

# Institutional Quality and Individual Preferences for Social Policy\*

Israel Marques, II

Draft version: August 20, 2015

## Abstract

Who supports social policy in settings where institutions are weak? Existing work on social policy preferences focuses on the developed world, where governments can credibly commit to policy, tax evasion is constrained, and governments are accountable. In this paper, I relax these assumptions. I argue that weak accountability under poor institutions allow government officials to expend less effort to collect social policy contributions, decreasing expected revenues. For most, this is akin to a dead-weight cost that saps support for redistribution. For those with a comparative advantage in tax evasion, however, this allows for free-riding on the contributions of others and decreases the costs of social policy. As institutional quality declines and tax evasion becomes easier, individuals with a comparative advantage in tax evasion should therefore be more likely to support redistribution. I test this argument using public opinion data from a survey of 28,000 individuals in 28 post-communist countries.

*Key words:* Shadow Economy, Preferences for Redistribution, Public Opinion, Tax Evasion, Comparative Political Economy

*JEL codes:* O15, O17, H53

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\*Research for this paper was supported in part by a fellowship from the National Research University – Higher School of Economics. I also acknowledge financial support from IREX (International Research and Exchanges Board) with funds provided by the United States Department of State through the Title VIII Program. I would like to thank Timothy Frye, Lucy Goodhart, Isabela Mares, Martin Adranaz, Sarah Berens, Thomas Remington, as well as participants of the Columbia University Graduate Student Conference, the Institute for Market Studies Seminar at the Higher School of Economics, and the Ronald Coase Workshop for insightful comments and suggestions on earlier versions of this paper. All errors in method and interpretation remain my own.

Who supports social policy in the developing world? Existing work on preferences for social policy has largely focused analytical attention on the more developed countries of the OECD, providing invaluable insights into the micro-foundations of preferences for the welfare state.<sup>1</sup> As a rule, however, institutions in these countries are strong and governments are generally able to credibly commit to policy. As a consequence, existing work has largely assumed that *de jure* social policy promises embedded in statute translate fairly closely into *de facto* benefits that individuals receive with only residual dead-weight costs, if any (*c.f.* Benabou and Ok (2001), Iversen and Soskice (2001), Meltzer and Richards (1981), Moene and Wallerstein (2001)). Conditions in the developing world are quite different, however. In many countries institutions are weak and the machinery of the state – whether due to weak state capacity or weak oversight and accountability – is unable to commit to distributing benefits according to legal prescriptions. Under such circumstances, state coffers become a leaky bucket that deny individuals the *de facto* benefits that they would expect given *de jure* policy promises. Consequently, for all we know about micro-level preferences, it is unclear if theory and evidence from the well-developed, wealthy countries of the OECD can explain support for social policy where institutions are weak and governments poorly constrained (Mares, 2005a, Mares and Carnes, 2009).<sup>2</sup>

The failure of existing micro-level work on social policy to consider the effect of institutional quality is surprising. Conceptualizing institutions as humanely devised constraints on human interaction (North, 1981)'s, work on the political economy of institutions and investment highlights how a lack of constraints creates credible commitment problems between the state and investors. Where institutions are poor, state officials can take advantage by engaging in weak or opportunistic policy enforcement and outright rent-seeking, which increases investor risk and transaction costs (North, 1990, North, Wallis, and Weingast, 2009, North and Weingast, 1989). Knowing this, rational actors invest at lower levels, since these additional costs weaken returns. In this paper, I argue that these insights can be extended to inform our understanding of preferences for social pol-

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<sup>1</sup>For a summary of findings on individual preferences, *c.f.* Alesina and Giuliano (2011). For important theoretical contributions tying these to macro-level variation in the welfare state, *c.f.* (Estevez-Abe, Iversen, and Soskice, 2001, Iversen, 2005). For broader discussions of the origins and trajectory of welfare states, *c.f.* Esping-Anderson (1990), Huber and Stephens (2001) and contributions in Hall and Soskice (2001), Pierson (2001a).

<sup>2</sup>It is worth noting that Mares (2005a) presents the only study of which I am aware that explicitly examines how poor institutions shape social policy outcomes and links these outcomes to a micro-level model. Her study only presents tests related to its macro-level predictions, however, setting aside the micro-level model.

icy. As with standard investments, individuals pay into the welfare state today expecting benefits, when eligible, tomorrow. Following standard models of social policy preferences, the attractiveness of these investments depends on individuals' expectations about the costs, benefits, and risks associated with social policy (Iversen and Soskice, 2001, Meltzer and Richards, 1981, Moene and Wallerstein, 2001). As with all investment, however, social policy contributions are vulnerable to opportunism and rent-seeking. Consequently, contributions may never be paid out in full or as legally stipulated, making poor institutions akin to dead-weight costs.

In this paper, I focus narrowly on one specific pathology of poor institutions: the inability of governments to fully collect taxes.<sup>3</sup> To preview the argument, I draw on work on state capacity, bureaucratic discretion, and tax evasion to argue that where institutions are poor, government officials are often unable or unwilling to expend costly effort to enforce tax compliance and collect social policy contributions. I argue that this has two important implications for who supports social policy. First, following Mares (2005a), I argue that where the government is unable to commit to collecting revenue as legally stipulated, rampant tax evasion dissipates the contributions meant to fund social policy, reducing the amount available for *de facto* distribution below *de jure* expectations. Standard models of social policy preferences would suggest that this is akin to a dead-weight cost, which reduces support for social policy (Becker, 1985, 1983, Meltzer and Richards, 1981).

Second, I advance a novel argument that the dead-weight costs of poor institutions are not evenly distributed. Drawing on recent work on the political economy of investment, I argue that some social groups can profit from weak institutions by insulating themselves from the state, whether by leveraging political connections or simply evading notice (*c.f.* Boix and Svobik (2013), Gehlbach and Keefer (2011), Haber, Maurer, and Razo (2003)). Applied to social policy, I argue that where institutions are weak and the state is unable or unwilling to ensure full tax compliance, those who are most difficult for the state to audit can take advantage to evade contributions. Depending on the design of social policy, this creates opportunities for free-riding. For tax evaders, certain types of social policy – particularly universal and redistributive types that are vulnerable to free-riding – become more attractive as institutional quality declines and evasion becomes easier.

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<sup>3</sup>My dissertation work argues that predictions about how institutional quality shapes social policy preferences depends on the pathologies that these institutions introduce into the social policy system. For more on alternative mechanisms linking institutions and preferences, see Marques (2015).

To test the arguments, I employ a unique survey of 28,000 individuals in 28 post-communist countries: the 2007 Life in Transition Survey. I choose to focus on the post-communist states of Eastern Europe and the former Soviet Union for several reasons. First, the individual level correlates of tax evasion are well-studied in this sample, simplifying the identification of potential evaders. Second, selecting this region helps to mitigate some forms of unobservable variable bias. Recent work highlights the importance of historical path dependence and mutually reinforcing institutions to welfare state outcomes and policy preferences ([Haggard and Kaufman, 2008](#), [Hall and Soskice, 2001](#), [Hausermann, 2010](#), [Pierson, 2001a, 1994](#)). My work is conscious of these important alternative explanations and leverages the region's common experience with Communism to mitigate such concerns. The Communist drive towards stamping out the private sector and establishing a command economy profoundly shaped attitudes towards markets and state intervention, both due to ideological education and its practical effects on everyday life ([Pop-Eleches and Tucker, 2014](#)).<sup>4</sup> This effect was particularly strong for social policy, where the state created a universal, inequality reducing welfare state in order to insure worker acquiescence for the command economy and to promote its ideology ([Alesina and Fuchs-Shundeln, 2007](#), [Cook, 1993](#), [Haggard and Kaufman, 2008](#)). Although one should not underplay the important variation in the extent to which Communist ideology and practice disrupted previous legacies, I argue that these disruptions created fundamental breaks with pre-communist legacies, making these countries more comparable than alternative groups of countries.<sup>5</sup>

This paper provides several contributions to the broader study of micro-level preferences for social policy. Theoretically, it joins a small body of work that draws attention to the importance of institutional quality for micro-level preferences [Ansell and Samuels \(2014\)](#), [Berens \(2012\)](#), [Mares \(2005a\)](#). It also advances a novel argument about the relationship between opportunities for free-riding and social policy preferences. Empirically, it is among the first of a growing set of studies to examine preferences for social policy in the Post-communist states, specifically, and the developed world, more broadly.<sup>6</sup> It also joins a growing trend in work on social policy preferences

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<sup>4</sup>For a discussion of the the Communist social policy system, *see* for example [Chandler \(2004\)](#), [Connor \(1997\)](#), [Deacon \(1983\)](#), [Ferge \(1979\)](#), [Flakierski \(1986\)](#), [Haggard and Kaufman \(2008\)](#), [Kende and Strmiska \(1987\)](#), [Milanovic \(1994\)](#), [Remington \(2011\)](#).

<sup>5</sup>For important studies demonstrating the importance of pre-communist variation in post-communist outcomes, *c.f.* [Darden and Grzymala-Busse \(2007\)](#), [Stark and Bruszt \(1998\)](#), [Stark \(1994\)](#).

<sup>6</sup>The most prominent studies of the Post-communist states are [Alesina and Fuchs-Shundeln \(2007\)](#) and [Pop-Eleches](#)

that highlights the intersection between macro-level factors and individual preferences. Recent evidence suggests that macro-level factors – including inequality and welfare state design (Finseraas, 2008a), ethnicity (Alesina and Glaeser, 2004, Alesina et al., 2001, Alesina and La Ferrara, 2004), and trade openness (Cameron, 1978, Garrett and Mitchell, 2001, Mares, 2005a, Rodrik, 1998, 1997) – condition individuals’ preferences for social policy. It also suggests that where such conditions vary more markedly – as in the developing world – preferences might look quite different, both in the aggregate and within otherwise similar groups in different country settings. My work joins this body of literature by exploring an under-studied macro-level determinant of support for social policy – institutional quality – and how it conditions the preferences of an important, but understudied, group – those who can potentially hide from the state.

In the next section, I outline my theory of support for social policy in settings where weak institutions hinder tax collection. Section 2 introduces the dataset, measures, and empirical strategy. Section 3 presents the main empirical results, along with robustness checks on the results. Section 4 concludes.

## 1 Social Policy Preferences and Institutional Quality

The starting point of most contemporary work on micro-level preferences for social policy is the Meltzer and Richards (1981) model, which focuses attention on two key aspects of social policy: redistribution and control. In this model, redistribution encompasses policy decisions about how the costs and benefits of social policy are distributed amongst individuals and firms. On one end of the redistribution spectrum, individuals’ contributions and benefits are completely decoupled, meaning that those who must pay more (for whatever reason) effectively subsidize the benefits of those who pay less or nothing at all. At the opposite end of the spectrum, one receives benefits commensurate with one’s contributions. Control, on the other hand, typically constitutes preferences

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and Tucker (2014). Haggard and Kaufman (2008) focus on macro-level determinants of social policy formation and reform in the region, but also discuss the implications of their historical institutionalist theory of social policy formation and reform for individual level preferences in the region. For prominent recent examples of work on the developing world, *c.f.* (Alesina and Glaeser, 2004, Alesina et al., 2001, Alesina and Giuliano, 2011, Alesina and La Ferrara, 2004, Ansell and Samuels, 2014, Berens, 2012, Cramar and Kaufman, 2011, Haggard et al., 2013, Ravallion and Loshkin, 2000, Wegner and Pellicer, 2011).

over whether there should be more or less state (as opposed to private) involvement in administering social policy. Although control is not an explicit variable in the [Meltzer and Richards \(1981\)](#), the emphasis in that model on ideal tax rates implicitly assumes that it is describing preferences over state run social policy systems. Subsequent extensions of the model, as well as work on social policy preferences in general, has tended to be more explicit about a focus on preferences for state controlled social policy (*c.f.* [Benabou and Ok \(2001\)](#), [Iversen and Soskice \(2001\)](#), [Mares \(2005a\)](#), [Moene and Wallerstein \(2001\)](#)).

Because the [Meltzer and Richards \(1981\)](#) greatly simplifies the exposition of my theory of institutionally driven preferences, it is worth reviewing briefly.<sup>7</sup> As this model (and others in this section) are mainly meant to fix ideas, I leave presentation of formal solutions to the forthcoming online appendix. In the standard [Meltzer and Richards \(1981\)](#) model, individuals pay a percentage of their individual income,  $\alpha_i$ , to the state in the form of a flat tax,  $\tau$ . This tax is used to finance a lump sum transfer to all citizens, which follows the budget constraint  $\sum_{i=1}^n \tau \alpha_i$ . Each individual therefore receives a transfer equal to the average productivity,  $\bar{\alpha}$  times the the tax rate,  $\tau$ . These transfers are subject to wastage that depends on the level of taxation. This can be expressed as  $\omega(\tau)$ , which is an increasing function of  $\tau$ . Based on this, the basic utility function of individuals can be written as:

$$u_i = \alpha_i(1 - \tau) + \bar{\alpha}\tau - \omega(\tau) \tag{1}$$

Equation 1 simply states that an individuals' utility is equal to their consumption, which is in turn composed of three terms representing their after-tax wages, social policy benefits, and any dead-weight costs associated with social policy, respectively. The key finding of the model is that when  $\omega = 0$ , all individuals who earn below the average income ( $\bar{\alpha}$ ) support redistributive social policy. This is because they take in more than they pay. Those above the average oppose redistribution, since they suffer a net loss.  $\omega > 0$  offsets the degree to which those below the average income profit from social policy, however, since it acts as an additional cost. As  $\omega$  increases, support for social policy declines, since it decreases the income range for which social policy benefits

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<sup>7</sup>The model I present is based on the individual-level version adapted by [Alesina and Giuliano \(2011\)](#), which is a bit clearer than the original.

outweigh the total costs (Becker, 1985, 1983).

