issues	1047
	1.3. Empirical incidence evaluations	1049
2.	Static general equilibrium models of tax incidence	1050
	2.1. Tax incidence in a one-sector general equilibrium model	1050
	2.2. Tax incidence in a two-sector general equilibrium model	1054
	2.3. Estimate of tax incidence in static general equilibrium models	1063
3.	Tax incidence in open economies	1065
	3.1. A simple model of factor mobility	1065
	3.2. Further implications of the simple open economy model	1067
	3.3. Incidence of the property tax	1068
4.		1070
	4.1. Tax incidence in a life-cycle, overlapping generations model	1071
	4.2. Income effects with intergenerational altruism and the possible neutrality	
	of intergeneration transfers	1078
	4.3. Transition effects	1079
	4.4. Asset prices and tax incidence	1082
5.	Conclusion	1088
R	eferences	1088
Corri	gendum	1093
Index		1095