

Chapter 5

Public Spending and Public Choice

5.1 What a Price System Can and Cannot Do

- 1) Which of the following terms describes the situation in which too few or too many resources go to a specific economic activity because of external benefits or costs?
- A) an technologically inefficient market
 - B) a market failure
 - C) a laissez-faire market
 - D) an external market

Answer: B

Diff: 1

Topic: 5.1 What a Price System Can and Cannot Do

AACSB:

Question Status: Previous Edition

- 2) Market failure occurs when
- A) a good is too expensive for the market to provide.
 - B) an unrestrained market economy leads to too few or too many resources going to a specific economic activity.
 - C) one good is superior to another and drives it out of the market.
 - D) the stock market experiences a very large loss.

Answer: B

Diff: 1

Topic: 5.1 What a Price System Can and Cannot Do

AACSB: Analytic skills

Question Status: Previous Edition

- 3) Consumers are sovereign when
- A) prices are decided by sellers.
 - B) they control the government.
 - C) they can prevent market failure.
 - D) they have the freedom to decide what they wish to purchase.

Answer: D

Diff: 1

Topic: 5.1 What a Price System Can and Cannot Do

AACSB: Reflective thinking skills

Question Status: Previous Edition

- 4) Market failures
- A) prevent the price system from attaining economic efficiency.
 - B) result in quantities and prices that are socially desirable.
 - C) strengthen economic efficiency by forcing unprofitable firms to close.
 - D) weaken the argument for government intervention in the economy.

Answer: A

Diff: 1

Topic: 5.1 What a Price System Can and Cannot Do

AACSB: Analytic skills

Question Status: Previous Edition

5) Which of the following is a benefit of the price system?

- A) The existence of positive externalities.
- B) The production of public goods.
- C) Consumers have what they want since politicians and business managers decide what is to be produced.
- D) The freedom of consumers to decide what they want to purchase.

Answer: D

Diff: 1

Topic: 5.1 What a Price System Can and Cannot Do

AACSB: Analytic skills

Question Status: Previous Edition

6) Which of the following statements is NOT true about the price system?

- A) The price system allows resources to flow from low-valued uses to high-valued uses.
- B) The price system encourages the production of public goods.
- C) Individuals have freedom to purchase what they want.
- D) The price system allows for economic efficiency.

Answer: B

Diff: 1

Topic: 5.1 What a Price System Can and Cannot Do

AACSB: Analytic skills

Question Status: Previous Edition

7) Market failures

- A) are usually caused by government interference in the economy.
- B) prevent the price system from attaining economic efficiency.
- C) encourage people to purchase more of a good than they really want.
- D) encourage businesses to produce more of a good than they really want to.

Answer: B

Diff: 1

Topic: 5.1 What a Price System Can and Cannot Do

AACSB: Analytic skills

Question Status: Previous Edition

8) When there are too few or too many resources going to an economic activity,

- A) a public good exists.
- B) a market failure exists.
- C) a regressive tax is in place.
- D) a free-rider problem exists.

Answer: B

Diff: 1

Topic: 5.1 What a Price System Can and Cannot Do

AACSB:

Question Status: Previous Edition

- 9) The price system will allocate resources efficiently except when
- A) consumers decide they want more of a good.
 - B) no externalities exist.
 - C) farmers decide to produce more corn.
 - D) market failures exist.

Answer: D

Diff: 1

Topic: 5.1 What a Price System Can and Cannot Do

AACSB:

Question Status: Previous Edition

- 10) When market failures occur,
- A) the invisible hand will correct for the market failures.
 - B) the price system will correct the market failures.
 - C) people will reduce their consumption.
 - D) the government can step in to correct the market failure.

Answer: D

Diff: 1

Topic: 5.1 What a Price System Can and Cannot Do

AACSB: Analytic skills

Question Status: Previous Edition

- 11) Market failures occur when
- A) externalities exist.
 - B) wages increase.
 - C) there is an increase in demand.
 - D) there is a change in quantity demanded.

Answer: A

Diff: 1

Topic: 5.1 What a Price System Can and Cannot Do

AACSB: Analytic skills

Question Status: Previous Edition

- 12) When the price system fails to generate an efficient allocation of resources,
- A) the market will always correct it.
 - B) consumers will spend less.
 - C) business will produce more.
 - D) too few or too many goods will be produced.

Answer: D

Diff: 2

Topic: 5.1 What a Price System Can and Cannot Do

AACSB:

Question Status: New

13) An example of a market failure is

- A) a firm is dumping toxic waste that is making people sick.
- B) when not everyone who wants to see a major league football game can.
- C) when there is an increase in demand and a shortage develops.
- D) unemployment.

Answer: A

Diff: 1

Topic: 5.1 What a Price System Can and Cannot Do

AACSB: Reflective thinking skills

Question Status: Previous Edition

14) Market failures include all of the following EXCEPT

- A) equalization of quantity supplied and quantity demanded
- B) public goods
- C) positive externalities
- D) negative externalities

Answer: A

Diff: 1

Topic: 5.1 What a Price System Can and Cannot Do

AACSB:

Question Status: Revised

15) A situation in which a market economy leads to too few or too many resources going to a particular economic activity is known as

- A) competition.
- B) excessive competition.
- C) destructive competition.
- D) a market failure.

Answer: D

Diff: 1

Topic: 5.1 What a Price System Can and Cannot Do

AACSB:

Question Status: Previous Edition

16) In its most ideal form, a price system allows

- A) firms to act in such a way that they eliminate scarcity.
- B) consumers to satisfy all their wants.
- C) resources to move from lower-valued uses to higher-valued uses through voluntary exchange.
- D) government policy makers to allocate resources to the uses which they consider to be in the best interests of society.

Answer: C

Diff: 2

Topic: 5.1 What a Price System Can and Cannot Do

AACSB: Analytic skills

Question Status: Previous Edition

17) Market failure occurs when

- A) the price system fails to generate an efficient allocation of resources.
- B) the price system fails to generate an equal distribution of income.
- C) the price system fails to generate an equal distribution of wealth.
- D) the price system allows consumers to make their own decisions.

Answer: A

Diff: 2

Topic: 5.1 What a Price System Can and Cannot Do

AACSB:

Question Status: Previous Edition

18) Market failures take place when

- A) a market fails to have the goods that consumers want.
- B) an underground market develops.
- C) market transactions lead to underproduction or overproduction of a good.
- D) producers stop production.

Answer: C

Diff: 1

Topic: 5.1 What a Price System Can and Cannot Do

AACSB: Analytic skills

Question Status: Previous Edition

19) When misallocation of resources for production of a good results in spillover effects on third parties, there is a

- | | |
|-------------------------|------------------------|
| A) market failure. | B) government failure. |
| C) legislative failure. | D) productive failure. |

Answer: A

Diff: 1

Topic: 5.1 What a Price System Can and Cannot Do

AACSB: Analytic skills

Question Status: Revised

20) Explain what market failure is. How does market failure relate to the price system? How does market failure relate to the role of government?

Answer: Market failure is a situation in which a market economy either allocates too few or too many resources to a specific economic activity. That is, it is a situation in which a market economy does not achieve economic efficiency. The price system achieves economic efficiency as long as there are not any market failures. But, when there are market failures, an unregulated price system does not achieve economic efficiency, and there is a potential role for government to intervene in some way to bring about an efficient situation.

Diff: 2

Topic: 5.1 What a Price System Can and Cannot Do

AACSB: Analytic skills

Question Status: Previous Edition

5.2 Correcting for Externalities

- 1) A situation in which a benefit or a cost associated with an economic activity spills over to third parties is called
- A) a public good.
 - B) a merit good.
 - C) an externality.
 - D) the free-rider problem.

Answer: C

Diff: 1

Topic: 5.2 Correcting for Externalities

AACSB:

Question Status: Previous Edition

- 2) An example of third parties in the market of automobiles is
- A) a pedestrian that is affected by the polluted air from automobiles.
 - B) a producer of automobiles.
 - C) a consumer of automobiles.
 - D) None of the above belongs to third parties.

Answer: A

Diff: 1

Topic: 5.2 Correcting for Externalities

AACSB: Reflective thinking skills

Question Status: Previous Edition

- 3) An externality can best be defined as
- A) a party not directly involved in a transaction.
 - B) a consequence of a transaction that spills over to affect third parties.
 - C) a right of an owner to use and exchange property.
 - D) a cost associated with the production of one more unit of output.

Answer: B

Diff: 1

Topic: 5.2 Correcting for Externalities

AACSB:

Question Status: Previous Edition

- 4) All of the following illustrate how government can correct for positive externalities EXCEPT
- A) subsidies.
 - B) regulation.
 - C) government financing and production.
 - D) charging effluent fees.

Answer: D

Diff: 1

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

- 5) Which of the following leads to an underallocation of resources to a specific economic activity?
- A) External costs
 - B) External benefits
 - C) Marginal costs
 - D) Effluent benefits

Answer: B

Diff: 1

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

- 6) A result of a positive externality in the production of a good is that
- A) the price system will over-allocate resources to the production of that good or service.
 - B) the price system will under-allocate resources to the production of that good or service.
 - C) the market supply will be too high.
 - D) the market demand will be too high.

Answer: B

Diff: 1

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

- 7) Which of the following is an example of a negative externality?
- A) There is an increase in injuries to pedestrians caused by accidents resulting from electronic billboards distracting drivers.
 - B) The opening of a new shopping mall increases the business of nearby restaurants.
 - C) A consumer pays a higher price than another consumer does for the same product.
 - D) Consumers pay a sales tax in addition to the price of a product.

Answer: A

Diff: 2

Topic: 5.2 Correcting for Externalities

AACSB: Reflective thinking skills

Question Status: Previous Edition

- 8) Suppose that the XYZ industry produces a product that results in negative external costs to society. This information suggests that
- A) resources are under-allocated to the industry.
 - B) the equilibrium market price of the product includes the external costs borne by society.
 - C) resources are over-allocated to the industry.
 - D) at the market price, quantity demanded is less than quantity supplied.

Answer: C

Diff: 1

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

- 9) When an external cost exists in the production of a good, firms tend to
- A) under-produce the good since society pays these costs.
 - B) over-produce the good.
 - C) keep production constant throughout the year.
 - D) under-allocate resources to the production of the good.

Answer: B

Diff: 2

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

- 10) If production of an item results in negative external costs, then
- A) the market price is below the socially preferred price that reflects the external costs.
 - B) the market price is above the socially preferred price that reflects the external costs.
 - C) market forces will always correct the problem.
 - D) the market quantity is too low from society's point of view.

Answer: A

Diff: 1

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

- 11) Which of the following will LEAST likely generate positive external benefits to society?
- A) Education
 - B) The use of cell phone services
 - C) Health care
 - D) Requiring drivers to undergo periodic eye examinations

Answer: B

Diff: 1

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

- 12) Suppose that the market price of good X equals the firm's cost of producing that good, but it does not reflect any costs imposed on society. Which of the following is FALSE?
- A) The good is priced too low.
 - B) An external benefit is associated with good X.
 - C) Resources are over-allocated in the production of good X.
 - D) Too much of good X is being produced.

Answer: B

Diff: 1

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

- 13) When a good causes positive external benefits to accrue to third parties, an unfettered market will
- A) under-allocate resources to the good causing the benefit.
 - B) over-allocate resources to the good causing the benefit.
 - C) cause the equilibrium quantity, established before the benefit is taken into account, to be produced more efficiently.
 - D) eliminate such goods.

Answer: A

Diff: 1

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

- 14) Society is likely to over-allocate resources to produce goods that
- A) are public goods.
 - B) are merit goods.
 - C) generate positive externalities.
 - D) generate negative externalities.

Answer: D

Diff: 1

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

- 15) Which of the following often involves positive external benefits?
- A) Water pollution
 - B) Drunken driving
 - C) Inoculation programs
 - D) Tobacco smoking

Answer: C

Diff: 1

Topic: 5.2 Correcting for Externalities

AACSB: Reflective thinking skills

Question Status: Previous Edition

- 16) A negative externality is a situation in which
- A) there is a spillover of benefits.
 - B) a cost associated with an economic activity is borne by a third party.
 - C) a firm is paying in excess of the total costs of producing a good.
 - D) none of the above.

Answer: B

Diff: 1

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

- 17) When a paper producer pollutes the air, economists argue that there is
- A) efficiency, if production is at its maximum level.
 - B) a positive externality.
 - C) an external cost.
 - D) a cost paid solely by the firm.

Answer: C

Diff: 1

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

- 18) An external cost, such as the cost generated by pollution, is
- A) a cost paid by consumers of the product.
 - B) a cost paid by producers of the product.
 - C) a cost paid by a third party or by society at large.
 - D) not a true opportunity cost of production.

Answer: C

Diff: 1

Topic: 5.2 Correcting for Externalities

AACSB:

Question Status: Previous Edition

- 19) Pollution is caused by a market failure, in an industry in which there is
- A) unemployment.
 - B) an over-allocation of resources in production.
 - C) excess demand.
 - D) excessive cost borne by the firm.

Answer: B

Diff: 2

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

- 20) A negative externality such as pollution can be corrected by
- A) a subsidy to producers.
 - B) a tax on producers.
 - C) a subsidy to consumers.
 - D) a stimulus to production.

Answer: B

Diff: 1

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

- 21) An externality exists when
- A) goods are sold in specific geographic locations.
 - B) some of the benefits or costs associated with a good are borne by third parties.
 - C) the government taxes a good.
 - D) the government subsidizes a good.

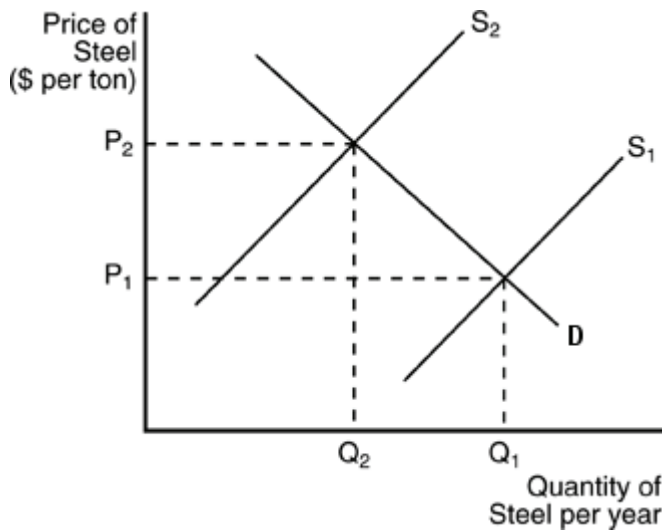
Answer: B

Diff: 1

Topic: 5.2 Correcting for Externalities

AACSB:

Question Status: Previous Edition



22) According to the above figure, if steel mills ignore the cost of pollution, the equilibrium quantity of steel will most likely be

- A) Q_1 .
- B) Q_2 .
- C) $Q_2 - Q_1$.
- D) none of the above.

Answer: A

Diff: 1

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

23) According to the above figure, , then the supply curve will

- A) shift from S_1 to S_2 .
- B) shift from S_2 to S_1 .
- C) remain at S_1 .
- D) shift either to the left or the right, but it is impossible to say without more information.

Answer: A

Diff: 1

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

- 24) According to the above figure, if steel mills are charged an effluent fee in order to bear the cost of pollution, what happens to the equilibrium price and equilibrium quantity?
- A) They are unchanged.
 - B) They change from P_1 and Q_1 to P_2 and Q_2 .
 - C) They change from P_2 and Q_2 to P_1 and Q_1 .
 - D) The equilibrium price increases from P_1 and P_2 , but the equilibrium quantity is unchanged.

Answer: B

Diff: 2

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Revised

- 25) Suppose that a per-unit subsidy is granted to each individual who consumes a product providing external benefits to society at large. Each individual's demand curve will shift _____, and the market demand curve for the product will shift _____.
- A) to the right; to the right
 - B) to the right; to the left
 - C) to the left; to the left
 - D) to the left; to the right

Answer: A

Diff: 1

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

- 26) The Do-Good Company produces goods that provide benefits to society –at-large. If consumers of Do-Good's products fail to take external benefits into account,
- A) the demand curve will be too far to the left.
 - B) the supply curve will be too far to the left.
 - C) the demand curve will be too far to the right.
 - D) the supply curve will be too far to the right.

