

Public Sector Microeconomic Analysis

ECO 2110

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Practice Exam #2

1. A non-categorical (unconditional) grant from a higher level to a lower level government has
 - a. Income and substitution effects
 - b. An income effect only
 - c. A substitution effect only.
 - d. Neither income nor substitution effects.

2. An open-ended matching grant from a higher level to a lower level government has
 - a. Income and substitution effects
 - b. An income effect only
 - c. A substitution effect only.
 - d. Neither income nor substitution effects.

3. The “fungibility” of funds indicates that
 - a. Old money is a good substitute for new money
 - b. Old money is a perfect substitute for new money
 - c. New money is a perfect substitute for old money
 - d. New money is a good substitute for old money.

4. Open-ended matching grants
 - a. will not increase government spending in recipient jurisdictions.
 - b. increase government expenditures in recipient jurisdictions more than nonmatching grants of an equal amount.
 - c. increase government expenditures in recipient jurisdictions less than nonmatching grants of an equal amount.
 - d. increase tax rates in recipient jurisdictions.

5. One reason why the federal government is in the business of giving unconditional grants is
 - a. the existence of revenue-raising imbalances among provinces
 - b. the tax competition among provinces
 - c. answer a. only.
 - d. both answers a. and b.

6. The purpose of a cost-benefit analysis of public projects is to determine the most
 - a. profitable private projects
 - b. welfare-enhancing public projects
 - c. profitable private projects and welfare-enhancing public projects.

7. Transfer payments (\$) between governments, persons and corporations are
 - a. relevant (included) in both the financial analysis and the economic analysis of projects.
 - b. relevant in a financial analysis of projects and irrelevant (excluded) in the economic analysis of projects.
 - c. relevant in an economic analysis of projects and irrelevant in a financial analysis of projects.
 - d. irrelevant in both financial and economic analyses of projects.

8. The existence of positive externalities results in
 - a. a less than optimal level of output.
 - b. a greater than optimal level of output.
 - c. harm to those directly involved.
 - d. harm to those indirectly involved.

9. Parties affected by externalities have an incentive to negotiate as long as
 - a. the surplus is positive regardless of the cost.
 - b. the cost of the negotiation is greater than the surplus that could be gained.
 - c. there is no surplus.
 - d. the cost of the negotiation is equal to the surplus that could be gained.

10. A motorist playing loud music will continue to drive around town, creating noise pollution wherever he goes, as long as
 - a. the cost to him is less than the benefit he derives from it.
 - b. there is an economic benefit to society.
 - c. he or she considers the noise a positive externality.
 - d. there are by-laws against noise pollution.
 - e. there is no cost to the other people in the town.

11. Paternalism occurs when people
 - a. don't care about the consumption of others.
 - b. care about the consumption of others.
 - c. feel that certain commodities should be distributed equally to all consumers.
 - d. are selfish.

12. The marginal external benefit of an inoculation is zero at the current level of annual supply of inoculations against polio. To achieve efficiency, a corrective subsidy must be provided to those being inoculated.
a. True; b. False
13. According to the Coase theorem, corrective taxes are necessary to internalize negative externalities when the transactions costs of exchanging property rights to use resources are zero.
a. True; b. False
14. If the marginal costs of reducing emissions vary among regions, then regulations requiring all regions to reduce their emissions by the same amount will achieve:
a. the efficient amount of pollution abatement.
b. more than the efficient amount of pollution abatement.
c. less than the efficient amount of pollution abatement.
d. more than the efficient amount of pollution abatement in some regions, but less than the efficient amount in other regions.
15. Which of the following is true in a Lindahl equilibrium for cooperative supply of a pure public good?
a. The sum of the tax shares per unit paid by each consumer is equal to the marginal social cost of the public good.
b. The sum of the tax shares per unit paid by each consumer is equal to the marginal social benefit of the good.
c. The sum of the tax shares per unit paid by each consumer is maximized.
d. both (a) and (b).
16. According to the Tiebout model of local government expenditures,
a. all local governments will supply the same kinds and amounts of services.
b. mobile citizens respond to differences in taxes and expenditures by moving to the jurisdiction that maximizes their well-being.
c. the average costs of government services is constant.
d. tax rates do not influence a citizen's choice of residence.
17. According to the Tiebout model of local government expenditures,
a. Externalities arise from local government behaviour.
b. Because of immobility, individuals are unable to join other communities that offer benefits similar to their preferences.
c. A citizen can always find a community offering public benefits that match her preferences.
d. People are ill-informed about the tax-benefit packages available in other communities.
18. If the rich and the poor are completely mobile in the Tiebout model, is it possible that richer communities will attract lower income persons because of the high quality of services in the richer communities.
a. True; b. False.

19. The central economic problem of fiscal federalism is:
- the division of taxing and expenditure functions among different levels of government.
 - the choice of the collective choice rule for central governments only.
 - the level of public goods to be provided by a central government only.
 - how to achieve an equitable distribution of income.
20. Which of the following rationales for income redistribution is Pareto efficient?
- Utilitarianism.
 - The Maximin Criterion.
 - Altruism
 - Plato rule.
21. One of the key assumptions underlying the modern interpretation of utilitarianism is
- Societal income is variable.
 - Marginal utility increases as income (or consumption) increases.
 - All members of a society have different incomes,
 - None of these answers.
22. In a representative democracy, there are
- elected politicians.
 - B) public employees.
 - special interests.
 - all of the above.
23. A person prefers large and small levels of national defense to medium-sized levels of national defense. This person
- is violating the law of transitivity.
 - has single-peaked preferences.
 - has multiple-peaked preferences.
 - can not achieve his or her most-preferred outcome.
24. Externalities require government intervention when
- violence will result between disputing parties.
 - there are only a few sellers in the market.
 - property rights are not clearly established.
 - the government imposes sales taxes.
25. Which method helps in obtaining the socially optimal level of output?
- Pigouvian taxes
 - regulation
 - property rights and bargaining
 - all of the above.
26. Marginal damages are hard to measure because
- they can be generated from multiple sources.
 - they are hard to graph.
 - they happen over time.
 - no one cares about them.

