

**Berlin Applied Micro Seminar**

**Tax setting and political accountability**

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*Abstract:*

When are voters most likely, if at all, to hold incumbents accountable for increasing taxes while in office? Using data over gubernatorial and state congressional elections in the US over the period 1950-2008 we investigate how electoral success is affected by tax setting policies. In specific, we test whether voters are rational in that they hold the governors responsible to a larger extent in states where the governor possesses a line-item veto over tax policies. The paper is an indirect test of a theoretical political-agency model where voters use elections in order to select more competent politicians and to discipline self-interested incumbents to behave. Preliminary results indicate that incumbent governors are indeed punished for raising taxes and more so if voters believe that they the governor is the one responsible for the decision to increase taxes. In addition we test whether voters' responses vary with the political affiliation of the governor. Here the results are weaker but to indicate that Democrats are punished to a larger extent than Republicans for increasing taxes.