

14335.0024: The Political Economy of Public Finance in Developing Countries

Wednesdays, 12:00-13:30
6 ECTS points (PO2008/09)/9 ECTS points (PO2015)

203 Gottfried-Keller-Str. 6
Room No.: 2
50931 Köln

Compact session: Saturday June 11th, 10:30am-18:30pm
100 Hauptgebäude
Hörsaal VIIa

Lecturers:

Dr. Sarah Berens, University of Cologne
Armin von Schiller, German Development Institute (DIE), Hertie School of Governance

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Preliminary

Outline of the Course

In this course we study challenges and obstacles for public finance in developing countries from a political economy perspective. We investigate the political and economic foundations of public revenue and expenditures and apply these insights to the context of less developed states. Public revenue refers to taxation (personal income tax, value added taxation, etc.) but also non-tax revenue such as foreign aid and rents from natural resources such as oil. It is vital to finance common goals as a society. Public expenditures, on the other hand, are needed to finance poverty reduction and the welfare state, public infrastructure, social order and public well-being. While researchers of public finance in high-income democracies are concerned with questions such as a tax increase or more or less expenditures for particular social policy programs, developing countries face questions that are much more substantial: Why is there so much tax evasion in developing countries and how can the informal economy be reduced? How to create a fiscal contract between voters and politicians when corruption is widespread? How does foreign aid affect political accountability and the incentive structure of politicians to pursue representation of the electorate? Why do countries that are rich in natural resources and lootable goods lack behind in terms of democratic quality?

In order to study these questions we will look at the incentive structure of relevant actors (e. g. politicians, voters, parties, public administrations, international donor community etc.) and their pay-off matrices.

In the first part of the seminar **(I)** we focus on the origins of the modern state and the evolution of tax systems. We read classical texts to discuss general theories of fiscal contracts and role of institutions for public choices. We take a first look at fiscal challenges of developing countries by studying how globalization and international markets affect local budgets in less developed states. In the second part **(II)** we take a closer look at political determinants of fiscal policies. Political parties pursue a variety of strategies to appeal to voters. We investigate how parties reconcile budgetary constraints with political goals and their aim for office. The third part **(III)** of the seminar is devoted to micro foundations of public finance, asking which factors determine preferences for redistribution, taxation and tax compliance in general. In the last part of the seminar **(IV)** we focus on the fiscal and political effects that international development cooperation and non-tax revenues in form of natural resources or foreign aid have in developing countries.

The goal of the seminar is to establish a genuine understanding of the political economy of fiscal policies in less developed states. The seminar provides participants with a broad set of classical political economy theories (with a strong emphasis on micro theories), examples from the research frontier on comparative political economy, development economics, public finance and a range of research designs and methodological approaches to draw upon for own research in this field.

Prerequisites

A good knowledge of general political science concepts, theories and basic quantitative and qualitative methods is required. Students should be able to understand and articulate themselves in English as this will be the general classroom language. Of course, perfection is not required but you should be able to make yourself understood. The term paper should be written in English as well.

Requirements

The sessions in class are designed as a very participatory seminar format. This means that the class also depends on your in-class participation. Each participant will prepare a **10 to 15 minutes presentation** based on additional material or own research on one of the seminar topics. In order to ensure the quality of participation we expect you to have prepared the required readings prior to class and to attend all meetings. The required reading is indicated as such, but you will also find *recommended* readings which are not required for class. The recommended readings list only serves as orientation in case that you intend to delve deeper into the particular research topic. A **reader with the required texts** for the sessions of the seminar can be bought at Copy Star (Zülpicher Straße 184, 50937 Cologne) at the beginning of April.

The **term paper** should bear on the themes discussed in class, be empirical in nature and contain no more than 6.000 words (approximately 15-20 pages). You should be clear about your theory, data and methodological approach. It is vital to develop a clear research design that supports your analytical interest. First ideas on the research question and the basic methodological approach for the term paper have to be submitted in form of a **one-page outline by June 29th** as PDF to the lecturers. The final term paper is due on **August 31st 2016** (24:00). Please submit your paper electronically as a PDF document to

sarah.berens@uni-koeln.de. Late papers will be punished. The final grade is composed of the term paper, in-class participation and the individual presentation.

In addition to the electronic paper version (which will be checked for plagiarism), please submit a paper version in the course of the week of the due date at the secretary of the [CCCP](#) (please check our homepage for opening hours). **The paper version must contain the following signed statement:**

http://www.cccp.uni-koeln.de/fileadmin/wiso_fak/cccp/Lehre/ErklaerungzuArbeiten.pdf

Registration

Please register via KLIPS. If you cannot use KLIPS, please register by sending an email to sarah.berens@uni-koeln.de and armin.schiller@die-gdi.de.

Basic Reading Recommendations (optional)

Acemoglu, D. and J. Robinson (2005) *The Economic Origins of Dictatorship and Democracy*. Cambridge: Cambridge University Press.

Humphreys, M. and Weinstein, J. M. (2009) Field Experiments and the Political Economy of Development. [American Review of Political Science](#).

