

**Public Policy 251**  
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**Fall 2008**  
Monday 2-4  
Room: 355 GSPP

## **MICROECONOMIC ORGANIZATION AND POLICY ANALYSIS**

### **I. OBJECTIVES**

This seminar is designed to enhance skills in conducting public policy analyses of alternative institutional structures based on microeconomic theories. Institutional structure refers generally to the framework, rules, or governing mechanisms under which economic transactions take place. It includes the applicable laws of property and contract, regulations and regulatory bodies, rules affecting government or nonprofit participation as a producer or consumer, and the cultural norms of the society. The analyses are typically of specific sectoral problems within a given economy, like alternative state regulatory methods for the telecommunications industry, or whether or not a school district should contract out for educational services to its students, or whether a water pollution tax should replace technical standards.

The readings stimulate thought along a number of dimensions important to the evaluation of institutional alternatives that arise in actual policy decisions. In the context of specific policy cases, we will examine analyses involving collective demand for public goods, bounded consumer and firm rationality, non-market organizations (bureaus, regulatory agencies, and non-profits), and technical progress in the public sector. Each student will undertake a significant analysis of institutional alternatives in a policy area of his or her choice.

### **II. REQUIREMENTS**

There are two course requirements:

- A. Satisfactory class participation.
- B. One written assignment.

Satisfactory class participation requires regular attendance, reading of assigned materials in advance of class discussion, and occasional responsibility for leading class discussion.

Reading assignments denoted as online without a specific address can be accessed through the UC MELVYL system. Usually the easiest way to find a specific journal article is to use MELVYL's search by journal title and identify the online source that covers the year of the article. Other readings are in a Course Reader, available from Copy Central.

The written assignment is to design and evaluate at least two institutional alternatives for organizing the resource allocation process in any policy area of your choice. One of the alternatives considered should be the status quo.

**You should submit a one-paragraph description of your topic for approval by September 22**, or sooner if possible. The paragraph should state the central problem you wish to consider, at least two policy alternatives, data and information sources you have identified, and academic literature that you expect to be helpful.

Each student will choose some class time to discuss the topic and present her or his work in progress. If class size permits, each student will do this twice: once early in the semester, to discuss the substantive problem and analytic approaches to it, and once later on, to discuss the student's completed first-cut of the analysis (this need not be in written form). The feedback from the later session should be used to revise the analysis before submitting the final version.

**The written assignment is due on or before December 8.** As a rough guideline to length, I would expect most papers to be 15-20 pages (double-spaced). Primary emphasis in grading will be on the treatment of efficiency consequences (although this need not be the primary motivation for the policy). You need not feel that the paper is a complete policy analysis; it can be viewed (if you wish) as the completion of one piece of a larger analysis. I am looking primarily for you to demonstrate substantial insight about the relationship between institutional structure and efficiency.

## READING LIST AND SCHEDULE

### I. INTRODUCTION

#### **WEEK 1: September 8 Course Objectives, Organization, Framework with Education Example**

Friedman, L., "Public Institutional Structure and Resource Allocation: The Analysis of Adjustment," in J. Crecine, ed., Research in Public Policy and Management, Vol. II Jai Press, Inc. (Greenwich, CT: 1981), pp. 303-325.

Murnane, Richard J. and Nelson, Richard R., "Improving the Performance of the Education Sector: The Valuable, Challenging, and Limited Role of Random Assignment Evaluations," Economics of Innovation and New Technology, 16:5, July 2007, pp. 307-322 (available online through MELVYL Informaworld Journals).

#### **WEEK 2: September 15 *Incentives and Privatization as Policies* (Applications: Defense, Job Training, Education, Medical Care)**

Hitch, C. and R. McKean, The Economics of Defense in the Nuclear Age, Part II, "Efficiency in Using Defense Resources," Harvard University Press (Cambridge, MA: 1960), pp. 105-239.

Barnow, Burt, "Exploring the Relationship between Performance Management and Program Impact: A Case Study of the JTPA," Journal of Policy Analysis and Management (JPAM), 19, No. 1, Winter 2000, pp. 118-141 (full text available through MELVYL).

Podgursky, Michael and Matthew Springer, "Teacher Performance Pay: A Review," JPAM, 26(4), Autumn 2007, pp. 909-950 (available through MELVYL Wiley Interscience).

D. Cutler, M. McClellan, and J. Newhouse, "How Does Managed Care Do It?" RAND Journal of Economics, 31, No. 3, Autumn 2000, pp. 526-548 (full text available on ABI/Inform Global database of MELVYL).