Answer: A

Diff: 1

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

- 27) Government can correct for negative externalities by
- A) decreasing taxes.
 - B) increasing taxes or regulation.
 - C) allowing the market system to correct the problem.
 - D) decreasing the costs to those responsible for the externality.

Answer: B

Diff: 1

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

28) In graphical form, the effect of imposing a tax on a good is shown as

- A) a leftward shift of the market supply curve.
- B) a rightward shift of the market supply curve.
- C) a downward movement along the market supply curve.
- D) no change to the market supply curve.

Answer: A

Diff: 1

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

29) If the production of a product results in significant external costs, an appropriate government policy might be to

- A) subsidize the production of the good.
- B) tax producers and thus shift the supply curve to the left.
- C) tax consumers' incomes and thus shift the demand curve to the left.
- D) subsidize consumers since the good is being under-consumed.

Answer: B

Diff: 1

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

30) An effluent fee

- A) is a reward to companies using production methods that create positive externalities.
- B) is also called a pollution subsidy.
- C) gives a firm the right to pollute if it pays a tax on what it discharges.
- D) is intended to influence the market by increasing supply and decreasing price.

Answer: C

Diff: 1

Topic: 5.2 Correcting for Externalities

AACSB:

Question Status: Previous Edition

31) To correct for the underproduction of products with positive externalities, the government must

- A) provide the incentives for the private sector to produce and consume the good.
- B) provide tougher regulations on the industry.
- C) increase taxes on the industry.
- D) fine the industry.

Answer: A

Diff: 2

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

- 32) Assume the production of a good gives rise to external benefits. The government may increase efficiency by
- A) subsidizing consumption of the good.
 - B) requiring all producers of the good to be licensed.
 - C) taxing production of the good.
 - D) imposing taxes on the good.

Answer: A

Diff: 1

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

- 33) When the production of one good spills benefits over to third parties, the government should consider all of the following EXCEPT
- A) subsidizing the consumption of the good.
 - B) subsidizing the production of the good.
 - C) creating tax incentives to encourage more consumption.
 - D) taxing the production or consumption of the good.

Answer: D

Diff: 1

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

- 34) A government action that can help correct positive externalities is
- A) a tax on producers of the good that provides external benefits.
 - B) a subsidy to consumers of the good that provides external benefits.
 - C) an effluent fee charged to producers of the good that provides external benefits.
 - D) regulations aimed at reduced production by sellers of the good that provides external benefits.

Answer: B

Diff: 1

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

- 35) A government subsidy is typically used
- A) to correct a negative externality.
 - B) to provide a government-inhibited good.
 - C) to reduce inflation.
 - D) to correct a positive externality.

Answer: D

Diff: 1

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

- 36) A subsidy is sometimes used by the government to correct the problems associated with
- A) negative externalities.
 - B) positive externalities.
 - C) public goods.
 - D) monopolies.

Answer: B

Diff: 1

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

- 37) When costs spill over to third parties, there is a(n)
- A) cost overrun
 - B) excessive competition.
 - C) negative externality.
 - D) government subsidy.

Answer: C

Diff: 1

Topic: 5.2 Correcting for Externalities

AACSB:

Question Status: Previous Edition

- 38) Which of the following is NOT an example of a negative externality?
- A) Inoculation against disease
 - B) Pollution
 - C) Playing a boom box loudly in a crowded park
 - D) Rush hour traffic

Answer: A

Diff: 2

Topic: 5.2 Correcting for Externalities

AACSB: Reflective thinking skills

Question Status: Previous Edition

- 39) Which of the following is an example of a positive externality?
- A) something obtainable at a zero price
 - B) a lower crime rate for a community in which residents receive more education
 - C) increased purchases of landscaping services by a homeowner that boost a neighbor's property value
 - D) a discount for consumers buying in large quantity

Answer: B

Diff: 1

Topic: 5.2 Correcting for Externalities

AACSB: Reflective thinking skills

Question Status: Previous Edition

- 40) A paint firm has just announced that it will be building a new plant in a small town that is currently experiencing a high level of unemployment. The new plant will create 500 new jobs in the area and will occupy unused land at the edge of town. The plant will also dump some harmful chemicals into the town's river. From an economic standpoint this dumping of chemicals

- A) is unimportant since the firm is reducing the unemployment in the region.
- B) creates a negative externality.
- C) is the production of a public good.
- D) creates a positive externality.

Answer: B

Diff: 3

Topic: 5.2 Correcting for Externalities

AACSB: Reflective thinking skills

Question Status: Previous Edition

- 41) Which of the following is an example of a positive externality?

- A) A neighbor's flower garden that you enjoy seeing
- B) Traffic congestion
- C) An increased supply of chocolate lowers chocolate prices for all consumers
- D) Pollution

Answer: A

Diff: 1

Topic: 5.2 Correcting for Externalities

AACSB: Reflective thinking skills

Question Status: Previous Edition

- 42) Which of the following is NOT an example of an externality?

- A) A bread company emits a wonderful aroma in the air that makes people smile.
- B) The neighbor's wind chimes interfere with your sleep.
- C) A firm fires 500 people.
- D) Cancer-causing chemicals are dumped into the drinking water supply of a city.

Answer: C

Diff: 1

Topic: 5.2 Correcting for Externalities

AACSB: Reflective thinking skills

Question Status: Previous Edition

- 43) My brother decides to leave his empty soda can on someone's lawn. This is an example of a

- A) public good.
- B) positive externality.
- C) neutral externality.
- D) negative externality.

Answer: D

Diff: 1

Topic: 5.2 Correcting for Externalities

AACSB: Reflective thinking skills

Question Status: Previous Edition

- 44) Safe Bank has an outside display which has the time and temperature that is always correct.

This is an example of

- A) an interference in the workings of the price system.
- B) a breakdown in communication between the bank and its customers.
- C) a negative externality.
- D) a positive externality.

Answer: D

Diff: 1

Topic: 5.2 Correcting for Externalities

AACSB: Reflective thinking skills

Question Status: Previous Edition

- 45) Which of the following is an example of a negative externality?

- A) A person buys a car that is a lemon
- B) A worker is injured on the job
- C) A new restaurant's success causes another to go out of business
- D) A new hotel ruins the view of the ocean for a few homeowners

Answer: D

Diff: 3

Topic: 5.2 Correcting for Externalities

AACSB: Reflective thinking skills

Question Status: Previous Edition

- 46) Markets tend to overallocate resources to the production of a good when

- A) there are negative externalities.
- B) there are positive externalities.
- C) there are public goods produced.
- D) equilibrium occurs.

Answer: A

Diff: 2

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

- 47) Markets tend to underallocate resources to the production of a good when

- A) there are negative externalities.
- B) there are positive externalities.
- C) there are public goods produced.
- D) equilibrium occurs.

Answer: B

Diff: 2

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

48) Which of the following statements is NOT true of external benefits?

- A) External benefits lead to an underallocation of resources to the production of the good that has the external benefit.
- B) External benefits lead to a price in the market that is too high.
- C) External benefits lead to too few of the goods that have the external benefit being produced.
- D) External benefits are a good thing for the allocation of resources because people are getting something at no cost.

Answer: D

Diff: 2

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

49) Which of the following statements is true of external costs?

- A) External costs should not be corrected since people will bear the costs whether they are corrected or not.
- B) There are no good ways to correct for the external costs.
- C) When external costs exist, the price of the good will be deceptively low leading to an overallocation of resources.
- D) External costs should only be corrected for if the correction will not increase the market price.

Answer: C

Diff: 2

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

50) When negative externalities exist, the private market equilibrium represents a

- A) market price which is too low and a market quantity which is too low.
- B) market price which is too low and a market quantity which is too high.
- C) market price which is too high and a market quantity which is too low.
- D) market price which is too high and a market quantity which is too high.

Answer: B

Diff: 3

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

51) When positive externalities exist, the private market equilibrium represents a

- A) market price which is too low and a market quantity which is too low.
- B) market price which is too low and a market quantity which is too high.
- C) market price which is too high and a market quantity which is too low.
- D) market price which is too high and a market quantity which is too high.

Answer: C

Diff: 3

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

52) Orchards provide services to beekeepers because the bees use the pollen to make honey. This is an example of

- A) a positive externality, and too many orchards exist in society.
- B) a positive externality, and too few orchards exist in society.
- C) a negative externality, and too many orchards exist in society.
- D) a negative externality, and too few orchards exist in society.

Answer: B

Diff: 2

Topic: 5.2 Correcting for Externalities

AACSB: Reflective thinking skills

Question Status: Previous Edition

53) To correct for negative externalities, the government

- A) should allow the price system do the correction.
- B) can impose a tax.
- C) can provide a subsidy to consumers.
- D) should create a public good.

Answer: B

Diff: 1

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

54) To correct for positive externalities the government

- A) should allow the price system to do the correction.
- B) can impose a tax.
- C) can give a subsidy.
- D) should create a public good.

Answer: C

Diff: 1

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

55) A tax is sometimes used by government to correct the problems associated with

- A) negative externalities.
- B) positive externalities.
- C) internal benefits.
- D) external benefits.

Answer: A

Diff: 1

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

56) A subsidy is sometimes used by government to correct the problems associated with

- A) negative externalities.
- B) positive externalities.
- C) internal benefits.
- D) external benefits.

Answer: B

Diff: 1

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

57) The funds that polluters pay that gives them the right to discharge into the air or water a certain amount of pollution are

- A) special subsidies.
- B) regulation fees.
- C) external costs.
- D) effluent fees.

Answer: D

Diff: 1

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

58) The purpose of an effluent fee is to

- A) reduce the amount produced of a good and to raise the market price.
- B) correct for pollution while keeping the price of the good the same as before the correction.
- C) reward people producing externalities.
- D) encourage producers to keep the quantity produced the same while lowering the price.

Answer: A

Diff: 2

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

59) The purpose of an effluent fee imposed on a firm is

- A) to increase output of its product by increasing the resources allocated to production.
- B) to increase output of its product by reducing the resources allocated to production.
- C) to reduce output by increasing production costs thereby reducing resources used.
- D) none of the above

Answer: C

Diff: 2

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

60) An effluent fee is more effective when imposed on

- A) the firm or producer of the product which generates pollution.
- B) the consumer of the product.
- C) neither the producer nor the consumer of the product.
- D) the supplier of the raw material used by the firm.

Answer: A

Diff: 2

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

- 61) An effluent fee is a
- A) subsidy given to the producer of a positive externality.
 - B) charge to a polluter that gives the right to discharge pollution into the air.
 - C) fine imposed on a polluter for dumping illegal pollution.
 - D) charge for a public good.

Answer: B

Diff: 1

Topic: 5.2 Correcting for Externalities

AACSB:

Question Status: Previous Edition

- 62) A possible solution to the problems of external benefits is
- A) to tax those receiving the extra benefits.
 - B) production of the good by government.
 - C) effluent fees.
 - D) to restrict the amount of the good through direct government regulation.

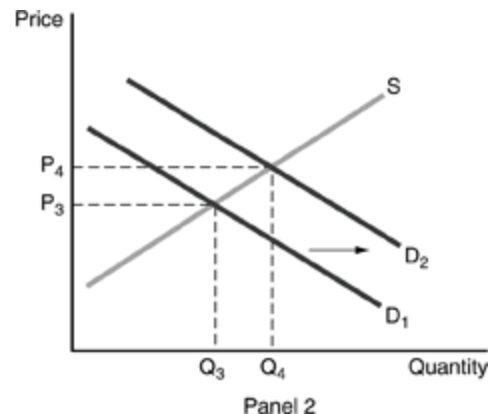
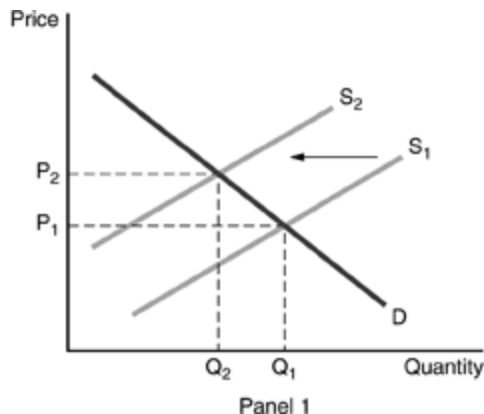
Answer: B

Diff: 2

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition



A shift from S_1 to S_2 reflects the change that happens when a negative externality is taken into account. A shift from D_1 to D_2 reflects the change that happens when a positive externality is taken into account.

- 63) Refer to the above figures. Which of the panels would be consistent with the situation in which external costs exist?
- A) Panel 1
 - B) Panel 2
 - C) Panels 1 and 2
 - D) Neither panel

Answer: A

Diff: 1

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

64) Refer to the above figures. Which of the panels would be consistent with the situation in which external benefits exist?

- A) Panel 1 B) Panel 2 C) Panels 1 and 2 D) Neither panels

Answer: B

Diff: 1

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

65) Refer to the above figures. A negative externality exists that has not been corrected. Price and quantity will be

- A) P_1 and Q_1 . B) P_2 and Q_2 . C) P_3 and Q_3 . D) P_4 and Q_4 .

Answer: A

Diff: 3

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

66) Refer to the above figures. A positive externality exists that has not been corrected. Price and quantity will be

- A) P_1 and Q_1 . B) P_2 and Q_2 . C) P_3 and Q_3 . D) P_4 and Q_4 .

Answer: C

Diff: 3

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

67) Refer to above figures. Prior to the shift of the curves, which panel and which curve involve the existence of negative externality?

- A) Panel 1 and S_1 B) Panel 1 and S_2
C) Panel 2 and D_1 D) Panel 2 and D_2

Answer: A

Diff: 3

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

68) Refer to the above figures. A negative externality existed but has been corrected. Price and quantity will be

- A) P_1 and Q_1 . B) P_2 and Q_2 . C) P_3 and Q_3 . D) P_4 and Q_4 .

Answer: B

Diff: 3

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

- 69) Refer to the above figures. If a positive externality that existed becomes corrected, price and quantity will become
- A) P_1 and Q_1 . B) P_2 and Q_2 . C) P_3 and Q_3 . D) P_4 and Q_4 .

Answer: D

Diff: 3

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

- 70) Refer to the above figures. An external cost exists. This will lead to a(n)
- A) underproduction equal to Q_1 minus Q_2 . B) overproduction equal to Q_4 minus Q_3 .
C) underproduction equal to Q_4 minus Q_3 . D) overproduction equal to Q_1 minus Q_2 .

Answer: D

Diff: 3

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

- 71) Refer to the above figures. An external benefit exists. This will lead to a(n)
- A) underproduction equal to Q_1 minus Q_2 . B) overproduction equal to Q_4 minus Q_3 .
C) underproduction equal to Q_4 minus Q_3 . D) overproduction equal to Q_1 minus Q_2 .

Answer: C

Diff: 3

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

- 72) Refer to the above figures. Externalities exist in both panels. After correcting for the externalities the prices should be
- A) P_1 and P_3 . B) P_1 and P_4 . C) P_2 and P_4 . D) P_2 and P_3 .

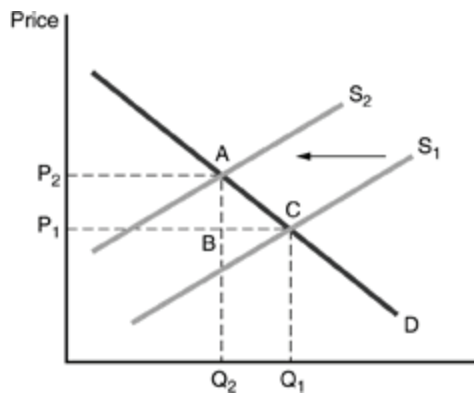
Answer: C

Diff: 3

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition



73) Refer to the above figure. An external cost exists. The amount of that cost is represented by

- A) P_2 .
- B) Q_1 .
- C) the vertical distance between point A and the supply curve S_1 .
- D) the distance between C and A.

Answer: C

Diff: 2

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

74) Refer to above figure in which negative externality existed. The government imposes a \$1.00 pollution tax on the producer. Supply shifts leftward.

- A) This tax will be shifted entirely to the consumer.
- B) This tax will be borne entirely by the producer.
- C) The amount of the tax shifted to the consumer depends on the consumer's reaction.
- D) The tax will be divided into equal amounts between consumer and producer.

