

**Economics 51 -- Tax Policy in Emerging Markets**  
January 2009 [Revised]

Class meets: 10:30 weekdays  
CDE Classroom  
Office hours: 2:30-4 Tu, Th

Professor Jon Bakija  
Office: SAB 330  
email: [jbakija@williams.edu](mailto:jbakija@williams.edu)  
Office phone: 597-2325

Course Description

Governments in developing and transition economies need to raise tax revenue to finance critical public goods, address other market failures and equity issues, and to avoid problems with debt and inflation. Even under ideal conditions, figuring out how to raise taxes in a way that balances efficiency, equity, and administrative feasibility is a hard problem. But taxation is especially challenging in emerging markets, because of the great difficulty involved in taxing much of the economic activity there, serious problems with tax evasion and administration, and the various imperfections in the economic environment in which taxes are collected. Taxes typically consume between a fifth and a third of the proceeds of economic activity in these nations, and they profoundly affect the incentives to undertake all varieties of economic activity. So in terms of economic growth and welfare, the stakes involved in improving tax policy are potentially quite large. This class will build on knowledge developed in the basic public economics course to provide a more in-depth investigation of the special problems involved in tax policy in developing and transition economies, and possible approaches to addressing these problems.

Course Schedule

The course will meet at 10:30AM each weekday from Tuesday January 6<sup>th</sup> through Wednesday January 28<sup>th</sup>. Each class will typically be about 90 minutes.

Course Requirements

Winter Study classes are intended to be a little less formal and lower-stress than regular semester classes, and on average the grades awarded tend to be high. My main expectation of you is that I want you to be conscientious about doing the reading in advance of each class, and to contribute constructively to the classroom discussion on each topic. This is a small class, which should make it easier to get some good discussions going and have an interactive class. Your grade will be based on the following factors:

1. Class participation. You must participate in class, which requires doing the reading carefully in advance of the class, and especially being prepared to answer any discussion questions that I pose about the readings. I will feel free to call on particular students to ask questions about the reading, and will keep track of how well people are answering the questions. Class participation will account for 30 percent of your grade.
2. Homework. There will be several short homework assignments, with questions similar to the type you were assigned in Econ 503 – for instance, problems that ask you to do some calculations that help illustrate some principle, or short essay-type questions that ask you to respond to some statement or question about what we've learned in class. These will account for 40 percent of your grade.
3. Short End-of-Term Paper. There will be a relatively short writing assignment due on the last day of class (Wednesday January 28<sup>th</sup>) that will ask you to synthesize some lessons and policy recommendations from various things we learned during the semester. Further details on this assignment will be provided soon. This will account for 30 percent of your grade.

#### Course Materials

All readings except those from Gruber's *Public Finance and Public Policy* textbook will be posted electronically on Blackboard. If you are interested in also getting a printed course packet (which you would have to pay for), let me know and I will arrange to get some made.

Topic and Readings	Date
<p><b>1. How Income Taxation Works</b></p> <p><b>[Required]</b> Slemrod, Joel, and Jon Bakija. 2008. "Personal Income Taxation" and "Basic Features of the U.S. Corporate Income Tax," excerpted from <i>Taxing Ourselves</i>, 4th ed., Cambridge: MIT Press, pp. 28-37, 40-44, 47-52.</p>	Tue Jan 6
<p><b>2. How Income Taxation Works in a Developing Country</b></p> <p><b>[Required]</b> Alm, James and Sally Wallace. 2006. "Can Developing Countries Impose an Individual Income Tax?" in <i>The Challenges of Tax Reform in a Global Economy</i>, James Alm, Jorge Martinez-Vazquez, and Mark Rider, eds., Springer, 2006, pp. 221-248.</p>	Wed Jan 7
<p><b>3. How the Value-Added Tax Works</b></p> <p><b>[Required]</b> Ebrill, Liam, Michael Keen, Jean-Paul Bodin, and Victoria Summers. 2002. "The Allure of the Value-Added Tax" <i>Finance and Development</i>, June.</p> <p><b>[Required]</b> Gruber, Ch. 25, "Value-Added Tax" (pp. 747-748 in 2nd ed., pp. 711-712 in 1st ed.)</p> <p><b>[Required]</b> Bird, Richard M., and Pierre-Pascal Gendron. 2007. "Is VAT Always the Answer?" Ch. 3 from <i>The VAT in Developing and Transitional Countries</i>. Cambridge and New York: Cambridge University Press, pp. 108-137.</p>	Thu Jan 8
<p><b>4. Value-Added Tax Design and Administration: Details</b></p> <p>Bird, Richard M., and Pierre-Pascal Gendron. 2007. "Key Issues in VAT Design," "Administering the VAT," and "Dealing with Difficulties." Chs. 7, 9, and 10 from <i>The VAT in Developing and Transitional Countries</i>. Cambridge and New York: Cambridge University Press, pp. 109-137, 161-192. <b>[Chapter 7 is required, Chapters 9 and 10 are optional]</b></p>	Fri Jan 9

