

Economics 517 / 389 -- Tax Policy in Emerging Markets
Spring 2010 [revised]

Class meets: 2:25-3:50pm M, Th
CDE Classroom
Office hours: 1:30-3:30pm Tues.
and by appointment

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Course Description

Taxes are half of what government does. So if you are interested in what government policy can do to promote efficiency, equity, and economic development, you should be interested in tax policy. Governments must raise tax revenue to finance critical public goods, address other market failures and distributional issues, and to avoid problems with debt and inflation. Taxes typically take up anywhere from ten to fifty percent of a country's income, they profoundly affect the incentives to undertake all varieties of economic activity, and the government expenditures that they finance have potentially large consequences for human welfare. So the stakes involved in improving tax policy are quite large. All of these issues are of great importance in developing and transitional countries (also known as "emerging markets"), but in these nations taxation is especially challenging because of serious problems with tax evasion and administration, among other things. This class provides an in-depth exploration of tax policy, with an emphasis on the challenges and issues most relevant in emerging markets. Topics addressed in this class include: how basic economic principles can be applied to help one think about the efficiency and equity consequences of tax policies; how the value-added tax, taxes on land and property, personal income taxes, and corporate income taxes are designed and administered and how they influence the economy; how various elements of tax design affect incentives to save and invest; ideas for fundamental reforms of these taxes; the implications of global capital flows and corporate tax avoidance for the design of tax policy; tax holidays and other special tax incentives for investment; empirical evidence on the influence of taxes on economic growth, foreign direct investment, labor supply, and tax evasion; theory and evidence in the debate over progressive taxes versus "flat" taxes; case studies of efforts to reform tax administration and reduce tax evasion and corruption; presumptive taxation; and the "unofficial" economy and its implications for tax policy.

Course Materials

There will be a limited amount of reading from a textbook for the course, *Public Finance and Public Policy* by Jon Gruber (any edition is fine). CDE fellows already have this book from the fall semester; undergrads should see me about this. All readings for the course except those from Gruber's textbook will be posted electronically on Blackboard and made available in printed course reading packets.

Course Requirements

- **Class participation** (*10% of the grade*). You are expected to come to class having done the assigned readings in advance, and be prepared to discuss questions about the reading. I may call on particular people to ask you to contribute.
- **Midterm exam** (*40% of the grade*). The midterm will be held outside of the regular class meeting time, in order to give everyone plenty of time to complete it. It is tentatively scheduled for **Friday April 9th** (time and place to be announced). Undergrads with a schedule conflict should make arrangements with me to take it at an alternate time.
- Approximately 3 **homework assignments** before the midterm (*5% of the grade*).
- **Two writing assignments, approximately 7 pages each** in the second half of the course (*45% of the grade*). These writing assignments will ask you to engage with the readings in the second half of the course, for example by making an argument for a particular side of a tax policy debate, or by critically evaluating some evidence. Further details will be provided later in the term.

There is no final exam for the course.

Course web page

The course web page is available through the site: <http://blackboard.williams.edu>

Honor code

All of the usual Williams honor code rules apply in this course. Your writing assignments should follow the Chicago author-date method of citation, and any words that are not your own must be enclosed in quotation marks and cited. For further details see:

<http://www.williams.edu/resources/acad_resources/survival_guide/CitingDoc/CitingContents.php>.

Working on the homework assignments in groups is encouraged. However, if you work out an answer as part of a study group, be sure you understand exactly how to arrive at the answer. You must write up the answer to the problem on your own, in your own words, and of course you must each turn in your own individual problem set. Turning in an identical problem set answer to a classmate is a violation of the honor code.

