

**Economics 849  
Public Finance  
Fall Semester 2009  
Tuesdays 1630-1910  
Robinson Hall A250**

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This course brings a catallactical-institutional orientation to bear on the theory of public finance. The course text is my *Fiscal Sociology and the Theory of Public Finance*, which is now available in paperback. The course will *not* proceed by reviewing what I wrote there; instead it will use that material as a point of departure for exploring public finance through a different window, to recall Friedrich Nietzsche. The book's subtitle describes it as "An Exploratory Essay." In his review of the book [*Quarterly Journal of Austrian Economics* 12 (2009): 88-94][[http://mises.org/journals/qjae/pdf/qjae12\\_1\\_9.pdf](http://mises.org/journals/qjae/pdf/qjae12_1_9.pdf)], Adam Martin took issue with my designation, saying that "it reads more like a manifesto for a budding research program than an exposition of particular propositions." Martin also closed his review by asserting that "the good news for young scholars seeking inspiration is that its [the book's] ideas tend to be more under- than over-developed." I hope you will find Martin's judgment to have been accurate; in any case, the accuracy of that judgment is something each of you will be able to test for yourself.

If we were playing music, I would like us to resemble a jazz quintet where I insert some riffs here and there, more than a sympathy orchestra where I would be the conductor. What I mean by this is that I do not aspire to have everyone on the same page, so to speak. Useful learning, which in my judgment is learning that leads to new articulations and publications, comes through wrestling with differences that we confront; I like classroom settings where those differences are in play. For this reason, I try systematically to err on the side of under-specifying your reading. I will suggest a few items below, but I also encourage you to create your own readings in light of your particular interests, and then seek to address what you get from those readings in light of the course material.

A few items are listed after the course schedule. These are all books that treat broad themes related to the course material, and each is available in paperback. While I hope that you will examine some of these, I also hope you read other materials as well and, more significantly, mix those readings with your own imaginations to generate new insights that might lead to interesting places. Students become accustomed to reading published work with an eye to taking exams. While I recognize that exams are part of our educational system, though not in this course, I suggest you cultivate the practice of reading with an eye that continually is looking for new ideas that you can articulate, as against absorbing old ideas that you can recollect.

With respect to our work over the semester, let me offer two quotes for you to keep with you on your journey: they should stand you in good stead.

- The first is buried in my long ago past. I believe I read it in reference to Isaac Newton, but I wouldn't swear by this. The quote, as I recall it, goes: "To see what all have seen; to say what none have said." This is mostly what I think we are trying to do in escaping the shackles of conventional thought. The phenomena are in front of us, plain to see, but we have to articulate them differently. After all, Archimedes most certainly was not the first person to have taken a bath.
- The second comes from Albert Einstein via Roger Koppl. The quote goes: "If we knew what we were looking for, we wouldn't call it research, would we?" If you feel confident about where you are heading before you start writing, you might be doing journalism but you aren't doing research. You need to learn to live with the ambiguity that the quote implies; indeed, you should learn to revel in that ambiguity, for only in the presence of such ambiguity is it possible that you are traveling someplace different.

After a preliminary session on 1 September, the remainder of the semester's work is divided into six units of two weeks each. Each of us will have work to do for each of those units. Most of my work will take place during the first session of the unit, while most of your work will take place during the second session. My work will be of two forms: (1) a review some of the background and the penumbra of associated ideas that are in play (though not engaging simply in presenting an alternative rendition of standard textual material, for this you can, and should, read on your own); (2) a submission of some written material relating to some ideas that I am presently wrestling with.

Your work for those second sessions will involve written submissions and oral presentations. A large number of conferences each year are organized where open invitations are posted for people to submit proposals to present papers. In a few instances those conferences request the submission of draft papers, but in most cases what is requested is a short proposal. For each of the six units, I will assume the position of conference organizer and send you a call for proposals. You will have a week to prepare your proposals, which you will submit at the end of the second session. You should also be prepared to present and discuss your proposal during that session. Soon thereafter, I will send you my evaluation of your proposal.