<p><b>5. Consumption Taxes vs. Income Taxes: A Comparative Analysis</b></p> <p><b>[Required]</b> Gruber, "Background: Present Discounted Value" (Ch. 4, pp. 102-103 in 2<sup>nd</sup> edition, p. 98 in 1<sup>st</sup> edition).</p> <p><b>[Required]</b> Gruber, "Fairer Treatment of Savers and Less Distortion to Savings Decision" (in Ch. 25, pp. 742-743 in 2<sup>nd</sup> ed., pp. 707-708 in 1<sup>st</sup> ed.)</p> <p><b>[Required]</b> Slemrod, Joel, and Jon Bakija. 2008. "A Consumption Base." Excerpted from <i>Taxing Ourselves</i>, 4<sup>th</sup> ed., Cambridge: MIT Press, pp. 194-216.</p> <p><b>[Required]</b> Graetz, Michael and Deborah Schenk. 2005. "Introduction to Income Tax Terminology" and "Note on Depreciation," excerpted from pp. 22-24 and pp. 329-332 of <i>Federal Income Taxation: Principles and Policies</i>, 5<sup>th</sup> ed. New York: Foundation Press.</p>	<p>Mon Jan 12</p>
<p><b>6. Innovative Consumption Tax Designs</b></p> <p><b>[Required]</b> Slemrod, Joel, and Jon Bakija. 2008. "How the Hall-Rabushka Flat Tax and X-Tax Work" excerpted from <i>Taxing Ourselves</i>, 4<sup>th</sup> ed., Cambridge: MIT Press, pp. 235-239.</p> <p><b>[Optional]</b> Bradford, David. 2005. "A Tax System for the 21<sup>st</sup> Century." in Alan Auerbach and Kevin Hassett, eds., <i>Toward Fundamental Tax Reform</i>. Washington: AEI Press. (Excerpt, pp. 11-24)</p> <p><b>[Required]</b> Keen, Michael, and King, John. 2002. "The Croatian Profit Tax: An ACE in Practice." <i>Fiscal Studies</i>, September 2002, v. 23, iss. 3, pp. 401-18.</p>	<p>Tue Jan 13</p>

<p><b>7. International Taxation: Introduction</b></p> <p><b>[Required]</b> Gruber, Ch. 24, "Treatment of International Corporate Income" (pp. 717-721 in 2nd ed., pp. 683-686 in 1st ed.)</p> <p><b>[Required]</b> Hines, Jim. 1999. "International Taxation for Beginners," [excerpted from pp. 306-308 of "Lessons from Behavioral Responses to International Taxation," <i>National Tax Journal</i>, v. 52, iss. 2, pp. 305-22.]</p> <p><b>[Required]</b> Sorenson, Peter Birch. 2007. "Taxing Capital Income: Some Basic Distinctions," and "Why Do Source Based Capital Income Taxes Survive?" Excerpted from "Can Capital Income Taxes Survive? And Should They?" <i>CESifo Economic Studies</i>, Vol. 53, No. 2 (June), pp. 173-177 and 181-186.</p>	<p>Wed Jan 14</p>
<p><b>8. International Taxation: Possible Reforms</b></p> <p><b>[Required]</b> Zodrow, George. "Capital Mobility and Source-Based Taxation of Capital Income in Small Open Economies," <i>International Tax and Public Finance</i>, Vol. 13, 2006, pp. 269–294.</p>	<p>Thu Jan 15</p>
<p><b>9. International Taxation: Cross-Country Evidence</b></p> <p><b>[Required]</b> Dharmapala, Dhammika, and James R. Hines. 2006. "Which Countries Become Tax Havens?" NBER Working Papers No. 12802.</p>	<p>Fri Jan 16</p>
<p><b>10. Industrial Policy and Tax Incentives</b></p> <p><b>[Optional]</b> Rodrik, Dani. 2008. "Normalizing Industrial Policy." Working Paper, Commission on Growth and Development. (Excerpt, pp. 1-17 and pp. 25-32)</p> <p><b>[Required]</b> McLure, Charles. 1999. "Tax Holidays and Investment Incentives: A Comparative Analysis." <i>Bulletin for International Fiscal Documentation</i>, Vol. 53, No. 8-9 (August-September 1999), pp. 326-39</p>	<p>Mon Jan 19</p>

