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## **ECONOMICS 230B, SECOND-HALF: LECTURE SCHEDULE SPRING 2006**

This is the second half of the second of two courses in the Public Sector Microeconomics sequence. This course covers material on behavioral responses to income taxation and welfare programs, optimal income taxation and redistribution, taxation of savings, and incentives to save for retirement programs.

Syllabus, reading list, papers, problem sets, and handouts are all posted on 230B website at: [http://emlab.berkeley.edu/users/webfac/chetty/e230b\\_07/e230b\\_07.shtml](http://emlab.berkeley.edu/users/webfac/chetty/e230b_07/e230b_07.shtml)

**Class meetings:** Mondays 10am-12pm, Room 639 Evans Hall

**Prerequisites:** First year graduate microeconomics (Economics 201A,B), First year graduate econometrics (Economics 240A), and first public sector microeconomics class 230A.

**Requirements:** Two problem sets (one by Chetty and one by Saez, problem sets do not count toward final grade), Final Examination on Monday, May 14<sup>th</sup>, 8-11am, (90% of the grade).

### **Section I: Behavioral Responses to Taxes and Transfers:**

1	March 19	Labor Supply responses to taxation
2	April 2	Responses to Welfare Programs and the EITC
3	April 9	Response of high income taxpayers to tax rates

### **Section II: Optimal Income Taxation and Redistribution**

4	April 16	Optimal Income Taxation
5	April 23	The Design of Optimal Welfare Programs and Sin Taxes

### **Section III: Taxation and Savings**

6	April 30	Taxation of Savings
7	May 7	Tax subsidies to savings: IRAs and 401(k)s

**230B - Public Economics II, Saez Part**

Spring 2007

**Bold: required reading****\*: reading emphasized in class****0. GENERAL REFERENCES:**

A. Atkinson and J. Stiglitz, *Lectures on Public Economics*, New York: McGraw Hill, 1980.

A. Atkinson, *Public Finance in Action: The Flat-Tax Proposal*, Oxford: Oxford University Press, 1995.

A. Auerbach and M. Feldstein, eds., *Handbook of Public Economics*, 4 Volumes, Amsterdam: North Holland, 1985, 1987, 2002, and 2003

\* B. Salanie, *The Economics of Taxation*, Cambridge: MIT Press, 2003.

Background Reading: Three most popular undergraduate textbooks  
(Useful for a simple description of the U.S. tax system and the main government programs)

J. Gruber, *Public Finance and Public Policies*, 2nd edition, Worth Publishers, 2006.

H. Rosen, *Public Finance*, 7<sup>th</sup> edition, McGraw Hill, 2005.

J. Stiglitz, *Economics of the Public Sector*, 3<sup>rd</sup> edition, Norton, 1999.

References on Empirical Methods:

J. Angrist et A. Krueger, "Instrumental Variables and the Search for Identification: From Supply and Demand to Natural Experiments," Journal of Economic Perspectives, 15 (4) (2001), pp. 69-87

M. Bertrand, E. Duflo et S. Mullainathan, "How Much Should we Trust Differences-in-Differences Estimates?," Quarterly Journal of Economics (2003)