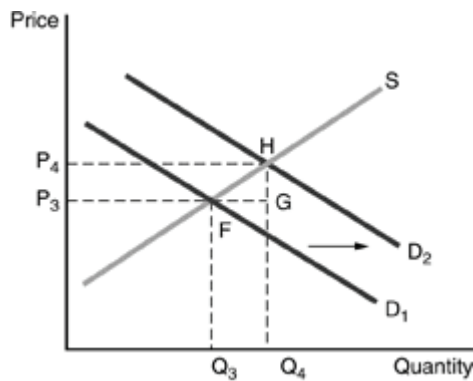
Answer: C

Diff: 2

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition



75) Refer to the above figure. An external benefit exists. The amount of that benefit is represented by

- A) P_4 .
- B) the vertical distance between D_1 and D_2 .
- C) the distance between G and F .
- D) P_3 .

Answer: B

Diff: 3

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

76) If the government wishes to correct the existence of positive externality, it could

- A) grant subsidies to consumers to stimulate demand.
- B) impose a tax on the producers to stimulate supply.
- C) impose taxes on consumers to stimulate demand.
- D) grant subsidies to producers to reduce supply.

Answer: A

Diff: 3

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

77) Graphically, the presence of an external cost that is ignored by producers can be shown as

- A) a market supply curve to the left of the market supply curve for where the producers have to pay for the external cost.
- B) a market supply curve to the right of the market supply curve for which the producers have to pay for the external cost.
- C) a market supply curve the same as the market supply curve for which the producers have to pay for the external cost.
- D) the absence of a market supply curve.

Answer: B

Diff: 1

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

- 78) The government might provide a subsidy when
- A) a negative externality exists.
 - B) an effluent fee has been unsuccessful.
 - C) it wants to increase the amount of a good consumed.
 - D) it wants to transform a negative externality into a positive externality.

Answer: C

Diff: 1

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

- 79) In graphical form, the presence of an external benefit that is ignored by consumers can be shown as
- A) a market demand curve to the left of the market demand curve for which the consumers take the external benefit into account.
 - B) a market demand curve to the right of the market demand curve for which the consumers take the external benefit into account.
 - C) a market demand curve the same as the market demand curve for which the consumers take the external benefit into account.
 - D) the absence of a market demand curve.

Answer: A

Diff: 1

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

- 80) All of the following are ways that the government can correct for positive externalities EXCEPT
- A) by subsidizing the consumption of the good.
 - B) producing the good itself.
 - C) by regulation.
 - D) by assessing an effluent fee.

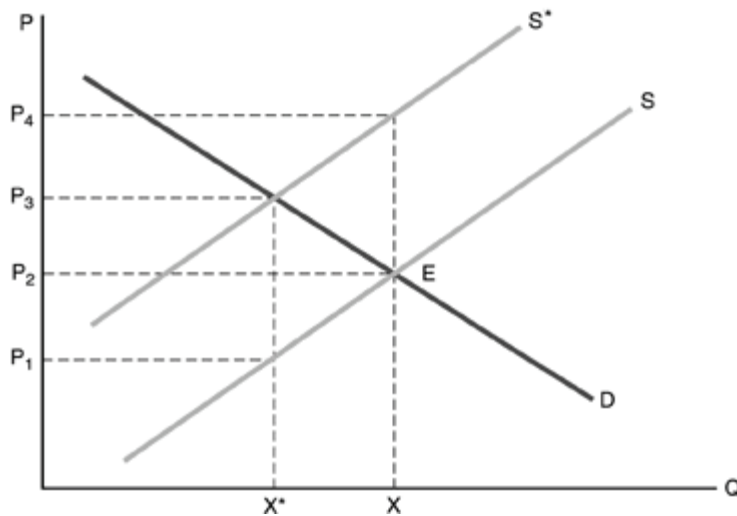
Answer: D

Diff: 1

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition



- 81) In the above figure, market equilibrium at point E yields the quantity X. The quantity X* is the socially optimal quantity. Point E indicates that currently there is
- A) a negative externality.
 - B) a positive externality.
 - C) a public good.
 - D) a positive externality with subsidy.

Answer: A

Diff: 2

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

- 82) In the above figure, market equilibrium at point E yields the quantity X. The quantity X* is socially optimal amount. The government can achieve the optimal outcome by
- A) setting the price at P₁.
 - B) establishing a tax of P₃ - P₁ per unit of the good sold.
 - C) establishing a tax of P₃ - P₂ per unit of the good sold.
 - D) setting the price at P₄.

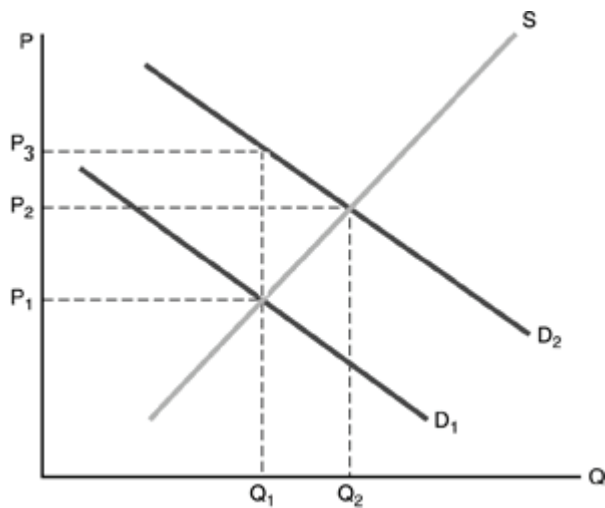
Answer: B

Diff: 3

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition



- 83) Refer to the above figure. The market equilibrium quantity is Q_1 . Point Q_2 represents the optimal amount of production. This indicates that there is
- A) a public good which should be produced.
 - B) regressive taxation of the product.
 - C) a positive externality.
 - D) a negative externality.

Answer: C

Diff: 3

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

- 84) Refer to the above figure. The market equilibrium quantity is Q_1 . Point Q_2 represents the optimal amount of production. The government can achieve the optimal outcome by
- A) setting the price at P_3 .
 - B) providing a per-unit subsidy to consumers equal to $P_3 - P_1$.
 - C) providing a per-unit subsidy to consumers equal to $P_2 - P_1$.
 - D) establishing a tax equal to $P_2 - P_1$ per unit of the good sold.

Answer: B

Diff: 3

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

- 85) In a free market system, competition generates economic efficiency only when
- A) individuals take into account the full opportunity cost of their actions.
 - B) consumers are motivated by a sense of the greater good, not their own self-interest.
 - C) firms are motivated by a sense of the greater good, not their desire for profit.
 - D) economic decisions are taken out the hands of individuals and placed in the hands of government officials.

Answer: A

Diff: 2

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

- 86) Costs that spill over to third parties are called
- A) opportunity costs.
 - B) external costs.
 - C) variable costs.
 - D) public costs.

Answer: B

Diff: 1

Topic: 5.2 Correcting for Externalities

AACSB:

Question Status: Previous Edition

- 87) What would happen in a free market system when production of a good generates negative externalities?
- A) There is a shortage of the good.
 - B) There is a surplus of the good.
 - C) The equilibrium quantity of the good is less than the efficient amount.
 - D) The equilibrium quantity of the good is more than the efficient amount.

Answer: D

Diff: 2

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

- 88) A firm that produces chemical solvents creates some air pollution because of the emissions from its manufacturing facilities. A tax is imposed on the firm, equal to the costs of environmental damage caused by a unit of the emissions. What is the result?
- A) The quantity of chemical solvents produced now will be the efficient amount.
 - B) Demand for the chemical solvents will increase.
 - C) Demand for the chemical solvents will decrease.
 - D) Consumers of the chemical solvents will be willing to pay the full amount of the tax, and so the quantity produced will be unaffected.

Answer: A

Diff: 3

Topic: 5.2 Correcting for Externalities

AACSB: Reflective thinking skills

Question Status: Previous Edition

- 89) Positive externalities arise when
- A) an unprofitable firm is shut down.
 - B) a profitable firm is regulated.
 - C) tax rates are reduced.
 - D) production of a good generates benefits that spill over to third parties.

Answer: D

Diff: 1

Topic: 5.2 Correcting for Externalities

AACSB:

Question Status: Previous Edition

- 90) When does a subsidy that benefits consumers result in a more efficient allocation of a resource?
- A) when the good being produced or consumed is not scarce
 - B) when the good being produced or consumed generates a negative externality
 - C) when the good being produced or consumed generates a positive externality
 - D) when the equilibrium price of the good is one that consumers don't like

Answer: C

Diff: 2

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

- 91) An externality is
- A) a third-party benefit or cost that is associated with the production of a good.
 - B) when external forces such as war or flood affect the market.
 - C) government intervention in the markets.
 - D) transaction costs.

Answer: A

Diff: 1

Topic: 5.2 Correcting for Externalities

AACSB:

Question Status: Previous Edition

- 92) When there is an external benefit, the unregulated market
- A) overproduces the good or service.
 - B) underproduces the good or service.
 - C) reaches the most efficient solution.
 - D) maximizes public welfare.

Answer: B

Diff: 1

Topic: 5.2 Correcting for Externalities

AACSB:

Question Status: Previous Edition

- 93) When there is an external cost, the unregulated market
- A) overproduces the good or service.
 - B) underproduces the good or service.
 - C) reaches the most efficient solution.
 - D) minimizes public welfare.

Answer: A

Diff: 1

Topic: 5.2 Correcting for Externalities

AACSB:

Question Status: Previous Edition

94) Inoculations of children against infectious diseases are

- A) an example of an external benefit.
- B) an example of an external cost.
- C) dangerous for society.
- D) an example of a public good.

Answer: A

Diff: 1

Topic: 5.2 Correcting for Externalities

AACSB: Reflective thinking skills

Question Status: Previous Edition

95) When a person throws a cigarette out of a car window and starts a brush fire, this is

- A) an example of an external benefit.
- B) an example of an external cost.
- C) an example of a public good.
- D) an example of market power.

Answer: B

Diff: 1

Topic: 5.2 Correcting for Externalities

AACSB: Reflective thinking skills

Question Status: Previous Edition

96) The government corrects for externalities in all of the following ways EXCEPT

- A) taxes.
- B) regulation.
- C) lobbying.
- D) subsidies.

Answer: C

Diff: 2

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

97) A situation in which the market system allocates too many resources to the production of a given activity is known as

- A) market allocation.
- B) market failure.
- C) market efficiency.
- D) market breakdown.

Answer: B

Diff: 1

Topic: 5.2 Correcting for Externalities

AACSB:

Question Status: Previous Edition

98) When a business produces a product that creates external costs,

- A) the company produces a level of output larger than would be produced without the external cost.
- B) the company produces a level of output smaller than would be produced without the external cost.
- C) the company produces a level of output which would be the same as it would produce without the external cost.
- D) the market provides the efficient level of output even with the existence of the external cost.

Answer: A

Diff: 2

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

- 99) If external benefits are taken into account in the market,
- A) the demand curve would shift to the left.
 - B) the supply curve would shift to the left.
 - C) the demand curve would shift to the right.
 - D) the supply curve would become vertical.

Answer: C

Diff: 2

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

- 100) "Second-hand" smoke, an often cited disadvantage of allowing smoking in restaurants, is referred to in economics as a(n)
- A) capital good.
 - B) externality.
 - C) economic cost.
 - D) negative investment.

Answer: B

Diff: 2

Topic: 5.2 Correcting for Externalities

AACSB: Reflective thinking skills

Question Status: Previous Edition

- 101) Graphically, the effects of an external cost can be shown as
- A) a leftward shift of the market demand curve.
 - B) a leftward shift of the market supply curve.
 - C) a downward movement along the market demand curve.
 - D) a rightward shift of the market supply curve.

Answer: B

Diff: 1

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

- 102) If a corporation were forced to absorb the cost of a spillover from the production of a good, this would likely cause the supply curve for the good to
- A) shift out.
 - B) shift to the left.
 - C) shift to the right.
 - D) None of the above are correct.

Answer: B

Diff: 2

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

- 103) Which of the following might be considered a positive externality?
- A) the pollination of an orange grove due to bees kept by a nearby beekeeper
 - B) individuals who did not get the flu, yet did not receive a flu shot when those around them did receive the shot
 - C) better fishing resulting from increased lake temperatures generated by the nearby power plant
 - D) All of the above are correct.

Answer: D

Diff: 2

Topic: 5.2 Correcting for Externalities

AACSB: Reflective thinking skills

Question Status: Previous Edition

- 104) Which of the following might be a method that the government could use to correct a negative externality?
- A) an effluent fee on waste from the production of goods that create negative externalities
 - B) government subsidies to producers of goods that create negative externalities
 - C) financing additional production of goods that create negative externalities
 - D) encouraging overallocation of resources of production of goods that create negative externalities

Answer: A

Diff: 2

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

- 105) Which of the following might be a method that the government could use to promote the production of a good that generates positive externalities?
- A) subsidies
 - B) regulations
 - C) financing additional production
 - D) All of the above are correct.

Answer: D

Diff: 2

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

- 106) Graphically, the effect of a government subsidy on a good is shown as
- A) a leftward shift of the market demand curve.
 - B) a rightward shift of the market demand curve.
 - C) a downward movement along the market demand curve.
 - D) no change to the market demand curve.

Answer: B

Diff: 1

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

107) Market failure means that

- A) the strike organized by unionized employees fails to achieve its goal.
- B) too many outdated products are offered for sale in the local supermarket.
- C) there is overallocation or underallocation of resources to certain economic activity.
- D) an unexpectedly harsh winter shuts down a factory.

Answer: C

Diff: 1

Topic: 5.2 Correcting for Externalities

AACSB:

Question Status: Previous Edition

108) An economic activity in which benefits or costs affect third parties is called

- A) a public good.
- B) a third-party good.
- C) the exclusion principle.
- D) an externality.

Answer: D

Diff: 1

Topic: 5.2 Correcting for Externalities

AACSB:

Question Status: Previous Edition

109) One way of addressing the associated market failure that generates both private costs and external costs is for this activity to be

- A) left alone.
- B) taxed.
- C) subsidized.
- D) banned.

Answer: B

Diff: 2

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

110) External costs can be defined as

- A) the cost associated with private production, but partially borne by society.
- B) the sum of all private production costs.
- C) the cost of running the federal government.
- D) the cost of providing all public goods and services.

Answer: A

Diff: 1

Topic: 5.2 Correcting for Externalities

AACSB:

Question Status: Previous Edition

111) When government intervenes in the production process because external costs exist, it typically attempts to shift the industry's

- A) demand curve to the right.
- B) demand curve to the left.
- C) supply curve to the right.
- D) supply curve to the left.

Answer: D

Diff: 2

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

112) When government intervenes in the production process because external benefits exist, it typically attempts

- A) to impose a tax on each unit produced.
- B) to shift the industry's demand curve to the left.
- C) to shift the industry's demand curve to the right.
- D) to shift the industry's supply curve to the left.

Answer: C

Diff: 2

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

113) Whether an externality is positive or negative, it is always

- A) evaluated by the Supreme Court of the United States.
- B) evaluated by the government.
- C) evaluated by the impact on the third party.
- D) judged by the profitability of the firm producing the product.

Answer: C

Diff: 2

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

114) An effluent fee is an example of

- A) a government policy to correct for an external benefit.
- B) a government policy to promote the production of a product with an external cost.
- C) a government policy to promote the production of a product with an external benefit.
- D) a government policy to correct for an external cost.

Answer: D

Diff: 1

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

115) An example of a negative externality created in the market system would be

- A) poverty.
- B) unemployment.
- C) an increased number of bird flu patients.
- D) water pollution.

Answer: D

Diff: 2

Topic: 5.2 Correcting for Externalities

AACSB: Reflective thinking skills

Question Status: Previous Edition

116) All of the following generate positive externalities EXCEPT

- A) public health programs.
- B) lower marginal tax rates.
- C) requiring proof of inoculation before entering college.
- D) requiring proof of inoculation before entering elementary school.

Answer: B

Diff: 1

Topic: 5.2 Correcting for Externalities

AACSB: Reflective thinking skills

Question Status: Previous Edition

117) One way that the government encourages the production of a good with positive externalities is to offer

- A) an effluent fee.
- B) a market to pollute.
- C) a subsidy.
- D) a pollution tax.

Answer: C

Diff: 1

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

118) If the production of ukuleles creates a negative externality that is not corrected for by the government, the equilibrium quantity of ukuleles is

- A) higher than optimal.
- B) lower than optimal.
- C) efficient.
- D) at a optimal level.