Schedule of Topics and Readings

	Date	Topic	Readings
1	Wed Feb 3	Introduction	<ul style="list-style-type: none"> Bahl, Roy W., and Richard M. Bird. 2008. "Tax Policy in Developing Countries: Looking Back--and Forward." <i>National Tax Journal</i> Vol. 61, no. 2. Just read pp. 279-292 (up to end of "TaxAdministration Yet Again.")
	Mon Feb 8	No class: CDE fellows in DC for World Bank conference. This class is to be rescheduled to Tuesday Feb. 9, time to be announced.	
2	Tue Feb 9	Supply-demand analysis of taxes	<ul style="list-style-type: none"> Gruber, Ch. 19, "General Equilibrium Tax Incidence" (pp. 563-568 in 2nd edition, pp. 534-539 in 2nd ed.) [Review Gruber pp. 545-558 in 2nd ed., or pp. 517-530 in 1st ed., if needed.] Gruber, Ch. 20, "Taxation and Economic Efficiency" (pp. 577-586 in 2nd ed., pp. 547-559 in 1st ed.). Slemrod, Joel, and Jon Bakija. 2008. "Corporations Don't Pay Taxes, People Do" and "Do Workers Bear Taxes on Capital" excerpted from <i>Taxing Ourselves</i>, 4th ed., Cambridge: MIT Press, pp. 131-132. Sorenson, Peter Birch. 2007. "Taxing Capital Income: Some Basic Distinctions." Excerpted from "Can Capital Income Taxes Survive? And Should They?" <i>CESifo Economic Studies</i>, Vol. 53, No. 2 (June), pp. 173-177.
3	Thu Feb 11	Indifference curve analysis of taxes	<ul style="list-style-type: none"> Rosen, Harvey S., and Ted Gayer. 2008. "Taxation and Efficiency." Excerpted from <i>Public Finance</i>, 8th ed. New York: McGraw-Hill Irwin, pp. 331-338. Gruber Ch. 21, Section 21.1 only (Labor supply with indifference curves). Gruber Ch. 22, sec. 22.1 part on saving with indifference curves only. [Review Gruber Ch. 2, Sec. 2.1, if needed.]
4	Mon Feb 15	Optimal taxation	<ul style="list-style-type: none"> Gruber, Ch. 20, "Optimal Commodity Taxation" (pp. 586-592 in 2nd ed., pp. 559-565 in 1st ed.). Slemrod, Joel. 1990. "Optimal Taxation and Optimal Tax Systems." <i>Journal of Economic Perspectives</i>. Vol. 4, no. 1. Excerpt, pp. 157-163.
5	Thu Feb 18	The economics of tax evasion	<ul style="list-style-type: none"> Gruber, Ch. 25, "Improving Tax Compliance" (pp. 726-730 in 2nd ed., pp. 692-695 in 1st ed.). Slemrod, Joel. 2007. "Cheating Ourselves: The Economics of Tax Evasion." <i>Journal of Economic Perspectives</i>. Vol. 21, no. 1: 25-48. Gordon, Roger, and Wei Li. 2009. "Tax Structures in Developing Countries: Many Puzzles and a Possible Explanation." <i>Journal of Public Economics</i>. Vol. 93, no. 7-8. [Excerpt, pp. 855-858 and 865.]

