

ECONOMICS 336—SEMESTER 2, 2009
Public Economics II: Public Choice

COURSE OUTLINE

Course Coordinator and Lecturer: Dr Eric Crampton

Course Description:

Public Choice applies economic theory and methodology to the study of nonmarket decision-making (typically political decision-making). As economists, we look not to the benevolence of the butcher for our meat but rather to his self-interest. What happens when we realize that politicians and voters are no different? Simply put, we achieve a much better understanding of real-world policy, economic and otherwise. The course provides an overview of positive and normative public choice theory, highlighting work in the economic theory of constitutions, voting rules, bureaucracy, democracy, collective action, dictatorship, the theory of clubs, expressive voting, political business cycles, lobbying, legislative structures, political competition, as well as criticisms of public choice theory. A familiarity with algebra is assumed on the part of students, as is a strong background in microeconomic theory; I will attempt to keep the calculus to $\lim_{x \rightarrow e}$ (very little).

Course Objectives:

In addition to gaining a broad flavour of the field of public choice, students will understand the median voter theorem, how differences in political institutions (electoral and legislative) translate into differences in expected policies, the theory of rent-seeking (lobbying) and its effects, Wittman's "efficient markets" critique of public choice and Caplan's "rational irrationality" rebuttal.

Assessment:

Three assignments, due 10 August, 14 September, and 5 October (handed out at least one week prior to the lecture session in which they are due), will be combined with a mid-term test and take-home final exam for evaluation. Quality participation in classroom (lecture and tutorial) discussion also contributes to the final grade. The mid-term exam will be held the evening of Wednesday, 19 August, 6:30 p.m. to 9:30 p.m. absent substantial clashes with other exams and pending room availability. The final exam will be distributed at 3 pm, Tuesday 13 October and will be due at 3 pm, Friday, 16 October. Expect that the exam will require 2 days' solid work to complete; if you have other assignments due for other courses that week, you might want to have them done before your exam is handed to you. The final exam is cumulative; concepts learned in the first half of the class will be essential in understanding the problems encountered in the second half. The Honour Code will be enforced quite strictly; while you are encouraged to consult your books and notes while completing the take-home final exam, any discussion of the exam problems with your classmates or other individuals is strictly prohibited.

Assessment Weighting:

The midterm will count for 30% of the final grade; the final exam counts for 40%. Homework assignments comprise 20% of the final grade and participation in tutorials counts for a further 10%. The weights are fixed and improvement late in the course will not bump up previous work's grades.

Problem Sets:

As we will go over the homework assignments during the tutorial sessions, late assignments cannot be accepted. There will be 3 homework assignments which will both review your understanding of the previous lectures and ask you to apply it in new and novel ways. The typical assignment will ask the student to provide a short New Zealand case study illustrating some aspect of theory discussed during recent lectures; however, not all assignments will be of this nature. Students must be prepared to present and discuss their assignment during the tutorial session following the lecture in which the assignment is due (depending on class size, expect to be called upon at least twice to present your assignment during tutorial sessions). Group work on assignments is not encouraged, though students should feel free to discuss the assignments with one another [i.e. feel free to chat with your colleagues when trying to wrap your head around a problem, but do your assignment on your own at home afterwards].

Tutorial Participation:

Quality of discussion of assignment during tutorials also contributes towards the participation component listed in Assessment Weighting (above). Come to the tutorial prepared to discuss the readings and, if you've just handed in an assignment, the questions from that assignment. I will come to each tutorial with a printout of the class list with your photos (as it will take me a couple of weeks to learn your names). I will ask questions about the readings, solicit discussion and debate of the ideas presented in the readings and how they relate to previous readings. Sometimes I'll call for volunteers to answer a question; other times I'll pick on people individually. If you make a quality contribution to the tutorial discussion, I'll put a tick beside your picture; if you demonstrate that you haven't done the reading, I'll put a dash. At the end of the year, I look at your net of ticks and dashes and assign a participation score that's monotonically increasing in the net number of ticks. It isn't very hard to get a decent participation grade, but it's pretty easy to get a zero (either don't show up for tutorials or just sit silently at the back).

Course Contents:

Please see the schedule and reading list for a detailed description of course contents. I also maintain a website for the course at http://www.econ.canterbury.ac.nz/personal_pages/eric_crampton/336.html . I recommend you consult it regularly for any updates. I'm happy to put up an RSS feed if enough folks use a reader; let me know.

