EC 410 Study Guide I Spring 2005
R. Congleton **Political Economy of Public Policy** GMU

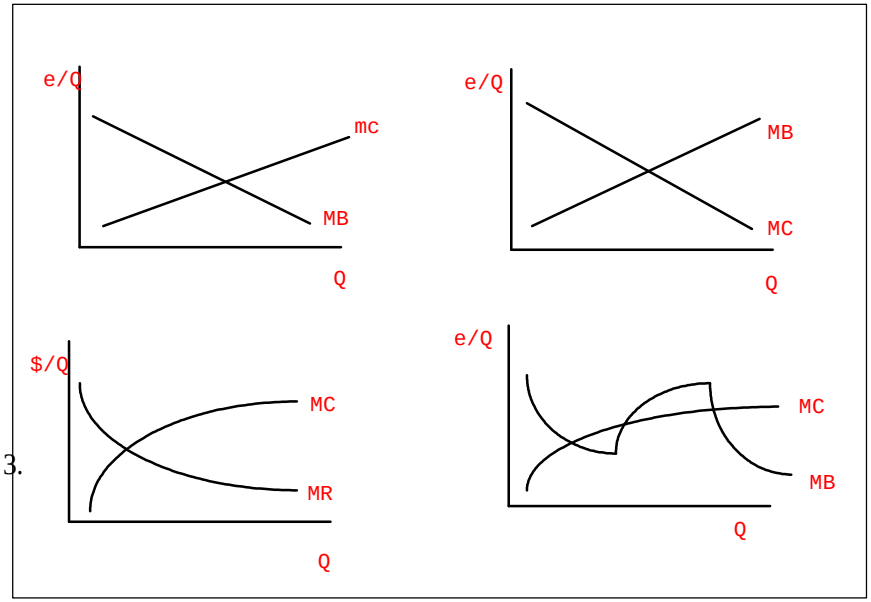
1. Identify and/or Define the following:

a. rational choice
b. consumer surplus
c. median voter
d. tax price
e. probabilistic voting
f. Pareto optimal
g. rational ignorance
h. structure induced equilibrium
i. supermajority
j. fiscal illusion
k. agency problem
l. Condorcet
m. Duncan Black
n. Anthony Downs
o. stationary bandit
p. proportional representation
q. party discipline
r. cyclic majority

2. Use the diagrams below to:

A. Find the net benefit maximizing quantity
B. Find the area(s) that characterize the individual's net benefit at that level
C. Derive a demand curve for the product or service

3.



4. Analyze a median voter model of government provision of a public service. Assume that three individuals have similar tastes (MBs) for the government service in question but face different tax prices (MCs).

A. Show the median voter's preferred public service level.
B. Demonstrate that it will "beat" all other service levels in a referendum.
C. Show that even if the service is a normal good, differences in the tax price may cause high income voters to prefer lower service levels than low income voters.
D. Repeat A&B assuming that the voters differ in their assessment of the marginal benefits of the service rather than marginal tax costs.

5. Develop a median voter model of Environmental protection.

A. In what sense does the median voter "pay" for environmental quality?
B. Why might the median voter be interested in paying for a environmental quality?
C. Use a diagram to depict the median voter's ideal program of environmental protection. (Label all important details, and explain briefly the nature of all of the curves used in your diagram.)
D. How would an increase in voter income affect his or her demand for environmental quality?

6. Use a median voter model to analyze social security programs--e.g. public retirement programs.

A. Characterize the optimal benefit level for the median voter.
B. Why does she not give more to the retired persons than this amount?
C. How would an increase in the median voter's age affect the size of program benefits?
D. How would an increase in the number of retired persons affect the median voter's preferred average benefit level?
E. In what sense, if any, can the median voter be said to adopt overly generous public pension programs?.

7. Develop a median voter model of transfers to the poor.

A. Why might the median voter be willing to pay for a welfare program?
B. Use a diagram to depict the median voter's ideal welfare program. (Label all important details, and explain briefly the nature of all of the curves used in your diagram.)
C. How would an increase in "welfare fraud" affect the median voter's demand for welfare programs?
D. How does the median voter's own income affect his or her demand?
E. Why might the median member of a labor union support welfare programs?
F. In what cases, might such programs be said to be "overly generous?" (Hint, apply the Paretian and/or social net benefit maximizing norms.)