Enthoven, Alain C. and Laura A. Tollen, "Competition in Health Care: It Takes Systems to Pursue Quality and Efficiency," Health Affairs (web exclusive), September 7, 2005, W5, pp. 420-433 (available at <http://content.healthaffairs.org/cgi/content/abstract/hlthaff.w5.420v1>).

## II. COLLECTIVE MECHANISMS OF DEMAND ARTICULATION

### A. *Collective Purchase Mechanisms (“Full” Delegation of Individual Consumer Authority)*

#### **WEEK 3: September 22 (Applications: Public Television, Governmental Data Collection)**

Davis, D. and C. Holt, Experimental Economics, Princeton University Press, (Princeton, NJ:1993), pp. 317-350, 360-364, 376-379.

Bohm, P., "Revealing Demand for an Actual Public Good," Journal of Public Economics, 24:2, July 1984, pp. 135-151 (available online through MELVYL ScienceDirect).

Falkinger, J. et al, "A Simple Mechanism for the Efficient Provision of Public Goods: Experimental Evidence," American Economic Review, 90, No. 1, March 2000, pp. 247-264 (available online through MELVYL).

Ferejohn, J., R. Noll, and R. Forsythe, “An Experimental Analysis of Decision-Making Procedures for Discrete Public Goods: A Case Study of a Problem in Institutional Design,” Calif. Institute of Technology, Social Science Working Paper #155, October, 1977.

Friedman, Lee and Rob Letzler, “The Theory and Practice of Public Good Selection: The Case of Legal Aid,” draft presented at the Annual Research Conference of the Association for Public Policy Analysis and Management, Fall 2005 (available online from my website under Public Economics at <http://gsppi.berkeley.edu/faculty/lfriedman/lee-s-friedman>).

### B. *Collective Information, Price, and Product Regulations (“Limited” Delegation of Individual Consumer Authority)*

#### **WEEK 4: September 29 (Applications: Retirement Policy, Higher Education Aid, Energy Consumption, Health Policy)**

##### *Regulatory Process*

Hahn, Robert W. and Paul C. Tetlock, “Has Economic Analysis Improved Regulatory Decisions?” Journal of Economic Perspectives 22(1), Winter 2008, pp. 67-84 (available online through MELVYL Atypon-Link).

##### *Regulation to Improve Consumer Choices (Information and Price)*

Colin Camerer et al, “Regulation for Conservatives: Behavioral Economics and the Case for ‘Asymmetric Paternalism’”, University of Pennsylvania Law Review, 151, No. 3, January 2003,

pp. 1211-1254 (available online through MELVYL EBSCOhost Business Source Premier or at <http://www.hss.caltech.edu/~camerer/paternPLR.pdf>).

Shlomo Benartzi and Richard Thaler, "Heuristics and Biases in Retirement Savings Behavior," Journal of Economic Perspectives, 21(3), Summer 2007, pp. 81-104 (available online through MELVYL Atypou-Link).

Friedman, Lee S., "Bounded Rationality versus Standard Utility-Maximization: A Test of Energy Price Responsiveness," in R. Rowda and J. Fox, eds., Judgments, Decisions, and Public Policy, Cambridge University Press (New York, NY: 2002), pp. 138-173 (available online at my website under Behavioral Economics at <http://gsppi.berkeley.edu/faculty/lfriedman/lee-s-friedman>).

Overman, E. and A. Cahill, "Information, Market Government, and Health Policy: A Study of Health Data Organizations in the States," JPAM, 13, No. 3, Summer 1994, pp. 435-453 (available online through MELVYL via Periodicals Archive Online or JSTOR).

**WEEK 5:      October 6 (Applications: Occupational Safety and Health, Air Quality)**

*Regulation to Improve Quality*

Hubbard, T., "An Empirical Examination of Moral Hazard in the Vehicle Inspection Market," The RAND Journal of Economics, 29, No. 2, Summer 1998, pp. 406-426 (available online through MELVYL).

Weil, D., "Assessing OSHA Performance: New Evidence from the Construction Industry," The Journal of Policy Analysis and Management, 20, No. 4, Fall 2001, pp. 651-674 (available online through MELVYL).

Ellerman et al, "Emissions Trading in the U.S.: Experience, Lessons, and Considerations for Greenhouse Gases," report for the Pew Center on Global Climate Change, May 2003 (available online at [http://www.pewclimate.org/docUploads/emissions\\_trading.pdf](http://www.pewclimate.org/docUploads/emissions_trading.pdf)).