These six essays collectively will count for 40 percent of your course grade. My standard of grading will be that of a conference organizer who is looking for creative and thoughtful work, particularly work that contains surprises

in contrast to well-constructed work that nonetheless has a pedestrian quality. A grade of A indicates that if I would invite you to present the paper. A grade of B indicates that I wouldn't invite you but that I acknowledge that the proposal exhibits decent understanding and workmanship all the same (but it doesn't contain imagination-induced surprises). A grade of C is a residual category whose meaning you can infer (and with a grade of F being attached to no-shows and their equivalents). While I think in this discrete fashion, almost invariably there will be cases that hover near some borderline which compel me to affix a plus or a minus to the grade. These essays should be a maximum of three pages of text in standard manuscript format, followed by a bibliography of between three and seven references that testify further about your thinking on the topic.

Another 40 percent of your course grade will be given for my judgment about the quality of a research paper you will write. The same publication-based grading framework will apply to these papers as I will apply to your shorter essays. This paper should not exceed 20 pages of text when submitted in standard manuscript format (double spacing, normal margins, etc.). For this assignment you should think of me as the editor of a *Handbook of Enterprise-Based Public Finance*, where I have issued a call for contributions. What I mean by enterprise-based public finance should be clear from my book and the first few class sessions. It's even possible that such a project might well materialize before too long, as Giuseppe Eusepi, of La Sapienza University of Rome, and I are pursuing a project on enterprise-based public finance.

The final 20 percent of your course grade will depend on my evaluation of your contributions to classroom discussion throughout the semester. With respect to classroom discussion, many of you are doubtlessly aware that typically I use the last few weeks of the semester to run mini-seminars on research papers; however, too many of you are registered this semester for me to do that. To some extent I have compensated for this by allowing for a greater volume of presentations of your ideas during the semester, but I recognize that this is not a perfect substitute for presenting a research paper.

## **Course Schedule**

### **Unit 0: 1 September**

*Alternative Frameworks for Public Finance*: FSTPF, Chapter 1

The point of this unit is simply to provide intellectual orientation for the remainder of the semester. The contemporary theory of public finance is heavily normative in its orientation, and with the work done through choice theoretic modeling of equilibrium states. The theory is used to address questions like how much should a government spend on education. The alternative theoretical framework

I pursue asks instead questions like how much will a government spend under alternative institutional arrangements, along with a whole plethora of questions that arise once you try to give a bottom-up, emergent account of the continual evolution in patterns of collective activity.

**Unit #1: 8 & 22 Sept.** [I will be away on 15 September]

*Society, Market, State, and Property Rights:* FSTPF, Chapters 2 & 3

Carl Menger argued that property rights, markets, and polities all originate in scarcity and the potential conflict that looms. This insight suggests an orientation toward public finance quite different from the standard Anglo-Saxon orientation wherein states are presumed to operate orthogonally to markets. What is called for, I believe, is ultimately a different articulation of the theory of property rights, which can be seen by reflecting on the common roots of property and propriety, by reflecting on what it means to treat economics truly as a social science as distinct from a science of household conduct or rational action, and by exploring the tangled relationship between conflict and cooperation and between markets and states.

**Unit #2: 29 Sept. & 6 Oct.**

*Politics, Entrepreneurship, and the Ecology of Enterprises:* FSTPF, Ch. 4

The theory of public finance typically embraces a theoretical antinomy wherein market activities are spontaneously ordered through entrepreneurial action while collective activities are organized through planning. This unit will pursue an alternative orientation where polities themselves are represented by an ecological configuration of enterprises that are generated through entrepreneurial activity, and with relationships among those enterprises often being intensely competitive. In other words, a polity is characterized not as a single enterprise but as a collection or order of enterprises: a polity, too, more fully resembles a jazz quintet than a symphony orchestra.