**E. Duflo, « Empirical Methods », mimeo MIT, 2002**

B. Meyer, "Natural and Quasi-Experiments in Economics", *Journal of Business and Economic Statistics*, 13(2), April 1995

**I. BEHAVIORAL RESPONSES TO TAXES AND TRANSFERS****A. Labor Supply Responses to Taxation****Classical Studies:**

- \* O. Ashenfelter and M. Plant. (1990) "Non-Parametric Estimates of the Labor Supply Effects of Negative Income Tax Programs," *Journal of Labor Economics*, 8.1 (January), S396-S415.
  - \* Francine D. Blau, Lawrence M. Kahn "Changes in the Labor Supply Behavior of Married Women: 1980-2000", NBER Working Paper No. 11230, March 2005
  - \* R. Blundell, A. . Duncan and C. Meghir, "Estimating Labor Supply Responses Using Tax Reforms," *Econometrica* 66 (July 1998), 827-862.
  - \* R. Blundell and T. MaCurdy. (1999) " Labor supply: a review of alternative approaches," in the *Handbook of Labor Economics*, Vol. 3A, O. Ashenfelter and D. Card, eds. Amsterdam: Elsevier Science or Institute for Fiscal Studies Working Paper W98/18 available at: <http://www.ifs.org.uk/staff/bm180899.pdf>
  - \* N. Eissa "Taxation and Labor Supply of Married Women: The Tax Reform Act of 1986 as a Natural Experiment" NBER Working Paper 5023, 1995.
- J. Hausman "Taxes and Labor Supply", in A. Auerbach and M. Feldstein, eds, *Handbook of Public Finance*, Vol I, North Holland 1987.
- J. Heckman "What Has Been Learned About Labor Supply in the Past Twenty Years?", *American Economic Review*, Vol. 83, No. 2, Papers and Proceedings (May, 1993), 116-121.
- \* G. Imbens, D. Rubin, and B. Sacerdote (2001) "The Causal Effect of Income on Labor Supply: Evidence From the Lottery Winner Survey." *American Economic Review*, Vol. 91, No. 4, September 2001.
- M. Killingsworth and J. Heckman. (1986) "Female Labor Supply: A Survey," *Handbook of Labor Economics*, vol. 1, chapter 2.
- Peter Kuhn, Fernando Lozano "The Expanding Workweek? Understanding Trends in Long Work Hours Among U.S. Men, 1979-2004", NBER Working Paper No. 11895, 2005.
- T. Lemieux, B. Fortin, and P. Fréchette (1994), "The Effect of Taxes on Labor Supply in the Underground Economy," *American Economic Review*, 84, 231-254.
- T. MaCurdy, H. Paarsch, and D. Green, "Assessing Empirical Approaches for Analyzing Taxes and Labor Supply," *Journal of Human Resources*, Summer 1990.
- \* T. Mroz (1987) "The Sensitivity of An Empirical Model of Married Women's Hours of Work to Economic and Statistical Assumptions," *Econometrica*, 55.4 (July), 765-799.
- J. Pencavel. (1986) "Labor Supply of Men: A Survey," *Handbook of Labor Economics*, vol. 1, chapter 1.
- Labor Supply and Behavioral Economics**
- \* Camerer, Colin, Linda Babcock, George Loewenstein and Richard Thaler (1997), "Labor Supply of New York City Cabdrivers: One Day at a Time", *Quarterly Journal of Economics*; 112(2), 407-41.
- H. Farber "Is Tomorrow Another Day? The Labor Supply of New York City Cab Drivers", *Journal of Political Economy*, 2005, vol. 113(1), 46-82.

- \* E. Fehr, and L. Goette (2003) "Do Workers Work more when Wages are High? Evidence from a randomized Field Experiment, IEW Working Paper # 125, forthcoming *American Economic Review*
- L. Friedberg (2000) "The Labor Supply Effects of the Social Security Earnings Test." *Review of Economics and Statistics* 82(1), 48-63.
- Liebman, J. and R. Zeckhauser (2003) "Schmeduling", Harvard University mimeo.
- Oettinger, Gerald S. (1999), An Empirical Analysis of the Daily Labor Supply of Stadium Vendors, *Journal of Political Economy*; 107(2), 360-92.
- \* E. Saez (2002) "Do Taxpayers Bunch at Kink Points?", UC Berkeley mimeo, 2002.

### **Macro labor supply studies**

- Aguiar, M. and AE. Hurst, (2006), "Measuring Trends in Leisure: The Allocation of Time over Five Decades", NBER Working Paper 12082.
- Alberto Alesina and Edward Glaeser, Bruce Sacerdote, (2006) "Work and Leisure in the United States and Europe: Why So Different?" NBER Macro Annual.
- M. Kimball and M. Shapiro (2004) "Labor Supply: Are the Income and Substitution Effects both Large or Both Small?", University of Michigan mimeo.
- \* Lee Ohanian, Andrea Raffo, Richard Rogerson (2006) "Long-Term Changes in Labor Supply and Taxes: Evidence from OECD Countries, 1956-2004", Working Paper.
- Prescott, Edward C., (2004), "Why Do Americans Work So Much More than Europeans?", Federal Reserve Bank of Minneapolis Quarterly Review, Vol. 28, No. 1, July, 2-13.