Answer: A

Diff: 2

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

119) What is market failure? How can the government correct market failure?

Answer: Market failure is a situation in which the market economy leads to too few or too many resources going to a specific economic activity as a result of externalities. External costs lead to too much supply in a market than otherwise. In this case, the government can correct the market outcome by imposing a tax and regulation. On the contrary, external benefits lead to too little market demand than otherwise. In this case, the government can correct the market outcome with subsidies and regulation.

Diff: 1

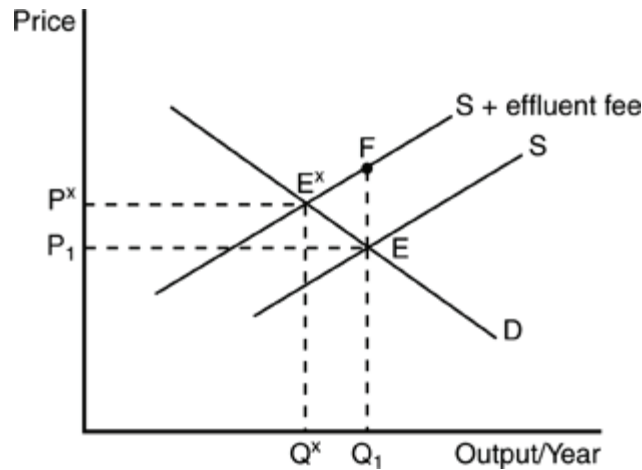
Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

120) What is an effluent fee? Graphically, show how an effluent fee can correct an externality.

Answer:



An effluent fee is a charge to a polluter that gives the right to discharge into the air or water a certain amount of pollution. In the above figure, the market solution is point E, with price of P_1 and output of Q_1 . The external cost of the pollution is equal to the distance FE, so an effluent fee equal to FE causes the firms to produce fewer units. The optimum is at E^* , with price of P^* , and output of Q^* .

Diff: 3

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

121) What is an externality? How do positive and negative externalities differ in their effects? How can government action correct positive and negative externalities?

Answer: An externality is a cost or benefit of an economic activity that is borne by third parties. A good generating a positive externality is underproduced and underconsumed. A good generating a negative externality is overproduced and overconsumed. The government can correct a positive externality by either producing the good itself or by providing a subsidy equal to the external benefit, and can correct a negative externality by either imposing a tax equal to the external cost or by direct regulation.

Diff: 2

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

- 122) Explain why an external cost leads to an over-allocation of resources to the production of a good.

Answer: An external cost is the cost associated with the production of a good that is not borne by the seller. Rather, the cost is borne by third parties. The seller calculates the amount of the good to produce by comparing private benefits and costs. By ignoring the external costs, the seller produces more of the good than would be the case if the seller actually had to bear the full costs of production. Hence, the seller overallocates resources to the production of the good.

Diff: 2

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

- 123) Explain why an external benefit leads to an under-allocation of resources to the production of a good.

Answer: An external benefit is the benefit associated with the consumption of a good that is not borne by the buyer. Rather, the benefit is borne by third parties. The buyer calculates the amount of the good to consume by comparing private benefits and costs. By ignoring the external benefit, the buyer consumes less of the good than would be the case if the buyer actually received the full benefits of consumption. Hence, society under allocates resources to the production of the good.

Diff: 2

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: New

- 124) What is the consequence of a positive externality in a market? What is the consequence of a negative externality? Why those consequences occur?

Answer: A positive externality leads to the equilibrium quantity of goods in a market that is less than the efficient amount from the society's perspective. A negative externality leads to the equilibrium quantity of goods in a market that is more than the efficient amount. A positive externality is not taken into account by consumers and hence is not reflected in the position of the market demand curve. This leads to an equilibrium market quantity below the socially preferred level. In contrast, a negative externality is not taken into account by producers and hence is not reflected in the position of the market supply curve. This leads to an equilibrium market quantity above the socially preferred level.

Diff: 1

Topic: 5.2 Correcting for Externalities

AACSB: Analytic skills

Question Status: Previous Edition

5.3 The Other Economic Functions of Government

- 1) The economic functions of government differ from the political functions of government in that
- A) the economic functions are carried out by the federal government, while the political functions are carried out by state and local governments.
 - B) the economic functions include policies that affect income redistribution, while the political functions involve things that affect the way exchange is carried out.
 - C) the economic functions involve things that affect the way exchange is carried out while the political functions include policies that affect income redistribution.
 - D) the economic functions are carried out by state and local governments, while the political functions are carried out by the federal government.

Answer: C

Diff: 2

Topic: 5.3 The Other Economic Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

- 2) Public goods are
- A) rival and exclusive.
 - B) rival, but not exclusive.
 - C) exclusive, but not rival.
 - D) neither exclusive nor rival.

Answer: D

Diff: 2

Topic: 5.3 The Other Economic Functions of Government

AACSB:

Question Status: Previous Edition

- 3) In the U.S. economy, which of the following is NOT a generally accepted economic function of government?
- A) Providing public goods
 - B) Distributing consumer goods
 - C) Ensuring economy-wide stability
 - D) Promoting competition in the marketplace

Answer: B

Diff: 1

Topic: 5.3 The Other Economic Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

- 4) The economic role of the legal system might best be described as
- A) promoting the productive efficiency of competitive markets.
 - B) identifying and producing public goods.
 - C) establishing the "rules of the game" and acting as a referee when disputes arise among market participants.
 - D) identifying and producing merit goods.

Answer: C

Diff: 1

Topic: 5.3 The Other Economic Functions of Government

AACSB:

Question Status: Previous Edition

5) Which of the following is NOT an economic function of the U.S. government?

- A) Promoting competition
- B) Providing public goods
- C) Promoting price stability
- D) Encouraging production of government-inhibited goods

Answer: D

Diff: 1

Topic: 5.3 The Other Economic Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

6) Which of the following is NOT an economic function of government?

- A) Providing a legal system
- B) Ensuring economic stability
- C) Providing government-inhibited goods
- D) Promoting competition

Answer: C

Diff: 1

Topic: 5.3 The Other Economic Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

7) Which of the following statements is TRUE?

- A) Government spending as a percent of total national income has continuously decreased since the 1950s.
- B) Transfer payments are money payments made by the government for which no goods or services are currently received.
- C) Education is the largest category of federal government expenditures.
- D) Transfers in kind include Welfare, Social Security, and unemployment insurance benefits.

Answer: B

Diff: 1

Topic: 5.3 The Other Economic Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

8) In the United States, the idea that the federal government should undertake actions to stabilize business activity

- A) was established in the Declaration of Independence.
- B) is a relatively new idea that developed in the years during and after the Great Depression.
- C) has been around since the early 1700s.
- D) developed during World War I.

Answer: B

Diff: 1

Topic: 5.3 The Other Economic Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

- 9) The legal system in the United States tends
- A) to support monopolies.
 - B) to actively discourage unionization.
 - C) to discourage the entry of new firms into industries.
 - D) to promote competition.

Answer: D

Diff: 1

Topic: 5.3 The Other Economic Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

- 10) The U.S. legal system mainly engages in activities that
- A) are dedicated to producing private goods.
 - B) focus on income redistribution.
 - C) involve defining and protecting property rights.
 - D) focus on producing public goods.

Answer: C

Diff: 1

Topic: 5.3 The Other Economic Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

- 11) Federal antitrust laws in the United States are intended to
- A) promote competition by prohibiting monopolies.
 - B) increase corporate earnings.
 - C) create new monopolies.
 - D) create only government-owned monopolies.

Answer: A

Diff: 1

Topic: 5.3 The Other Economic Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

- 12) To protect the competitive economic system by restricting the formation of monopolies, the government has passed and enforced
- A) regulatory laws.
 - B) antitrust laws.
 - C) tort laws.
 - D) zoning laws.

Answer: B

Diff: 1

Topic: 5.3 The Other Economic Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

- 13) Federal antitrust laws in the United States are enforced
- A) solely by the Federal Trade Commission.
 - B) solely by the Department of Justice.
 - C) by the Department of Justice and by the Federal Trade Commission.
 - D) by the Department of Commerce.

Answer: C

Diff: 1

Topic: 5.3 The Other Economic Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

- 14) Which of the following does NOT describe the intended purpose of the antitrust laws of the United States?
- A) To promote competition within the economic system
 - B) To reduce the power of monopolies
 - C) To prohibit certain economic activities that promote trade
 - D) To restrict the formation of monopolies

Answer: C

Diff: 1

Topic: 5.3 The Other Economic Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

- 15) U.S. antitrust laws view monopolies as undesirable because
- A) monopolies restrain trade and promote inefficiencies.
 - B) monopolies create inferior products.
 - C) monopolies produce only capital goods.
 - D) monopolies produce only cheap, low quality goods.

Answer: A

Diff: 2

Topic: 5.3 The Other Economic Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

- 16) The purpose of antitrust legislation is
- A) to reduce unemployment.
 - B) to reduce the power of monopoly.
 - C) to increase the power of monopoly.
 - D) to maximize employment for a given price level.

Answer: B

Diff: 1

Topic: 5.3 The Other Economic Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

- 17) A firm that has a great deal of control over the price of a good is said
- A) to function in a black market.
 - B) to create a tax incidence.
 - C) to have monopoly power.
 - D) to be in an antitrust position.

Answer: C

Diff: 1

Topic: 5.3 The Other Economic Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

- 18) Which one of the following is NOT a characteristic of public goods?
- A) They are indivisible.
 - B) It is difficult to charge people on the basis of how much they use.
 - C) Public goods can be used by increasing numbers of people at no additional cost.
 - D) Public goods are subject to the principle of rival consumption.

Answer: D

Diff: 1

Topic: 5.3 The Other Economic Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

- 19) When an Australian citizen enjoys military protection in Australia without contributing to the cost of Australia's defense budget, then
- A) this citizen is a free rider.
 - B) Australia is a free rider.
 - C) this citizen receives no benefits if Australia is attacked.
 - D) Australia's defense budget will run out of funds.

Answer: A

Diff: 1

Topic: 5.3 The Other Economic Functions of Government

AACSB: Reflective thinking skills

Question Status: Previous Edition

- 20) Which of the following is an example of the free-rider problem?
- A) A neighbor who refuses to help pay for a street light that is intended to help reduce crime
 - B) A student who refuses to buy a college catalog
 - C) A law enforcement officer who receives a uniform from the police department
 - D) A fast food employee who is provided food at work

Answer: A

Diff: 2

Topic: 5.3 The Other Economic Functions of Government

AACSB: Reflective thinking skills

Question Status: Previous Edition

21) Public goods are

- A) any goods or services produced by the government.
- B) provided to additional users at no additional cost.
- C) provided only by the capitalistic system.
- D) provided only by the communist system.

Answer: B

Diff: 1

Topic: 5.3 The Other Economic Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

22) The principle feature of private goods is that

- A) they cannot be rented or purchased.
- B) consumption by one person reduces the quantity available to others.
- C) no one can be excluded from consumption of the product.
- D) externality problems associated with their production are always negative.

Answer: B

Diff: 1

Topic: 5.3 The Other Economic Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

23) One characteristic of a public good is that it

- A) is available for consumption by only a few individuals at any particular time.
- B) always eliminates the free-rider problem.
- C) can be consumed simultaneously by many individuals.
- D) can be easily subdivided into small units.

Answer: C

Diff: 1

Topic: 5.3 The Other Economic Functions of Government

AACSB:

Question Status: Previous Edition

24) Which of the following would be best classified as a private good?

- A) A missile defense system
- B) Police force
- C) Radio frequency
- D) Clothing

Answer: D

Diff: 1

Topic: 5.3 The Other Economic Functions of Government

AACSB: Reflective thinking skills

Question Status: Previous Edition

25) Public goods are unlikely to be provided by the private sector because

- A) the production of the good creates negative externalities.
- B) no one can be excluded from the consumption of the good.
- C) the consumption of the good creates negative externalities.
- D) the exclusion principle does not apply to public goods.

Answer: B

Diff: 1

Topic: 5.3 The Other Economic Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

26) The free-rider problem is encountered when

- A) someone benefits from the consumption of a public good without paying his or her full share.
- B) all individuals who consume a public good pay for it.
- C) all goods consumed and produced are private goods.
- D) all individuals are willing to pay for what they consume.

Answer: A

Diff: 1

Topic: 5.3 The Other Economic Functions of Government

AACSB:

Question Status: Previous Edition

27) In the absence of government,

- A) public goods are likely to be overprovided.
- B) market failure is less likely to occur.
- C) public goods are likely to be underprovided.
- D) the free-rider problem is more likely to occur.

Answer: C

Diff: 2

Topic: 5.3 The Other Economic Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

28) The opportunity cost of providing a public good to an additional individual is

- A) infinite.
- B) zero.
- C) impossible to determine.
- D) high because of the exclusion principle.

Answer: B

Diff: 3

Topic: 5.3 The Other Economic Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

- 29) Private goods are those goods
- A) that violate the principle of rival consumption.
 - B) for which no public market exists.
 - C) that can only be consumed by one individual at a time.
 - D) to which the non-exclusion principle applies.

Answer: C

Diff: 1

Topic: 5.3 The Other Economic Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

- 30) Which of the following goods is NOT subject to the free-rider problem?
- A) National defense
 - B) The local police force
 - C) Public fireworks
 - D) A public transit system

Answer: D

Diff: 1

Topic: 5.3 The Other Economic Functions of Government

AACSB: Reflective thinking skills

Question Status: Revised

- 31) The distinguishing characteristic of private goods is that
- A) the principle of rival consumption does not apply to them.
 - B) their use is exclusive to the people who purchase them.
 - C) they can be sold but not rented.
 - D) they can be sold or rented, but not borrowed.

Answer: B

Diff: 1

Topic: 5.3 The Other Economic Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

- 32) A fundamental aspect of public goods is that they
- A) are just like private goods EXCEPT that everybody wants to consume the same amount.
 - B) have positive externalities.
 - C) are characterized by the principle of rival consumption.
 - D) can be consumed jointly by many people simultaneously.

Answer: D

Diff: 1

Topic: 5.3 The Other Economic Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

- 33) Which of the following is an example of a public good?
- A) Amtrak rail transport services
 - B) Services of the U.S. Post Office
 - C) The provision of medical care
 - D) The provision of national defense

Answer: D

Diff: 1

Topic: 5.3 The Other Economic Functions of Government

AACSB: Reflective thinking skills

Question Status: Previous Edition

- 34) Public goods are characterized by the free-rider problem because
- A) no one can be excluded from the benefits of public goods once they are produced.
 - B) public goods are usually things that people really do not want to consume.
 - C) public goods are characterized by the principle of rival consumption.
 - D) public goods can easily be subdivided into small units.

Answer: A

Diff: 2

Topic: 5.3 The Other Economic Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

- 35) Which of the following types of goods is subject to the free-rider problem?
- A) A private good
 - B) A public good
 - C) A product that creates a positive externality
 - D) A product that creates a negative externality

Answer: B

Diff: 2

Topic: 5.3 The Other Economic Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

- 36) Which of the following is best characterized as a public good?
- A) A public library
 - B) A church
 - C) Primary education
 - D) Police protection

Answer: D

Diff: 1

Topic: 5.3 The Other Economic Functions of Government

AACSB: Reflective thinking skills

Question Status: Previous Edition

- 37) Public goods are basically
- A) rival in consumption.
 - B) nonrival in consumption.
 - C) depletable in consumption.
 - D) nondepletable in consumption.

Answer: B

Diff: 1

Topic: 5.3 The Other Economic Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

- 38) Which event was most important in promoting the belief that the U.S. government should work to ensure economy-wide stability?
- A) World War II
 - B) The Civil Rights Movement
 - C) The California Gold Rush
 - D) The Great Depression

Answer: D

Diff: 1

Topic: 5.3 The Other Economic Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

39) What are the three goals of the Employment Act of 1946?

- A) Keep the peace, improve public education, and protect the environment
- B) Improve the education system, provide more job training, and expand the number of government jobs
- C) Full employment, price stability, and economic growth
- D) Full employment, better schools, and lower income taxes

Answer: C

Diff: 1

Topic: 5.3 The Other Economic Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

40) The Employment Act of 1946 reflects which one of the following functions of government?

- A) Providing a legal system
- B) Improving economy-wide stabilization
- C) Correcting externalities
- D) Providing public goods

Answer: B

Diff: 2

Topic: 5.3 The Other Economic Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

41) Which law specifically mandated the federal government's responsibility for economy-wide stability?