Implicit in the model above, and most work on social policy, is the notion that contributions today will be collected and paid out tomorrow as prescribed by law.<sup>8</sup> While dead-weight costs do siphon some social policy funds in ways unforeseen in statute, these costs are generally treated in most models as something of an error term and not subject to serious analysis (*c.f.* Iversen and Soskice (2001), Moene and Wallerstein (2001)). Consider, however, that social policy shares some characteristics with investment: contributions made today are paid back tomorrow, subject to eligibility criteria. If this is the case, then work on the political economy of investment suggests that weak institutions challenge this assumption, however.

In his seminal work North (1990) argues there is a fundamental commitment problem between the Weberian state and its citizens with respect to investment. The state's monopoly on violence in its territory makes it the *de facto* final arbiter of property rights protection and contract enforcement in its domain (North, 1981, Tilly, 1992, Weber, 1947). Given this monopoly, there is little to prevent the state, from revising property rights and contracts at the expense of the citizenry where it suits the state's interests. Because investments today only bear fruit tomorrow, they are particularly vulnerable to decisions by the state to alter or selectively enforce policy in ways that allow it to generate rents (North, Wallis, and Weingast, 2009, North and Weingast, 1989). Moreover, in the absence of sanctions, an interested external higher authority, long time horizons, or other incentives it is the optimal strategy to break commitments where one can profit (*c.f.* Olson (2000, 1993)). Drawing on Coase (1960)'s pioneering work on transaction costs, North (1990) argues that the state's incentives to opportunistically meddle with investments effectively create dead-weight costs, making investment less attractive. Only strong institutions – human constraints on human interaction (North, 1990) – can create mechanisms that allow the state to commit to social policy.

If social policy is akin to investment, then weak institutions have a number of potential implications for social policy and preferences. In this paper I focus narrowly on the implications of poor institutions for revenue collection.<sup>9</sup> Tax collection is a costly endeavor that requires a real,

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<sup>8</sup>Although for an important exception, *c.f.* Kato (2003), who emphasizes the extent to which the government can credibly commit to using additional revenue to expand welfare state generosity as a factor for explaining welfare state funding reforms in the OECD. Pierson (2001b) also discusses expectations about the solvency of the welfare state as an important factor motivating reforms.

<sup>9</sup>For a more thorough discussion, see Marques (2015) Chapter 1.

credible threat of audit or punishment to insure compliance (*c.f.* [Allingham and Sandmo \(1972\)](#), [Alm, Martinez-Vazquez, and McClellan \(2014\)](#)). As in other policy spheres, lower level bureaucrats are key to the day-to-day operations of the tax system, particularly with respect to insuring that individuals and firms comply with their obligations ([Shipan, 2004](#)). Work on bureaucracy has long highlighted a fundamental principal-agent problem at the heart of the relationship between the bureaucracy and policy enforcement. In particular, bureaucrats can take advantage of the informational advantages of their positions in order to bend policy to match their preferences, minimize their effort, or maximize rents ([Huber and Shipan, 2002](#), [McNollgast, 1987](#), [Weingast and Moran, 1983](#)). Although this literature has highlighted ways in which these lower level officials can be bound to implement policy as prescribed by statute, these solutions are themselves dependent on institutional constraints. In weak institutional settings, where such constraints are absent by definition, bureaucrats' opportunities to ignore or manipulate statutes for their own benefit multiply ([Beazer, 2012](#)).

With respect to policies that require costly effort to enforce, bureaucrats can benefit from selectively enforcing the law so as to economize on effort. This is particularly important with respect to taxation policy. Existing work has shown that the amount of effort that government officials must put into collecting taxes varies both within and across industries based on business structure, firm size, and the mobility of assets ([Alm, 2012](#)). Those whose business requires large stocks of fixed capital or use immobile assets, such as heavy industry, large-scale agriculture, or extractive sectors, are much easier for tax officials to monitor and tax ([Easter, 2002](#), [Gehlbach, 2008](#), [Haber, Maurer, and Razo, 2003](#)). Conversely, those involved in businesses with mobile assets, such as small firms, retail, and human capital intensive services, require much more costly effort to monitor ([Alm, 2012](#), [Kleven et al., 2011](#), [Slonimczyk, 2012](#)). Similarly businesses dominated by cash transactions and high employee turnover are also difficult to monitor ([Gimpelson and Zudina, 2012](#), [Ovtcharova and Popova, 2001](#), [Yakovlev, 2001](#)). Faced with high auditing costs, officials are more likely to shirk on their responsibility to collect taxes from such groups, allowing them to engage in tax evasion and free-riding, and instead focus on extracting taxes from the more easily monitored ([Easter, 2002](#)). Such shirking is particularly associated with, and helps to perpetuate, weak institutions [Gehlbach \(2008\)](#).

Mares (2005a) applies the argument specifically to social policy, noting that as institutional quality declines low-level bureaucrats are less likely to fully collect social policy contributions. The unwillingness of the authorities to pursue tax evaders effectively turns social policy funds into a leaky bucket, where evasion siphons off *de jure* revenue and results in *de facto* shortages and lower benefits. Mares (2005a) argues that this is akin to imposing additional dead-weight costs on individuals, modeling the cost as a function of the extent of tax evasion. Returning to equation 1, one can approximate Mares' model by defining dead-weight costs as  $\omega(\tau, q)$ , where  $q$  is the strength of institutions (and therefore the strength of tax enforcement) and  $\frac{\partial \omega}{\partial q} < 0$ . As should be readily apparent, the individual's utility is decreasing in  $\omega_i$ , which means that it is decreasing in  $\tau$  but increasing in  $q$ . The better institutions, the lower dead-weight costs and the more individuals support social policy. Again, implicit in this argument is that weak institutions decrease support for *state-run* social policy, since it is the state that is weakly constrained. Privately run solutions may still be viable, although this depends on the ability of actors to make agreements and enforce contracts outside the aegis of the state. Consequently, Mares would predict:

**Hypothesis 1.** *As institutional quality decreases, the probability that the average member of the populace or firm supports social policies that are more redistributive and vest control in the state decreases.*

Whereas Mares (2005a) focuses primarily on the average member of the populace, however, it is important to note that not everyone loses in settings where tax evasion is rampant. Indeed, those who can hide a portion of their income from authorities potentially stand to gain quite a lot if social policy benefits are not tied to contributions. So long as the ability to evade taxes outweighs negative utility from the dead-weight costs of rampant evasion, tax evaders can profit from social policy. Put another way, the tax savings from evasion may counterbalance (or even outpace) the overall loss in benefits from poor institutions. To see this, imagine another extension to the basic Meltzer and Richards (1981) model that allows individuals to hide some portion of their wages and evade part of their tax bill. Utility now takes the form:

$$u_i = \alpha(1 - \eta_i t) + \bar{\alpha}\tau - \omega_i(\tau, \bar{\eta}) \quad (2)$$

where  $\eta_i$  captures the proportion of wages the individual reports to the tax authorities and is subject to taxation. We define it is a function of individual characteristics,  $x_i$ , and the strength of institutions,  $q$ . We assume that individuals with  $x_i = 0$  do not have characteristics that allow them to evade taxes, resulting in  $\eta_i = 1$ , while individuals with  $x_i = 1$  are able to evade taxes such that  $0 < \eta_i < 1$ . We further assume that for individuals with  $x_i = 1$  the proportion of taxes paid is increasing in institutional quality  $q$  or  $\frac{\partial \eta}{\partial q} > 0$ . Following the spirit of Mares' model  $\omega_i$  is dead-weight cost that is a function of the tax rate  $\tau$  and the average level of tax evasion  $\bar{\eta}$  and decreases the amount the state has to redistribute.

Intuitively, equation 2 provides several important insights. First, recall that in the standard [Meltzer and Richards \(1981\)](#) model, support for redistribution is declining in income,  $\alpha$ , since higher wages imply higher taxes. The ability to hide income offsets this relationship, however, since the lower  $\eta_i$  the more of one's income can be hidden from the state. Consequently, one would expect support for social policy to be decreasing in  $\eta_i$ , *ceteris paribus*, since lower reported wages result in lower taxes. Second, conditional on the characteristics,  $x_i$ , that allow one to evade taxes, we would also expect that support for redistribution amongst tax evaders is also decreasing in institutional quality. This is because by definition  $\frac{\partial \eta}{\partial q} > 0$ , which implies that it is more difficult to hide taxes where institutional quality is good. Better institutions therefore decrease the effectiveness of tax evasion and decrease the benefits of free-riding. Third, the exact relationship between the proportion of taxes an individual pays,  $\eta_i$ , and the average proportion of taxes paid by society as a whole,  $\bar{\eta}$ , is also important. For free-riders to support redistribution, personal cost savings from hiding wages must out pace increases in the overall dead-weight costs of social policy brought on by tax evasion. Finally, it is worth noting that equation 2 has no real implications for existing theory based on income, demographic, or risk-based predictors of support for social policy. These should continue to hold predictive power in settings where free-riding is rampant, even though overall support for social policy may be lower. Taken together, we would expect:

**Hypothesis 2.** *As institutional quality decreases, the probability that those with facility in evading taxes support social policy that is more redistributive and vests control in the state increases.*

## 2 Data Sources and Methodology

In this paper, I make use of the Life in Transition Survey (LiTS) of 29,000 respondents conducted by the European Bank for Reconstruction and Development across 29 transition countries in 2006.<sup>10</sup> In keeping with the focus of this dissertation on the post-communist world, I exclude Turkey from my analytical sample. While dropping Turkey may entail some loss of external validity, doing so creates a sample in which all countries experienced state socialism, thus helping to somewhat mitigate causal issues related to historical legacies.<sup>11</sup> To form the sample, households were randomly selected in a two stage process. Within households, the nominal head of household was asked questions about wellbeing, assets, and economic satisfaction. Afterwards, a randomly selected household member over the age of 18 was asked to give responses to additional questions. In the analysis below, I take the respondent who answered questions at this second stage as the unit of analysis.<sup>12</sup>

In order to measure attitudes towards state-controlled, redistributive social programs, I make use of the following question from LiTS 2006:

*Do you think the state should be involved in the following- Reducing the gap between the rich and the poor.*

- 1) Not Involved
- 2) Moderately Involved
- 3) Strongly Involved

Responses are summarized in figure 1. This question clearly taps the control and redistribution dimensions of social policy, as it references a leveling effect between the rich and the poor as well

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<sup>10</sup>LiTS 2006 covers Albania, Armenia, Azerbaijan, Belarus, Bosnia and Herzegovina, Bulgaria, Croatia, Czech Republic, Estonia, Former Yugoslav Republic of Macedonia, Georgia, Hungary, Kazakhstan, Kyrgyz Republic, Latvia, Lithuania, Moldova, Montenegro, Mongolia, Poland, Romania, Russia, Serbia, Slovak Republic, Slovenia, Tajikistan, Turkey, Ukraine, Uzbekistan.

<sup>11</sup>For a further development of this argument, *c.f.* [Pop-Eleches and Tucker \(2014\)](#). In unreported robustness checks, I include Turkey in the main analyses presented in the next section. Results remain robust to this permutation.

<sup>12</sup>Results are also robust to using the characteristics of the household's breadwinner. For more information on the methodology of the survey, including information on PSU selection, selection of respondents from selected households, and interviewing techniques, *see* [EBRD \(2007\)](#), [Synovate \(2006\)](#).

as the state's role in it. Moreover, LiTS is the only survey of which I am aware that taps welfare state preferences in all the post-communist countries and this is the 2006 survey is the only version with a direct question on social policy preferences.<sup>13</sup> Nonetheless, it is worth keeping in mind the limitations of the question. First, the wording of the question and responses make it difficult to disentangle control and redistribution. Respondents who oppose social policy may oppose social policy in general, but not care about the state's role, or may support social policy and be skeptical of the state.

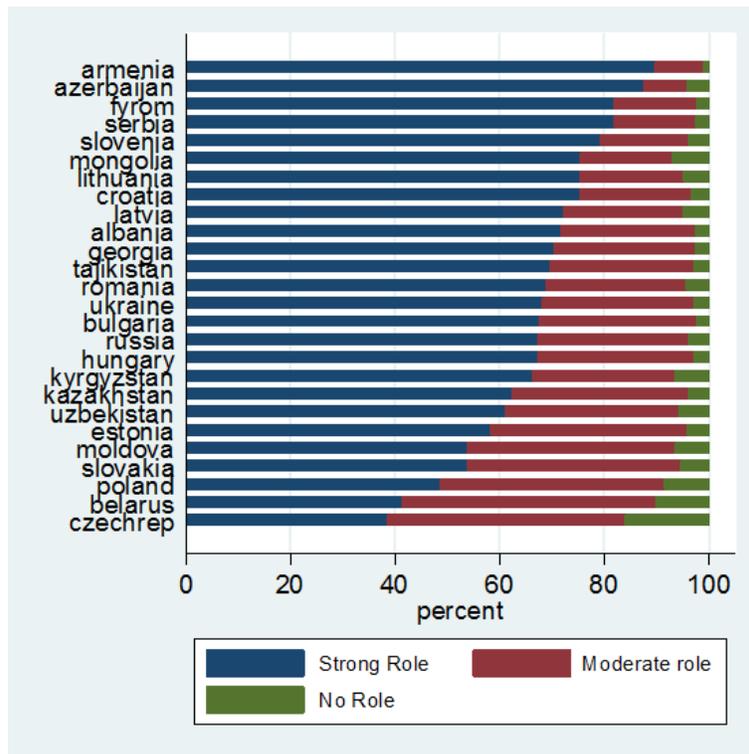


Figure 1: Preferences for a State Policy (LiTS)

Second, the dependent variable does not capture trade-offs between an increasing role of government programs in narrowing the inequality gap and the increasing costs of such programs. As [Kenworthy and McCall \(2008\)](#) point out, respondents might feel differently about redistribution if they believe they are likely to bear the tax burden to fund it. My framework predicts that variation

<sup>13</sup>[Pop-Eleches and Tucker \(2014\)](#) use an alternative, in which they construct an index using the dependent variable discussed here and questions about whether spending for specific groups should be increased. I forgo this approach, as the index lumps together several questions about the priority of spending without clearly delineating between social policy dimensions. Most individual components are either not about social policy (public goods provision in numerous areas) or have little to do with the specific social policy dimensions here (attitudes towards poverty and inequality).

in preferences for redistribution follow from heterogeneity in subjects' expectations about the net costs and benefits, however. Consequently, the omission of cost considerations is less problematic, since individuals will only consider their contributions and net losses from poor institutions in cases where this is truly important to them. If anything omitting cost considerations from the question should flatten responses and introduce bias against finding a result. Finally, the lack of specificity in the question as to how redistribution will occur and who receives it means that respondents could have very different programs in mind when formulating answers to the question. As a consequence, results based on this instrument may mask a great deal of heterogeneity in actual attitudes towards specific programs. Unfortunately, there is no principled way to separate out these effects using this data.