Reading:

There is only one required text for this class.

Caplan, Bryan. 2007. *The Myth of the Rational Voter*. Princeton University Press.

The book is available via the University bookstore and also via Amazon.com (\$20 US or thereabouts via Amazon).

There is an extensive reading list for this course. Most articles are available online via our library's e-journal holdings. On the first day of lectures I will provide a CD-Rom with copies of all articles not

available via the library and with a copy of your second text for the class; do not lose it as I will not replace it. You are expected to thoroughly read and understand all readings. Tutorial sessions will frequently involve intense debate of issues raised in the assigned readings; be prepared by having completed a critical reading of the assigned texts prior to the relevant lecture and tutorial session. This course is very reading intensive; do not sign up for the class unless you are prepared to do the readings. If you prefer print version of the readings, you can purchase the course reader via the usual outlet. There's nothing in the print version that isn't on the CD-Rom, but it's cheaper to buy the reader than to print out all of the articles and book chapters.

We are this year trialling some chapters from a draft text written by Max Stearns and Todd Zywicki. The relevant chapters are replicated in the reader.




Dishonest Practice:

It is dishonest practice to communicate with another student during the test or exam, to copy another student's work, to plagiarise, or to willingly allow your own work to be copied by someone else. Dishonest practice can result in a student receiving zero for that piece of assessment, receiving a fail in the course, a fine, or suspension or expulsion from the University.

In particular, I urge you not to copy things you find online or elsewhere when doing the assignments. Dragging students into the HoD's office to sort this sort of thing out is pleasant for nobody, but least of all for you. I have a variety of mechanisms for detecting plagiarism and am really rather good at it. It is perfectly fine to do research when working on your assignments, but you have to cite other people's ideas or words when you're using them. A handout on plagiarism and appropriate citation is included in the course reader (CD ROM and print version). Please consult this before completing any written work, as well as the library resources there referenced. Any instance of plagiarism on a piece of assessment will result in a minimum penalty of a zero for that piece of assessment. If it happens on two assignments, I will refuse to grade your take-home final exam script. **Note that a single instance of plagiarism in the take-home exam can result in a grade of zero for the entire exam.** You will be required to sign and attach a cover sheet to each piece of written work confirming that you understand and agree to this policy.

Aegrotat Assessment:

In the event of illness or other factor that results in a student missing a piece of assessment or having impaired performance, a student may apply for an aegrotat assessment. Please note, however, that according to university rules, a student may only receive an aegrotat pass or grade if the Head of Department is "satisfied that the student would, in the absence of the impairment, have attained at least a pass or that grade", and "an aegrotat grade or pass may be awarded only where the student has been able to complete a substantial part of the course and a substantial part of the assessment for that course at a satisfactory level". It is therefore important to take each piece of assessment seriously even if it has a low weighting. Students are also strongly advised to attend tests or exams at all possible, even if they are ill.




- Note:**
-  indicates a selection available online
 -  indicates a selection available in the reader/CD
 -  indicates a selection available in your required text

Section I: Constitutional political economy: moving from the state of nature

Week 1: Public goods, externalities, and comparative institutions

- Why collective action?
- The “Club Goods” alternative?
- Social benefits, private benefits, social costs, private costs, and optimization
- Tragedy of the commons
- Externalities
- Coase on property rights and externalities
- Demsetz on the comparative institutional framework: market failure and political failure






Readings:

-  Buchanan, James. 2003. “Public choice: politics without romance.” *Policy* 19(3): 13-18.
-  Lemieux, Pierre. 2004. “The public choice revolution.” *Regulation* (Fall): 22-29.
-  Tullock, Gordon. 1998. “Externalities and government.” *Public Choice* 96: 411-415.

Week 2: Emerging from the state of nature: towards a constitutional political economy

- Law as a public good: will the market provide?
- Hobbesian approaches: Olson’s permanent bandit
- Lockean approaches:
 - Nozick on the state as emergent
 - Hypothetical consent and veil mechanisms
 - Rawls
 - Buchanan’s contractarian turn
- Buchanan’s Contractarian political economy
 - Utility-enhancing constraints
 - Constitutions as contracts

Readings:

-  Buchanan, James and Gordon Tullock. 1999 [1962]. “A generalized economic theory of constitutions.” Chapter 6, pp. 63-84, in *The Calculus of Consent*. Available at <http://oll.libertyfund.org/>
-  Caplan, Bryan and Edward Stringham. 2003. “Networks, law, and the paradox of cooperation.” *Review of Austrian Economics* 16(4): 309-26.
-  Cowen, Tyler and Daniel Sutter. 2005. “Conflict, cooperation and competition in anarchy.” *Review of Austrian Economics* 18(1): 109-15.
-  Olson, Mancur. 1993. “Dictatorship, democracy, and development.” *American Political Science Review* 87(3): 567-76.
-  Stearns, Max and Todd Zywicki. 2007. “Constitutions”. Chapter 8. pp. 1-12, 17-21.