6	Mon Feb 22	Value-added taxation (VAT): the basics	<ul style="list-style-type: none"> • Ebrill, Liam, Michael Keen, Jean-Paul Bodin, and Victoria Summers. 2002. "The Allure of the Value-Added Tax" <i>Finance and Development</i>, June. • Gruber, Ch. 25, "Value-Added Tax" (pp. 747-748 in 2nd ed., pp. 711-712 in 1st ed.) • Bird, Richard M., and Pierre-Pascal Gendron. 2007. <i>The VAT in Developing and Transitional Countries</i>. Excerpts from Chapters 3 and 7. Cambridge and New York: Cambridge University Press.
7	Thu Feb 25	Taxes on land and property	<ul style="list-style-type: none"> • Bahl, Roy W., and Richard M. Bird. 2008. "Tax Policy in Developing Countries: Looking Back--and Forward." <i>National Tax Journal</i> Vol. 61, no. 2. [Just read pp. 293-295, section on "Fiscal Decentralization and Property Taxation"]. • Skinner, Jonathan. "Prospects for Agricultural Land Taxation in Developing Countries." <i>World Bank Economic Review</i>. Vol. 5, No. 3, 1991. pp. 493-511.
8	Mon Mar 1	Income taxation 1	<ul style="list-style-type: none"> • Gruber Ch. 18, Section 18.3 ("Measuring the Fairness of Tax Systems") only. • Slemrod, Joel and Jon Bakija. 2009. <i>Taxing Ourselves</i>, 4th edition. Cambridge MA: MIT Press. [Excerpt from Ch. 2, pp. 28-46, 47-52]. • Gruber Ch. 22, Section 22.1 portion on "Inflation and the Taxation of Savings" only.
9	Thu Mar 4	Income taxation 2	<ul style="list-style-type: none"> • Slemrod, Joel and Jon Bakija. 2009. <i>Taxing Ourselves</i>, 4th edition. Cambridge, MA: MIT Press. [Excerpt from Ch. 8, pp. 270-282] • Gruber, "Background: Present Discounted Value" (Ch. 4, pp. 102-103 in 2nd edition, p. 98 in 1st edition). • Gruber Ch. 24, "Corporate Taxation." Introduction and sections 24.1, 24.2, and 24.5 only (pp. 689-700 and 709-716 in 2nd edition; pp. 657-666 and 675-683, in 1st edition).
10	Mon Mar 8	Income taxation in developing countries	<ul style="list-style-type: none"> • 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.
11	Thu Mar 11	Consumption taxation vs. income taxation	<ul style="list-style-type: none"> • Gruber, "Fairer Treatment of Savers and Less Distortion to Savings Decision" (in Ch. 25, pp. 742-743 in 2nd ed., pp. 707-708 in 1st ed.) • Slemrod, Joel, and Jon Bakija. 2008. "A Consumption Base." Excerpted from <i>Taxing Ourselves</i>, 4th ed., Cambridge: MIT Press, pp. 194-216. • Bakija, handout on taxes and incentives to invest (to be distributed in class).
12	Mon Mar 15	Consumption taxation vs. income taxation	<ul style="list-style-type: none"> • Slemrod, Joel, and Jon Bakija. 2008. "A Consumption Base." Excerpted from <i>Taxing Ourselves</i>, 4th ed., Cambridge: MIT Press, pp. 194-216. • Bakija, handout on taxes and incentives to invest (to be distributed in class).

13	Thu Mar 18	Innovative consumption tax designs	<ul style="list-style-type: none"> • Slemrod, Joel and Jon Bakija. 2009. <i>Taxing Ourselves</i>, 4th edition. Cambridge MA: MIT Press. [Excerpt, pp. 235-239 and pp. 260-262.] • Bahl, Roy, and Sally Wallace. 2007. "From Income Tax to Consumption Tax? The Case of Jamaica." <i>FinanzArchiv</i> 63, no. 3: 396-414. • 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.
14	Mon Apr 5	International Taxation 1	<ul style="list-style-type: none"> • Gruber, Ch. 24, Section 24.6, "Treatment of International Corporate Income" (pp. 717-721 in 2nd edition, pp. 683-686 in 1st edition). • 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.] • Clausing, Kimberly. 2009. "Multinational Firm Tax Avoidance and Tax Policy." <i>National Tax Journal</i>, Vol. 62 No. 4 [Excerpt, pp. 703-717 only.] • Grubert, Harry, and Joel Slemrod. 1998. "The Effect of Taxes on Investment and Income Shifting to Puerto Rico." <i>Review of Economics and Statistics</i> 80, no. 3. [Excerpt, pp. 367-368 only.] • Honohan, Patrick, and Brendan Walsh. 2002. "Catching Up with the Leaders: The Irish Hare." <i>Brookings Papers on Economic Activity</i> [Excerpt, pp. 54-57 only.]
	Thu Apr 8	Optional review for midterm exam	
	Fri Apr 9	Midterm exam (time and place to be announced)	
15	Mon Apr 12	International Taxation 2	<ul style="list-style-type: none"> • Sorenson, Peter Birch. 2007. "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), [Excerpt, pp. 181-186]. • Zodrow, George. 2006. "Capital Mobility and Source-Based Taxation of Capital Income in Small Open Economies," <i>International Tax and Public Finance</i>, Vol. 13, [Excerpt, pp. 275-286].
16	Thu Apr 15	International Taxation 3	<ul style="list-style-type: none"> • Dharmapala, Dhammika, and James R., Jr. Hines. 2009. "Which Countries Become Tax Havens?" <i>Journal of Public Economics</i> 93, no. 9-10: 1058-1068.
17	Mon Apr 19	International Taxation 4	<ul style="list-style-type: none"> • Margalioth, Yoram. 2003. "Tax Competition, Foreign Direct Investments, and Growth: Using the Tax System to Promote Developing Countries." <i>Virginia Tax Law Review</i>, Vol. 23 [Excerpt, pp. 175-191]. • 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.