Jonathan Leape, "The London Congestion Charge," Journal of Economic Perspectives, 20, No. 4, Fall 2006, pp. 157-176 (available online through MELVYL).

**WEEK 6      October 13                      Student proposals**

**WEEK 7:     October 20                      Student proposals**

**WEEK 8:    October 27    (Applications: Electricity, Telecommunications)**

*Rate of Return Regulation, Incentive Contracting, and Deregulation*

Friedman, L. and C. Weare, “The Two-Part Tariff, Practically Speaking,” Utilities Policy, 3, No. 1, January 1993, pp. 62-80 (available online through MELVYL).

Vogelsang, I., “Incentive Regulation & Competition in Public Utility Markets: A 20-Year Perspective,” Journal of Regulatory Economics, 22, No. 1, July 2002, pp. 5-27 (available online through MELVYL).

Gagnepain, P. and M. Ivaldi, “Incentive Regulatory Policies: The Case of Public Transit Systems in France,” Rand Journal of Economics, 33, No. 4, Winter 2002, pp. 605-629 (available online through the MELVYL Expanded Academic database).

Joskow, P., “Markets for Power in the U.S.: An Interim Assessment”” The Energy Journal, 27, No. 1, January 2006, pp. 1-37 (available online through MELVYL, EBSCO and Expanded Academic databases).

Friedman, L., “California's Electricity Crisis: The Long and the Short of It,” International Journal of Public Policy, forthcoming 2008, pp. 1-28 (available on my web page under Utility Regulation and Restructuring at <http://gsppi.berkeley.edu/faculty/lfriedman/lee-s-friedman>).

Stephen Thomas, “Evaluating the British Model of Electricity Deregulation,” Annals of Public and Cooperative Economics, 75, No. 3, September 2004, pp. 367-398 (available online through MELVYL).

### **III.    INSTITUTIONAL CHOICES OF SUPPLY**

#### *A.    Government, Nonprofit, and Profit-Seeking Enterprises*

**WEEK 9:    November 3 (Applications: Non-Profit Tax Exemption, Hospitals, Schools)**

Hansmann, H., “The Role of Nonprofit Enterprise,” in S. Rose-Ackerman, The Economics of Nonprofit Institutions, Oxford University Press (New York, NY: 1986), pp. 57-84.

Werker, Eric and Faisal Ahmed, “What Do Nongovernmental Organizations Do?” Journal of Economic Perspectives, 22(2), Spring 2008, pp. 73-92 (available through MELVYL Atypon-Link).

Sanders, S., "The Common Sense of the Nonprofit Hospital Tax-Exemption: A Policy Analysis," JPAM, 14, No. 3, Summer 1995, pp. 446-466 (available online through MELVYL via Periodicals Archive Online or JSTOR).

Picone, G., S. Chou and F. Sloan, "Are for-profit hospital conversions harmful to patients and to Medicare?" Rand Journal of Economics, 33, No. 3, Autumn 2002, pp. 507-523 (available online through MELVYL Expanded Academic database).

Ladd, H., "School Vouchers: A Critical View," Journal of Economic Perspectives, 16, No. 4, Fall 2002, pp. 3-24 (available online through MELVYL).

Neal, D., "How Vouchers Could Change the Market for Education," Journal of Economic Perspectives, 16, No. 4, Fall 2002, pp. 25-44 (available online through MELVYL).

### ***B. Dynamic Considerations: Innovating, Adapting***

#### **WEEK 10    November 10 (Applications: Education, Criminal Justice)**

Nelson, R., "Capitalism as an Engine of Progress," in R. Nelson, The Sources of Economic Growth, Harvard University Press (Cambridge, MA: 1996)

Richard R. Nelson and Sidney G. Winter, "Evolutionary Theorizing in Economics," Journal of Economic Perspectives, 16(2), Spring 2002, pp. 23-46 (available online through MELVYL).

Friedman, L., "Public Sector Innovations and Their Diffusion: Economic Tools and Managerial Tasks," in A. Altshuler and R. Behn, Innovation in American Government, The Brookings Institution (Washington, DC: 1997), pp. 332-359.

Berman, P. and B. Nelson, "Replication: Adapt or Fail", in A. Altshuler and R. Behn, Innovation..., pp. 319-331.

**WEEK 11:    November 17            Student Presentations**

**WEEK 12:    November 24            Student Presentations**

**WEEK 13:    December 1                Student Presentations**

**WEEK 14:    December 8                No Class, Papers Due**