Section II: Collective action**Week 3: Making social choices directly**

- Voting systems and paradoxes
 - Majority rule and its alternatives
 - Cycling and intransitivity
- Arrow and the social welfare function
- The median voter model
- Complicated alternatives: the Demand Revealing Process

Readings:

- 📖 Stearns, Max and Todd Zywicki. 2007. “An introduction to social choice”. Chapter 3, pp. 1-32. Ignore sections C&D, pp. 11-17, unless you really don’t get cycling.
- 📖 Riker, William H. 1986. “The Flying Club”. Chapter 3, pp. 18-33, of The Art of Political Manipulation. Yale University Press.
- 📖 Tideman, T. Nicolaus and Gordon Tullock. 1976. “A new and superior process for making social choices.” *Journal of Political Economy* 84(6): 1145-59.

Week 4: Representative Government

- Selection of representatives
- Structure of government: Presidential and Parliamentary regimes, division of powers
- Implications of forms of representative selection for party structure; Duverger’s law
- Median voter and party competition
- Empirics on institutions and outcomes

Readings:

- 📖 Cowen, Penelope Brook, Tyler Cowen, and Alexander Tabarrok. 1992. “Unicameralism and Bicameralism”. Chapter 4, pp. 4.1-4.25 in An Analysis of Proposals for Constitutional Change in New Zealand. New Zealand Business Roundtable. Available at <http://www.nzbr.org.nz/documents/publications/Brook-Cowen%20Cowen%20Tabarrok%201992%20NZBR%20Analysis%20of%20Proposals%20for%20Constitutional%20Change.pdf>

(I’ll put the link on the course website when we get close to week 4)

- 📖 Persson, Torsten. 2003. “Consequences of constitutions.” *NBER Working Paper* 10170.
- 📖 Riker, William H. 1986. “Camouflaging the Gerrymander”. Chapter 6, pp. 66-77, of The Art of Political Manipulation. Yale University Press.
- 📖 Stearns, Max and Todd Zywicki. 2007. “Constitutions”. Chapter 8. pp. 12-17; pp 25-29.
- 📖 Note: if you are unfamiliar with New Zealand’s Parliamentary system, Chapter 2 of Cowen, Cowen and Tabarrok gives a wonderful summary as of 1992. Section.5 to end Chapter 3 provides a nice analysis of MMP and PR in general; these are great refreshers. I’m not going to grill you about either in tutorial this week, but I expect you to know how your Parliamentary system works and its general history.

Week 5: Weakest Link? Voters and democracy.

- Rational ignorance
- Economics of imperfect information
- Political knowledge and rational ignorance
- “Cueing” and voter optimization
- Olson’s Logic

Readings:

- ☞ Downs, Anthony. 1957. “An economic theory of political action in a democracy.” *Journal of Political Economy* 65(2): 135-50.
- ☞ Lupia, Arthur and Richard Johnston. 2001. “Are Voters to Blame? Voter competence and elite maneuvers in referendums”. Chapter 9, pp. 191-210, in Mendelsohn, Matthew and Andrew Parkin, eds., Referendum Democracy: Citizens, Elites and Deliberation in Referendum Campaigns. Available at <http://www-personal.umich.edu/~lupia/Papers/lupiajohnston2001.pdf>
- ☞ Somin, Ilya. 1998. “Voter ignorance and the democratic ideal.” *Critical Review* 12(4): 413- 58.