8. Use marginal cost and marginal benefit curves to show the extent of information that an individual would "rationally" acquire.

   A. Use marginal cost and benefit curves to show the effects of "biased" assessments of a program's benefits or costs.

   B. Discuss some possible implications of rational ignorance for democratic decision making.

   C. Would the problem of rational ignorance be greater in political "markets" than in ordinary economic markets?

   D. Use MB and MC curves to show how "transparency" can affect incentives to gather information and also political outcomes.

   E. Do political campaigns increase or decrease rational ignorance? Why?

9. Voting Cycles

   A. Use a three person three possibility matrix to demonstrate the majority rule cycle problem.

   B. Use a three person 2-dimensional issue space to demonstrate that voting cycles are very likely as soon as a second issue dimension is added.

   C. Identify all the Pareto optimal outcomes in "B", and demonstrate that it is possible to get majority approval for moves out of the Pareto set.

   D. Discuss how institutional arrangements can reduce the likelihood of such majority cycles.

   E. Show a three person configuration of ideal points that is cycle free in a 2-dimensional issue space.

10. Agency problems exist whenever an "agent" has interests that differ systematically from those of its "principal."

    A. Under what circumstances might an elected representative have interests that differ from those of the median voter?

    B. How does electoral competition reduce agency problems?

    C. How does rational ignorance increase agency problems?

    D. Are their also agency problems within government?

11. Institutional reform is one possible way of reducing the problems of voter cycles, voter ignorance, and principal agent problems.

    A. Suggest several institutional arrangements which affect voting outcomes.

    B. Discuss alternative methods by which such institutional alternatives might be appraised.

    C. In what ways, if any, are the politics of institutional reform different from that of ordinary legislation?

12. To the extent that policy outcomes reflect an institutionally induced equilibrium of self-interested politically active individuals, policy reform will require institutional reform.

    A. Analyze geometrically the stabilizing effect of voting on issues one at a time.

    - Show that a spatial voting model implies an equilibrium in this case even in two-dimensional policy spaces. Does the order in which issues are voted on matter affect the policy decision?

    B. Now assume that one of the voters (perhaps the leader of the House) can control the order in which policies are voted on.

    - Show the best outcome that he can achieve for him or herself after a series of 3 votes, beginning with a status quo in the Pareto set.
    - Does the distribution of voter preference matter for this result? Can an agenda setter avoid the median voter outcome in a two dimensional issue space? (Assume that voter preferences lie along a straight line.)

    C. Are there any reasons to believe that current policies are not the results of *ordinary* spatial political equilibria? Why or why not?

13. Under proportional representation (PR), the legislature is composed of candidates selected from party lists in proportion to the number of votes received by the political parties.

    A. How does the median PR legislator's preference differ (if it does) from that of the median voter?

    B. How does the number of political parties represented in parliament differ from that of a plurality (first past the post) system like that of the United States?

    C. How does the effect of party discipline differ in plurality and PR systems? (Illustrate these differences with a diagram.)

14. Suppose that instead of an elected median voter government, an individual is randomly picked from the population as a whole and appointed dictator for life.

    A. Discuss reasons why a revenue maximizing dictator might provide public services.

    B. Assume that the public service increases the size of the tax base at a decreasing rate (MB), and expenditures on the public service reduce the dictators possibilities for private consumption (MC). Use a diagram to show the Dictator's preferred service level.

    C. Discuss changes in a Dictator's circumstances that might cause him to increase this service level.

    D. How would the policies of a randomly chosen dictator with one year terms differ from a dictator appointed for life? Explain your reasoning.

15. Almost all government policies are implemented by unelected employees of national, regional, and local governments.

A. Use marginal cost and marginal benefit curves to characterize bureaucrat's decision to implement a particular policy in a case without agency problems and with agency problems.

B. Explain how "agency incentives" and selection processes will affect the magnitude of agency problems within a bureaucracy.

C. Niskanen developed a particular form of agency problem. Use marginal benefit and marginal cost curves to depict the "all or nothing" budget of a budget maximizing bureaucrat.

D. Explain how conditional budgets can be used to solve (some) agency problems, and discuss the limits of this method of management.