18	Thu Apr 22	Cross-country evidence on taxes and economic growth	<ul style="list-style-type: none"> • 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]. • 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.
19	Mon Apr 26	Evidence on taxes and labor supply	<ul style="list-style-type: none"> • Gruber, Ch. 21, Section 21.2 only ("Taxation and Labor Supply -- Evidence"). • Bakija, Jon. 2010. "Tax Rates and Labor Supply in OECD Countries."
20	Thu Apr 29	The Russian "flat tax" reform	<ul style="list-style-type: none"> • Duncan, Denvil and Klara Sabrianova-Peter. 2010. "Does Labor Supply Respond to a Flat Tax? Evidence from the Russian Flat Tax Reform." <i>Economics of Transition</i>. Vol. 18, No. 2, pp. 365–404.
21	Mon May 3		<ul style="list-style-type: none"> • Gorodnichenko, Yuriy, Jorge Martinez-Vazquez, and Klara Sabirianova Peter. 2009. "Myth and Reality of Flat Tax Reform: Micro Estimates of Tax Evasion Response and Welfare Effects in Russia." <i>Journal of Political Economy</i> 117, no. 3 [Excerpt, pp. 504-536, 542-543 and 546-547.]
22	Thu May 6	Tax rates and tax evasion	<ul style="list-style-type: none"> • 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, [Excerpt, pp. 53-63 and 66-75] • Mishra, Prachi, Arvind Subramanian, and Petia Topalova. 2008. "Tariffs, Enforcement, and Customs Evasion: Evidence from India." <i>Journal of Public Economics</i> 92, no. 10-11: 1907-1925.
Friday, May 7, 4:00pm. Deadline for writing assignment #1.			
23	Mon May 10	Reform of tax administration	<ul style="list-style-type: none"> • 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]. • 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. • McCarten, William. 2006. "The Role of Organizational Design in the Revenue Strategies of Developing Countries: Benchmarking with VAT Performance." In <i>The Challenges of Tax Reform in a Global Economy</i>, 413-439. New York: 2006.
24	Thu May 13	Taxing the informal sector; presumptive taxation	<ul style="list-style-type: none"> • Yitzhaki, Shlomo. 2007. "Cost Benefit Analysis of Presumptive Taxation." <i>FinanzArchiv</i> Vol. 63 no. 3, pp. 311-326. • La Porta, Rafael, and Andrei Shleifer. 2008. "The Unofficial Economy and Economic Development." <i>Brookings Papers on Economic Activity</i> (Fall). [Excerpt]
Wednesday May 19th, 4:00pm. Deadline for writing assignment #2.			