Section III: Agency relationships and government**Week 6: Agency and democracy I**

- Representative government as principal-agent problem
- Political sausage-making: logrolling, bargaining, and the pork-barrel
- The “law” of 1/N
- Introduction to rent-seeking

Readings

- ☞ Stratmann, Thomas and Martin Baur. 2002. “Plurality rule, proportional representation, and the German *Bundestag*: how incentives to pork-barrel differ across electoral systems.” *American Journal of Political Science*. 46(3): 506-14.
- 📖 Stearns, Max and Todd Zywicki. 2007. “Interest Group Theory and Rent-Seeking”. Chapter 2. pp. 1-6 and 8-15.
- ☞ Tullock, Gordon. 1959. “Problems of majority voting.” *Journal of Political Economy* 67(6): 571-79.
- 📖 Tullock, Gordon. 1967. “The welfare costs of tariffs, monopolies and theft.” *Western Economic Journal* 5: 224-32. Note: Available only via the reader.

BREAK**MIDTERM EXAM**

Week 7: Agency and democracy II

- Rent-seeking
- Which principal? Which agents? Voters, MPs, Cabinet, and Bureaucracy
- The Transitional Gains Trap
- Political Business Cycles

Readings

- ☞ Cowen, Penelope Brook, Tyler Cowen, and Alexander Tabarrok. 1992. An Analysis of Proposals for Constitutional Change in New Zealand. New Zealand Business Roundtable. Chapter 2.
- 📖 Stearns, Max and Todd Zywicki. 2007. "Interest Group Theory and Rent-Seeking". Chapter 2. pp. 6-8, 18-26.
- 📖 Stearns, Max and Todd Zywicki. 2007. "The Executive". Chapter 6. pp. 10-22.
- ☞ Tullock, Gordon. 1975. "The transitional gains trap." *Bell Journal of Economics* 6(2): 671-78.
- 📖 Yandle, Bruce. 1983. "Viewpoint: bootleggers and Baptists – the education of a regulatory economist." *Regulation* 12 (May/June): 12-16.

Week 8: Political competition

- Lobbying and menu-auction approaches
- Political advertising and campaign contributions
- Federalism & Tiebout competition
- Restrictions on political competition

Readings

- ☞ Ansolabehere, Stephen, John de Figueiredo and James Snyder, 2003, "Why is there little money in U.S. politics?" *Journal of Economic Perspectives* 17:1 (winter) pp. 105-130.
- ☞ Geddis, Andrew. 2007. "Rethinking the funding of New Zealand's election campaigns". *Policy Quarterly* 3:1, pp. 3-10.
- ☞ Stratmann, Thomas. 2005. "Some talk: Money in politics. A (partial) review of the literature." *Public Choice* 124: 135-56.
- 📖 Stearns, Max and Todd Zywicki. 2007. "Constitutions". Chapter 8. pp. 31-36; 39-42

Section IV: Critiques and responses**Week 9: Wittman's efficient markets critique**

- Inefficiency results and assumptions: are we assuming the ladder?
- Competition, information, and transactions costs

Readings

- ☞ Caplan, Bryan. 2007. "Classical public choice and the failure of rational ignorance." Chapter 4, pp. 94-113 in The Myth of the Rational Voter.
- ☞ Wittman, Donald. 1989. "Why democracies produce efficient results." *Journal of Political Economy* 97(6): 1395-1424

Week 10: Expressive voting and rational irrationality I

- The analytics of decisiveness
- Expressive and instrumental considerations at the ballot box
- Inefficient unanimity!

Readings

☞ Brennan, Geoffrey. 2008. "Psychological dimensions in voter choice." *Public Choice* 137:3-4 (December), pp. 475-89.

☞ Caplan, Bryan. 2007. *The Myth of the Rational Voter*, chapters 1-3, pp. 5-93.

Note: skim chapter 2 to get the gist of the argument; don't worry about memorising stats.

☞ Stearns, Max and Todd Zywicki. 2007. "Introduction to the economic analysis of collective decision-making". Chapter 1. pp. 19-24.

Week 11: Expressive voting and rational irrationality II

- Caplan's Rational Irrationality framework

Readings

☞ Caplan, Bryan. 2007. *The Myth of the Rational Voter*, chapters 5-7, pp. 114-181.

Week 12: Putting it all together

- Comparative institutions: minimizing failure
- Expressive politics and the re-thinking of public choice and constitutional political economy

Readings:

☞ Grofman, Bernard. 2004. "Reflections on public choice." *Public Choice* 118: 31-51.

☞ Hanson, Robin. 2003. "Shall we vote on values, but bet on beliefs?" *unpub. ms.* Available at <http://hanson.gmu.edu/futarchy.pdf>

☞ Sunstein, Cass. 2008. "Neither Hayek nor Habermas." *Public Choice* 134: 1-2 (January), pp. 87-95.