S. Gupta, B. Clements and G. Inchauste, "Fiscal Policy for Economic Development," in *Helping Countries Develop: The Role of Fiscal Policy* (Washington, DC: International Monetary Fund, 2004), pp.1-22.

I FUNDAMENTALS

13.04.2016

1. Introduction

S. Gupta, B. Clements and G. Inchauste, "Fiscal Policy for Economic Development," in *Helping Countries Develop: The Role of Fiscal Policy* (Washington, DC: International Monetary Fund, 2004), pp.1-22.

20.04.2016

2. Origins of the modern state:

North, D. and B. Weingast. 1989. "Constitutions and Commitment: The Evolution of Institutions Governing Public Choice in Seventeenth Century England," *The Journal of Economic History* XLIX(4): 803-832.

Tilly, C. 1992. *Coercion, Capital, and European States: Chapter 3* (pp. 67-95).

Recommended:

- Besley, T. and Persson, T., 2009. The Origins of State Capacity: Property Rights, Taxation, and Politics. *American Economic Review*, 99(4), pp. 1218–44
- Moore, M. (2008), *Between Coercion and Contract: Competing Narratives on Taxation and Governance*, in D. Brautigam, O. Fjeldstad & M. Moore, eds,

'Taxation and State-Building in Developing Countries', Cambridge University Press., Cambridge, United Kingdom, pp. 34–63.

27.04.2016

3. Origins of tax systems

Mares, I. and D. Queralt. 2015. "The Non-Democratic Origins of Income Taxation." *Comparative Political Studies*. 48(14): 1974- 2009

Scheve, K. and D. Stasavage. 2010. "The Conscription of Wealth: Mass Warfare and the Demand for Progressive Taxation." *International Organization* 64(4):529–561.

Recommended:

- Beramendi, P. and D. Queralt (2015) "The Electoral Origins of the Fiscal State." Working Paper.
- Ardanaz, M. and Scartascini, C. (2013) "Inequality and Personal Income Taxation: The Origins and Effects of Legislative Malapportionment". *Comparative Political Studies*, 46(12), 1636–1663.

04.05.2016

4. The fiscal challenges of developing countries

Wibbels (2006) "Dependency revisited: International markets, business cycles, and social spending in the developing world." *International Organization* 60: 433-468.

Aizenman, J. & Jinjarak, Y. (2009), "Globalisation and Developing Countries- a Shrinking Tax Base?", *Journal of Development Studies* 45(5), 653–671.

Recommended:

- Bird, R. M., Martinez-Vazquez, J. and Torgler, B., 2008. Tax Effort in Developing Countries and High Income Countries: The Impact of Corruption, Voice and Accountability. *Economic Analysis and Policy*, 38(1), pp. 55-71.
- Besley, T. and T. Persson, "Why Do Developing Countries Tax So Little?" *Journal of Economic Perspectives*, Vol. 28, No. 4 (2014), pp. 99-120.

II POLITICAL DETERMINANTS OF FISCAL POLICIES

11.05.2016

5. Political institutions and policy making

Scartascini, C., E. Stein and M. Tommasi (2013) "Political Institutions, Intertemporal Cooperation, and the Quality of Policies". *Journal of Applied Economics* 16(1): 1-32.

Brender, A., and A. Drazen. (2005). "Political budget cycles in new versus established democracies." *Journal of Monetary Economics* 52(7) 1271-1295.

Recommended:

- Hallerberg, M., C. Scartascini, and E. Stein. (2009). "The Budget Process as a Political Arena" in Hallerberg, Mark, Carlos Scartascini, and Ernesto Stein (Eds).

- Who Decides the Budget. Inter-American Development Bank and David Rockefeller Centre for Latin American Studies (Harvard University Press): 295 -318.
- Shi, M., and J. Svensson. (2006) "Political budget cycles: Do they differ across countries and why?" *Journal of Public Economics* 90.(8)1367-1389.

18.05.2016

No class! Ascension Day Week!

25.05.2016

6. Party politics and fiscal policies

- Beramendi, P. and D. Rueda. (2007). "Social Democracy Constrained: Indirect Taxation in Industrialized Democracies." *British Journal of Political Science* 37: 619–641.
- Timmons, J. F. (2010), "Taxation and Credible Commitment: Left, Right, and Partisan Turnover", *Comparative Politics* 42(2): 207–227.

Recommended:

- Hart, A. (2010). "Death of the Partisan? Globalization and Taxation in South America, 1990—2006." *Comparative Political Studies* 43.3: 304-328.
- Hanusch, M., and P. Keefer. (2014) "Younger parties, bigger spenders? Party Age and Political Budget Cycles." *European Economic Review* 72: 1-18.

01.06.2016

7. Regime type and public spending

- Harding, R. and D. Stasavage. (2014). "What Democracy Does (and Doesn't Do) for Basic Services: School Fees, School Inputs, and African Elections." *Journal of Politics* 76: 229–245.
- Lake, D. A. and M. A. Baum. 2001. "The Invisible Hand of Democracy." *Comparative Political Studies* 34(6):587–621.