- A) The Employment Act of 1946
- B) The Sherman Act of 1890
- C) The Great Depression Act of 1930
- D) The Miller Act of 1960

Answer: A

Diff: 2

Topic: 5.3 The Other Economic Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

42) The economic functions of government include

- A) determining prices.
- B) setting wages in the public sector.
- C) protecting property rights.
- D) welfare.

Answer: C

Diff: 2

Topic: 5.3 The Other Economic Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

43) All of the following are economic functions of the government EXCEPT

- A) providing a legal system.
- B) determining the wage rate for most jobs.
- C) promoting competition in the market.
- D) providing public goods.

Answer: B

Diff: 1

Topic: 5.3 The Other Economic Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

- 44) The economic functions of the government deal with
- A) discouraging smoking in youths.
 - B) making sure supply equal demand.
 - C) promoting economic efficiency.
 - D) excess demand.

Answer: C

Diff: 1

Topic: 5.3 The Other Economic Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

- 45) Providing public goods is a(n)
- A) economic function of government.
 - B) political function of government.
 - C) economic and political function of government.
 - D) price system function.

Answer: A

Diff: 1

Topic: 5.3 The Other Economic Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

- 46) The political functions of government differ from the economic functions of government in that
- A) the political functions relate to income distribution while the economic functions relate to the way exchange is carried out.
 - B) the political functions are performed at the federal government while the economic functions are at the state and local government levels.
 - C) the political functions involve elections and the court systems while the economic functions involve taxation and transfers.
 - D) the President deals with the economic functions while Congress deals with the political functions.

Answer: A

Diff: 3

Topic: 5.3 The Other Economic Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

- 47) The difference between the economic and political functions of government is that
- A) the economic function is concerned with the Federal Taxation system while the political function is not.
 - B) the economic function is concerned with correcting for market failures while the political function is not.
 - C) the economic function is concerned with the reallocation of income while the political function is not.
 - D) the economic function encourages merit goods while the political function discourages demerit goods.

Answer: B

Diff: 1

Topic: 5.3 The Other Economic Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

- 48) The provision of a legal system is an important economic function of the government because
- A) lawyers and judges tend to be high-income people.
 - B) people need to feel safe when they go to work.
 - C) the legal system affects how exchange takes place through its enforcement of contracts.
 - D) the legal system affects the distribution of income through its awarding of damages in accident claims.

Answer: C

Diff: 1

Topic: 5.3 The Other Economic Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

- 49) Which of the following legal subjects is most concerned with the economic function of the legal system?
- A) Criminal law
 - B) Public goods
 - C) Antitrust legislation
 - D) Civil rights

Answer: C

Diff: 1

Topic: 5.3 The Other Economic Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

- 50) The government tries to protect the competitive economic system by passing and enforcing
- A) price controls.
 - B) tariff legislation.
 - C) antitrust laws.
 - D) building codes and zoning laws.

Answer: C

Diff: 1

Topic: 5.3 The Other Economic Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

- 51) A government agency charged with enforcing antitrust laws is
- A) the Federal Reserve Board.
 - B) the National Labor Relations Board.
 - C) the Council of Economic Advisors.
 - D) the Federal Trade Commission.

Answer: D

Diff: 1

Topic: 5.3 The Other Economic Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

- 52) Private goods are goods
- A) that carry a price.
 - B) for which price is greater than zero.
 - C) for which the more one person has the less is available for someone else.
 - D) that are produced by the government.

Answer: C

Diff: 1

Topic: 5.3 The Other Economic Functions of Government

AACSB:

Question Status: Previous Edition

53) All of the following are characteristics of public goods EXCEPT

- A) Public goods can be used by more people at no additional cost.
- B) The good can be consumed by everyone at the same time without reducing what is available for anyone else.
- C) The exclusion principle.
- D) The goods are perfectly divisible.

Answer: D

Diff: 2

Topic: 5.3 The Other Economic Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

54) Public goods are desired because

- A) people want and value them but the private sector will not make them available.
- B) we want the government to spend our tax dollars.
- C) they came in small units.
- D) they make supply equal to demand for private goods.

Answer: A

Diff: 1

Topic: 5.3 The Other Economic Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

55) An example of a public good is

- A) software produced by Microsoft.
- B) housing subsidies.
- C) the car I own.
- D) the fire department.

Answer: D

Diff: 1

Topic: 5.3 The Other Economic Functions of Government

AACSB: Reflective thinking skills

Question Status: Previous Edition

56) The distinguishing characteristic of a public good is

- A) noncompetitive production.
- B) durability.
- C) exclusivity.
- D) nonrival consumption.

Answer: D

Diff: 2

Topic: 5.3 The Other Economic Functions of Government

AACSB:

Question Status: Previous Edition

- 57) Which of the following statements is true about the difference between a public and private good?
- A) Both public and private goods are owned by individuals but public goods can be shared while private goods cannot be shared.
 - B) The government produces private goods while corporations produce public goods.
 - C) Consumption of a private good by one person reduces the amount available for others while the consumption of a public good does not reduce the amount available for others.
 - D) Resources are used to produce private goods but are not used to produce public goods.

Answer: C

Diff: 2

Topic: 5.3 The Other Economic Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

- 58) The difference between a private good and a public good is that
- A) private goods are government-sponsored goods while public goods are government-inhibited goods.
 - B) externalities are always created in the production process but not in the production of public goods.
 - C) private goods make us happy while public goods do not.
 - D) the exclusion principle applies to a private good but not to a public good.

Answer: D

Diff: 1

Topic: 5.3 The Other Economic Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

- 59) Which of the following is an example of a public good?
- A) Flood control
 - B) Post Office
 - C) Health care
 - D) Welfare

Answer: A

Diff: 1

Topic: 5.3 The Other Economic Functions of Government

AACSB: Reflective thinking skills

Question Status: Previous Edition

- 60) A lighthouse that serves a dangerous coastal area is built. The lighthouse cost \$500,000 to build and serves 500 ships a month. If the shipping in the area increases so that 750 ships pass by a month, the increase in additional costs of providing the light to these new ships is
- A) \$500,000.
 - B) \$250,000.
 - C) \$250.
 - D) \$0.

Answer: D

Diff: 2

Topic: 5.3 The Other Economic Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

- 61) A free rider is someone who
- A) hops on the bus for free.
 - B) enjoys the flowers I have planted and does not compensate me for them.
 - C) creates a negative externality.
 - D) buys a ticket for a movie.

Answer: B

Diff: 1

Topic: 5.3 The Other Economic Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

- 62) The free-rider problem is
- A) the use of private goods in one state by residents of another state.
 - B) the incentive that people have to avoid paying for a public good.
 - C) the incentive that people have once they are receiving welfare to keep getting welfare.
 - D) that people cannot be forced to accept public goods.

Answer: B

Diff: 1

Topic: 5.3 The Other Economic Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

- 63) In the spring, I enjoy the fragrance coming from my neighbors' flowers. The fragrance is an example of
- A) a negative externality.
 - B) a private good.
 - C) the need for antitrust legislation.
 - D) a free rider.

Answer: D

Diff: 1

Topic: 5.3 The Other Economic Functions of Government

AACSB: Reflective thinking skills

Question Status: Previous Edition

- 64) The free-rider problem plagues public goods because
- A) public goods are not produced by profit-maximizing firms and hence can be produced only at a loss to society.
 - B) once public goods are produced it is not possible to exclude anyone from consuming these goods.
 - C) the government can refuse to serve a citizen.
 - D) the public doesn't care about public goods.

Answer: B

Diff: 2

Topic: 5.3 The Other Economic Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

- 65) A fundamental reason that governments provide public goods is
- A) the free-rider problem.
 - B) negative externalities are part of the production process.
 - C) public goods are merit goods.
 - D) they are perfectly divisible.

Answer: A

Diff: 1

Topic: 5.3 The Other Economic Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

- 66) Ms. Smith is given a voucher for an apartment in a public housing project. The apartment
- A) is not subject to the principle of rival consumption.
 - B) is not a public good.
 - C) has widespread benefits and concentrated costs.
 - D) is subject to the exclusion principle.

Answer: B

Diff: 1

Topic: 5.3 The Other Economic Functions of Government

AACSB: Reflective thinking skills

Question Status: Previous Edition

- 67) Private schools are able to exclude students from attending classes they offer unless students have been accepted and paid tuition and fees. This suggests that education is
- A) subject to the principle of rival consumption.
 - B) subject to the free-rider problem.
 - C) not subject to the exclusion principle.
 - D) a public good.

Answer: A

Diff: 2

Topic: 5.3 The Other Economic Functions of Government

AACSB: Reflective thinking skills

Question Status: Previous Edition

- 68) Which of the following functions of government gives property owners the incentive to use their property efficiently?
- A) making sure that courts are lenient on people who steal private property
 - B) the protection of property rights
 - C) the enforcement of antitrust legislation
 - D) the financing of public goods

Answer: B

Diff: 3

Topic: 5.3 The Other Economic Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

- 69) Why does our government enforce antitrust legislation?
- A) because monopolies are known to be unfair to their stockholders
 - B) because monopolies are known to be unfair to their employees
 - C) because the government wants to create competition in markets in the interests of promoting efficiency
 - D) because the government wants to create competition in markets in the interests of promoting an equal distribution of income

Answer: C

Diff: 2

Topic: 5.3 The Other Economic Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

- 70) Which of the following is the best example of a public good?
- A) inoculation against a contagious disease
 - B) a streetlight
 - C) garbage collection
 - D) Internet access

Answer: B

Diff: 2

Topic: 5.3 The Other Economic Functions of Government

AACSB: Reflective thinking skills

Question Status: Previous Edition

- 71) Why are public goods provided by the government, rather than by the private sector?
- A) because they are large-scale projects that require the kind of financing only governments can generate through the issuance of bonds
 - B) because it would be difficult for a private sector firm to make a profit providing a public good, since consumers who benefit would not have to pay for it
 - C) because no one really benefits from public goods
 - D) because private sector firms do not have the foresight to plan for public goods

Answer: B

Diff: 2

Topic: 5.3 The Other Economic Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

- 72) When does the free-rider problem arise?
- A) when someone who benefits from a good does not have to contribute to paying for it
 - B) when a firm does not have to advertise, because its customers recommend the product to their friends
 - C) when policymakers ignore opportunity costs in making decisions
 - D) when production of a good generates pollution

Answer: A

Diff: 1

Topic: 5.3 The Other Economic Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

73) Which of the following would be considered an economic function of government?

- A) providing a legal system
- B) promoting competition
- C) providing public goods
- D) All of the above are correct.

Answer: D

Diff: 1

Topic: 5.3 The Other Economic Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

74) The legal system provided by the government is necessary for the smooth working of markets because

- A) it keeps criminals off of the streets.
- B) it defines and protects property rights.
- C) it is set up in the U.S. constitution.
- D) it ensures that producers maximize their profits.

Answer: B

Diff: 2

Topic: 5.3 The Other Economic Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

75) The U.S. antitrust laws

- A) aid monopolies in their quest to dominate the market for a good or service.
- B) are outdated and rarely used anymore.
- C) promote competition.
- D) are administered by the Department of Commerce.

Answer: C

Diff: 1

Topic: 5.3 The Other Economic Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

76) Public goods

- A) are overproduced by unrestrained markets.
- B) are simply private goods that the government provides.
- C) cannot be consumed by more than one person without the degradation of the value of the good.
- D) can be consumed by more than one person without degradation of the value of the good.

Answer: D

Diff: 2

Topic: 5.3 The Other Economic Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

77) Public goods face the

- A) principle of rival consumption.
- B) free-rider problem.
- C) law of overproduction.
- D) exclusion principle.

Answer: B

Diff: 2

Topic: 5.3 The Other Economic Functions of Government

AACSB: Analytic skills

Question Status: Revised

78) Which of the following could best be categorized as a public good?

- A) an apartment in a public housing project
- B) a pumpkin pie
- C) public fireworks
- D) a race track

Answer: C

Diff: 1

Topic: 5.3 The Other Economic Functions of Government

AACSB: Reflective thinking skills

Question Status: Revised

79) The "principle of rival consumption" applies to which of the following?

- A) national defense
- B) the free-rider problem
- C) the exclusion principle
- D) a private good

Answer: D

Diff: 1

Topic: 5.3 The Other Economic Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

80) The concept that Mr. Jones is going to enjoy the benefits of police protection even though he no longer pays taxes is called

- A) the free-rider problem.
- B) the negative externality principle.
- C) the principle of rival consumption.
- D) the principle of anti-trust.

Answer: A

Diff: 2

Topic: 5.3 The Other Economic Functions of Government

AACSB: Reflective thinking skills

Question Status: Previous Edition

81) Many nations are consistently accused of enjoying the benefits of membership in the United Nations, yet they provide few or no funds to support the organization. This is an example of

- A) the principle of rival consumption.
- B) the free-rider problem.
- C) the negative externality problem.
- D) the property rights problem.

Answer: B

Diff: 2

Topic: 5.3 The Other Economic Functions of Government

AACSB: Reflective thinking skills

Question Status: Previous Edition

- 82) An important characteristic of private goods is
- A) the nonexclusion principle.
 - B) the principle of rival consumption.
 - C) the principle of joint consumption.
 - D) the principle of conspicuous consumption.

Answer: B

Diff: 2

Topic: 5.3 The Other Economic Functions of Government

AACSB:

Question Status: Revised

- 83) The non-exclusion principle means
- A) no one can be excluded from the benefits of a public good, even if the person does not pay for it.
 - B) no one can be excluded from the benefits of a private good, even if only one person pays for it.
 - C) no one who pays for a public good can be excluded from receiving the benefits of a public good.
 - D) people who do not pay for a public good can be excluded from receiving its benefits.

Answer: A

Diff: 2

Topic: 5.3 The Other Economic Functions of Government

AACSB:

Question Status: Revised

- 84) Which of the following would be classified as a public good?
- A) state lotteries
 - B) telephone service
 - C) cable TV programming
 - D) national defense

Answer: D

Diff: 1

Topic: 5.3 The Other Economic Functions of Government

AACSB: Reflective thinking skills

Question Status: Previous Edition

- 85) A characteristic of a public good is that a public good is provided
- A) to some businesses, but not to others.
 - B) only in some states.
 - C) to low income residents in some states.
 - D) to many individuals at no additional cost.

Answer: D

Diff: 1

Topic: 5.3 The Other Economic Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

86) Receiving a voucher for an apartment in a public housing project would be an example of a good that satisfies

- A) the principle of rival consumption.
- B) the definition of a public good.
- C) the definition of a good with a positive externality.
- D) the nonexclusion principle.

Answer: A

Diff: 2

Topic: 5.3 The Other Economic Functions of Government

AACSB: Reflective thinking skills

Question Status: Previous Edition

87) To an economist, a free rider is a person who

- A) uses private goods without paying for them.
- B) benefits from consuming public goods without paying for them.
- C) consumes demerit goods.
- D) uses the public transportation system without paying for it.

Answer: B

Diff: 2

Topic: 5.3 The Other Economic Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

88) A characteristic of a public good is

- A) rival consumption.
- B) the exclusion principle.
- C) the free-rider problem.
- D) clear property rights.

Answer: C

Diff: 2

Topic: 5.3 The Other Economic Functions of Government

AACSB:

Question Status: Previous Edition

89) Explain why economists consider it to be one of the economic functions of government to provide a legal system.

Answer: A market economy relies heavily on contracts and property rights. Property rights must be defined and protected if people are going to make investments in resources, and if people are going to exchange assets. Contracts must also be enforced. By providing a legal system, the government can ensure that a market system will function better.

Diff: 1

Topic: 5.3 The Other Economic Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

90) How do public goods differ from private goods?

Answer: A private good is characterized by the principle of rival consumption, which means that one person's consumption of a good reduces the amount available for someone else. A public good is not characterized by the principle of rival consumption. Public goods can be used by more people at no additional cost. Further, once the good is produced, it is usually impossible, or at the very least difficult, to exclude anyone from consuming it.

Diff: 1

Topic: 5.3 The Other Economic Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

91) Explain why public goods can be classified as market failure? Explain what problem arises when public goods are produced?

Answer: When the market fails to provide certain goods and services, there is a clear case for government intervention. If left to the free market mechanism, no public goods would be provided and, as a result, there would be a clear market failure. Public goods can be used by one person without reducing availability of the good for consumption by others (non-rival) at no additional cost and once the good is produced, it is usually impossible, or at the very least difficult, to exclude anyone from consuming it (non-excludable). Due to these results, consumers can take advantage of public goods without contributing sufficiently to their creation. This is called the free rider problem.