Figure 1 summarizes responses to the survey instrument across countries. Looking at the sample as a whole, it is interesting that the overwhelming majority of respondents – 68.72% – believe in strong state involvement in redistribution, whereas 26.67% believe in moderate state involvement. Only 4.61% of respondents believe the state should not redistribute at all. Interestingly, there does not appear to be a large difference in responses related to institutional quality. Figure fig:scatter4 presents a scatter plot with preferences for social policy along one axis and two measures that capture different aspects of institutional quality along the other. The first is the World Bank's Rule of Law measure, which captures confidence in the law and the extent to which actors abide by it, while the second is the Freedom House democracy index, which captures accountability. I discuss these in more depth in the next section. For now, it is worth noting that there seems to be no clear relationship between support for social policy and these measures.

## 2.1 Measuring Institutions

Recall that in this dissertation, institutions are quite broadly defined as humanly devised constraints on human interactions (North, 1981). In the free-rider mechanism, tax evasion is enabled by weak constraints on low ranking officials, who take advantage of weak supervision and punishment (i.e. low state capacity) under poor institutions to avoid expending effort going after tax evaders. Under this mechanism, officials only exert effort to enforce tax laws with respect to individuals and businesses who are visible to the state and easy to audit. Conceptually, this means that the measure

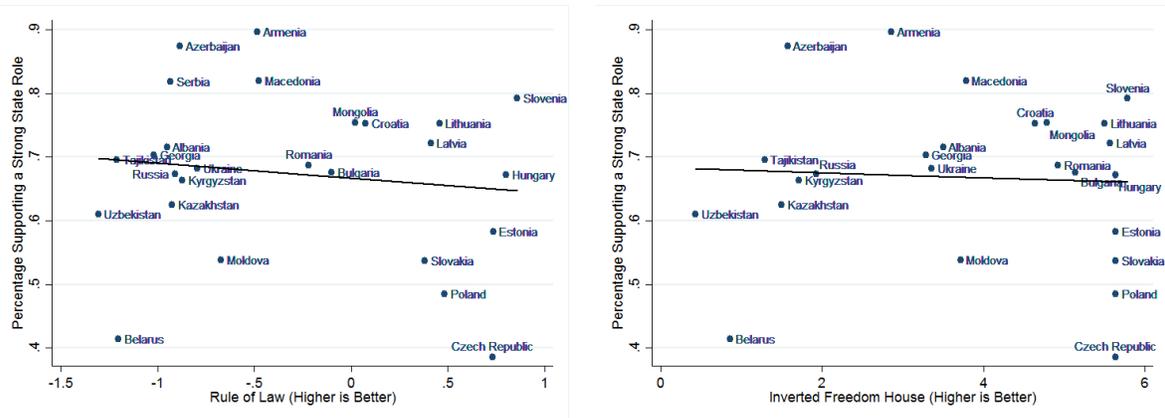


Figure 2: Support for Social Policy and Institutional Quality

of institutional quality used to test the theory should capture the extent to which lower level officials are bound to implement policy as written. Therefore, in my analysis I focus primarily on measures that reflect the quality and consistency of policy implementation and the ability of the state to police tax evasion. This being said, cross-national measures of institutional quality are highly correlated in ways that make it difficult to be sure that they accurately capture the conceptual weaknesses in institutional quality they are meant to.<sup>14</sup> As a consequence, it is sometimes difficult to evaluate *how* institutional quality shapes preferences for social policy. Nonetheless, this cross-national test provides a good first-cut test.

To capture the concept of interest – the extent to which institutions bind officials and constrain them to enforce tax policy – I make use of two primary measures. The first is the government effectiveness sub-component of the World Bank’s World Governance Indicators project [Kaufmann et al. \(2010\)](#). This index was constructed using a weighted aggregation of measures of the quality of public and civil services, their degree of independence from political pressure, the quality of policy implementation, and the state’s ability to credibly commit to policy. Conceptually, this measure neatly encapsulates the inconsistent tax policy enforcement that enables tax evaders to avoid making social policy contributions and enables free-riding. The second is a related measure from the World Governance Indicators project – the rule of law index – that captures confidence in the law and the extent to which actors abide by it. Again, conceptually this measure reflects

<sup>14</sup>For thorough discussions of the usefulness of these measures, see [Munck and Verkuilen \(2002\)](#), [Trier and Jackman \(2008\)](#).

the extent to which actors believe policy in general – and by extension tax policy – will actually be enforced, informing beliefs about how easy tax evasion should be to get away with. Whereas the government effectiveness indicator focuses on the government and bureaucracy as enablers of evasion, however, the rule of law indicator focuses on the social propensity to cheat or break the law more broadly. Both are important, albeit different, aspects of institutional quality.

I supplement the Government Effectiveness and Rule of Law indices with a more objective measure of the ability to evade taxes: a direct estimate of the size of the informal economy. Developed by [Schneider, et al. \(2010\)](#), this measure defines the informal economy as all business activity not reported to the government relative to GDP [Schneider, et al. \(2010\)](#). This measure was developed for 151 countries and makes use of data on government size, labor market characteristics, and government effectiveness (from the World Bank) to fit a MIMIC (Multiple Indicators Multiple Causes) model that predicts the share of the informal sector in the total economy.<sup>15</sup> While not a direct measure of institutional quality, per se, it nevertheless provides a measure of the extent to which the government fails to control tax evasion and monitor economic activity, which is key to the free-riding mechanism. It follows that the larger the informal economy, the more likely it is that tax evaders believe they will be able to get away with free-riding on social policy. For ease of interpretation, I rescale the variable so that it measures the size of the formal economy. Therefore higher values imply better institutions as with the other measures used here.

Some studies have used the ratio of tax revenues in GDP as a proxy for the ability of states to collect taxes ([Musgrave, 1987](#)). In this paper, I reject this approach for several reasons. First, theoretically, decisions about tax revenue often have as much to do with policy priorities as actual state capacity. According to the UN, average levels of tax revenue as a share of GDP in the US and Japan were 10.18% and 17.53%, respectively, between 1994 and 2009, which contrasts with an average of 33% for Greece. One would be hard pressed to say the latter had better tax collection capacity than the former given recent events, but that is what tax revenue in GDP measures would imply. Second, empirically, tax revenue as a share of GDP is poorly comparable across countries. Work on revenue mobilization has shown that decisions about the level of tax to GDP are

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<sup>15</sup>See [Schneider, et al. \(2010\)](#) for details on the procedure and a discussion of its limitations relative to other techniques. I select the 151 country measure, despite its lower quality, in order to preserve the maximum number of countries in my estimation. Selecting the higher quality 120 country measure would result in losing 6 countries, bringing my sample down to 20 second-level units.

not exogenous, but depend greatly on institutional quality, economic structure, and demographics (Musgrave, 1987, Prest, 1979). These factors place limits on taxation that must be accounted for in order to create a comparable measure (Le et al., 2008).

Tax capacity, defined as the ratio of actual tax revenue in GDP to potential tax revenue in GDP, is one attempt to overcome problems with tax revenue in GDP as a proxy for tax collection.<sup>16</sup> Again, however, this measure suffers from the fact that as a ratio of actual tax revenues to predicted ones, tax capacity is a political choice, not just one dependent on state capacity. This results in strange values of the measure from the standpoint of measuring state capacity. For example, Le et al. (2012)'s version of the measure rates the US (0.77), China (0.48), and Japan (0.47) lower than Argentina (0.95), Russia (0.81), and Ukraine (0.96). In addition, potential values are calculated (in part) based on institutional quality, which means that the measure expects less of countries with poor institutions by construction. Consequently, it seriously underestimates how weak constraints enable abuse and is unsuitable for studies chiefly concerned with such constraints.

In addition to my three preferred measures, I also examine a related element of institutional quality: accountability. Although political accountability at the highest levels need not constrain tax officials or insure that they expend costly effort to insure tax compliance, it has been shown to be an effective check on the behavior of lower level officials. To measure accountability, I also use additional measures of institutional quality that capture political accountability at the highest levels – Polity IV, Freedom House Nations in Transit, and the World Bank's Voice and Authority measure (Gehlbach and Keefer, 2011, Haber, 2007, Qian, 2003, Rodrik, 2000a). From the Polity IV measure, I make use of the Xconst measure, which assesses formal constraints on the executive by other parts of the government (Marshal et al., 2013). The Freedom House measure instead emphasizes civil liberties and political rights, taking a broader approach to democracy along Schumpeterian lines (Freedom House, 2012, Schumpeter, 1943). The Voice and Authority index similarly focuses on the ability of citizens to select their leaders, freedom of expression, association, and media, and the extent to which formal structures and institutions bind government officials (Kaufman et al., 2006). Intuitively, while even highly accountable officials at the highest levels may not be able to control lower level bureaucrats or abstain from opportunistic manipulation of social policy, they

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<sup>16</sup>Le et al. (2012) is the most recent and complete dataset generated using this technique. For prior attempts, *c.f.* Bird et al. (2004), Le et al. (2008), Lotz and Morss (1967), Stotsky and WoldeMariam (1997).

should nonetheless be more likely to behave properly than weakly accountable politicians (Beazer, 2012, McNollgast, 1987, Weingast and Moran, 1983).

Finally, I also include the control of corruption sub-component of the World Governance Indicators measure in my analysis. This measure captures the use of public power for private gain. Although the mechanism linking corruption to preferences for social policy flows most intuitively through political connections (the misappropriation mechanism), rather than the possibility of free-riding, it is still related to both accountability and the degree to which officials can commit to policy enforcement and tax collection.

My analysis carries a number of limitations. First, as I discuss in more detail below, due to the small number of countries it is difficult to include a large number of country level variables in the model. Attempting to include multiple measures in the regression and induce a “horse race” to see which lose significance, aside from being atheoretical, would create identification problems. Second, the high degree of correlation between the various measures and indices complicates the ability to separate out the effects of each cleanly. Significance could be due to strong correlations rather than the validity of specific mechanisms. Finally, the relatively small number of country level observations (25–27 depending on the measure of institutions) creates a strong bias against finding any direct, unconditional effect of institutional quality on preferences for social policy. While multi-level modeling produces relatively unbiased and consistent estimates of individual and cross-level effects in cases where the number of second level units is low, estimates of the second level unit effects themselves are likely to have strongly biased standard errors (Cameron, Gelbach, and Miller, 2008, Gelman and Hill, 2007, Leoni, 2009). Consequently, we are unlikely to find direct evidence of a direct effect of institutions here, although we should be able to detect conditional ones (i.e. macro- micro-level variable interactions).

In order to construct these measures, I make use of values averaged from 2000 to 2005.<sup>17</sup> Data from Polity IV is unavailable for Bosnia, and the Schneider, et al. (2010) index excludes Bosnia, Serbia, and Uzbekistan. In order to insure greater comparability across measures, I exclude Bosnia from my analysis entirely, but only exclude Uzbekistan and Serbia in specifications with

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<sup>17</sup>I also attempt using 2005 values and across the entire post-communist period as robustness checks. Results remain qualitatively similar.

the Schneider index.<sup>18</sup>

## 2.2 Measuring the Ability to Evade Taxes

In order to proxy for individual's ability to evade taxes, I draw on extensive work on tax evasion and informality in order to construct proxies for individual's ability to evade taxes.<sup>19</sup> Theoretically, characteristics associated with tax evasion in the literature are thought to increase auditing costs for the state. Faced with increasingly high auditing costs for particular groups, the state – particularly in settings where institutional quality and state capacity are weak – prefers to ignore such groups, focusing revenue collection on the easily monitored (Easter, 2002, Gehlbach, 2008). Here, I draw on three characteristics commonly associated with the ability to evade taxes.

The first characteristic that I exploit is self-employed status. Theoretically the self-employed are uniquely positioned to evade taxes, because the small scale of their activity and tendency towards cash transactions (at least on the part of the smallest firms) make it difficult to monitor their activity closely (Slemrod, 2007, Torrini, 2005). The inability to closely monitor the self-employed, in turn, creates opportunities for them to hide income and profits from the authorities, effectively avoiding the tax enforcement apparatus. Such individuals are also more likely to be able to avoid signing formal employment contracts, further insulating them from taxes.<sup>20</sup> Empirical work has provided ample evidence for this relationship, documenting the ability of self-employed individuals to evade taxes even in countries understood to have high levels of institutional quality (Engstrom and Holmlund, 2009, Feldman, 2007, Johansson, 2005, Kleven et al., 2011, Pissarides and Weber, 1989) as well as in the post-communist countries (Gorodnichenko et al., 2009, Slonimczyk, 2012) and developing countries more broadly (Pietrobelli et al., 2004). At the same time, at least in Eastern Europe, the self-employed are also particularly likely to have benefited from the transition away from the planned economy, as they were able to take advantage of liberalization to profit from

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<sup>18</sup>Including Bosnia in specifications for Freedom House and the various World Governance Indicators measures does not substantially alter the results.

