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Econ 4620 Public Economics S2014: Seminar assignment for 24 February

Please, prepare for the seminar.

Problem 1
Consider the Ramsey model (RM) with heterogeneous agents and the Mirrlees model (MM) with mixed taxation.

1. To what extent do the respective models capture distributional concerns?
2. Why do consumption shares appear in the RM but not in the MM?
3. To what extent do the repective models capture distortions of the consumption bundle?
4. Give a survey of concerns not captured by RM and MM that may nonetheless be relevant for setting commodity taxes.

Problem 2
Explain how a commodity tax can relax the self-selection constraint in the MM.

Problem 3
Discuss how an extended version of the Mirrlees model (MM) can shed light on the question how to tax returns to savings.

Problem 4
State the content and main implications of the Diamond-Mirrlees production efficiency lemma.

Problem 5
Suppose that because of soaring oil prices the fuel price (on petrol, diesel, etc) is much higher than before. As consumers pay VAT on fuel some politicians have argued that government revenue has increased a lot due to larger amount of VAT from fuel consumption. They have further argued that the increase in VAT on fuel should enable the government to lower other taxes.
Discuss these arguments.

Problem 6
Where a commodity generates an external cost there is case for imposing an externality-correcting tax, often referred to as a Pigouvian tax. Consider such a good. Suppose also that there is a general VAT in the economy. Denote by v the VAT rate. Suppose that the cost of producing the good in question, not including the external cost, is normalised to unity, and assume that the good generates an external cost e per unit. It is debated how to tax the good. One option is to set the total tax per unit, denoted by t, equal to $t=v+e$. The alternative is to set $t=e+v+ve$. Disregarding labour supply incentives for the moment, what would you recommend?