Diff: 2

Topic: 5.3 The Other Economic Functions of Government

AACSB: Analytic skills

Question Status: New

92) What is the purpose of antitrust legislation?

Answer: Antitrust legislation makes illegal certain economic activities. These activities involve restraining trade and inhibiting free competition among rival firms in the marketplace. The aim is to reduce the economic power of monopolies.

Diff: 1

Topic: 5.3 The Other Economic Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

93) What is the free-rider problem, and how is it related to public goods?

Answer: The free-rider problem arises from the exclusion principle. Since no one can be excluded from the benefits of a public good, even if they don't contribute towards paying for the good, people have an incentive to let other people pay for the good and to not contribute themselves. If everyone free rides, the good will not get produced. Hence, public goods usually are provided by the government and paid for by taxes.

Diff: 2

Topic: 5.3 The Other Economic Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

- 94) Explain why ensuring economic stability is an economics function of government?

Answer: Our economy sometimes faces the problems of high unemployment and rising prices. Perhaps most importantly, the federal government attempts to guide the overall pace of economic activity, attempting to maintain steady growth, high levels of employment, and price stability. By adjusting spending and tax rates (fiscal policy) or managing the money supply and controlling the use of credit (monetary policy), it can slow down or speed up the economy's rate of growth -- in the process, affecting the level of prices and employment.

Diff: 3

Topic: 5.3 The Other Economic Functions of Government

AACSB: Analytic skills

Question Status: New

- 95) Suppose a valley periodically floods. A dam can be built in the river that would prevent the flooding. Explain how flood control provided by building the dam arguably fits the characteristics of a public good.

Answer: The dam would be indivisible since it must be a certain size in order to be effective. Once flood control is provided, new homes can be protected at no additional cost. Any one home's protection does not reduce the protection from flooding for any other home. It would be impossible to exclude someone from the benefits of the flood control, so flood control arguably is a public good.

Diff: 2

Topic: 5.3 The Other Economic Functions of Government

AACSB: Reflective thinking skills

Question Status: Previous Edition

- 96) What are the key characteristics of a public good?

Answer: A public good is not subject to the principle of rival consumption in the sense that it can be provided to different individuals without additional costs. A public good is also subject to the free-rider problem in the sense that persons can benefit from the good without paying for it.

Diff: 1

Topic: 5.3 The Other Economic Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

5.4 The Political Functions of Government

- 1) By definition, a government-sponsored good
- A) is a good that is deemed socially desirable.
 - B) is a good that should be available only to upper-income groups.
 - C) is always provided at a zero price.
 - D) does not affect society's general welfare.

Answer: A

Diff: 1

Topic: 5.4 The Political Functions of Government

AACSB:

Question Status: Previous Edition

2) In the United States, which of the following is an example of a government-inhibited good?

- A) Museums
- B) Concerts
- C) Cigarettes
- D) Sports stadiums

Answer: C

Diff: 1

Topic: 5.4 The Political Functions of Government

AACSB: Reflective thinking skills

Question Status: Previous Edition

3) In the United States, which of the following is an example of a government-sponsored good?

- A) Cable T.V.
- B) Concerts
- C) Cigarettes
- D) Coffee

Answer: B

Diff: 1

Topic: 5.4 The Political Functions of Government

AACSB: Reflective thinking skills

Question Status: New

4) A friend of yours receives a government voucher for an apartment in a public housing project.

This apartment represents

- A) a government-sponsored good.
- B) the free-rider problem.
- C) a public good.
- D) the drop-in-the-bucket problem.

Answer: A

Diff: 1

Topic: 5.4 The Political Functions of Government

AACSB: Reflective thinking skills

Question Status: Previous Edition

5) Under present U.S. law, cocaine is an example of

- A) a government-sponsored good.
- B) a capital good.
- C) a public good.
- D) a government-inhibited good.

Answer: D

Diff: 1

Topic: 5.4 The Political Functions of Government

AACSB: Reflective thinking skills

Question Status: Previous Edition

6) Under present U.S. law, which one of the following is a government-inhibited good?

- A) Housing
- B) Medical care
- C) Heroin
- D) Education

Answer: C

Diff: 1

Topic: 5.4 The Political Functions of Government

AACSB: Reflective thinking skills

Question Status: Previous Edition

- 7) A government-inhibited good is a good which
- A) is not subject to the principle of mutual exclusivity.
 - B) the political process has deemed socially undesirable.
 - C) can be consumed by one individual without affecting the consumption of another individual.
 - D) the political process has deemed socially desirable.

Answer: B

Diff: 1

Topic: 5.4 The Political Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

- 8) A government-sponsored good is one that
- A) everybody is willing to support with funding contributions.
 - B) is inherently valuable.
 - C) the political process has determined socially desirable.
 - D) everybody will receive concrete benefits from.

Answer: C

Diff: 1

Topic: 5.4 The Political Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

- 9) A government-inhibited good is one that
- A) cannot be individually consumed.
 - B) would be underproduced by the private market.
 - C) should be subsidized to correct the market failure and productive inefficiency.
 - D) has been deemed socially undesirable via the political process.

Answer: D

Diff: 1

Topic: 5.4 The Political Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

- 10) Which of the following is a government-inhibited good?
- | | |
|---------------------|---------------------|
| A) A lighthouse | B) National defense |
| C) Public education | D) Cocaine |

Answer: D

Diff: 1

Topic: 5.4 The Political Functions of Government

AACSB: Reflective thinking skills

Question Status: Previous Edition

- 11) A transfer payment is a payment
- A) made by the government to its current workers.
 - B) associated with items exported to other nations.
 - C) for in-kind services provided to the government.
 - D) for which no services or goods are rendered.

Answer: D

Diff: 1

Topic: 5.4 The Political Functions of Government

AACSB:

Question Status: Previous Edition

- 12) Which of the following is a transfer payment?

- I. Social Security
 - II. Unemployment benefits
- A) I only B) II only C) Both I and II D) Neither I nor II

Answer: C

Diff: 1

Topic: 5.4 The Political Functions of Government

AACSB: Reflective thinking skills

Question Status: Previous Edition

- 13) An example of an in-kind transfer is

- A) national defense.
- B) Social Security.
- C) low-cost public housing.
- D) Unemployment benefits.

Answer: C

Diff: 1

Topic: 5.4 The Political Functions of Government

AACSB: Reflective thinking skills

Question Status: Previous Edition

- 14) Money payments made by governments to individuals for which no services or goods are concurrently rendered are known as

- A) transfer payments.
- B) government-sponsored payments.
- C) government-inhibited payments.
- D) black market payments.

Answer: A

Diff: 1

Topic: 5.4 The Political Functions of Government

AACSB:

Question Status: Revised

- 15) Examples of transfer payments are

- A) wages, profits, and rents.
- B) Social Security checks and unemployment insurance payments.
- C) salaries of educators, police, and firefighters.
- D) federal government spending for national defense.

Answer: B

Diff: 1

Topic: 5.4 The Political Functions of Government

AACSB: Reflective thinking skills

Question Status: Previous Edition

16) Which of the following does NOT involve transfers in kind?

- A) Public housing
- B) Food stamps
- C) Medicare
- D) Salaries of government employees

Answer: D

Diff: 1

Topic: 5.4 The Political Functions of Government

AACSB: Reflective thinking skills

Question Status: Previous Edition

17) A political function of government is to

- A) encourage the consumption of government-sponsored goods.
- B) provide public goods.
- C) correct for externalities.
- D) encourage the workings of the price system.

Answer: A

Diff: 1

Topic: 5.4 The Political Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

18) Which of the following is a political function of government but is not a central economic function?

- A) Determining who has a right to vote
- B) Determining government-sponsored and government-inhibited goods
- C) Providing a legal system to adjudicate property rights
- D) Redistributing income from some individuals to others

Answer: B

Diff: 1

Topic: 5.4 The Political Functions of Government

AACSB: Analytic skills

Question Status: Revised

19) A government-sponsored good is one that

- A) is desirable to no one but ruled desirable by the court system nonetheless.
- B) everyone agrees is socially desirable.
- C) freely competitive markets have determined is socially desirable.
- D) the political process has determined is socially desirable.

Answer: D

Diff: 1

Topic: 5.4 The Political Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

- 20) If a nation's government determines that consumption of cigarettes should be discouraged, then this means that the government has judged cigarettes to be a(n)

A) government-sponsored good. B) exclusive good.
C) government-inhibited good. D) public good.

Answer: C

Diff: 2

Topic: 5.4 The Political Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

- 21) A government-inhibited good is one that

A) the political process has determined is socially undesirable.
B) the political process has determined is socially desirable.
C) freely competitive markets have determined is socially desirable.
D) we want to encourage the consumption of.

Answer: A

Diff: 1

Topic: 5.4 The Political Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

- 22) A payment that is made by the government for which no goods or services are given in return is known as

A) a public good. B) a transfer payment.
C) a negative externality. D) a free rider.

Answer: B

Diff: 1

Topic: 5.4 The Political Functions of Government

AACSB:

Question Status: Previous Edition

- 23) If a government determines that the provision of services by museums should be encouraged, then this means that the government has judged museum displays to be a(n)

A) government-sponsored good. B) exclusive good.
C) government-inhibited good. D) public good.

Answer: A

Diff: 2

Topic: 5.4 The Political Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

- 24) Establishing rules for voter registration is an example of a(n)

A) economic function of government. B) political function of government.
C) public good. D) transfer payment.

Answer: B

Diff: 1

Topic: 5.4 The Political Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

25) A government-inhibited good is often

- A) produced by the government.
- B) subsidized.
- C) taxed.
- D) advertised.

Answer: C

Diff: 2

Topic: 5.4 The Political Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

26) A government-sponsored good is often

- A) produced by the government.
- B) subsidized.
- C) taxed.
- D) advertised.

Answer: B

Diff: 2

Topic: 5.4 The Political Functions of Government

AACSB: Analytic skills

Question Status: New

27) Which of the following is NOT an example of a transfer payment?

- A) Social Security
- B) Unemployment benefits
- C) Welfare
- D) Interest payments on government bonds

Answer: D

Diff: 1

Topic: 5.4 The Political Functions of Government

AACSB: Reflective thinking skills

Question Status: Previous Edition

28) Which of the following is NOT related to the government's political function of income redistribution?

- A) Providing money transfer payments
- B) Excise tax on gasoline
- C) Social Security
- D) In-kind transfers

Answer: B

Diff: 2

Topic: 5.4 The Political Functions of Government

AACSB: Reflective thinking skills

Question Status: Previous Edition

29) Which of the following types of goods would most likely be classified as a government-inhibited good?

- A) heroin
- B) marijuana
- C) tobacco
- D) All of the above are correct.

Answer: D

Diff: 2

Topic: 5.4 The Political Functions of Government

AACSB: Reflective thinking skills

Question Status: Previous Edition

- 30) Examples of transfers-in-kind include
- A) tax rebates on both the federal and state levels.
 - B) taxes on alcohol and tobacco.
 - C) food stamps and public housing.
 - D) political advertising.

Answer: C

Diff: 1

Topic: 5.4 The Political Functions of Government

AACSB: Reflective thinking skills

Question Status: Previous Edition

- 31) What type of policy does the government adopt in dealing with government-inhibited goods?
- A) It subsidizes their consumption.
 - B) It subsidizes their production.
 - C) It provides them as public goods.
 - D) It taxes, regulates, or prohibits their use.

Answer: D

Diff: 1

Topic: 5.4 The Political Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

- 32) A public museum is an example of a
- A) government-sponsored good.
 - B) public good.
 - C) good which generates a positive externality.
 - D) good which generates a negative externality.

Answer: A

Diff: 1

Topic: 5.4 The Political Functions of Government

AACSB: Reflective thinking skills

Question Status: Previous Edition

- 33) Which of the following checks issued by the government represents a transfer payment?
- A) The federal government pays a defense contractor for development of a missile system.
 - B) The federal government pays a retiree her Social Security benefits.
 - C) The state of Oregon pays a construction firm for its work in repairing a state highway.
 - D) The state of Illinois pays groundskeepers at the state capitol building their weekly wages.

Answer: B

Diff: 2

Topic: 5.4 The Political Functions of Government

AACSB: Reflective thinking skills

Question Status: Previous Edition

- 34) Government-sponsored goods are those goods
- A) that society views desirable through the political process.
 - B) that companies give away as promotional prizes.
 - C) that have lower than average negative externality.
 - D) that only low-income individuals consume.

Answer: A

Diff: 1

Topic: 5.4 The Political Functions of Government

AACSB:

Question Status: Previous Edition

- 35) An example of a transfer payment is
- A) the President's salary.
 - B) unemployment insurance benefits.
 - C) a payment to a defense contractor.
 - D) court costs paid by the defendants in a law suit.

Answer: B

Diff: 1

Topic: 5.4 The Political Functions of Government

AACSB: Reflective thinking skills

Question Status: Previous Edition

- 36) Which of the following is NOT an example of a transfer payment?
- A) unemployment compensation
 - B) food stamps
 - C) government salaries
 - D) Social Security benefits

Answer: C

Diff: 1

Topic: 5.4 The Political Functions of Government

AACSB: Reflective thinking skills

Question Status: Previous Edition

- 37) Fred receives a \$14,000.00 per year grant by the federal government because he is disabled. This is a
- A) demerit good.
 - B) transfer payment.
 - C) non-rival good.
 - D) free rider problem.

Answer: B

Diff: 2

Topic: 5.4 The Political Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

- 38) How does the government carry out income redistribution?

Answer: Income redistribution can be carried out by a combination of progressive taxation and transfer payments. Transfer payments are money payments made by the government to people for which no goods or services are rendered. Transfers can also be "in-kind," that is, in the form of a good or service.

Diff: 1

Topic: 5.4 The Political Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

- 39) According to the textbook, what are the two key political functions of government in a market economy?

Answer: The two functions of government that are political rather than economic include (1) the regulation and provision of government-sponsored and government-inhibited goods, and (2) income redistribution.

Diff: 1

Topic: 5.4 The Political Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

- 40) How does a government-sponsored good differ from a public good?

Answer: A public good is characterized by the fact that consumption is not rival and by the presence of the free-rider problem. Government-sponsored goods are private goods that the political process has deemed desirable.

Diff: 2

Topic: 5.4 The Political Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

- 41) Is there any common characteristic shared by government-inhibited goods and government-sponsored goods? Explain briefly.

Answer: Government-inhibited and government-sponsored goods do not have any inherent characteristics that qualify them as such; instead, through the political process, people collectively make judgments about which goods and services are "good" for society and which are "bad."

Diff: 1

Topic: 5.4 The Political Functions of Government

AACSB: Analytic skills

Question Status: Previous Edition

5.5 Public Spending and Transfer Programs

- 1) As a share of total national income, government spending generally has
- A) been constant over the last fifty years.
 - B) increased over the last fifty years.
 - C) decreased over the last fifty years.
 - D) increased until ten years ago, and then decreased steadily.

Answer: B

Diff: 1

Topic: 5.5 Public Spending and Transfer Programs

AACSB: Analytic skills

Question Status: Previous Edition

- 2) Social Security and Medicare are clear examples of
- A) capitalism.
 - B) market-determined services.
 - C) market failures and externalities.
 - D) governmental intervention in the market.

Answer: D

Diff: 3

Topic: 5.5 Public Spending and Transfer Programs

AACSB:

Question Status: Previous Edition

- 3) According to your text, which of the following represents the largest source of tax receipts for the *Federal* government?
- A) sales taxes
 - B) individual income taxes
 - C) corporate income taxes
 - D) property taxes

Answer: B

Diff: 3

Topic: 5.5 Public Spending and Transfer Programs

AACSB: Analytic skills

Question Status: Previous Edition

- 4) Government payment of a per-unit subsidy for medical care causes
- A) the market supply curve to shift upward.
 - B) the market demand curve to shift downward.
 - C) a reduction in the price that providers of medical care receive for each unit of care provided.
 - D) an increase in the quantity of medical care demanded above the quantity demanded in the absence of the subsidy.

Answer: D

Diff: 2

Topic: 5.5 Public Spending and Transfer Programs

AACSB: Analytic skills

Question Status: Previous Edition

- 5) Recipients of Medicare tend to demand a greater quantity of low-value, high-cost services because
- A) the services are readily available.
 - B) recipients are coerced into demanding such services.
 - C) the government mandates that they demand such services.
 - D) the services are heavily subsidized.