<sup>19</sup>For a useful review of this literature, *c.f.* Alm (2012).

<sup>20</sup>It is important to note that countries vary widely in their coverage of the self-employed and in how this coverage is financed. While some countries exclude the self-employed completely, others include them. Tax arrangements also vary, although there is a tendency towards use of income and payroll taxes. This obviously has important implications for the relationship of the self-employed to the welfare state and ability to free-ride on it. In my main specifications below, I control for variation in coverage to account for this.

filling niches never envisioned by the plan (Earle and Zuzana, 2000). Consequently, in addition to being better at hiding income, the self-employed in the post-communist bloc are also likely to be high income, making taxes (and social policy) unattractive.

To measure self-employed status, I make use of a dummy variable equal to one if individuals reported that they have been self-employed at any time during the last year.<sup>21</sup> All told 8.2% of LiTS respondents reported that they were entrepreneurs or self employed. Table 1 provides some summary statistics on the self-employed and the general populace. On the whole, this group tends to be younger, male, better educated, and (on average) in a higher income decile than the rest of the population. They tend to be most concentrated in the retail and agriculture sectors, and tend to be service workers (i.e. shop owners) or involved in crafts and related trades. As expected, these are precisely the sorts of individuals one would expect to be able to hide income or avoid payrolls.

Table 1: Characteristics of Groups Likely to Evade Taxes

	Full Sample	Self-Employed	Evasive Sectors	Evasive occupation
Age	46.5 (17.7)	41.54 (12.24)	38.37 (11.6)	41.64 (11.8)
Percentage Male	42	61	59	43
Education	Secondary	Vocational (Post-secondary)	Vocational (Post-secondary)	Higher Education
Income Decile	5.49 (2.87)	6.59 (2.84)	6.51 (2.67)	7.31 (2.48)
Self-employed	8.2	–	42	16.8
Sector (Modal)	Unemployed/Retired	Retail	–	Education
Sector (2nd)	Agriculture	Agriculture	–	Retail
Occupation (Modal)	Professionals	Service Workers	Service Workers	–
Occupation (2nd)	Service workers	Craft and related trades	Craft and related trades	–

Means are given for age and income decile, median for education, percentage males for gender, and the top 2 modal categories for sector and occupation.

Second, I also make use of the well-documented relationships between particular sectors and the ability to evade taxes. Straightforwardly, sectors with relatively high asset mobility, high turnover, and a propensity towards cash transactions are more likely to be able to evade payroll and other taxes (Fiorio and D’amuri, 2005, Gimpelson and Zudina, 2012, Yakovlev, 2001). Importantly, though, one would only expect this relationship for firms below a certain size, as the larger firms grow the easier they are to monitor, particularly in settings with weak institutions (Easter, 2002, Gehlbach, 2008). To capture this, I introduce a dummy variable equal to 1 for individuals who report working in either the construction or retail sectors and who work in firms with less

<sup>21</sup>For each occupation, respondents were asked “In this job did/do you work?” with response categories “1) For wages (worked for an employer)”, “2) As self employed or for a company you partly or fully own”, or “3) As an independent farmer”. Respondents were coded as self-employed if they responded with the second category.

than 16 employees.<sup>22</sup> All together, this group represents approximately 6% of all respondents. As Table 1 indicates, individuals in this group tend to be younger than both the average member of the population and the self-employed. Those in evasive sectors are more likely to be male and (on average) in a higher income decile than the broader populace, although these levels are comparable with the self-employed. This is in part, because 42% of respondents in this category report being self-employed and, like the self-employed, the majority of respondents in these sectors tend to be service workers or be involved in crafts and related trades. I refer to this group as the evasive sector in my analysis below.

Finally, I also make use of a measure based on individuals' occupations. Empirical work on tax evasion has shown that in addition to the self-employed and workers in retail, workers in industries with relatively weak paper trails for inputs and outputs are also likely to be able to engage in tax evasion, since compliance monitoring for such groups is particularly difficult (Kleven et al., 2011). In particular, empirical work has highlighted relatively skilled, high income occupational groups such as engineers, doctors, financial services agents, accountants, lawyers, and business owners as being particularly likely to hide income (Artavanis, Morse, and Tsoutsoura, 2012). In the post-communist settings, such groups have strong incentives to hide income, as wage decompression for these groups, along with deregulation and the opportunity to open private practices, insured these groups high incomes (Brainerd, 1998, Milanovic, 1999, Svejnar, 1999). Moreover, in countries with poor enforcement or loopholes in payroll or income taxation, such workers were particularly well-positioned to bargain for "black cash", annuities, or other wage structures that minimized their tax contributions (Yakovlev, 2001), facilitating free-riding on social policy. Making use of a survey question that asks individuals to place themselves into occupational categories for each of their jobs, I create a dummy variable indicating whether the respondent currently works in a high income, low paperwork occupation or as a manager or businesses owner: occupations that lend themselves to evasion.<sup>23</sup> For simplicity, I refer to this group as professionals henceforth.

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<sup>22</sup>The only instrument for firm size asks employees to estimate whether their employer has 1-15 employees, 16 - 100 employees, or more than 100 employees. I select the smallest category, as this group can most easily evade taxes. All results reported in the following section are robust to including those with employers in the 16 – 100 employee range. These estimates are available upon request.

<sup>23</sup>The occupational categories for this group roughly correspond to groups 1 and 2 in the Standard Occupational Classification 2000 and include professionals such as engineers, mathematicians, architects, computing professionals, medical doctors, dentists, pharmacists, lawyers, accountants, authors, and similar occupations, as well as managers and firm owners. Note that in the specifications below, results are robust to the exclusion of the first group – managers

Approximately 11% of respondents are professionals. As with those in evasive sectors and the self-employed, this group tends to be younger than average, although the percentage of males in this group (43%) is comparable to that of the populace as a whole. Interestingly, the average income decile for this group is much higher than the population average or those of the self-employed and those involved in evasive sectors. Only 16.8% of this group work as self-employed and the modal sector is education, with the next largest concentration of this group being in retail.<sup>24</sup>

## 2.3 Modeling Strategy

As a first step, I replicate the design of many existing studies of preferences for social policy in order to establish some basic intuitions about who supports social policy in the post-communist countries. The goal of this first test is to examine many of the major findings from previous work detailed in Table ???. I do this by estimating a simple, logit model with clustered standard errors and the latent form:

$$Y_{ic} = \alpha + \beta_1 X_i + \beta_2 Z_i + \delta_c + \epsilon_{(ic)} \quad (3)$$

Where  $Y_i$  is a binary variable based on the instrument on preferences for a state role in social policy introduced in section 2. The variable takes on a value of 1 if individuals support a strong state-role in closing the gap between the rich and the poor (e.g. a more redistributive, state-run system) and 0 otherwise.<sup>25</sup>  $X_i$  is a vector of individual-level variables of interest for individual  $i$  discussed below,

and business owners – as well as controlling for self-employment. More information on these categories and the validity of occupational self-reporting as compared to alternative ways of assigning respondents to occupations can be found in Denisova et al. (2009).

<sup>24</sup>While it may seem odd that the majority of this group are involved in education, evidence indicates that they are not normal public school teachers. Many of the individuals involved in education are in the private sector and in higher income deciles, although there is a large block of low-income, public sector education workers in the category. Unfortunately, due to the design of the LiTS survey it is difficult to back out specifics.

<sup>25</sup>I recode in this way, because of ambiguity in interpreting the answers of those who favor a moderate state role. Due to the fact that the survey instrument taps both control and redistribution dimensions, moderate responses may reflect preferences for less redistributive social policy, but support for state involvement if redistributive programs are inevitable. It may also reflect preferences for redistributive programs that are tempered by qualms about the state. The logic of those who oppose state involvement is likely similar, albeit more extreme. Consequently, the differences between these two categories are less theoretically interesting than comparison to those who favor strong state involvement: who are likely in favor of both redistribution and state involvement in it. Robustness checks using ordered probit models nonetheless produce similar results.

$Z_i$  is a vector of control variables for individual  $i$ ,  $\delta$  is a vector of country specific fixed effects for each country  $c$ , and  $\epsilon$  is the error term.

The vector  $X$  contains individual level variables that proxy for class and risk. In line with existing work, my main proxy for class-based theories is household individual income. As proxies for risk-based theories (and to capture different facets of risk), I then include measures of current unemployment, and individuals' perceptions of their own health. I also include measures of human capital as another way of getting at risk related to skill profile. I assign a dummy variable equal to one if individuals have worked as skilled professionals (doctors, lawyers, etc.). This particular group faced heavy wage compression and marginalization under the planned economy, but had skills uniquely suited to rapidly liberalizing economies during the transition. As a consequence, this group drove wage decompression during transition and was in high demand (Brainerd, 1998, Earle and Zuzana, 2000, Milanovic, 1999, Svejnar, 1999). One would therefore expect such individuals to have more portable skills, and therefore less risk, than others. Although this conception differs from the way risk models such as (Iversen and Soskice, 2001) conceive of skills, it is the only available measure. As noted above, however, this variable may also be proxying for ability to evade taxes in settings with weak institutions. LiTS also includes extensive questions about individuals' life history during the transition period, creating the possibility of using measures of revealed risk. Individuals who have suffered individual economic hardship the past are likely at risk in the future. Using available instruments, I include variables capturing the number of years during the transition period in which individuals faced cuts in their food consumption or wages, had to sell assets, and the number of years the individual was unemployed during the transition.

Finally, I also include an extensive set of control variables. These include age, gender, where the respondent is located (rural, urban, or metropolitan), household size, and minority status. Unfortunately, LiTS includes no traditional measure of ideological bias (i.e. party affiliation): an important control variable. In order to control for the possibility that individuals are ideologically biased, I include a measure of the respondents' opinion on the fairness of re-privatization. Previous work has argued both that reprivatization is a critical component of economic reform (Megginson, 2005), and has also used opinions towards it as a gage for pro-market sentiments (*c.f.* Berinsky and Tucker (2006), Denisova et al. (2009)). To the extent that attitudes towards re-privatization

reflect pro- or anti-market bias, using this attitude as a control allows us to account for ideology. In a similar vein, I also include a question about the respondent’s preferences for planned versus market economies. Finally, I also include a more problematic, variable that measures preferences for redistribution more directly. The variable mirrors the dependent variable, but omits reference to the state’s role. Consequently, it can be interpreted as a clean measure of preferences for redistribution. Although the similarity of this measure to the dependent variable poses the risk of effectively having the same variable on both the left and right hand sides of the equation, it is one of the only available ideological instruments. Including both of these variables increases confidence that results reflect bias against the state playing a role in redistribution, rather than against redistribution in general.

The second part of my analysis focuses on testing my theory of preferences for social policy under weak institutions. In order to estimate this relationship, I make use of a Multi-level Hierarchical (MLH) logit model. Multi-level models have advantages over rival estimation techniques for examining cross-level interactions (individual x region interactions), because they allow one to estimate the direct effects of both the macro-level variables of interest and their interactions, while also providing some defense against omitted variables in the form of fixed or random effects. These specifications also allow for the introduction of other macro-level variables of interest. Finally, an MLH approach makes fewer assumptions about the correlation of the error terms across macro-level units (Gelman and Hill, 2007, Stenbergen and Jones, 2002).<sup>26</sup>.

My specification takes the form:

$$Y_{ic} = \alpha_0 + \gamma_1 institutions_c + \beta_1 evasion_i + \rho_1 evasion_i * institutions_c + \gamma_2 Z_c + \beta_2 X_i + \xi_{1c} + \eta_c + \epsilon_i \quad (4)$$

*Institutions* and *evasion* are the proxies for institutional quality and the ability to evade taxes discussed in sections 2.1 and 2.2 (respectively),  $X_i$  is a vector of individual-level control variables for individual  $i$ , and  $Z_c$  is a vector of country level control variables for country  $c$ . The parameters  $\xi_{1c}$ ,  $\eta_c$ , and  $\epsilon_i$  represent a random slopes on the individual measure of evasion needed for the cross-level interaction to be identified properly, country specific varying intercepts, and the individual level

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<sup>26</sup>For an interesting discussion and simulation results illustrating the superiority of MLH models to traditional analytical techniques in survey settings where macro-level variation is of interest, see Leoni (2009)

error term, respectively. Following [Gelman and Hill \(2007\)](#) this equation can be thought of and interpreted as a standard regression, albeit one with six sets of predictors and three error terms.<sup>27</sup>

With respect to individual controls, I include all of the variables included in the purely individual-level regression. Of the variables indicating ideological bias, I only include the measure of support for reprivatization in my main specifications. As country level controls, I include two key country level variables, a country average of GDP per capita for the five years prior to the survey (2000 – 2005) and an index of the generosity of social policy.<sup>28</sup> The later is an update of the index of social policy (pensions, healthcare, unemployment, and disability insurance) first introduced by [Mares \(2005a\)](#) and captures both the scope of social policy coverage and the degree to which contributions and benefits are linked in each country in the year the LiTS survey was conducted (2006).<sup>29</sup> By controlling for pre-existing social policy (both the scope and the generosity of coverage), it is possible to partially separate out attitudes towards state control of social policy from attitudes towards the adequacy of existing social policy programs, as well as to control for policy variation that may *prima facie* complicate free-riding.