Recommended:

- Kenny, L. W. and Winer, S. L., (2006). "Tax Systems in the World: An Empirical Investigation into the Importance of Tax Bases, Administration Costs, Scale and Political Regime." *International Tax and Public Finance* 13(2): 181-215.
- Cheibub, J. A., (1998). "Political regimes and the extractive capacity of governments: taxation in democracies and dictatorships". *World Politics*, 50(3):349-376.

08.06.2016

8. Ethnicity and public spending

- Horowitz, D. 1986/2000. *Ethnic Groups in Conflict*. Chapters TBA (1-2, or 3-4).
- Kasara, K. (2007) "Tax me if you can: Ethnic geography, Democracy, and the Taxation of Agriculture in Africa." *American Political Science Review* 101.01: 159-172.

Recommended:

- Chandra, K. (2006). “What is Ethnic Identity and does it Matter?” *Annual Review of Political Science* 9: 397-424.
- Gisselquist, R. M., S. Leiderer, M. Niño-Zarazúa. (2016) Ethnic Heterogeneity and Public Goods Provision in Zambia: Evidence of a Subnational “Diversity Dividend”, *World Development*, 78: 308-323.

III. MICRO FOUNDATION OF PUBLIC FINANCE

11.06.2016 (Saturday! 10:30-18:00)

9. Preferences for Redistribution

Shayo, M. (2009). “A Model of Social Identity with an Application to Political Economy: Nation, Class, and Redistribution.” *American Political Science Review* 103: 147–174.

Dion and Birchfield (2012) Economic Development, Income Inequality, and Preferences for Redistribution. *International Studies Quarterly* 54: 315-334.

Recommended:

- Beramendi, P. and Rhem, P. (2015) Who Gives, Who Gains? Progressivity and Preferences. *Comparative Political Studies*. Online first.
- Barnes, L. (2015) ‘The Size and Shape of Government: Preferences over Redistributive Tax Policy’, *Socio-Economic Review*, 13 (1): 55-78.

11.06.2016 (Saturday! 10:30-18:00)

10. Tax Compliance

Alm, J., McClelland, G. H. and Schulze, W. D. (1992) ‘Why Do People Pay Taxes?’, *Journal of Public Economics*, 48(1),:21–38.

Timmons, J. F. (2005). “The Fiscal Contract: States, Taxes, and Public Services.” *World Politics* 57: 530–567.

Recommended:

- Torgler, B. (2005) ‘Tax Morale in Latin America’, *Public Choice*, 122(1), 133–157.
- Castro, L., and C. Scartascini (2015). "Tax Compliance and Enforcement in the Pampas: Evidence from a field experiment." *Journal of Economic Behavior & Organization* 116: 65-82.

IV. THE ROLE OF NON-POLITICAL ACTORS AND OTHER SOURCES OF STATE REVENUE

11.06.2016 (Saturday! 10:30-18:30)

11. The fiscal effects of foreign aid

Remmer, K. (2004), Does foreign aid promote the expansion of government? *American Journal of Political Science*, 48, 1: 77–92.

Morrissey, O. (2014). Aid and Fiscal Behaviour: What does the Evidence Show? *World Development*. 69: 98-105

Recommended:

- Easterly, W. 2003. "Can Foreign Aid Buy Growth?" *Journal of Economic Perspectives* 17(3): 23-48.
- Mosley, P. (2015), 'Fiscal Composition and Aid Effectiveness: A Political Economy Model', *World Development* 69, 106 – 115.

11.06.2016 (Saturday! 10:30-18:30)

12. The political effects of foreign aid

Eubank, N. (2012). "Taxation, political accountability and foreign aid: Lessons from Somaliland". *Journal of Development Studies*, 48(4), 465–480.

Baskaran, T. 2014. "Taxation and democratization". *World Development* 56: 287-301.

Recommended:

- Bermeo, S. B.. (2011). "Foreign Aid and Regime Change: A Role for Donor Intent" *World Development*, 39 (11): 2021-2031,
- Moore, M. (2004): "Revenues, state formation, and the quality of governance in developing countries." *International Political Science Review* 25(3) 297-319.

15.06.2016

No class!

22.06.2016

No class!

29.06.2016

14. The Resource Curse

Bates, R. (2008) *When Things Fell Apart: State Failure in Late-Century Africa*. Cambridge University Press (pp. 3-129).

Recommended:

- Morrison, K. M. "Oil, nontax revenue, and the redistributive foundations of regime stability." *International Organization* 63.01 (2009): 107-138.
- McGuirk, E. F. (2013): The Illusory Leader: Natural Resources, Taxation and Accountability, in: *Public Choice* 154 (3-4), 285-313. –

06.07.2016

14. Final Discussion

Hallerberg, M., and C. Scartascini (2015). "Explaining Changes in Tax Burdens in Latin America: Does Politics Trump Economics?". Inter-American Development Bank Working Paper, No. 613.