Answer: D

Diff: 2

Topic: 5.5 Public Spending and Transfer Programs

AACSB: Analytic skills

Question Status: Previous Edition

- 6) The current Medicare system is designed so that it actually encourages
- A) cost reductions.
 - B) higher costs of medical services.
 - C) higher costs only for surgeries.
 - D) lower drug costs for recipients.

Answer: B

Diff: 2

Topic: 5.5 Public Spending and Transfer Programs

AACSB: Analytic skills

Question Status: Previous Edition

- 7) Government payment of a per-unit subsidy for medical care causes the out-of-pocket price that consumers pay for care to be
- A) less than the price that producers receive for providing care.
 - B) greater than the price that producers receive for providing care.
 - C) greater than the market clearing price without the subsidy.
 - D) equal to zero.

Answer: A

Diff: 2

Topic: 5.5 Public Spending and Transfer Programs

AACSB: Analytic skills

Question Status: Previous Edition

- 8) Compared with the market clearing price of a health care service covered by Medicare, the Medicare program pays a _____ price to health care providers and charges a _____ price to consumers.
- A) lower, lower
 - B) lower, higher
 - C) higher, lower
 - D) higher, higher

Answer: C

Diff: 2

Topic: 5.5 Public Spending and Transfer Programs

AACSB: Analytic skills

Question Status: Previous Edition

- 9) The goal of Medicare is to
- A) help the poor and indigent pay their hospital bills.
 - B) prevent poverty in urban cities.
 - C) subsidize medical expenses for the elderly.
 - D) subsidize costs incurred by doctors.

Answer: C

Diff: 1

Topic: 5.5 Public Spending and Transfer Programs

AACSB: Analytic skills

Question Status: Previous Edition

- 10) Subsidies paid to the health care industry for Medicare patients are paid by
- A) Congress.
 - B) the Teamsters union.
 - C) current taxes.
 - D) the Federal Reserve.

Answer: C

Diff: 2

Topic: 5.5 Public Spending and Transfer Programs

AACSB: Reflective thinking skills

Question Status: Previous Edition

- 11) Public education is priced below market price largely as a result of
- A) government subsidy programs.
 - B) under-funded public education.
 - C) rising test scores by students.
 - D) taxpayers who contribute little to the funding of public education.

Answer: A

Diff: 2

Topic: 5.5 Public Spending and Transfer Programs

AACSB: Analytic skills

Question Status: Previous Edition

- 12) All of the following are major sources for financing public education EXCEPT
- A) income taxes.
 - B) sales taxes.
 - C) property taxes.
 - D) government fees.

Answer: D

Diff: 2

Topic: 5.5 Public Spending and Transfer Programs

AACSB: Reflective thinking skills

Question Status: Previous Edition

- 13) When state and local governments provide public schools with a per-unit subsidy to provide educational services, the price that the schools providing these services receive is
- A) less than the price that consumers pay to receive educational services.
 - B) less than the amount of the per-unit subsidy that the schools receive.
 - C) greater than the market clearing price without the subsidy.
 - D) equal to zero.

Answer: C

Diff: 1

Topic: 5.5 Public Spending and Transfer Programs

AACSB: Analytic skills

Question Status: Previous Edition

- 14) According to your text, one reason for flat or falling achievement scores even in the face of substantially higher education subsidies may be that
- A) the additional funds are being siphoned off by dishonest school board members.
 - B) some of the funds are going to social services rather than to enhance learning activities.
 - C) students are so unmotivated that no amount of spending will ever improve scores.
 - D) most parents do not support the schools or their children's educational activities.

Answer: B

Diff: 2

Topic: 5.5 Public Spending and Transfer Programs

AACSB: Analytic skills

Question Status: Previous Edition

- 15) One reason the Medicare system costs so much is
- A) the amount of medical services is determined by the equilibrium of supply and demand.
 - B) the supply of medical services does not respond to price changes.
 - C) supply and demand analysis does not apply.
 - D) beneficiaries are entitled to receive services for which the per-unit cost exceeds their own personal out-of-pocket payment.

Answer: D

Diff: 1

Topic: 5.5 Public Spending and Transfer Programs

AACSB: Reflective thinking skills

Question Status: Previous Edition

- 16) Which of the following is a major reason why the Medicare program is in such financial trouble?
- A) Workers are not paying enough into the program.
 - B) The government set reimbursement rates too high.
 - C) Because medical services are subsidized by the government, both consumption by the elderly and the cost of services have increased.
 - D) There is a shortage of medical school applicants.

Answer: C

Diff: 2

Topic: 5.5 Public Spending and Transfer Programs

AACSB: Reflective thinking skills

Question Status: Previous Edition

- 17) The major economic effect of Medicare subsidies is
- A) that the number of physicians has decreased since compensation is low.
 - B) to increase the price of medical services and reduce the quantity demanded.
 - C) to increase the price of medical services and increase the quantity demanded.
 - D) to lower the price of medical services and reduce the quantity demanded.

Answer: C

Diff: 1

Topic: 5.5 Public Spending and Transfer Programs

AACSB: Analytic skills

Question Status: Previous Edition

- 18) Medicare subsidies will cause people to
- A) perceive the price they pay per unit of medical services to be lower than the price received by the provider.
 - B) perceive the price they pay per unit of medical services to be higher than the price received by the provider.
 - C) perceive the price they pay per unit of medical services to be exactly equal to the price received by the provider.
 - D) demand fewer services.

Answer: A

Diff: 1

Topic: 5.5 Public Spending and Transfer Programs

AACSB: Analytic skills

Question Status: Previous Edition

- 19) Medicare subsidies will cause people to
- A) consume less medical services than in the absence of the subsidies.
 - B) consume more medical services than in the absence of the subsidies.
 - C) consume the same amount medical services as they would if there were no subsidies.
 - D) be sicker because of inferior care.

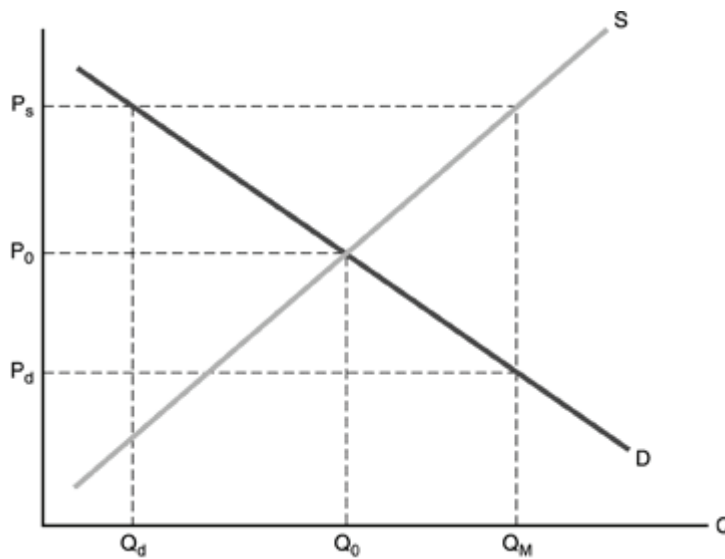
Answer: B

Diff: 1

Topic: 5.5 Public Spending and Transfer Programs

AACSB: Analytic skills

Question Status: Previous Edition



- 20) Refer to the above figure. Medicare subsidies have increased the price of medical services to P_s . The perceived price on the part of consumers is
- A) P_s .
 - B) P_0 .
 - C) P_d .
 - D) undetermined without more information.

Answer: C

Diff: 1

Topic: 5.5 Public Spending and Transfer Programs

AACSB: Analytic skills

Question Status: Previous Edition

21) Refer to the above figure. Medicare subsidies have increased the price of medical services to P_S .

The quantity demanded of medical services is

- A) Q_M .
- B) Q_0 .
- C) Q_d .
- D) undetermined without more information.

Answer: A

Diff: 1

Topic: 5.5 Public Spending and Transfer Programs

AACSB: Analytic skills

Question Status: Previous Edition

22) In the above figure, the total dollar amount of the Medicare subsidies provided by the government is equal to

- A) the difference between P_S and P_0 multiplied by Q_M .
- B) the difference between P_S and P_d multiplied by Q_M .
- C) the difference between P_0 and P_d multiplied by Q_d .
- D) the difference between P_S and P_d multiplied by Q_0 .

Answer: B

Diff: 1

Topic: 5.5 Public Spending and Transfer Programs

AACSB: Analytic skills

Question Status: Previous Edition

23) Refer to the above figure. Medicare subsidies have increased the price of medical services to P_S .

Which of the following statements is true about the effect the Medicare subsidy has had on the consumption of medical services?

- A) The amount of medical services provided has decreased from Q_0 to Q_d as a result of the subsidy.
- B) The amount of medical services provided has increased from Q_0 to Q_M as a result of the subsidy.
- C) The amount of medical services provided has increased from Q_d to Q_M as a result of the subsidy.
- D) The amount of medical services provided has remained unchanged as a result of the subsidy.

Answer: B

Diff: 3

Topic: 5.5 Public Spending and Transfer Programs

AACSB: Analytic skills

Question Status: Previous Edition

- 24) In the above figure, if a Medicare subsidy that had previously been paid by the government has now been eliminated, the result will be
- A) an increase in the price received by producers, from P_0 to P_S .
 - B) a decrease in the price received by producers, from P_S to P_0 .
 - C) an increase in the price paid by consumers, from P_0 to P_S .
 - D) a decrease in the price paid by consumers, from P_S to P_0 .

Answer: B

Diff: 3

Topic: 5.5 Public Spending and Transfer Programs

AACSB: Analytic skills

Question Status: Previous Edition

- 25) Refer to the above figure. In the absence of a subsidy,
- A) Q_d would be demanded and Q_M would be supplied.
 - B) the price P_d would be charged and quantity Q_M demanded.
 - C) the quantity Q_0 and price P_0 would prevail in the market.
 - D) None of the above is correct.

Answer: C

Diff: 3

Topic: 5.5 Public Spending and Transfer Programs

AACSB: Analytic skills

Question Status: Previous Edition

- 26) The funding of public education is
- A) a private program.
 - B) a subsidy program.
 - C) done by voluntary contributions.
 - D) provided by Social Security.

Answer: B

Diff: 1

Topic: 5.5 Public Spending and Transfer Programs

AACSB:

Question Status: Previous Edition

- 27) Which of the following statements about public education is TRUE?
- A) Over the last 40 years, there has been an increase in spending for public education, while there has not been a significant increase in performance.
 - B) Over the last 40 years, there has been a decrease in public spending for public education, while there has not been a significant increase in performance.
 - C) Most of the increases in public spending on public education have gone into programs that have increased student learning.
 - D) Over the last 40 years there has been no decline in any of the measures of student performance in public education.

Answer: A

Diff: 1

Topic: 5.5 Public Spending and Transfer Programs

AACSB: Analytic skills

Question Status: Previous Edition

- 28) If the government pays a per-unit subsidy to the producer of a service, we would expect to see a(n)
- I. increase in the quantity demanded.
 - II. decrease in the out-of-pocket price paid by consumers.
 - III. increase in the quantity supplied by producers.
- A) I only
 - B) both I and II only
 - C) both II and III only
 - D) I, II, and III

Answer: D

Diff: 1

Topic: 5.5 Public Spending and Transfer Programs

AACSB: Analytic skills

Question Status: Previous Edition

- 29) Over the past 40 years, there has been an increase in spending on public education without a significant increase in student performance. One explanation given by economists on why student performance has not improved is that
- A) not enough funds have been spent on public education.
 - B) schools are providing high-priced services that are not valued by parents.
 - C) the quantity of educational services has not increased beyond the pre-subsidy equilibrium.
 - D) too much competition for educational services.

Answer: B

Diff: 1

Topic: 5.5 Public Spending and Transfer Programs

AACSB: Analytic skills

Question Status: Previous Edition

- 30) In public education, the value of the services provided is
- A) greater than the value that parents and students place on the services.
 - B) equal to the value that parents and students place on the services.
 - C) less than the value that parents and students place on the services.
 - D) zero since they are a public good.

Answer: A

Diff: 1

Topic: 5.5 Public Spending and Transfer Programs

AACSB: Analytic skills

Question Status: Previous Edition

- 31) Measures of student performance have not increased even though per-pupil government subsidies have increased because
- A) there is a need for more funds to be spent.
 - B) we have declining enrollment in public schools.
 - C) parents and children value the last unit of educational services received more than the cost.
 - D) parents and children value the last unit of educational services received less than the cost.

Answer: D

Diff: 1

Topic: 5.5 Public Spending and Transfer Programs

AACSB: Analytic skills

Question Status: Previous Edition

- 32) By subsidizing the provision of public education, the government
- A) generates an increase in the quantity of educational services demanded..
 - B) pushes the per-unit price that consumers pay for educational services below the market clearing price..
 - C) pushes the per-unit price that producers of educational services receive above the market clearing price.
 - D) All of the above

Answer: D

Diff: 1

Topic: 5.5 Public Spending and Transfer Programs

AACSB: Analytic skills

Question Status: Previous Edition

- 33) Government outlays include all of the following EXCEPT
- A) dividend payments.
 - B) spending on the military.
 - C) electricity for the Capital Building.
 - D) letterhead stationery.

Answer: A

Diff: 1

Topic: 5.5 Public Spending and Transfer Programs

AACSB: Analytic skills

Question Status: Previous Edition

- 34) Government spending as a percent of national income
- A) peaked during the Reagan administration.
 - B) peaked during World War II.
 - C) has been steadily climbing since 1850.
 - D) has been almost constant this century.

Answer: B

Diff: 1

Topic: 5.5 Public Spending and Transfer Programs

AACSB: Analytic skills

Question Status: Previous Edition

- 35) The largest spending category for state governments is
- A) welfare.
 - B) health care.
 - C) education.
 - D) highway construction.

Answer: C

Diff: 1

Topic: 5.5 Public Spending and Transfer Programs

AACSB: Analytic skills

Question Status: Previous Edition

- 36) What effect have Medicare subsidies had on the consumption of medical services?
- A) The consumption of medical services has been unaffected, because people don't consider the financial cost when seeking services related to their health.
 - B) The consumption of medical services has been unaffected, because government restrictions have prevented patients from seeking a level of care above and beyond what they would choose if they had to pay for medical treatment out of pocket.
 - C) The consumption of medical services has increased because Medicare subsidies give people the incentive to seek more care than they would otherwise.
 - D) The effect cannot be measured because it is difficult to quantify the amount of resources devoted to our health care system.

Answer: C

Diff: 3

Topic: 5.5 Public Spending and Transfer Programs

AACSB: Reflective thinking skills

Question Status: Previous Edition

- 37) How have some patients been harmed by Medicare reimbursement caps?
- A) They have been discharged from the hospital too soon, so that the hospital can cut costs.
 - B) They have been kept in the hospital too long, so that the hospital can get a higher reimbursement amount.
 - C) They have had to undergo unnecessary procedures, so that the hospital can get a higher reimbursement amount.
 - D) They have had to wait too long for essential procedures.

Answer: A

Diff: 1

Topic: 5.5 Public Spending and Transfer Programs

AACSB: Reflective thinking skills

Question Status: Previous Edition

- 38) Public schools
- A) allow students to get an education without incurring any opportunity cost.
 - B) provide education at a price below the market price.
 - C) provide education at a price above the market price.
 - D) have done a better job of educating their students in science, math, reading, and writing as the subsidies they receive have increased over the years.

Answer: B

Diff: 2

Topic: 5.5 Public Spending and Transfer Programs

AACSB: Reflective thinking skills

Question Status: Previous Edition

- 39) Economically speaking, the design of Medicare
- A) encourages the consumption of medical services.
 - B) discourages the consumption of medical services.
 - C) helps to decrease the cost of care to non-Medicare patients.
 - D) discourages the provision of medical services.

Answer: A

Diff: 2

Topic: 5.5 Public Spending and Transfer Programs

AACSB: Reflective thinking skills

Question Status: Previous Edition

- 40) Medicare is an example of a third-party payment for medical services that
- A) causes providers to supply less of medical services than they would without the payment.
 - B) causes buyers to consume more of medical services than they would without the payment.
 - C) does not cause any change in the equilibrium position for medical services which existed without the subsidy.
 - D) causes the price of medical services to rise for the consumer once the payment is provided.