Before turning to the analysis, it is worth noting that the design outlined here potentially suffers from various causal inference problems. First, preferences for social policy and institutional quality may be co-determined by unobservable economic and political variables that have been omitted from the specification. One such cause could relate to historical factors, whether Communist era or pre-Communist ([Pop-Eleches and Tucker, 2014](#)). Second, institutional quality may be endogenous to expectations about tax evasion, with authorities constructing institutions based on expectations about the ease of tax collection ([Gehlbach, 2008](#)). Finally, preferences for social policy could well be endogenous to institutions, if elites construct the latter in order to contain demand for redistribution ([Acemoglu and Robinson, 2006](#), [Boix, 2003](#))

With respect to omitted variables, I use the sample itself to help control for the effects of the most problematic – historical and institutional legacies on preferences ([Alesina and Fuchs-Shundeln, 2007](#), [Pop-Eleches and Tucker, 2014](#)). Since all of countries in the sample experi-

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<sup>27</sup>For more on the logic behind the formulation of the model, see [Gelman and Hill \(2007\)](#)

<sup>28</sup>The small number of countries in the sample suggests caution in including a larger number of macro-level controls, therefore I do not do so in my preferred specifications. Nonetheless, in section 3.3 I test the robustness of my results against a wide array of additional country-level variables.

<sup>29</sup>Details on the construction of the index are presented in Appendix 5.

enced long spells under Communism, recent historical and institutional legacies are more comparable across this sample than any other, although some variation remains related to exposure to Communism. Nonetheless, in the robustness section that follows my main results, I offer additional attempts to control for some omitted variables that might co-determine institutions and preferences: inequality, resource rents, economic liberalization an reform, and variation within the post-communist countries in the effects of Communist legacies. Dealing with reverse causality is trickier, however, since the need to use multi-level models precludes instrumental variable strategies. Instead of dealing with this directly here, I refer concerned readers to [Marques \(2015\)](#), which provides evidence on the arguments used by actors during social policy debates. To the extent that actors really do consider how institutional quality shapes welfare state outcomes, it provides reassurance that – at least for contemporary preferences – the institutions are driving preferences.

While identifying a direct effect of institutional quality may be difficult due to endogeneity and omitted variable concerns, the conditional hypothesis advanced here – that individuals able to engage in tax evasion are more likely to oppose social policy in settings with good institutions – faces fewer problems. Here, I argue that identification can be achieved so long as we assume that these causal inference problems effect both types of responses (those able to evade and general members of the populace) in the same ways within a given country. If this is the case, then one can interpret my main specification (4) as an estimate of differences-in-differences between those who can evade taxes, on the one hand, and the populace at large, on the other, across settings with good and bad institutions (*c.f.* [Denisova et al. \(2009\)](#)). This estimate should be unbiased, so long as the assumption holds, and should give greater confidence in estimates of the cross-level effect.

## 3 Results

### 3.1 Pooled Individual Level Results

Table 2 explores the individual level determinants of support for social policy in the post-communist countries. Model 2.1 unsurprisingly provides strong support for class-based models of preferences for social policy, in which income determines support for social policy ([Meltzer and Richards](#),

1981). The clearest proxy – income decile – is a negative, significant predictor of support for a strong state role in redistributive social policy, as we would expect given existing work.<sup>30</sup> Education, which is sometimes also used as a proxy for income, is negative and not significant at conventional levels in this specification. The non-result on this variable is unsurprising, however, since education for most individuals in the sample would have occurred under Communist rule, where the skills taught would not necessarily correspond to highly sought (and remunerated) skills on the labor market.<sup>31</sup>

Risk stories, those in which correlates of risk drive preferences, also receive fairly strong support in model 2.1 (Iversen and Soskice, 2001, Moene and Wallerstein, 2001, Rehm, 2009). The measures of current risk – unemployment and poor self-assessment of one’s health – are both significant and positive predictors of support for social policy.<sup>32</sup> With respect to variables associated with human capital, which are sometimes proxies for risk, the story is mixed. As noted, education does not take on a significant sign in Table 2, even though it has been more or less robust in previous studies.<sup>33</sup> The professional dummy variable, however, is both negative and significant, indicating individuals with strong human capital and highly sought after skills oppose state-led social policy. This can be taken as supportive of risk-based theories of social policy preferences, given the labor market demand for such individuals in post-communist economies.

Several control variables were also significant at conventional levels. Age has a positive relationship with support for social policy in all models of Table 2, indicating that the older one is, the more supportive of a strong state role in social policy. This result may partially be a function of the strong correlation with this variable and exposure to Communist legacies (Pop-Eleches and Tucker, 2014). Women are also more likely to support social policy than men in this sample. These results are in line with previous work on social policy in other settings, as noted in Table ???. Other control variables – pensioners, household size, minority, and residency (urban versus rural) – were not significant predictors of support for social policy. With the exception of the pensioner dummy, these results are unsurprising from the standpoint of previous empirical results. The pensioner

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<sup>30</sup>For a summary of the results of previous studies, please refer to Marques (2015) Chapter 1.

<sup>31</sup>For a deeper discussion and justification of this point, *c.f.* Guriev and Zhuravskaya (2009).

<sup>32</sup>Although, *see* Iversen and Soskice (2001) and (Rehm, 2009) for discussions of the problems with using actual unemployment as an appropriate measure of risk.

<sup>33</sup>*See* table ??? for a summary.

dummy is likely insignificant mostly do to strong multi-collinearity with age, however, which is the primary criteria pension eligibility in this country sample.

Models 2.2 – 2.4 introduce various measures designed to control for the political ideology of respondents. All three proxy measures – opposition to re-privatization, opposition to the market economy, and support for redistribution (without references to the state) – for ideology are positive and significant, indicating that individuals with more “leftist” or anti-market ideologies are more likely to support state-led social policy. The results of Model 2.1 prove robust to the addition of these variables.

Finally, Model 2.5 introduces three proxy variables for hardships that individuals might have faced in the previous ten years, a test of the risk theory consistent with explanations focusing on past experience of material deprivation. The more years during the transition period that individuals had to make cuts in food consumption, the more likely they were to support state-led social policy, a result which holds at conventional levels of statistical significance. Interestingly, however, the number of years individuals faced wage cuts was not significant at conventional levels, although it is a positive predictor of support for social policy. This may have to do with the fact that the vast majority of individuals are coded as not having faced any wage cuts in the original dataset (i.e. coded as 0 rather than missing), which seems implausible given the experience of the transition. Similarly, individuals who did not earn wages in many years were also more likely to support social policy, although the result is not significant at conventional levels. Again, these results suffer from the same issue as the wage cuts variable. Finally, hardship as measured by asset sales was also not a significant predictor of support for social policy and its sign unexpectedly negative. As before, responses for this variable seem implausibly low given the transition. While there is little support for the risk theory using measures of material deprivation in this sample, this is likely due to problems with the survey instrument or the data, rather than the theory itself.

### **3.2 Cross-level Interaction Results**

Table 3 introduces the first of the three main tests by examining the relationship between self-employment, institutional quality, and preferences over redistribution and state control. Individual

level results are omitted for parsimony, with the exception of the main individual level variable of interest – the self-employment dummy. Results for these variables remain roughly the same as in table 2. and are available upon request. All macro-level variables in this and the remaining specifications have been centered on their mean values for ease of interpretation.<sup>34</sup> Of note at the individual level, the self-employment dummy variable is negative and significant, indicating that the self-employed oppose social policy. At the purely country level, Table 3 indicates that for the most part the direct effects of the macro-level variables are positive, supporting the notion that fears of mismanagement and/or waste in poor institutional settings serve as a drag on support for redistributive social policy. Interestingly, however, none of the institutional measures are significant predictors of attitudes towards state-led redistribution among individuals at conventional levels. This is a bit surprising, but may simply be due to the extremely small number of country level observations in the sample.

Turning to the cross-level interaction of interest, table 3 provides some evidence for the free-rider mechanism. As expected, the interaction between the institutional quality measures and the self-employment dummy is negative in all of the models in table 3. Further, the interactions which include the measure of government effectiveness, rule of law, the Freedom House measure of democracy, the Voice and Authority index, and control of corruption are significant at the 95% confidence level, while the degree of formal activity,<sup>35</sup> is significant at the 90% level. The negative signs on the co-efficients suggest that as institutional quality increases, support for social policy amongst the self-employed decreases, creating a preference cleavages between them and the general populace. This finding is consistent with the main hypothesis being tested here: individuals who are particularly well-positioned to free ride on social policy are more likely to support a weak link between contributions and benefits in settings with poor institutions, where free-riding is easier to get away with. Conversely, they are less likely to support such social policy in settings with good institutions, where it is harder.

An important thing to note, however is that while the interaction between the self-employment

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<sup>34</sup>Standardizing individual variables to the “grand mean” (the mean value of the entire sample) gives the results the interpretation that a unit increase in the macro-level variable influences the probability that an individual with characteristics equal to the sample mean will prefer a strong state role in redistribution by a percentage equal to the co-efficient (Gelman and Hill, 2007).

<sup>35</sup>Recall the original (Schneider, et al., 2010) measure was rescaled.

dummy and the institutional measures that best get at state capacity and the ease of tax evasion – measures of policy enforcement (Government Effectiveness index), the extent to which actors abide by the law (Rule of Law), and the size of the formal economy (Schneider Estimate) – is significant, so too are the interactions with measures of weak institutional quality that reflect other pathologies of poor institutions. Indeed, only the interaction between self-employment and the Polity IV measure of constraints on the executive fails to reach significance at conventional levels.<sup>36</sup> Although these measures are extremely highly correlated, the fact that all of these are significant implies that there may be more than one aspect of institutional quality at play here.

Figure 3 provides a sense of the substantive effects of being self-employed at different levels of institutional quality. For each specification in table 3 I generate a set of predicted probabilities of support (and 95% confidence intervals) for the median self-employed individual across the range of institutional quality.<sup>37</sup> To insure comparability across measures, the institutional variables have been rescaled into percentiles of the country sample: countries with the weakest institutions in the sample are located at the 1st percentile and those with the best are at the 99th. Across all measures, support for a strong state role in redistributive programs for the median self-employed individual universally declines as institutional quality improves across all measures. The largest decline occurs with the informality index, with movement from the 1st to the 99th percentile resulting in a 35% decline in support for a strong state role in social policy. The shortest declines occur with the government effectiveness and freedom house scores, where support for a strong state role in social policy declines by about 15%. This finding is consistent with the expectations of the free-rider hypothesis. Such effects are substantively very large, with even shorter transitions (such as between the 50th and 75th percentile) generating substantively large effects between 6% and 10%. By contrast [Rehm \(2009\)](#)'s micro-level study estimates effects along the magnitude of 3% to 6% effects for income and occupational unemployment along similar ranges.

Figure 3 also provides predicted probabilities for the median non-self employed individual for comparison. As a general rule, support for social policy for a median, non self-employed

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<sup>36</sup>This results should not be too surprising. Corruption and lack of constraints at the highest levels of government do not necessarily trickle down to the actual experiences of citizens ([Treisman, 2007](#)). As individuals are more likely worried about local bureaucrats than the presidential administration, measures that get at how institutions constrain more general governmental malfeasance are likely to have more explanatory power.

<sup>37</sup>Predicted probabilities are generated using a quasi-Bayesian approach.

individual is mostly flat across the voice and authority index. It improves slightly as the government effectiveness and freedom house measures increase, although this increase is within the 95 percent confidence interval. For the other institutional quality measures, however, support for social policy among the non-self-employed declines along with the quality of institutions. The steepest decline occurs with the index of informal activity, where the preferences of individuals decline by about 20% as one moves from the 1st to the 99th percentile. The shortest decline is with the Rule of Law measure, where support declines by about 15% as one moves from the 1st to the 99th percentile. While interesting, it is important to read these results cautiously, as the main effects of institutions were not significant in our main specification. This finding is interesting, because it suggests weak support for the Macro-economic risk mechanism, in which support for social policy decreases as institutions improve due to lessening macro-economic volatility.

The key takeaway from figure 3, is that in all specifications the self-employed and non self-employed have similar preferences when institutions are weak. By most measures, these two groups are statistically indistinguishable for countries below the 25th percentile of institutional quality.<sup>38</sup> Afterwards, self-employed individuals are less likely to support a strong state role in social policy than the non-self-employed. More importantly, the 95% confidence intervals for the estimated probabilities of support for state-run social policy do not overlap, suggesting that the cleavage is significant at conventional levels. Critically, the magnitude of the cleavage increases as institutional quality decreases. This finding is consistent with the free-riding mechanism, which posits that the self-employed only support redistributive, state-controlled social policy in settings where they can free-ride and will oppose it otherwise.

While not strictly part of the hypotheses being tested in this paper, the fact that self-employed and non self-employed individuals have similar preferences at the lowest levels of institutional quality is interesting. The most straightforward explanation has to do with how poor institutions change the utility function of self-employed individuals by enabling tax evasion. Recall that the self-employed typically have higher than average income in the post-communist states, so where

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<sup>38</sup>The Voice and Authority index and the Freedom House measure are exceptions. With the Voice and Authority index the self-employed are statistically more likely to support a strong state role in social policy below the 6th percentile and are indistinguishable between the 6th percentile and the 35th percentile. With the Freedom House measure, the probability of support for a strong state role in social policy between the self-employed and the non self-employed is indistinguishable below the 20th percentile.

tax evasion is not possible, they bear a heavier taxation burden (and oppose the welfare state). If the free-riding mechanism is correct, support for social policy at lower level stems from the ability of the self-employed (and other groups like them) to evade taxes. For support for social policy among the self-employed to be similar to the rest of the populace, therefore, they would need to be evading enough to put them at or below the tax rate of the general populace.

Empirically, this is not particularly far fetched. Consider the case of Russia, which is in the bottom 25th percentile along all of the measures of institutional quality used here – the point at which divergences in support for social policy amongst the self-employed and non self-employed begin to emerge. Evidence from Russia suggests that evasion is easy and widespread for the self-employed and others in the informal sector ([Gimpelson and Zudina, 2012](#)). Using data from a survey of 10,000 Russians, [Slonimczyk \(2012\)](#) for example finds that only 60% of informal sector entrepreneurs (i.e. business owners) claim to remit social taxes to authorities, versus 95% for formally registered entrepreneurs. For those who do not own businesses, but engage in self-employed activity, this figure falls to around 6%. Thus, evasion rates are quite large in poor institutional settings and may go a long way towards explaining why support rates for the self-employed and non self-employed are similar at low levels of institutional quality. As institutional quality improves, however, evasion ceases to be an option and the self-employed likely pay rates more similar to other wealthy individuals, thus making them less supportive.