<p><b>11. Cross-Country Evidence on Taxes and Economic Growth</b></p> <p><b>[Required]</b> Slemrod, Joel. 1995. "What Do Cross-Country Studies Teach Us About Government Involvement, Prosperity, and Economic Growth?" <i>Brookings Papers on Economic Activity</i>, No. 2. [Excerpt, pp. 373-381]</p> <p><b>[Required]</b> Lee, Young; Gordon, Roger H. "Tax Structure and Economic Growth" <i>Journal of Public Economics</i>, June 2005, v. 89, iss. 5-6, pp. 1027-43.</p>	<p>Tue Jan 20</p>
<p><b>12. Corruption in Tax Administration</b></p> <p><b>[Optional]</b> Chand, Sheetal K., and Karl O. Moene. "Controlling Fiscal Corruption." <i>World Development</i>, Vol. 27, No. 7, 1999. [Excerpt, pp. 1129-1130 and 1134-1140].</p> <p><b>[Optional]</b> Fjeldstad, Odd-Helge. 2003. "Fighting Fiscal Corruption: Lessons from the Tanzania Revenue Authority." <i>Public Administration and Development</i>, No. 23, 2003, pp. 165-175.</p> <p><b>[Required]</b> Fjeldstad, Odd-Helge. 2005. "Revenue Administration and Corruption," U4 Issue. Christian Michelsen Institute, Utstein Anti-Corruption Resource Center. No. 2. &lt;<a href="http://www.cmi.no/publications/file/?2558=revenue-administration-and-corruption">http://www.cmi.no/publications/file/?2558=revenue-administration-and-corruption</a> &gt; (19 pages)</p>	<p>Wed Jan 21</p>
<p><b>13. Evidence on How Tax Rates affect Tax Evasion</b></p> <p><b>[Optional]</b> Fisman, Raymond and Edward Miguel. 2008. "The Smuggling Gap." Chapter 3 from <i>Economic Gangsters: Corruption, Violence, and the Poverty of Nations</i>. Princeton, NJ: Princeton University Press, pp. 53-75.</p> <p><b>[Required]</b> Levin, Jörgen and Lars M Widell. 2007. "Tax Evasion in Kenya and Tanzania: Evidence from Missing Imports." Working Paper, Örebro University. (19 pages)</p>	<p>Thu Jan 22</p>

<p><b>14. Evidence on How Tax Rates affect Tax Evasion and Labor Supply</b></p> <p><b>[Required]</b> Ivanova, Anna, Michael Keen and Alexander Klemm. 2005. "The Russian Flat Tax Reform." <i>Economic Policy</i>, July, pp. 399-444.</p>	<p>Fri Jan 23</p>
<p><b>15. Taxes on Land and Property; Presumptive Taxes</b></p> <p><b>[Required]</b> Skinner, Jonathan. "Prospects for Agricultural Land Taxation in Developing Countries." <i>World Bank Economic Review</i>. Vol. 5, No. 3, 1991. pp. 493-511.</p> <p><b>[Required]</b> Yitzhaki, Shlomo. 2007. "Cost Benefit Analysis of Presumptive Taxation." <i>FinanzArchiv</i> Vol. 63 no. 3, pp. 311-326.</p>	<p>Mon Jan 26</p>
<p><b>16. Taxes on Natural Resources</b></p> <p><b>[Optional]</b> Boadway, Robin and Michael Keen. 2008. "Theoretical Perspectives On Resource Tax Design." Working Paper, September 18.</p>	<p>Tue Jan 27</p>
<p><b>17. Conventional Wisdom on Good Tax Policy and Challenges to It</b></p> <p><b>[Required]</b> Avi-Yonah, Reuven and Yoram Margalioth. "Taxation in Developing Countries: Some Recent Support and Challenges to the Conventional View," <i>Virginia Tax Law Review</i>, 27(1), Summer 2007, pp. 1-21.</p> <p><b>[Optional]</b> Keen, Michael. Forthcoming. "VAT, Tariffs, and Withholding: Border Taxes and Informality in Developing Countries." <i>Journal of Public Economics</i>. (12 pages) [This paper has some rather technical parts – don't worry about the math, just try to understand the argument that he is making in words.]</p>	<p>Wed Jan 28</p>