### **B. Responses to Welfare Programs and the EITC**

**David H. Autor, Susan Houseman, "Do Temporary Help Jobs Improve Labor Market Outcomes for Low-Skilled Workers? Evidence from Random Assignments" NBER Working Paper No. 11743, 2005.**

M. Bane and D. Ellwood (1994), *Welfare Realities: From Rhetoric to Reform*, Harvard University Press: Cambridge.

Marianne Bitler, Jonah Gelbach, Hylary Hoynes, "What Mean Impacts Miss: Distributional Effects of Welfare Reform Experiments," NBER working paper No. 10121, November 2003, revised August 2005.

R. Blank, "Evaluating Welfare Reform in the U.S." *Journal of Economic Literature*. Vol 40:4, December 2002, 1105-66.

Dynarski, Susan. "Does Aid Matter? Measuring the Effect of Student Aid on College Attendance and Completion." *American Economic Review* 93.1 (March 2003): 279-288.

N. Eissa and H. Hoynes, "The Earned Income Tax Credit and the Labor Supply of Married Couples", *Journal of Public Economics*, Volume 88, Issues 9-10, Pages 1931-1958, August 2004.

**N. Eissa and J. Liebman, "Labor Supply Response to the Earned Income Tax Credit", Quarterly Journal of Economics 111 (1996), 605-637**

J. Grogger "The Effects of Time Limits, the EITC, and Other Policy Changes on Welfare Use, Work, and Income Among Female-Headed Families", *Review of Economic and Statistics*, 2004 forthcoming.

J. Grogger and C. Michalopoulos, "Welfare Dynamics under Time Limits," *Journal of Political Economy*, 2003, 111.

J. Hotz and K. Scholz, "The Earned Income Tax Credit", in *Means-Tested Transfer Programs in the United States*, R. Moffitt (ed.), The University of Chicago Press and NBER, 2003, 141-197

\* J. Ifcher (2002) "Leaving Welfare and Joining the Labor Force: Does Job Training Help? Evidence from an Innovative Intervention in New York City", UC Berkeley Ph.D. Thesis.

\* Lawrence F. Katz, Jeffrey R. Kling and Jeffrey B. Liebman "Moving to Opportunity in Boston: Early Results of a Randomized Mobility Experiment", Quarterly Journal of Economics 116 (May 2001), 607-54.

W. Kopczuk, and C. Pop-Eleches (2005), "Electronic Filing, Tax Preparers, and Participation in the Earned Income Tax Credit", NBER Working Paper, forthcoming Journal of Public Economics.

A. Krueger and B. Meyer, "Labor Supply Effects of Social Insurance", NBER Working Paper 9014 (2002) or *Handbook of Public Economics*, volume 4, 2003.

**B. Meyer and D. Rosenbaum, "Welfare, the Earned Income Tax Credit, and the Labor Supply of Single Mothers", Quarterly Journal of Economics 116 (3) (August 2001), 1063-1114.**

\* B. Meyer and J. Sullivan (2004) "The Effects of Welfare and Tax Reform: The Material Well Being of Single Mothers in the 1980s and 1990s", *Journal of Public Economics* 88, 1387-1420

Charles Michalopoulos, Philip K. Robins and David Card, When financial work incentives pay for themselves: evidence from a randomized social experiment for welfare recipients, *Journal of Public Economics*, Volume 89, Issue 1, January 2005, Pages 5-29.

C. Murray (1984), *Loosing Ground: American Social Policy, 1950-1980*, Basic Books: New York.

Moffitt, Robert. "Incentive Effects of the U.S. Welfare System: A Review." *Journal of Economic Literature* 30 (March 1992): 1-61.

\* R. Moffitt, "Welfare Programs and Labor Supply", in A. Auerbach and M. Feldstein, *Handbook of Public Economics*, Volume 4, Chapter 34, Amsterdam: North Holland, 2003 or NBER Working Paper 9168 September 2002.

D Neumark et W. Wascher, "Using the EITC to Help Poor Families: New Evidence and a Comparison with the Minimum Wage", NBER Working Paper n°7599 (2000)

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J. Rothstein, "The Mid-1990s EITC Expansion: Aggregate Labor Supply Effects and Economic Incidence" Princeton University Working Paper, August 2005.

R. Schoeni and R. Blank. "What Has Welfare Reform Accomplished? Impacts on Welfare Participation, Employment, Income, Poverty, and Family Structure." NBER Working Paper 7627, March 2000.