**Unit #3: 20 & 27 Oct.** [No class 13 October for Columbus Day holiday]

*The Economic organization of political enterprises:* FSTPF, Ch. 5

While the establishment of an enterprise reflects some form of entrepreneurial vision, any such enterprise must confront a variety of challenges that are present in any framework of team production. Among other things, problems of agency must be dealt with, cash flows must be generated and distributed, and dispersed knowledge must be assembled and put to use. For market-based enterprises, the presence of transferable ownership does a good deal of work in securing well-working teams. For politically-based enterprises, ownership is not

transferable so a different approach must be taken to the organization of team production.

**Unit #4: 3 & 10 Nov.**

*Revenues, Expenditures: Bridging the Budgetary Gap:* FSTPF, Ch. 6

I have described a parliamentary assembly as a peculiar investment bank, though I would also note that I think that all modern polities face pretty much the same budgetary setting. Somewhere I recall Joseph Schumpeter describing a state's budget as pointing to its essence once the accompanying ideological cant had been stripped away. While plenty of ideological cant accompanies democratic regimes, similar cant accompanies other regimes as well. In this vein, Carolyn Webber and Aaron Wildavsky, in their lengthy treatment of budgetary history, described budgeting as an on-going conflict among people over how they are to live together. This unit will seek to take that peculiar investment bank analogy further than it has been taken so far by exploring the positive theory of budgetary processes.

**Unit #5: 17 & 24 Nov.**

*Federalism and intergovernmental relations:* FSTPF, Ch. 7

Most work in public finance treats government as a single entity. It is rare, however, that a person faces a single government. The more common situation is to face a multiplicity of governments, each with some ability to tax, spend, and regulate. Governments and their enterprises come continually into contact with one another. This situation likewise characterizes market-based firms, only the institutional frameworks within which agreements are made and conflicts settled (or not) differ. I would note also that I regard relationships among national units of government as much a suitable subject of examination as relationships among governments within a nation.

**Unit #6: 1 & 8 Dec.**

*Constitutional Foundations of Public Finance:* FSTPF, Ch. 8

The title of Ch. 8 is "Fiscal Sociology and the Challenge of Societal Agriculture," but I regard the material as the same despite the difference in titles. In any case, almost all of the contemporary theory of public finance has been written from a normative orientation of seeking to advise or tell governments what should be done to achieve some end. In contrast, I am emphasizing positive analytical issues. It is also the case that positive analysis can carry normative oomph, often more strongly when it is not couched in directly normative language. Ludwig von Mises on several occasions said something to the effect that if you

wanted peace and prosperity embrace capitalism, while if you wanted famine, pestilence, destruction, and death, embrace socialism [at this point, though, you might want to recall G. B. Shaw: “a socialist is a communist who lacks the courage of his convictions”]. In doing this, Mises was stating a purely positive conclusion of economic analysis and not making a normative argument. Something similar is my object of aspiration in this unit.

### **A Few References** (all available in paperback, I believe)

1. John Cullis and Philip Jones, *Public Finance and Public Choice*. I used the second edition of this book when I last taught this course in 2000. Originally, I thought I would use this book again this semester, for the book presents a reasonably polyphonic treatment of two approaches to public finance. In the end I decided not to do this because I couldn't resolve my quandary about what book actually to order. The second edition is fine, but the publisher has announced a third edition, only it's not available as of this writing so I haven't seen it. The publisher announces that the third edition is both longer and cheaper than the second edition. Being cheaper is a benefit (\$70 vs. \$89). Being longer is ambiguous; I'd have to take a look to make a judgment. I have seen a number of cases where the longer, revised edition is worse in my judgment, typically because the initial integrity of the volume has been compromised by inserting additional material, often in response to suggestions by outsiders. I did note that Amazon contains a number of used copies, though my recollection is that the number was less than the number of you signed up for this class. So I abandoned my thought of adopting the book; nonetheless, I would recommend it (the second edition anyway) to anyone who wanted a solid survey of orthodox public finance, written by authors who are not wholly captivated by the orthodox formulations.