Tables 4 and 5 test the conditional effect of two additional measures of the ability to evade taxes – working in a sector associated with tax evasion and professional occupation – on support for a strong state role in social policy. The main effect of being in an evasive sector is not significant at conventional levels in any of the specifications in Table 4, although the sign is negative as expected. This may be due to the extremely small number of such individuals in the sample (6%) or due to the imprecise nature of the measure. By contrast, the dummy variable for professionals is significant and negative, as expected, in Table tab:indivprof.

With respect to the interactions of interest, in both cases, the results mirror those from Table tab:indivselfemp. The interaction between working in a sector associated with tax evasion and the measures of institutional quality are negative and significant in all cases except for the Polity IV measure of constraints on the executive. Similarly, the main effect of the professional dummy

is both negative and significant at conventional levels in in Table 5, as expected. In both cases, the results suggest that as institutional quality improves, support for social policy among professionals declines, consistent with the free-riding mechanism.

Finally, Figures 4 and 5 illustrate the substantive effects of the various models in tables 4 and 5. As with figure 3, figure 5 indicates that the preferences of professionals and the median individual are statistically indistinguishable at low levels of institutional quality. Their preferences diverge as institutional quality improves, however, with the preferences of professionals declining more steeply. A similar pattern holds for individuals associated with sectors with facility in evading taxes (table 4), although the results are worth discussing in more depth because they are a bit different from those of the other two measures. At levels of institutional quality below the 25th percentile for most measures of institutions, the median individual in an evasive sectors appears much more likely to support social policy than her counterpart in the general populace. The confidence intervals for predictions of support for social policy for these groups overlap for most measures between the 25th and 62nd percentile, after which the general populace is most supportive of social policy. This contrasts with self-employed and professionals, whose support for social policy is indistinguishable from that of the general populace at low levels of institutional quality and diverge as institutional quality decreases. Likely, this may have to do with the fact that this group is a mix of self-employed (42%) and low wage service sector workers. Regardless, these tests provide additional evidence in support of the free-rider hypothesis.

### 3.3 Robustness checks

In order to guard against specification problems and alternative explanations for the results in the previous section, I ran a variety of robustness checks.<sup>39</sup> I began by checking whether results were robust to other methodologies often used in the literature – traditional OLS and logit models with cluster-corrected errors and multi-level OLS, yielding results that are qualitatively similar to those reported in the previous section. I then checked the robustness of the MLH results presented above to various individual level specification problems. First, individuals’ preferences could be a function of the characteristics of the head of household (the primary breadwinner) rather than

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<sup>39</sup>Results of these tests are not presented here but are available upon request.

their own. I substituted the characteristics of the head of household (income, employment, etc.) and recoded the three proxies for ease of tax evasion according to data on the head of household. Results continue to hold, indicating that preferences are formed based not only on the individual's situation, but on that of their broader household. Second, I introduced specifications with the two alternative measures of ideology – support for planned economies and support for redistribution (without references to the state) – discussed in section 2.3. Third, I also checked whether the main results are robust to the inclusion of hardship measures, indicating how badly individuals fared during the economic collapse that followed the political collapse of Communism. Finally, because the retired make up a very large proportion of the survey sample and can be expected to have preferences quite different than that of the rest of the population, I also reran my specifications omitting those over the age of 65. None of these permutations substantially alters the results.

Moving to macro-level specification errors and alternative explanations, I then introduced a number of additional country-level variables into my main specifications. Inequality, rentier state dynamics, and government spending are all additional variables suggested by the literature (Berens, 2012, Ross, 2001, Wilensky, 1975). I checked the robustness of the main results using the GINI index, a measure of resource rents as a percentage of GDP, and government expenditures as a percentage GDP to proxy for these additional variables.<sup>40</sup> Results can be found in the online appendix. None of these additions alters the main results much, although the interaction between the Polity IV executive constraints and evasive sectors does become negative and significant. In unreported specifications, I also check whether non-linearities between the main variables of interest at the individual level and these additional macro-level results could be driving the relationship.<sup>41</sup> Again, results are robust to all of these permutations.

Similarly, a more rapid pace of economic reform (and expectations on return on human capital and investment) may be responsible for diverging attitudes across the sample, rather than institutions per se. This is especially of concern in the post-communist setting, where transitions to the market economy were accompanied by simultaneous reforms of political and market institutions that were deeply intertwined Frye (2010), Gehlbach (2008). To account for this possibility, I also introduced several variables created by the EBRD to evaluate the pace of economic reform in the

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<sup>40</sup>All data obtained from the World Bank.

<sup>41</sup>These specifications are available upon request.

transition economies into my main specifications ([EBRD, 2012](#)). The EBRD's indices of economic reform include measures of the extent of large and small-scale privatization, the extent to which the government has passed and enforces anti-monopoly legislation and has lowered barriers to business entry, and price liberalization. Results are presented in the online appendix. Of the newly introduced variables, only the variable measuring anti-monopoly reform is significant at conventional levels, with the result holding true for all specifications and all proxies for ease of tax evasion. The greater reform in competition policy and the lower the barriers to entry, the weaker support for social policy. Even after accounting for the reform process, results again remain largely the same as the base specifications reported above, although the interaction between self-employment and the measure of formality now fails to reach conventional levels of significance.

In unreported regressions I also explored whether the construction of macro-level variables made a difference in the results. Use of 2006 values (the year before the survey was conducted) of the institutional variables or averages taken over the full post-communist period make little difference, although the [Schneider, et al. \(2010\)](#) measure drops slightly below conventional significance levels in all specifications when these permutations are used.<sup>42</sup>

Turning to alternative interpretations of my results, the most important is that the institutional legacies of Communism are actually driving variation in preferences. At the macro-level, the legacies of communism had profound effects on the socio-economic structures of the post-communist states, the institutions adopted, and subsequent reform ([Easter, 2002](#), [Gehlbach, 2008](#)). At the micro-level, communist indoctrination might also play a role, inculcating Communist values such as class solidarity and preferences for a strong social safety net ([Pop-Eleches and Tucker, 2014](#)). Both dynamics might actually explain my results, since institutional quality is deeply related to the historical legacy of Communism. To rule out this interpretation, I take two steps. First, following [Pop-Eleches and Tucker \(2014\)](#), I introduce a variable into my main specifications for each individual that measures the number of years they lived under Communist rule.<sup>43</sup> Because Communist party membership is also an important channel of socialization, I also include a dummy variable equal to one if the individual was a member of the Communist party. As in [Pop-Eleches and Tucker \(2014\)](#), including these variables together results in only the Communist party membership

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<sup>42</sup>These specifications are also available upon request.

<sup>43</sup>For comparability I use [Pop-Eleches and Tucker \(2014\)](#)'s historical data.

variable being significant. Crucially, however, including these variables does not strongly alter the main results (see the online appendix).

Finally, it is interesting to see whether the effects of a characteristic associated with tax evasion are persistent. That is, does having worked as self-employed, in a sector associated with evasion, or as a professional continue to shape preferences even after one has changed jobs?<sup>44</sup> To examine this, I recoded the main independent variables of interest to create three categories – those who belonged to each group (self-employed, evasive sectors, or evasive occupations) at any point since the fall of communism, those who only belonged during the first five years of the transition, and those who belonged during the most recent five years. In the absence of the ability to focus on the preferences of people who did not grow up under communism (they are too young to be included), the comparison of those with more and less professional experience under communism might give some additional leverage on the legacies story.

Interestingly, when these variables are substituted for the skill variables in our main regressions, the results remain largely the same.<sup>45</sup> This implies that preferences are sticky for individuals, even after retirement or job changes, and that the process of transition has not significantly altered the magnitude of the effect. It also implies that those with a characteristic associated with evasion that worked mostly during the communist period had similar preferences to those with similar characteristics who worked completely after the communist era. While far from ideal, this test gives us some confidence that the observed effects do not reflect differentials in the extent to which communist legacies are shaping preferences amongst different cohorts. It instead suggests that individuals' preferences are guided by opportunities afforded to them by the market economy.

## 4 Conclusion

In this paper, I provided three important pieces of empirical evidence important to understanding social policy preferences. First, for the most part, support for social policy among citizens of the Post-communist states largely follow patterns observed elsewhere. Income and factors associated

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<sup>44</sup>In a sense, this is a test of [Iversen and Soskice \(2001\)](#)'s assumptions that people with specific skills' preferences stay the same, even when they are employed in a sector that doesn't make use of their skills.

<sup>45</sup>For parsimony I do not report these results here, but they are available upon request.

with risk are the most important predictors of support for social policy in pooled regressions. Second, despite the fact that existing work applies rather well to social policy preferences in the Post-communist states, there is still much variation to be explained. In particular, current models largely ignore substantial levels of cross-national variation in the magnitude and signs of co-efficients for several important determinants of social policy. This suggests that these individual level factors might be conditioned on macro-level differences between countries.

The final contribution, and the most critical, is to provide evidence consistent with the notion that support for social policy is conditional on institutional quality. I focus on the observable implications of institutions for the preferences of tax evaders. I find that as institutional quality declines and tax evasion becomes easier to get away with, those with characteristics that best position them to take advantage and evade taxes become more supportive of social policy that is more redistributive and rooted in state control. Substantively, the results indicate that these groups favor social policy at about the same rate as the general populace when institutions are poor, but that a preference cleavages opens up between these groups and the rest of the population as institutional quality improves and tax evasion becomes more difficult. Moreover, the extent to which institutions shape preferences is on par with, and in some cases larger, than the magnitude of other important effects such as income. At the same time, there is little evidence that institutions shape preferences for social policy for the average member of the population, although this may be due to issues with the number of countries included.

The findings of this paper suggest two things for the broader literature on the political economy of authoritarianism. First, they suggests that to the extent that key groups that would be more likely to oppose redistribution in democracies professionals and entrepreneurs have preferences largely in keeping with those of the rest of the population, authoritarian rulers do not face a trade-off between retaining support from these groups and buying further support from the poor through redistribution. This casts doubt on theories advanced by [Acemoglu and Robinson \(2006\)](#) and [Boix, 2003](#)). This in turn suggests that the willingness of some authoritarian regime to engage in systematic social transfers, and the relative stability that such strategies generate, may be partially due to the fact that key groups that would normally oppose such transfers entrepreneurs and professionals in particular have preferences similar to the average population and do not object.

Second and related, the finding also suggests that the actual demands of the population more broadly may be quite different under varying shades of autocratic regimes. Because preferences diverge in some sectors of the population as a country becomes more democratic, the available menu of transfers the authoritarian can make without antagonizing different social groups should diminish. If this is true, this chapter provides an interesting starting point for analyses of the variation in transfer payments across regime types, and provides a strong political as opposed to economic argument for this variation.

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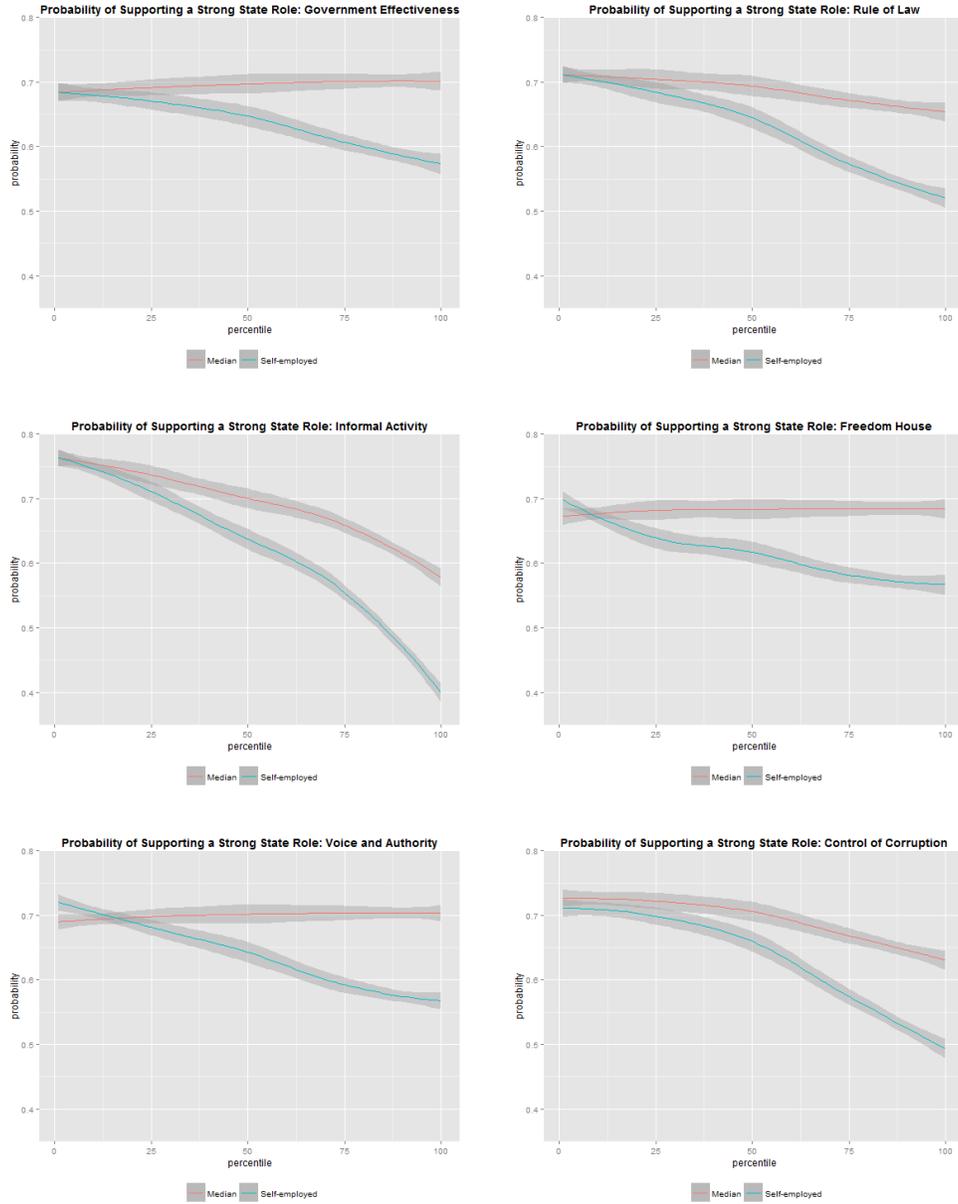