### **C. The response of high incomes to taxation**

G. Break, "Income Taxes and Incentives to Work: An Empirical Study", *American Economic Review*, 47(5), September 1957, 529-549.

D. Feenberg and J. Poterba, "Income Inequality and the Incomes of Very High Income Households: Evidence from Tax Returns", in J. Poterba, ed., *Tax Policy and the Economy*, Volume 7, 145-177, Cambridge and London: MIT Press, 1993.

**M. Feldstein, "The Effect of Marginal Tax Rates on Taxable Income: A Panel Study of the 1986 Tax Reform Act", *Journal of Political Economy*, 103(3), June 1995, 551-572.**

M. Feldstein, "Behavioral Responses to Tax Rates: Evidence from the Tax Reform Act of 1986", *American Economic Review*, 85(2), May 1995, 170-174.

A. Goolsbee, "It's Not About the Money: Why Natural Experiments Don't Work on the Rich", NBER Working Paper No. 6395, February 1998.

\* A. Goolsbee, "What Happens When You Tax the Rich? Evidence from Executive Compensation", *Journal of Political Economy*, April 2000.

\* L. Lindsey, "Individual Taxpayer Response to Tax Cuts, 1982-1984: With Implications for the Revenue Maximizing Tax Rate", *Journal of Public Economics*, 33(2), July 1987 173-206.

R. Moffitt and M. Wilhelm, "Taxation and the Labor Supply Decisions of the Affluent", NBER Working Paper No. 6621, June 1998.

\* T. Piketty and E. Saez, "Income Inequality in the United States, 1913-1998", *Quarterly Journal of Economics*, 116, 2003, 1-39.

**E. Saez, "Reported Incomes and Marginal Tax Rates, 1960-2000: Evidence and Policy Implications", in J. Poterba, ed., *Tax Policy and the Economy*, Volume 18, Cambridge: MIT Press, 2004.**

\* E. Saez and M. Veall, "The Evolution of High Incomes in North-America: Lessons from the Canadian Evidence", *American Economic Review*, June 2005.

J. Slemrod, "High-Income Families and the Tax Changes of the 1980s: The Anatomy of Behavioral Response", in M. Feldstein and J. Poterba, eds., *Empirical Foundations of Household Taxation*, Chicago: University of Chicago Press, 1996, 169-189.

J. Slemrod, "Income Creation or Income Shifting? Behavioral Responses to the Tax Reform Act of 1986", *American Economic Review*, 85(2), May 1995, 175-180.

J. Slemrod, *Does Atlas Shrug? The Economic Consequences of Taxing the Rich*, Harvard University Press, 2000.

J. Slemrod and S. Yitzhaki, "Tax Avoidance, Evasion, and Administration", in A. Auerbach and M. Feldstein, *Handbook of Public Economics*, Volume 3, Chapter 22, Amsterdam: North Holland, 2002.

## **II. OPTIMAL INCOME TAXATION AND REDISTRIBUTION**

### **A. Optimal Income Taxation in the Mirrlees Model**

- \* Atkinson, A.B., Stiglitz, J.E., "The design of tax structure: Direct versus indirect taxation." *Journal of Public Economics* 6, 1976, 55-75.
- \* P. Diamond, "Optimal Income Taxation: An Example with a U-Shaped Pattern of Optimal Marginal Tax Rates", *American Economic Review*, 88, March 1998, 83-95.
- L. Kaplow, L., 2004. "On the undesirability of commodity taxation even when income taxation is not optimal", NBER wp No. 10407, forthcoming *Journal of Public Economics*.
- \* H. Kleven, C. Kreiner, and E. Saez, 2006, "The Optimal Income Taxation of Couples", NBER Working Paper No. 12685, November 2006.

### **G. Laroque, 2005 "Indirect taxation is superfluous under separability and taste homogeneity: A simple proof", *Economic Letters*, 87, 141-144.**

J. Mirrlees, "An Exploration in the Theory of Optimal Income Taxation", *Review of Economic Studies*, 38, 1971, 175-208.

T. Piketty, "La Redistribution Fiscale face au Chomage", *Revue Francaise D'Economie*, 12(1), 1995, 157-201.

E. Sadka, "On Income Distribution, Incentives Effects and Optimal Income Taxation", *Review of Economic Studies*, 43(2), 1976, 261-268.