27. Externalities can be positive because
- marginal damages do not last over time.
 - utility can be impacted positively as well as negatively.
 - there is no concept for marginal benefit.
 - positive externalities are subsidies.
28. Reducing output from the privately optimal level to the socially optimal level will
- cause a loss of consumption to consumers.
 - reduce marginal damages.
 - reduce the production costs.
 - cause all of the above.
29. Marginal damages
- must always be considered in social marginal costs.
 - must not be considered in social marginal costs.
 - must sometimes be considered in social marginal costs.
 - have nothing to do with social marginal costs.
30. A tax levied on each unit of pollution is
- a income tax.
 - a emissions fee.
 - a flat tax.
 - an international tax.
31. A cap-and-trade policy
- has a set number of permits.
 - allows polluters to trade permits.
 - caps the total level of pollution allowed.
 - all of the above.
32. Command-and-control regulations
- are less flexible than incentive-based regulations.
 - come from the private sector.
 - have technology standards as a type of control.
 - a & c.
 - a & b.
33. Government growth has been caused by
- citizens who want larger government.
 - lots of public lands available in the West.
 - increases in privatization.
 - inflation.
34. Which of the following is an disadvantage of a decentralized system?
- Single-peaked preferences.
 - Scale economies in tax collection
 - Fostering intergovernmental competition.
 - Kenneth Arrow's Impossibility Theorem

35. Which of the following is an advantage of a decentralized system?
- a. Single-peaked preferences.
 - b. Scale economies in tax collection
 - c. Fostering intergovernmental competition.
 - d. Kenneth Arrow's Impossibility Theorem
36. A Pigouvian subsidy
- a. can not exist with externalities.
 - b. is the same thing as a Pigouvian tax.
 - c. is measured in terms of Pigouvian dollars.
 - d. moves production to the socially optimal level of output.
37. As a general rule, zero pollution is not socially desirable because
- a. there would be no production.
 - b. the Environmental Protection Agency (EPA) needs to have something to do.
 - c. no pollution would lead to global warming.
 - d. all of the above.
38. When each individual has consistent preferences, but those of the community are not consistent, it is known as
- a. agenda manipulation.
 - b. majority rule.
 - c. voting paradox.
 - d. logrolling.

Questions 39 to 46

	<u>Firm A</u>	<u>Firm B</u>	<u>Firm C</u>
Current pollution level (tons)	600	400	500
Marginal abatement cost	\$40	30	35
Tradable permits distributed	400	400	400
Tradable permits bought			
Tradable permits sold			
Permits available after purchases and sales			
Pollution reduction (tons)			
Final pollution level (tons)			

39. If the market price of a pollution permit is \$36, firm A will
- a. buy 200 permits
 - b. buy 100 permit
 - c. sell 100 permits
 - d. sell 200 permits
 - e. None of these answers.
40. If the market price of a pollution permit is \$36, firm B will
- a. buy 200 permits
 - b. buy 100 permit

- c. sell 100 permits
 - d. sell 200 permits
 - e. None of these answers.
41. If the market price of a pollution permit is \$36, firm C will
- a. buy 200 permits
 - b. buy 100 permit
 - c. sell 100 permits
 - d. sell 200 permits
 - e. None of these answers.
42. If the market price of a pollution permit is \$36, firm A's pollution level with pollution permits will be
- a. 600 tonnes
 - b. 400
 - c. 300
 - d. 200
 - e. None of these answers.
43. If the market price of a pollution permit is \$36, firm A's pollution level with pollution permits will be
- a. 600 tonnes
 - b. 400
 - c. 300
 - d. 200
 - e. None of these answers.
44. If the market price of a pollution permit is \$36, firm A's pollution level with pollution permits will be
- a. 600 tonnes
 - b. 400
 - c. 300
 - d. 200
 - e. None of these answers.
45. With pollution permits, the total cost of reducing pollution levels from 1500 to 1200 tonnes will be
- a. \$8,500
 - b. \$9,000
 - c. \$10,000
 - d. \$12,500
 - e. None of these answers.
46. With command and control (i.e., regulation), the total cost of reducing pollution levels from 1500 to 1200 tonnes will be
- a. \$8,500
 - b. \$9,500
 - c. \$10,500
 - d. \$12,500

e. None of these answers.

<u>Questions</u>	<u>Answers</u>
1	B
2	A
3	D
4	B
5	D
6	B
7	B
8	A
9	D
10	A
11	B
12	B
13	B
14	C
15	D
16	B
17	C
18	A
19	A
20	C
21	D
22	D
23	C
24	C
25	D
26	A
27	B
28	D
29	A
30	B
31	D
32	D
33	A
34	B
35	C
36	D
37	A
38	C
39	A
40	C
41	C
42	A
43	C
44	C
45	C
46	D