2. James M. Buchanan, *Public Finance in Democratic Process*; James M. Buchanan, *Demand and Supply of Public Goods*. These books were originally published in 1967 and 1968 respectively, well before such fields as public choice and constitutional economics appeared on the intellectual landscape. These books are now available inexpensively from Liberty Fund. These books sought to pursue a positive theory of public finance at a time when the intellectual environment was much more hostile to such efforts than it is now. Buchanan's work subsequently moved in a more normative and constitutional direction. On several occasions, I have thought of *Fiscal Sociology and the Theory of Public Finance* as an effort to bridge a 40-year gap in the articulation of an alternative vision for a theory of public finance. I now look on these books more for the inspiration and orientation they provide than for their substantive content.

3. Jane Jacobs, *Systems of Survival: A Dialogue on the Moral Foundations of Commerce and Politics*. This small book is pertinent for both the first and the last units. The book unfolds as a dialogue among several characters over the claim

that human action and social life involves a continuing contest between two moral syndromes, which she labels as commercial and guardian. She also explores what she calls “monstrous hybrids.” The control of such hybrids points in a constitutional direction, which would make the book relevant for the last unit, but it is also relevant for the market-state relationship that is explored in the first unit.

4. With respect to the first unit, let me also mention Norbert Elias’s *The Society of Individuals*. Elias was a sociologist from the early to middle 20<sup>th</sup> century who worked with notions of spontaneous order (which have been pretty much absent from sociology for a good half-century, though a revival seems in the offing), and who was deeply thoughtful about the reciprocal character of the I-We relationship. He is best known for *The Civilizing Process*, which is much longer and which is a spontaneous order treatment of the evolution of manners. Elias was displaced to London in the 1930s, where he roomed with Asik Radomysler, who died way too young, having published but one paper, in *Economica* in 1946, and which I commend strongly to all of you.

5. Gordon Tullock, *The Politics of Bureaucracy*. This book is available inexpensively through Liberty Fund as an item in Tullock’s Collected Works. While the subject is bureaucracy and team production, Tullock is not concerned to develop comparative static statements about equilibrium conditions. Rather, he is concerned to explain the characteristic features of team production processes in the absence of market prices and firm values, and to do so within an environment where there is rivalry within organizations and not just rivalry among organizations. In other words, Tullock’s theory of bureaucracy is situated within a treatment of polities as orders and not as organizations.

6. Dirk Kraan, *Budgetary Decisions: A Public Choice Approach*. This book seems to me to be overly technical and excessively enamored with some formal representations, but it is nonetheless a serious effort to deal with budgeting from within a public choice orientation toward the material; moreover, it is written by someone who has participated actively in these processes in The Netherlands. Budgeting has been neglected within public finance because of the dominance of the choice-theoretic and planning orientation. Within a polycentric and emergent orientation, however, budgeting and budgetary processes will come to command increasing attention.

7. Walter Hettich and Stanley Winer, *Democratic Choice and Taxation*. This book seeks to explain tax structures as equilibrium responses to competition among competitions within a framework of probabilistic voting. My attitude toward this book is similar to my attitude toward Kraan’s book: it presents a variety of interesting topics to think about while inspiring me to search for alternative lines of formulation.

8. Vincent Ostrom, *The Political Theory of a Compound Republic*. With a unitary government you face only a single entity that can tax and regulate you; with a federal system of government, you face multiple entities that can act independently to tax and regulate you. How is this multiple jeopardy a good thing, a person might reasonably wonder. Ostrom seeks to answer this type of question here by addressing the architectural framework of the American constitutional founding in light of some central ideas of public choice. In this regard it is interesting to note that when Buchanan and Tullock wrote *The Calculus of Consent*, they regarded themselves as doing little more than laying out in economic-theoretical language the underlying ideas that must have informed the American constitutional founding.

9. Carolyn Webber and Aaron Wildavsky, *A History of Taxation and Expenditure in the Western World*. I would not have mentioned this book except that I referred to it earlier. It's a fine book, full of interesting and thoughtful material. But it's lengthy, about as long as *Human Action*. It also suffers from a problem that seems to plague all such historical surveys: the treatment lengthens as it moves closer to the present (and yet it is the older periods that typically are more shrouded in mystery). It is a history woven around a presumption of societies as arenas of continuing contestation, which I find more appealing and enlightening than presumptions grounded in concord and equilibrium.