### **E. Saez, "Using Elasticities to Derive Optimal Income Tax Rates", *Review of Economics Studies*, 68, 2001, 205-229, Sections 1-3, and 5.**

B. Salanie, *The Economics of Taxation*, Cambridge: MIT Press, 2003, Chapter 4.

N. Stern, "On the Specification of Models of Optimum Income Taxation", *Journal of Public Economics*, 1976, 6, 123-162.

J. Stiglitz, "Pareto Efficient and Optimal Taxation and the New New Welfare Economics", in A. Auerbach and M. Feldstein, Volume 2, 991-1041.

### **B. The Design of Optimal Transfer Programs**

### **G. Akerlof, "The Economics of Tagging as Applied to the Optimal Income Tax", *American Economic Review*, 68(1), March 1978, 8-19.**

A.B. Atkinson, "Income Maintenance and Social Insurance," in A. Auerbach and M. Feldstein, eds., Handbook of Public Economics Volume 2 (Amsterdam: North Holland, 1987), 779-908.

T. Besley and S. Coate, "Public Provision of Private Goods and the Redistribution of Income", *American Economic Review*, 81(4), September 1991, 979-984.

- \* T. Besley and S. Coate, "Workfare versus Welfare: Incentives Arguments for Work Requirements in Poverty-Alleviation Programs", *American Economic Review*, 82(1), March 1992, 249-261.

S. Coate, "Altruism, the Samaritan's Dilemma, and Government Transfer Policy", *American Economic Review*, 85(1), March 1995, 46-57.

S. Coate, S. Johnson, and R. Zeckhauser, "Pecuniary Redistribution through In-Kind Programs", *Journal of Public Economics*, 55(1), September 1994, 19-40.

A. Nichols and R. Zeckhauser, "Targeting Transfers Through Restrictions on Recipients", *American Economic Review*, 72(2), May 1982, 372-377.

**E. Saez, "Optimal Income Transfer Programs: Intensive Versus Extensive Labor Supply Responses", Quarterly Journal of Economics 117 (2002), 1039-1073.**

- \* B. Salanie, *The Economics of Taxation*, Cambridge: MIT Press, 2003, Chapter 8.
  - \* H. Varian, "Redistributive Taxation as Social Insurance," Journal of Public Economics, 14 (1980), 49-68.
- R. Zeckhauser "Optimal Mechanisms for Income Transfer" *AER*, 61(3), June 1971

### **C. Optimal Sin Taxes**

G. Becker and K. Murphy, 1988, "A theory of Rational Addiction", *Journal of Political Economy*, 96(4), 675-700.

- \* Douglas Bernheim and Antonio Rangel, "Addiction and Cue-Triggered Decision", *American Economic Review*, 2004, 94(5):1558-90.

J. Gruber and B. Koszegi, 2001. "Is Addiction Rational? Theory and Evidence", *Quarterly Journal of Economics*, 116(4), 1261-1305.

T. O'Donoghue and M. Rabin, 2005. "Optimal Sin Taxes", Working Paper, UC Berkeley.

## **III. TAXATION AND SAVING**

### **A. Optimal Capital Income Taxation**

#### **Infinite Horizon Models**

**D. Bernheim, "Taxation and Saving," in A. Auerbach and M. Feldstein, *Handbook of Public Economics*, Volume 3, Chapter 18, Amsterdam: North Holland, 2002, Section 2.1, or NBER Working Paper No. 7061, 1999.**

C. Chamley, "Optimal Taxation of Capital Income in General Equilibrium with Infinite Lives", *Econometrica*, 54(3), May 1986, 607-622.



V. V. Chari, L. Christiano, and P. Kehoe, "Optimal Fiscal Policy in a Business Cycle Model", *Journal of Political Economy*, August 1994, 102, 617-652.

V. V. Chari and P. Kehoe, "Optimal Fiscal and Monetary Policy", NBER Working Paper No 6891, 1999, forthcoming *Handbook of Macroeconomics*, 2000, Sections 1 and 2.

