

NAME: _____

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Economics 230B
Winter 2003

FINAL EXAMINATION

You may use the full 150 minutes allotted for this exam. I anticipate that it will take 90 minutes or less. There are a total of 90 points which correspond to minutes anticipated per question. No outside materials are permitted.

Section 1 (40 points)

True/False/Uncertain *explain*. Credit depends largely on explanation.

1. The existence of the flypaper effect rejects the median voter model and supports the budget-maximizing bureaucrat model. (5 pts.)

2. The state of Efficiencia has decided to give grants to towns to supplement their educational spending. The state can choose between a conditional lump sum grant and a matching grant. The state wants to choose the grant structure that leads to the biggest increase in local educational spending for a given cost to the state. The state should choose a conditional block grant since it targets government dollars more effectively. (5 pts.)

3. Even if all of the other assumptions of the Tiebout model are maintained, if the method of finance is other than a head tax there is no way to guarantee that a local public goods equilibrium will exist or that it will be efficient. (10 pts.)

4. "Transfer neutrality" means that any redistribution of resources towards people who would privately provide a public good will yield no effect on the level of public good provided. To increase the level of public goods, the redistribution must enlarge the set of private contributors. (5 pts.)

5. Empirical and experimental work support the “warm glow” model. (5 pts.)

6. The revelation principle is good news and the Gibbard-Satterthwaite Theorem is bad news for designers of mechanisms. (5 pts.)

7. Preferences for publicly provided-goods *with* private alternatives are more likely to violate single-peakedness than are preferences for publicly-provided goods *without* private alternatives. (5 pts.)

c. Imagine that the sole policy dimension for you to affect with new revenue is class size. Now that you know how much a given increase in test scores is valued by voters, how will you decide how much to spend on reducing class size? You do not have the ability do any new research on the effects of class size, and must draw upon the existing literature. In your answer, also explain why you find existing estimates to be credible or not. (8 pts.)

d. Why might you, as the local social planner, not produce a socially optimal level of education? Be specific about whose social welfare you are trying to maximize. (2 pts.)

2. Essay (28 pts.)

You work for the General Accounting Office and are called in to evaluate the efficacy of *newly expanded federal grants* by \$5 million to an *existing* California state government job training program spending \$20 million per year (participants enroll for one year). At the same time that this grant was received, California and all states were affected by an unfunded federal mandate to expand health insurance coverage to the poor. You have data on the earnings of participants in the program for the three years before they entered the program and three years after. Your colleague, who has not taken Econ 230, suggests that you compare the outcomes of participants in the expanded program with those of participants in the program before it received federal grants to come up with the effect of receiving a federal grant to job training on labor force outcomes (earnings, employment) of participants. That is, he wishes to interpret the effect as the effect one would get by giving the money to any state. He does not plan to use data on the three years before the participants enter the program, and is very pleased because you can control for individual-level fixed effects. Tell your colleague the many ways his approach is flawed and what a more appropriate approach would be. *Use all the information given above* to inform your approach and be specific about how your findings should be interpreted.