Answer: B

Diff: 2

Topic: 5.5 Public Spending and Transfer Programs

AACSB: Reflective thinking skills

Question Status: Previous Edition

- 41) The economic problem with Medicare financing is that
- A) there is a built-in incentive to provide fewer services by doctors.
 - B) there is a built-in incentive to travel to Canada to receive medical services.
 - C) the cost of providing services is falling annually.
 - D) there is a built-in incentive to consume more services.

Answer: D

Diff: 2

Topic: 5.5 Public Spending and Transfer Programs

AACSB: Reflective thinking skills

Question Status: Previous Edition

- 42) Which of the following is NOT a consequence of the introduction of the Medicare program?
- A) an increased quantity of medical services demanded
 - B) an increased ability for the elderly to obtain medical services
 - C) an increased ability for the poor to obtain medical services
 - D) a reduced demand for medical services

Answer: D

Diff: 1

Topic: 5.5 Public Spending and Transfer Programs

AACSB: Reflective thinking skills

Question Status: Previous Edition

- 43) The government's policy of reducing payments for physicians' services has generated a relative
- A) increase in the number of physicians in the program.
 - B) reduction in the number of physicians in the program.
 - C) reduction in the demand for medical services.
 - D) increase in the income of the physicians remaining in the program.

Answer: B

Diff: 1

Topic: 5.5 Public Spending and Transfer Programs

AACSB: Reflective thinking skills

Question Status: Previous Edition

- 44) The total amount that the U.S. government spends to support a covered type of health care service under the Medicare system equals
- A) the per-unit subsidy provided to producers of that service times the quantity of the service demanded by consumers at a below-equilibrium out-of-pocket price of the service.
 - B) the per-unit subsidy provided to producers of that service times the equilibrium quantity of the service demanded at the market clearing price that would arise in the absence of Medicare.
 - C) the below-equilibrium, out-of-pocket price that consumers pay for the service times the quantity of the service provided by producers at that out-of-pocket price.
 - D) the below-equilibrium, out-of-pocket price that consumers pay for the service times the quantity of the service demanded by consumers at that out-of-pocket price.

Answer: A

Diff: 2

Topic: 5.5 Public Spending and Transfer Programs

AACSB: Reflective thinking skills

Question Status: Previous Edition

- 45) The amount of government spending on education per public school student has _____ since 1960, and the achievement level of students has generally _____ since that time.
- A) increased; increased
 - B) decreased; decreased
 - C) increased; decreased
 - D) decreased; increased

Answer: C

Diff: 2

Topic: 5.5 Public Spending and Transfer Programs

AACSB: Reflective thinking skills

Question Status: Previous Edition

46) Medicare

- A) subsidizes the care of older people, which gives them NO incentive to consume more medical services.
- B) subsidizes the care of older people, which gives them an incentive to consume more medical services.
- C) subsidizes the care of young people, which gives them an incentive to consume less medical services.
- D) subsidizes the care of middle aged people, which gives them an incentive to consume more medical services.

Answer: B

Diff: 2

Topic: 5.5 Public Spending and Transfer Programs

AACSB: Reflective thinking skills

Question Status: Revised

47) Which of the following is NOT a transfer payment?

- A) Medicare
- B) Social Security retirement payments
- C) Social Security disability payments
- D) spending on national defense

Answer: D

Diff: 1

Topic: 5.5 Public Spending and Transfer Programs

AACSB: Reflective thinking skills

Question Status: Previous Edition

48) Which of the following is heavily subsidized by state and local governments?

- A) Medicare
- B) Social Security
- C) public education
- D) food stamps

Answer: C

Diff: 1

Topic: 5.5 Public Spending and Transfer Programs

AACSB: Reflective thinking skills

Question Status: Previous Edition

49) What happens in public schools when government funds subsidize education?

- A) There is a shortage of schools.
- B) The quality of education rises.
- C) The cost of providing the education is less than what the student pays.
- D) The cost of providing the education is more than what the students pays.

Answer: D

Diff: 2

Topic: 5.5 Public Spending and Transfer Programs

AACSB: Analytic skills

Question Status: Previous Edition

50) If public subsidies for education were eliminated, what would you expect as an outcome in the market for educational services?

- A) More students would enroll in school.
- B) The price students pay to attend school would equal the value of an additional unit of education consumed.
- C) There would be no correlation between the price students pay and the cost of providing the educational services.
- D) The quality of education would deteriorate.

Answer: B

Diff: 2

Topic: 5.5 Public Spending and Transfer Programs

AACSB: Analytic skills

Question Status: Previous Edition

51) Medicare and Social Security are examples of

- A) transfer payment programs.
- B) public goods.
- C) programs that do not respond to rational economic incentives.
- D) the efficient allocation of resources under a free market system.

Answer: A

Diff: 3

Topic: 5.5 Public Spending and Transfer Programs

AACSB:

Question Status: Previous Edition

52) What is one result of the Medicare subsidy?

- A) The health care industry is more efficient than it otherwise would be.
- B) Patients may elect to have some treatments that are of low value to them but that are costly to provide.
- C) The elderly population in the United States receives a lower quality of medical care than what is provided for the elderly population in other countries.
- D) The number of physicians in the United States has declined.

Answer: B

Diff: 3

Topic: 5.5 Public Spending and Transfer Programs

AACSB: Analytic skills

Question Status: Previous Edition

53) Public elementary and high school education in the United States is provided

- A) as a free good.
- B) as a subsidized good.
- C) at the market clearing price.
- D) in an amount less than the equilibrium quantity.

Answer: B

Diff: 1

Topic: 5.5 Public Spending and Transfer Programs

AACSB: Reflective thinking skills

Question Status: Previous Edition

54) Education in the United States is

- A) subsidized mainly by state and local governments.
- B) funded by the federal government only.
- C) paid for by the parents of students in public school system.
- D) paid for by Social Security taxes.

Answer: A

Diff: 1

Topic: 5.5 Public Spending and Transfer Programs

AACSB: Reflective thinking skills

Question Status: Previous Edition

55) According to your text, which of the following represents the largest component of *federal* spending?

- | | |
|--------------|---------------------|
| A) Education | B) Social Security |
| C) Medicare | D) National Defense |

Answer: B

Diff: 1

Topic: 5.5 Public Spending and Transfer Programs

AACSB:

Question Status: Revised

56) Use the concept of supply and demand to explain why an increase in Medicare subsidies can lead to an increase in health care spending by the government.

Answer: Medicare reduces the price that the elderly people have to pay for health services, so that an increase in the subsidy will lead to an increase in the quantity demanded of health services. As a result, the government ends up paying more in total health care spending.

Diff: 2

Topic: 5.5 Public Spending and Transfer Programs

AACSB: Analytic skills

Question Status: Previous Edition

57) Briefly explain why government subsidies are a reason for the declining student performance in public education.

Answer: This is due to the incentive problems of government subsidies in public education. Many public schools may face little or no competition from unsubsidized education providers, and they may provide subsidized services but contribute little to student learning.

Diff: 2

Topic: 5.5 Public Spending and Transfer Programs

AACSB: Reflective thinking skills

Question Status: Previous Edition

5.6 Collective Decision Making: The Theory of Public Choice

- 1) One of the most important characteristics of the price system is that
- A) consumers are the ones who ultimately decide what is produced.
 - B) politicians are the ones who ultimately decide what is produced.
 - C) competition among sellers is reduced.
 - D) all exchanges are regulated by the government.

Answer: A

Diff: 1

Topic: 5.6 Collective Decision Making: The Theory of Public Choice

AACSB: Analytic skills

Question Status: Previous Edition

- 2) When comparing market and public sector decision making, which statement is NOT true?
- A) Self-interest is the motivating force in each decision making arena.
 - B) In both decision making sectors, majority rule is how things are done.
 - C) In both decision making sectors, there are scarcity constraints.
 - D) Collective (political) outcomes and economic outcomes may differ.

Answer: B

Diff: 1

Topic: 5.6 Collective Decision Making: The Theory of Public Choice

AACSB: Analytic skills

Question Status: Previous Edition

- 3) All of the following are assumptions of both market and public-sector decision making EXCEPT:
- A) Decisions are based on majority rule.
 - B) Decisions are motivated by individuals' self-interest.
 - C) Opportunity costs exist in decisions.
 - D) Choices reflect incentives faced by decision makers.

Answer: A

Diff: 1

Topic: 5.6 Collective Decision Making: The Theory of Public Choice

AACSB: Analytic skills

Question Status: Previous Edition

- 4) Which of the following is FALSE about public-sector decision making?
- A) Decisions are based on majority rule.
 - B) The price charged to consumers is often less than its full opportunity cost.
 - C) Decisions involve no opportunity cost.
 - D) Incentives play a role in decision making.

Answer: C

Diff: 1

Topic: 5.6 Collective Decision Making: The Theory of Public Choice

AACSB: Analytic skills

Question Status: Previous Edition

- 5) An important assumption in the theory of public choice is that
- A) individuals will act within the political process to maximize their individual well-being.
 - B) individuals will act within the political process to maximize their collective well-being.
 - C) individuals will only operate outside the political process when their well-being is involved.
 - D) scarcity does not exist in the government sector.

Answer: A

Diff: 1

Topic: 5.6 Collective Decision Making: The Theory of Public Choice

AACSB:

Question Status: Previous Edition

- 6) In which of the following ways is the private market sector similar to the public sector in terms of decision making?
- A) Prices determine the demand for goods and services in each sector.
 - B) There is competition for scarce resource in both sectors.
 - C) Both sectors may use a type of "force" if necessary.
 - D) Votes by individual voters are basically equal in importance with dollars spent by individuals on goods.

Answer: B

Diff: 2

Topic: 5.6 Collective Decision Making: The Theory of Public Choice

AACSB: Analytic skills

Question Status: Previous Edition

- 7) Which of the following characterizes the largest difference between the way decisions are made in the private sector versus the public sector?
- A) The incentive system for individuals to perform efficiently are vastly different.
 - B) The workers themselves are really quite different types of people.
 - C) In both sectors individuals will try to maximize their own individual gains over the gains of others.
 - D) Costs and resources are vastly different in each sector.

Answer: A

Diff: 2

Topic: 5.6 Collective Decision Making: The Theory of Public Choice

AACSB: Analytic skills

Question Status: Previous Edition

- 8) Government goods are provided to the consumer at a zero price. This means that
- A) the cost to society is zero.
 - B) the political system is run by proportional rule.
 - C) people are getting something for nothing.
 - D) the cost of the goods is the value of the resources used to produce the good.

Answer: D

Diff: 1

Topic: 5.6 Collective Decision Making: The Theory of Public Choice

AACSB: Analytic skills

Question Status: Previous Edition

- 9) Which of the following is TRUE about the political and market systems of voting?
- A) The political voting system functions according to proportional rule, while the market voting system functions according to majority rule.
 - B) The political voting system functions according to majority rule, while the market voting system functions according to proportional rule.
 - C) The political voting system functions according to minority rule, while the market voting system functions according to majority rule.
 - D) The political system and the market system are identical.

Answer: B

Diff: 1

Topic: 5.6 Collective Decision Making: The Theory of Public Choice

AACSB: Analytic skills

Question Status: Previous Edition

- 10) What is the assumption underlying public-choice theory?
- A) Elected officials believe in cooperating with one another and they seek to avoid competition among themselves.
 - B) The costs and benefits of being efficient are the same whether one is in the private sector or in the public sector.
 - C) Individuals act within the political process to improve their own individual well-being.
 - D) Resources in the public sector are not scarce.

Answer: C

Diff: 2

Topic: 5.6 Collective Decision Making: The Theory of Public Choice

AACSB:

Question Status: Previous Edition

- 11) The theory of public choice suggests that
- A) government agencies tend to be inefficient because the people running them do not understand the concept of opportunity cost.
 - B) government agencies tend to be inefficient because they are subject to institutional arrangements in which managers do not have an incentive to be efficient.
 - C) the goods provided by government, whether public or private goods, are not scarce.
 - D) you can lower your tax bill if you are careful not to consume too many government resources, regardless of what your neighbors do.

Answer: B

Diff: 2

Topic: 5.6 Collective Decision Making: The Theory of Public Choice

AACSB: Analytic skills

Question Status: Previous Edition

12) A difference between the market and the public sector is that

- A) scarcity exists only in the market sector.
- B) government can use force, while the market does not.
- C) we can only vote in the public sector.
- D) the cost of private goods to society is zero.

Answer: B

Diff: 1

Topic: 5.6 Collective Decision Making: The Theory of Public Choice

AACSB: Analytic skills

Question Status: New

13) The theory of public choice

- A) is the theory of how government decides on what military hardware to purchase.
- B) considers government decision-making efficient.
- C) is the study of collective decision making.
- D) is the study of how negative externalities can be reduced.

Answer: C

Diff: 1

Topic: 5.6 Collective Decision Making: The Theory of Public Choice

AACSB:

Question Status: Previous Edition

14) Scarcity

- A) affects both market and public sector decision making.
- B) affects market, but not public sector decision making.
- C) affects public sector, but not market decision making.
- D) is really not an issue in such a wealthy nation as the United States.

Answer: A

Diff: 2

Topic: 5.6 Collective Decision Making: The Theory of Public Choice

AACSB: Analytic skills

Question Status: Previous Edition

15) The market and public sector are similar in that

- A) there is competition amongst the participants in both sectors.
- B) the resources used in both sectors are scarce.
- C) the participants in both sectors react to incentives.
- D) All of the above are true.

Answer: D

Diff: 1

Topic: 5.6 Collective Decision Making: The Theory of Public Choice

AACSB: Analytic skills

Question Status: Previous Edition

- 16) A difference between the market and the public sector is that
- A) competition exists only in the market sector.
 - B) resources are only scarce for the market sector.
 - C) decision making is by majority rule in the public sector but not in the market sector.
 - D) only the public sector produces private goods.

Answer: C

Diff: 1

Topic: 5.6 Collective Decision Making: The Theory of Public Choice

AACSB: Analytic skills

Question Status: Previous Edition

- 17) The incentive structure is a
- A) system of rewards and punishments that individuals consider when making decisions.
 - B) system determined by the federal government that gives certain states more federal funds.
 - C) system of infrastructure in the United States that improves commerce.
 - D) system of checks and balances in the government.

Answer: A

Diff: 1

Topic: 5.6 Collective Decision Making: The Theory of Public Choice

AACSB:

Question Status: Previous Edition

- 18) If U.S. consumers increase their spending on hybrid cars by 60 percent, and 60 percent more hybrid cars are produced, this is known as the
- A) majority rule.
 - B) proportional rule.
 - C) government rule.
 - D) profit rule.

Answer: B

Diff: 2

Topic: 5.6 Collective Decision Making: The Theory of Public Choice

AACSB: Reflective thinking skills

Question Status: Previous Edition

- 19) Briefly explain the similarities and differences of decision making by the market sector and the public sector.

Answer: The similarities of the two sectors include the presence of opportunity costs, competition by serving individual interests, and an incentive structure. The main differences between decisions by the two sectors are that the public sector often makes decisions on goods at zero price, by use of force, and by a majority voting system instead of "dollar votes."

Diff: 2

Topic: 5.6 Collective Decision Making: The Theory of Public Choice

AACSB: Analytic skills

Question Status: Previous Edition

20) List and explain the four key assumptions in the theory of public choice.

Answer: The key assumptions in the theory of public choice are (1) individuals are motivated by self-interest, which implies individuals will act within the political process to maximize their *individual* (not collective) well-being, (2) opportunity costs exist, which means every government action has an opportunity cost, (3) competition is present, which implies elected representatives will always be in competition for available government funds and (4) individuals in government face an incentive structure, which means if a bureaucrat provides poor representation, the organization's owners — the taxpayers — have no immediate mechanism for expressing their dissatisfaction.

Diff: 1

Topic: 5.6 Collective Decision Making: The Theory of Public Choice

AACSB: Analytic skills

Question Status: Revised

21) What are the voting rules followed by the political system as opposed to the market system?

Answer: In the political system, one person gets one vote, while in the market system, each one dollar that a consumer spends counts separately. The political system is run by majority rule, while the market system is run by proportional rule. In the market system, the spending of dollars indicate intensity of want, while this is not the case in the political system due to its all-or-nothing nature.

Diff: 2

Topic: 5.6 Collective Decision Making: The Theory of Public Choice

AACSB: Analytic skills

Question Status: Previous Edition