WWS 593j: Combining Theory and Data to Evaluate Policy

Princeton University
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Fall 2019, Session II
237 JR Rabinowitz Building
W 7:00pm – 10:00pm
(With exception that class on 11/13 will take place on 11/12 from 4:30pm-7:30pm and class on 12/11 will take place 12/10 from 4:30pm-7:30pm.)
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(subject: WWS593j)

Overview

Many key policy debates, including raising top taxes, EITC expansion, and health insurance reform, involve assessing how policy changes would affect economic activity, government budgets, and the distribution of resources. This course will explore several policy areas and focus on applied economic and empirical methods to show how economists combine theory and data to evaluate such policies. The goal is to enhance applied modeling skills and provide students with methods and practical examples of how these policies are evaluated in agencies such as the Congressional Budget Office, the Joint Committee on Taxation, the US Treasury, and state- and municipal-level economic development agencies.

After illustrating how these approaches apply to inequality and intergenerational mobility and covering key applied tools, we will evaluate local economic development policies, the Tax Cuts and Jobs Act, Ultra-millionaire wealth taxation, enhancing the EITC, raising top taxes, and other policies. For each policy, we will usually start with applied theory of how the policy change could affect behavior, and then turn to how to structure the empirical analysis in light of the theory, estimate effects and important parameters, and then assess policy implications.

Course Outline (subject to change)

1. Combining theory and data to understand inequality and intergenerational mobility
   a. Topics: market and non-market causes of inequality, intergenerational mobility, pay disparities
   b. Methods: linking applied theory to regression, elasticities, calibration, potential outcomes and selection, Roy models, decomposition techniques

   a. Topics: translating estimates of the causal effects of policies into welfare analyses, asymmetric information and adverse selection in health insurance, value of public programs, safety net take up
   b. Methods: discrete choice, treatment effect heterogeneity, counterfactuals, envelope theorem, marginal value of public funds

3. Local economic development and place-based policies
   a. Topics: regional disparities, empowerment zones, local business tax incentives, migration decisions, firm location, state and local fiscal policy
   b. Methods: local labor market models, event studies, revenue estimation, minimum distance
   a. Topics: growth, revenue, and distributional effects of tax changes, corporate
taxation and investment, wealth disparities, tax avoidance, mechanical and
behavioral responses
   b. Methods: investment models and user cost of capital, revenue scoring,
distributional analysis, mechanical and behavioral effects

5. Raising Top Taxes, Expanding the EITC, Raising the minimum wage
   a. Topics: labor force participation, labor supply models, mechanical and behavioral
responses, minimum wage
   b. Methods: Using individual-level data and simulation to do revenue scoring,
distributional analysis, behavioral responses, using structural methods to model
the effects of new policies, difference in difference in practice

**Office Hours:**
Office hours will be by appointment.

**Grades:**
The course grade will be determined as follows:

- Weekly participation: 15%
- Four small group problem sets: 60%
- Final small group empirical project: 25%

**Course Format and Requirements:**
The first class will describe the course, illustrate how to connect theory and data to analyze
policy issues, and then provide an introductory discussion of recent theory and evidence on
inequality and intergenerational mobility. Starting with the second class, each class will begin
with a discussion of the following week’s problem set, and then move on to that week’s content.

**Participation**
Attendance and participation in class discussion are important components of the class. Students
are expected to come to class having read and thought about the materials and problem set.

**Four problem sets (small groups of three or fewer students)**
Every week at the start of class will begin with a review of a problem set (due at midnight the
day before class). Here’s an outline of the problem set topics (subject to change):

1. After the first class, use decomposition techniques to analyze the gender wage gap or
geographic disparities in wages. Due midnight the night before the 2nd class.
2. Use discrete choice to analyze labor force participation decisions or 2016 voting
decisions (or polling for the 2020 primary candidates pending data availability)
3. Million dollar plants or tax revenue/distributional effects of raising state corporate taxes
4. How much revenue would the Warren and Sanders wealth tax raise?

**Problem set presentation**
Starting with the second week of class, each class session will have one group of students jointly lead a discussion of the problem set by presenting their analysis and bringing up points of discussion. We will schedule these during the first week of class at the break.

Final empirical project due at the end of the term (small groups of three or fewer students)
Each student (group) will conduct an empirical analysis of one of the topics listed below. The empirical project will consist of a write up of their results with supporting tables and figures. The topic must be different than the topics that each student selected to work on for the problem sets (there is some overlap in topics). Here are potential topics (subject to change):

1. How much tax revenue could be raised by taxing the rich?
2. Does the EITC pay for itself?
3. How would median worker compensation (wages + benefits) have evolved if health care costs grew with inflation? Or if healthcare costs were Medicare costs per beneficiary adjusted for demographic and cost differences?
4. Tax Reform
   a. What are the revenue, growth, and distributional effects of raising capital gains taxes to personal income tax rates?
   b. What are the revenue, growth, and distributional effects of eliminating step up basis at death?
   c. What are the revenue, growth, and distributional effects of extending the EITC to childless adults?
   d. What are the revenue, growth, and distributional effects of the LIFT ACT which makes EITC more generous?
5. How much would New Jersey have to raise taxes or cut spending to prevent it’s pension obligations from growing as a share of GDP?
6. What are the effects of building a stadium for local economic growth?
7. How much growth since 1980 went to the top 1% (using panel data rather than repeated cross sections)? How does this vary by type of income? How do health benefits fit in?
8. How much does each state collect in federal tax revenue and how much does it receive in federal spending? How does that vary by tax and program? How has that changed overtime?
9. How will changing demographics affect social security and Medicare revenues and expenditures in the coming decades?
10. How progressive are state+local+federal taxes in the US (measured as tax liability/national income) in recent years? How has this varied over time and by program?
11. Other topics (approval from instructor required)

**Lecture Schedule and Readings (subject to change):**

**Week 1: Inequality and Intergenerational Mobility**


**Week 2: Applied Tools for Policy Evaluation and Welfare Analysis**


Week 3: Local Economic Development and place-based policies


https://www.aeaweb.org/articles?id=10.1257/aer.20141702

https://eml.berkeley.edu/~pkline/papers/TVA_web.pdf


Supplemental:


**Week 4: Capital Tax Reform – Tax Cuts and Jobs Act, Wealth Taxation, Capital Gains**


Joint Committee on Taxation, December 2017.
- Macroeconomic Analysis Of The Conference Agreement For H.R. 1, The "Tax Cuts And Jobs Act"
- Distributional Effects Of The Conference Agreement For H.R.1, The "Tax Cuts And Jobs Act"
- Estimated Budget Effects Of The Conference Agreement For H.R.1, The "Tax Cuts And Jobs Act"
- [https://www.jct.gov/publications.html?func=select&id=76](https://www.jct.gov/publications.html?func=select&id=76)


Sarin, Natasha and Larry Summers, 2019, “Be very skeptical about how much revenue Elizabeth Warren’s wealth tax could generate” Washington Post


https://www.aeaweb.org/articles?id=10.1257/jep.29.1.47


Joint Committee on Taxation, 2015, “History, Present Law, and Analysis of the Federal Wealth Transfer Tax System,”
https://www.jct.gov/publications.html?func=startdown&id=4744


Week 5: Raising Top Taxes, Expanding EITC, and time permitting Raising the Minimum Wage