Figure 3: Simulated Probability of Support for a Strong State Role in Social Policy for the Self-employed

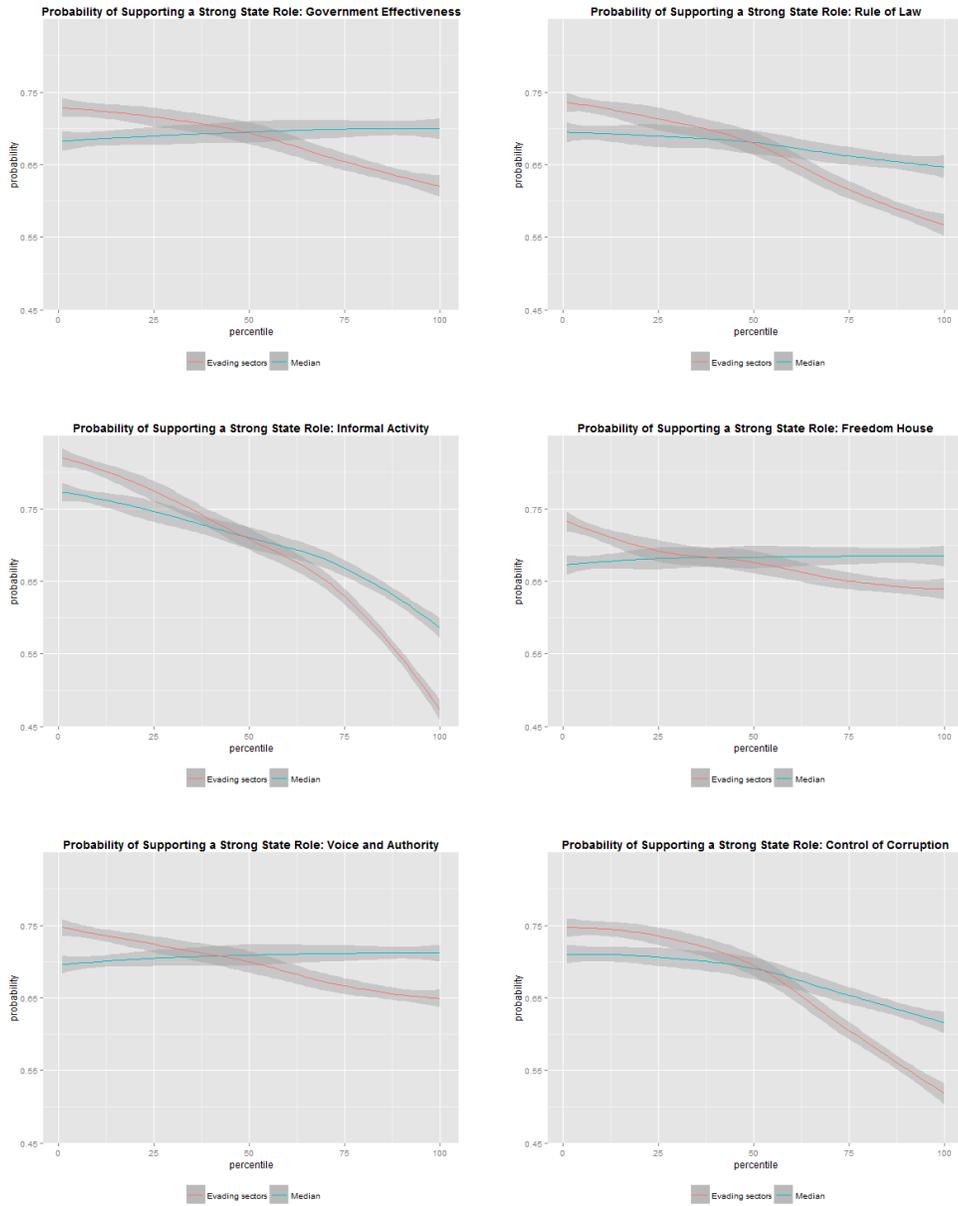


Figure 4: Simulated Probability of Support for a Strong State Role in Social Policy for Those Working in Sectors Associated with Evasion

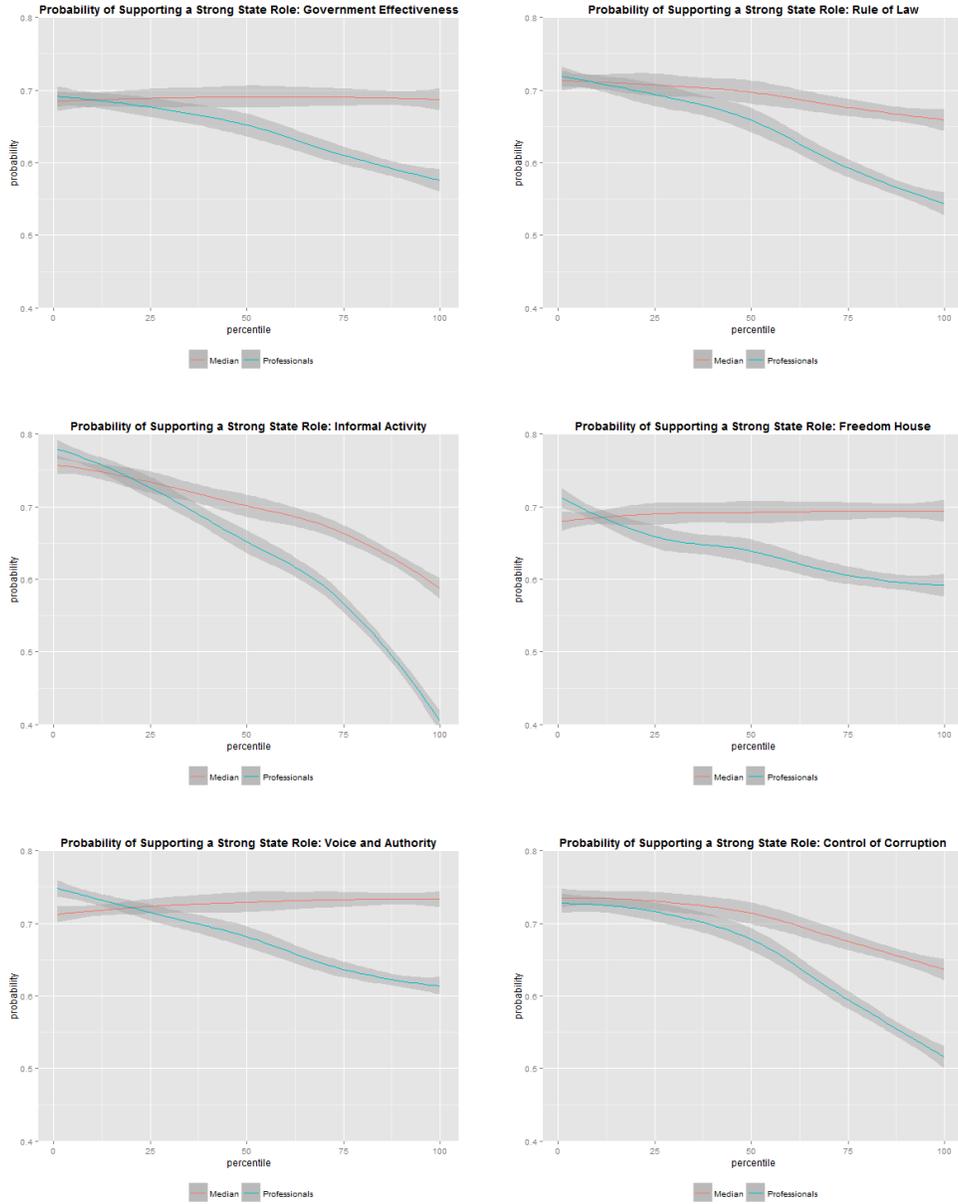


Figure 5: Simulated Probability of Support for a Strong State Role in Social Policy for Professionals

Table 2: Preferences for State-led Role in Redistribution – Individual Level Results

	(1)	(2)	(3)	(4)	(5)
Age	0.007*** (0.002)	0.007*** (0.002)	0.007*** (0.002)	0.008*** (0.002)	0.009*** (0.002)
Gender	-0.115*** (0.036)	-0.114*** (0.037)	-0.103*** (0.035)	-0.100*** (0.037)	-0.108*** (0.039)
<i>I = Male</i>					
Education	-0.028 (0.017)	-0.026 (0.017)	-0.018 (0.018)	-0.022 (0.016)	-0.036* (0.021)
<i>Higher = More Education</i>					
Household Size	0.024 (0.032)	0.018 (0.032)	0.030 (0.031)	0.016 (0.034)	-0.009 (0.034)
Income Decile	-0.027*** (0.010)	-0.024** (0.009)	-0.023** (0.010)	-0.028*** (0.010)	-0.028** (0.011)
Unemployed	0.086** (0.041)	0.080** (0.039)	0.081* (0.042)	0.081** (0.041)	0.121** (0.052)
<i>I = yes</i>					
nwpensioner	0.049 (0.075)	0.037 (0.076)	0.041 (0.075)	0.017 (0.075)	0.016 (0.081)
<i>I = yes</i>					
Health Assessment	0.139*** (0.023)	0.124*** (0.021)	0.130*** (0.022)	0.132*** (0.023)	0.127*** (0.027)
Lower = More Healthy					
Minority	0.031 (0.062)	0.022 (0.066)	0.025 (0.062)	0.047 (0.064)	0.063 (0.073)
<i>I = yes</i>					
Urban Resident	-0.065 (0.116)	-0.078 (0.116)	-0.064 (0.117)	-0.067 (0.117)	-0.060 (0.118)
<i>I = yes</i>					
Rural Resident	-0.024 (0.112)	-0.042 (0.112)	-0.026 (0.112)	-0.022 (0.113)	0.024 (0.117)
<i>I = yes</i>					
Professional	-0.223*** (0.069)	-0.202*** (0.069)	-0.211*** (0.068)	-0.224*** (0.071)	-0.193*** (0.068)
<i>I = yes</i>					
Re-privatization		0.524*** (0.043)			
<i>Higher = More Anti-market</i>					
Plan			0.138*** (0.035)		
<i>Higher = More Anti-market</i>					
Redistribution				0.403*** (0.041)	
<i>Higher = More Anti-market</i>					
Sum yrs. wages earned					0.002 (0.006)
Sum yrs. assets sold					-0.020 (0.018)
Sum yrs. food cut					0.021*** (0.006)
Sum yrs. wages cut					0.015 (0.012)
Constant	0.649*** (0.152)	0.541*** (0.151)	0.549*** (0.153)	-0.715*** (0.217)	0.611*** (0.165)
Observations	25,958	25,803	25,924	25,946	18,814
Pseudo-R2	0.0734	0.0831	0.0752	0.0996	0.0751
Log Likelihood	-15180	-14936	-15130	-14744	-11144

Cluster corrected standard errors in parentheses

\*\*\* p<0.01, \*\* p<0.05, \* p<0.1

Table 3: Preferences for Social Policy and Institutional Quality – Self-employed

	(1)	(2)	(3)	(4)	(5)	(6)	(7)
	Social Policy						
Self-employed	-0.236***	-0.236***	-0.268***	-0.227**	-0.245***	-0.236***	-0.236***
<i>I</i> = yes	(0.087)	(0.087)	(0.100)	(0.100)	(0.094)	(0.087)	(0.087)
Log GDP	-0.062	0.013	0.030	-0.024	-0.055	-0.056	0.067
	(0.230)	(0.212)	(0.150)	(0.128)	(0.175)	(0.202)	(0.223)
Social Policy Index	-0.008	-0.005	0.009	-0.005	0.004	-0.007	-0.005
(See below)	(0.025)	(0.025)	(0.025)	(0.025)	(0.025)	(0.024)	(0.024)
Government Effectiveness	0.040						
(Higher = Better)	(0.341)						
Gov. Effect. x Self-employed	-0.235**						
	(0.092)						
Rule of Law		-0.090					
(Higher = Better)		(0.313)					
RoL x Self-employed		-0.234**					
		(0.092)					
Formality (S. Index)			-0.015				
(Higher = More Formality)			(0.013)				
Formality x Self-employed			-0.013*				
			(0.008)				
Executive Constraints				-0.021			
(Higher = Better)				(0.065)			
Exec. Constr. x Self-employed				-0.030			
				(0.046)			
Freedom House (inverted)					0.011		
(Higher = Better)					(0.105)		
FH x Self-employed					-0.103**		
					(0.050)		
Voice and Authority						0.025	
(Higher = Better)						(0.234)	
VoA x Self-employed						-0.235**	
						(0.092)	
Control of Corruption							-0.203
(Higher = Better)							(0.367)
CoC x Self-employed							-0.234**
							(0.092)
Constant	0.609	0.514	0.112	0.524	0.216	0.594	0.523
	(0.734)	(0.754)	(0.749)	(0.735)	(0.753)	(0.714)	(0.716)
Individual controls	Yes						
Country varying slopes	Yes						
Self-employment varying slope	Yes						
Number of groups	25	25	23	25	24	25	25
Observations	24,803	24,803	22,805	24,803	23,805	24,803	24,803
chi2	770.9	771.0	743.9	759.7	754.5	770.9	771.2
Log Likelihood	-14433	-14433	-13297	-14435	-13964	-14433	-14432

Individual controls are those discussed in section 2.3.

