

Wasteful government, tax evasion, and the provision of public goods

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Abstract

The paper considers the question of whether public goods should be provided by the government or through private provision. The results cast doubt upon the role of the government as a provider and suggest instead that it may be better employed as a facilitator of private provision. These arguments are strengthened if consumers can engage in tax evasion or the government is wasteful in its use of resources. The paper also reveals that tax evasion can emerge as the best response to inequitable government policy. © 2000 Elsevier Science B.V. All rights reserved.

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1. Introduction

It is a widely accepted principle that the government should supply public goods. From elementary textbooks onwards, government provision of public goods is cited as the natural response to one of the classic forms of market failure. But why should this be so? The existence of a market failure does not imply that the government can solve it, or that one course of action is necessarily preferable to another. Private individuals willingly contribute significant sums to charities,

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many of which are engaged in the supply of public goods. This is true even in areas such as health care where the government makes significant provision of its own. Rather than have the government directly engaged in the provision of public goods, can incentives not be designed to encourage private charity and direct it to appropriate ends? The existence of wastefulness in the operation of government, such as that caused through excessive bureaucracy, could only magnify the benefits of such a policy.

Any assessment of these claims needs to take into account the traditional issues of public finance such as the trade-off between efficiency and equity and the limitations on the information set of the government. This is true both in the evaluation of the success of government provision and in the consideration of alternative mechanisms. In addition to this, it must also be realized that the provision of public goods takes place within the political arena and idealized solutions may fall foul of political realities. The political culture of an economy will influence what the government wants to do, how it tries to do it, and how successful it is. The interplay between the government and the governed must have significant implications for how best to provide public goods.

The purpose of the present paper is to explore some of the interconnections between political culture and the provision of public goods. By moving away from standard assumptions, it aims to provide a re-assessment of the motives for tax evasion and to establish how this interacts with public good provision. It reconsiders the correct balance between the government as a facilitator of private provision and as a provider in its own right. In covering this ground, the paper is linked to several branches of the literature. Much of it is built upon recent developments in the analysis of the private provision of public goods, most especially those of Itaya et al. (1997, 1998). It also utilizes important results from Bernheim (1986), Andreoni (1990) and Boadway et al. (1989). In the tax evasion literature, it has close links with Cowell and Gordon (1988) but there are some fundamental differences between the two. Finally, the results on public good provision relate to the literature that has followed Samuelson (1954).

The paper assumes throughout that the government is benevolent and attempts to maximize social welfare. This may be seen as a generous interpretation of government behavior but it serves two useful purposes. Firstly, it allows comparison of the results here with those elsewhere in the literature thus making clear the role of tax evasion and the wasteful government. Secondly, it provides a benchmark for comparisons with alternative assumptions on the motivation of government. Some comments on this are given in Section 6. However, the fact that the government is well intentioned in trying to work in the interests of the population does not mean that it is beyond reproach. Indeed, one of the major features of the analysis is that the government is characterized as being less efficient than the private sector, which can have a variety of interpretations including those of excessive bureaucracy and corruption. The aim of the paper is to investigate the influence of this inefficiency upon tax policy and the provision of public goods.

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