E. Farhi and I. Werning, "Inequality, Social Discounting and Estate Taxation" NBER Working Paper No. 11408, 2005.

Golosov, Michael, Kocherlakota, Narayana, and Aleh Tsyvinski, "Optimal Indirect and Capital Taxation." *Review of Economic Studies*, 2003.

K. Judd, "Redistributive Taxation in a Simple Perfect Foresight Model." *Journal of Public Economics*, 28, 1985, 59-83.

- \* N. Kocherlakota, "Advances in Dynamic Optimal Taxation," working paper, September 2005.
  - \* R. Lucas, "Supply-Side Economics: An Analytical Review", *Oxford Economics Papers* 42 (April 1990): 293-316.
  - \* T. Piketty, "Income Inequality in France, 1901-1998", CEPR discussion paper No. 2876, 2001. (appendix)
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### **Overlapping-Generation Models**

H. Cremer and P. Pestieau, "Wealth Transfer Taxation: A Survey", in *Handbook of Giving, Reciprocity and Altruism*, L.-A. Gerard-Varet, S-C. Kolm and J. Mercier Ythier, eds., 2004.

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- \* M. King, "Savings and Taxation," in G. Hughes and G. Heal, eds., *Public Policy and the Tax System* (London: George Allen Unwin, 1980), 1-36.
- A. Sandmo, "The Effects of Taxation on Savings and Risk-Taking," in A. Auerbach and M. Feldstein, *Handbook of Public Economics* vol. 1, chapter 5, pp. 293-308.

### **Taxation of Capital with Uninsurable Income Risk and Borrowing Constraints**

P. Aghion and P. Bolton, "A Trickle-Down Theory of Growth and Development with Debt-Overhang", Review of Economic Studies 64 (1997), pp.151-172

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\* Pérez-González, Francisco, "Inherited Control and Firm Performance" forthcoming American Economic Review, 2007.

T. Piketty, "The Dynamics of the Wealth Distribution and the Interest Rate with Credit Rationing", Review of Economic Studies 64 (2) (April 1997), pp.173-189

T. Piketty, "Theories of Persistent Inequality and Intergenerational Mobility", in Handbook of Income Distribution (Chapter 8, pp.429-476), Eds. Tony Atkinson and François Bourguignon, North-Holland, 2000.

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## **B. Targeted Tax Subsidies to Saving**

**D. Bernheim, "Taxation and Saving," in A. Auerbach and M. Feldstein, *Handbook of Public Economics*, Volume 3, Chapter 18, Amsterdam: North Holland, 2002, Section 4, or NBER Working Paper No. 7061, 1999.**

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S. Venti and D. Wise, "Individual Response to Retirement Savings Programs: Results from US Panel Data.," mimeo 1995.

**C. Information, Peer effects, and Behavioral Effects in Retirement Savings**

Bayer, Patrick B., Bernheim, B.D., Scholz, K., 1996. "The Effects of Financial Education in the Workplace: Evidence from a Survey of Employers." NBER Working Paper No. 5655.

Bernheim, B.D., Garrett, D.M., 1996. "The Determinants and Consequences of Financial Education in the Workplace: Evidence from a Survey of Households." NBER Working Paper No. 5667.

- \* Choi, J., Laibson, D., Madrian, B., "Reducing the Complexity Costs of 401(k) Participation Through Quick Enrollment™", Harvard University Working Paper, 2005.

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Choi, J., Laibson, D., Madrian, B. and Metrick A. "For Better or For Worse: Default Effects and 401(k) Savings Behavior". In David Wise, editor, Perspectives on the Economics of Aging, pp. 81-121. Chicago: University of Chicago Press, 2004, also NBER Working Paper No. 8651, 2001.

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- \* Duflo, Esther and Emmanuel Saez, 2003. "The Role of Information and Social Interactions in Retirement Plan Decisions: Evidence from a Randomized Experiment." *Quarterly Journal of Economics*, 118(3), 815-842.

**Duflo, Esther, William Gale, Jeffrey Liebman, Peter Orszag, and Emmanuel Saez (2006). "Saving Incentives for Low- and Middle-Income Families: Evidence from a Field Experiment with H&R Block." *Quarterly Journal of Economics*.**

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- \* Poterba, James (2004) *Risk and Individual Choice in Accumulating Retirement Saving*, Munich Lectures in Economics, MIT Press: Cambridge, MA, (2003).
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