Standard errors in parentheses. Freedom House and Formality inverted from original variables. See text.

\*\*\* p<0.01, \*\* p<0.05, \* p<0.1

Table 4: Preferences for Social Policy and Institutional Quality – Evading Sectors

	(1)	(2)	(3)	(4)	(5)	(6)	(7)
	Social Policy	Social Policy	Social Policy	Social Policy	Social Policy	Social Policy	Social Policy
Evasive Sector	-0.039 (0.062)	-0.044 (0.063)	-0.026 (0.066)	-0.036 (0.064)	-0.019 (0.065)	-0.039 (0.063)	-0.040 (0.063)
Log GDP	-0.072 (0.228)	-0.004 (0.212)	0.023 (0.149)	-0.038 (0.127)	-0.064 (0.174)	-0.065 (0.201)	0.045 (0.223)
Social Policy Index	-0.008 (0.025)	-0.005 (0.025)	0.008 (0.025)	-0.006 (0.025)	0.003 (0.025)	-0.008 (0.024)	-0.005 (0.024)
Government Effectiveness (Higher = Better)	0.039 (0.339)						
Gov. Effect. x Evasive Sector	-0.241*** (0.084)						
Rule of Law (Higher = Better)		-0.082 (0.313)					
RoL x Evasive Sector		-0.226*** (0.083)					
Formality (S. Index)			-0.015 (0.013)				
Formality x Evasive Sector			-0.014** (0.006)				
Executive Constraints (Higher = Better)				-0.018 (0.065)			
Exec. Constr. x Evasive Sector				-0.074** (0.029)			
Freedom House (inverted) (Higher = Better)					0.009 (0.104)		
FH x Evasive Sector					-0.083** (0.034)		
Voice and Authority (Higher = Better)						0.021 (0.232)	
VoA x Evasive Sector						-0.171*** (0.065)	
Control of Corruption (Higher = Better)							-0.183 (0.367)
CoC x Evasive Sector							-0.258*** (0.095)
Constant	0.632 (0.728)	0.431 (0.753)	0.142 (0.746)	0.558 (0.730)	0.245 (0.748)	0.621 (0.709)	0.444 (0.715)
Individual controls	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Country varying slopes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Self-employment varying slope	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Number of groups	25	25	23	25	24	25	25
Observations	24,803	24,803	22,805	24,803	23,805	24,803	24,803
chi2	793.8	785.4	776.8	791.2	777.6	791.7	785.2
Log Likelihood	-14444	-14448	-13305	-14444	-13976	-14444	-14448

Individual controls are those discussed in section 2.3.

Standard errors in parentheses. Freedom House and Formality inverted from original variables. See text.

\*\*\* p<0.01, \*\* p<0.05, \* p<0.1

Table 5: Preferences for Social Policy and Institutional Quality – Professionals

	(1)	(2)	(3)	(4)	(5)	(6)	(7)
	Social Policy	Social Policy	Social Policy	Social Policy	Social Policy	Social Policy	Social Policy
Professional	-0.195*** (0.074)	-0.195*** (0.074)	-0.223*** (0.078)	-0.190** (0.083)	-0.204*** (0.078)	-0.195*** (0.074)	-0.195*** (0.074)
Log GDP	-0.055 (0.228)	0.019 (0.210)	0.034 (0.149)	-0.021 (0.127)	-0.047 (0.174)	-0.050 (0.200)	0.067 (0.221)
Social Policy Index	-0.009 (0.025)	-0.006 (0.025)	0.007 (0.025)	-0.006 (0.025)	0.002 (0.025)	-0.009 (0.024)	-0.007 (0.024)
Government Effectiveness (Higher = Better)	0.033 (0.338)						
Gov. Effect. x Professional	-0.222*** (0.074)						
Rule of Law (Higher = Better)		-0.095 (0.310)					
RoL x Professional		-0.221*** (0.074)					
Formality (S. Index)			-0.015 (0.013)				
Formality x Professional			-0.016** (0.006)				
Executive Constraints (Higher = Better)				-0.023 (0.064)			
Exec. Constr. x Professional				-0.028 (0.037)			
Freedom House (inverted) (Higher = Better)					0.007 (0.104)		
FH x Professional					-0.097** (0.040)		
Voice and Authority (Higher = Better)						0.020 (0.232)	
VoA x Professional						-0.222*** (0.074)	
Control of Corruption (Higher = Better)							-0.196 (0.363)
CoC x Professional							-0.221*** (0.074)
Constant	0.636 (0.727)	0.541 (0.747)	0.162 (0.747)	0.556 (0.726)	0.260 (0.747)	0.624 (0.707)	0.556 (0.710)
Individual controls	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Country varying slopes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Self-employment varying slope	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Observations	24,803	24,803	22,805	24,803	23,805	24,803	24,803
Number of groups	25	25	23	25	24	25	25
chi2	737.3	737.3	717.5	717.5	717.8	737.3	737.5
Log Likelihood	-14427	-14427	-13289	-14431	-13959	-14427	-14427

Individual controls are those discussed in section 2.3.

Standard errors in parentheses. Freedom House and Formality inverted from original variables. See text.

\*\*\* p<0.01, \*\* p<0.05, \* p<0.1

Table 6: Variable Descriptions and Summary Statistics

Variable Name	Variable Description	Mean	Std.	Min.	Max	N
	<i>Dependent Variable</i>					
Preferences for a State Role in Re-distribution	Do you think the state should be involved in the following: reducing the gap between the rich and the poor? (1) Not involved (2) Moderately involved or (3) Strongly involved in reducing the gap between the rich and the poor.	2.65	0.564	1	3	28991
	<i>Demographic Controls</i>					
Age	Respondent age	46.516	17.722	17	97	29000
Household size	Number of Reported Household members not counting the respondent.	1.022	0.803	0	5.5	29002
Gender	(1) Male (0) Female	0.415	0.493	0	1	29002
Minority status	Do you consider yourself as a member of an ethnic minority in this country? (0) No (1) Yes	0.107	0.308	0	1	28976
Self-reported Health	How would you assess your health? (1) very good; (2) good; (3) medium; (4) bad; (5) very bad.	1.721	0.996	0	4	28998
	<i>Economic and Ideological Controls</i>					
Respondent education	What is the highest degree you obtained? (1) no degree/education (2) compulsory school education (3) secondary education (4) professional; vocational school/training (5) higher professional degree (University) (6) Post Graduate Degree	1.435	1.05	0	3	28995
Consumption Decile	Country specific consumption deciles constructed by EBRD. Underlying consumption variable was calculated using annualized consumption expenditure per (equalized) household member; with children under 14 entering with a weight of 0.3.	5.499	2.873	1	10	29002
Wage earning years	In the past 15 years or so our country has undergone many major changes. Peoples lives have been affected in different ways. I would like to inquire how transition has affected your work trajectory and your life in general: Years worked for wages (for an employer) 1989-2006	6.823	6.895	0	18	29008
Retired	For respondents who report they are not working: What is the main reason you are not looking for a job: Retired and no working? (0) No (1) Yes	0.236	0.425	0	1	29002
Unemployed	For individuals who report not having worked in the last 7 days: Even though you did not work during the past 7 days, do you have a job which you will return to? (0) Yes (1) No	0.461	0.499	0	1	29007
Attitudes towards reprivatization	In your opinion, what should be done with most privatised companies? (0) Left in the hands of the current owners with no change or Left in the hands of the current owners provided they pay what they are worth (1) Re Nationalise and kept in state hands or Re Nationalise and then re-privatise again using more transparent processes	0.466	0.499	0	1	28797
	<i>Evasion</i>					
Self-employed	In this job (current job) do you work: As self employed or for a company you partly or fully own? (0) No (1) Yes	0.082	0.275	0	1	29002
Low-visibility sector	In what industry did/do you do this job (current job)? (0) non-retail and construction industry (1) retail or construction	0.06	0.237	0	1	29008

Professionals (high skill, low paperwork)	Dummy variable equal to one if respondent is working as a legislator; senior government official; enterprise manager; director/chief executive; business owner; physicist; engineer; mathematician; architect; computing professional; medical doctor; dentist; pharmacist; teacher; lawyer; accountant; author; professional; religious or similar profession.	0.108	0.340	0	1	290002
	<i>Institutional quality</i>					
Government Ef- fectiveness	Index which aggregates various surveys, reports, and indices in order to measure the quality of public and civil services, their degree of independence from political pressure, the quality of policy implementation, and the state's ability to credibly commit to policy (Kaufmann et al., 2010).	-0.121	0.694	-1.47	1.038	26003
Rule of Law	Index which aggregates various surveys, reports, and indices in order to measure confidence in social rules and the degree to which actors abide by them. Particularly focuses on the quality of contract enforcement, judicial and law enforcement bodies, and likelihood of crime (Kaufmann et al., 2010).	-0.308	0.707	-1.31	0.858	26003
Formality	Inverse of Schneider, et al. (2010) Index. Index constructed using MIMIC method to estimate size of unreported economic activity. See paper for further details.	60.79	12.48	31.65	80.91	24002
Polity IV index	Extent of institutional constraints on the decision-making powers of chief executives, whether individuals or collectives. Variable coded by research teams according to pre-established criteria (Marshall et al., 2013).	5.167	2.092	-0.47	7	26006
Freedom House	Index of democracy created from expert ratings which takes into consideration political and electoral processes; the degree of social pluralism and participation; government functioning; and civil liberties: freedom of expression and association; Rule of Law; and other individual rights. Raw Freedom House scores range from 1-7; with lower numbers corresponding to more democratic regimes; however scores have been inverted in this paper such that higher values indicate more democratic regimes (Freedom House, 2012).	3.774	1.762	0	5.786	25003
Voice and Au- thority	Index which aggregates various surveys, reports, and indices in order to measure participation and the degree to which basic freedoms such as freedom of expression; association; and media are present. Higher values indicate more prevalent (Kaufmann et al., 2010)	-0.024	0.889	-1.84	1.23	26003
Control of Cor- ruption	Index which aggregates various surveys, reports, and indices in order to measure the use of public power for private gain and which encapsulates petty and grand corruption, as well as state capture (Kaufmann et al., 2010). Country level controls	-0.024	0.887	-1.84	1.228	26003
Social Policy In- dex	Please see appendix of this chapter	28.86	5.005	16	36	25002
GDP per Capita	Average real GDP per capita in US dollars: 2000 – 2005 (EBRD 2009)					
Inequality	Average of available Gini-coefficient of inequality from 2000 – 2005. (WDI 2005)	32.904	3.873	25.5	41.717	25003
Expenditures	Average government expenditures as a percentage of GDP from 2000 – 2005 (EBRD 2009)					
Resource Rents	Average resource rents as a percentage of GDP from 2000 – 2005. (World Bank Global Series)	9.366	18.03	0.156	166.2	26004

## 5 Appendix: Social Policy Index

The social policy index is an updated version of the measure introduced in [Mares \(2005a\)](#), which makes use of country legislation to code the scope of social policy coverage and the degree to which contributions and benefits are linked. Following [Mares \(2005a\)](#), I focus on four types of social policies: old-age insurance, health-care insurance, work-related disability insurance, and unemployment insurance based on data supplies by [Social Security Administration \(2006\)](#). Intuitively, the index starts by assigning each country a score of 10, indicating social policy with no contribution-benefit link and full, universal coverage. Points are then deducted for each major occupational group that is excluded from social policy and based on the extent to which individuals are discriminated against based on actuarial criteria. The more discrimination, the tighter contributions and benefits are linked and the less redistribution across occupational groups and segments of the populace. Variation in contributions, benefits, or retirement age by occupational type are all regarded as discriminatory and lower scores accordingly, although income based discrimination does not result in a reduced score.<sup>46</sup> With respect to the major occupational groups, I follow [Mares \(2005a\)](#) in focusing on a) agricultural workers b) the self-employed, and c) workers in small firms. Finally, it is important to note that many Post-communist countries have multi-tiered pension systems that combine a universal, flat rate pension with contributory systems. For these systems, I provide an average of the coded value of each pillar.

The specific criteria for assigning each social policy type a value on the index is:

10 – Universalistic, solidaristic social policy for which all country residents are eligible.

9 – Compulsory contributory insurance that covers all employed persons and all major occupational groups. Social policy is subsidized by the state and there is no discrimination in social policy benefits aside from income.

8.5 – As a 9, but without state subsidies.

8 – Compulsory contributory insurance that covers all employed persons, but one major occupational group is excluded. Social policy is subsidized by the state and there is no discrimination

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<sup>46</sup>Results above are robust to alternative definitions of discrimination that focus solely on contributions and benefits, ignoring early retirement and other such considerations.

in social policy benefits aside from income.

7.5 – As an 8, but without state subsidies.

7 – Compulsory contributory insurance that covers all employed persons, but two or more major occupational group are excluded. Social policy is subsidized by the state and there is no discrimination in social policy benefits aside from income.

6.5 – As a 7, but without state subsidies.

6 – Compulsory contributory insurance that covers all employed persons, but two or more major occupational group are excluded. Social policy must be subsidized. Risk-based discrimination in social policy benefits, contributions or retirement age exist.

5.5 – As a 6, but without state subsidies.

5 – Privately managed social policy which covers at least 50% of the economically active population. No state subsidies are offered.

4 – Provident fund.

3 – Employer liability.

2 – Means-tested social assistance.

1 – Purely voluntary insurance or special systems, but only for narrow occupational groups.

0 – No social policy.