Sample Multiple-Choice Questions

Circle the letter of each correct answer.

1. Which of the following characterizes a public good?
   (A) People who do not pay for the good can be excluded from using it.
   (B) If one person uses the good, it does not prevent others from using it.
   (C) It is easy to determine who must pay for the good.
   (D) The good is produced by the public sector.
   (E) The good exhibits positive externalities.

2. The free rider problem is associated with
   (A) all market goods.
   (B) goods that are exclusionary.
   (C) bus transportation.
   (D) the production of public goods.
   (E) the production of public transportation.

3. Which of the following best meets the criteria of a public good?
   (A) A phone card
   (B) An airline ticket
   (C) National defense
   (D) A college education
   (E) A restaurant

4. The market system fails to produce public goods because
   (A) there is no need or demand for such goods.
   (B) private firms cannot restrict the benefits of such goods to consumers who are willing to pay for them.
   (C) public enterprises can produce such goods at lower cost than can private enterprises.
   (D) their production seriously distorts the distribution of income.
   (E) a person unwilling to pay can be excluded from the benefits that the product provides.

5. Which of the following are economic functions of government?
   I. Enforcing laws and contracts
   II. Providing public goods
   III. Correcting market failures
   (A) I only
   (B) II only
   (C) III only
   (D) II and III only
   (E) I, II, and III

6. In a market economy, the distribution of income is
   (A) equitable because people who are willing to work earn income.
   (B) primarily determined by the prices of scarce resources people own.
   (C) primarily determined by the government through its power to tax.
   (D) distributed on the basis of need.
   (E) always more equal than in a command economy.
7. If the production of a good creates negative externalities, the private market will produce
(A) too much of the good at too low a price.
(B) too much of the good at too high a price.
(C) too little of the good at too high a price.
(D) too little of the good at too low a price.
(E) the right amount of the good at the correct price.

8. If the production of a good creates positive externalities, the private market will produce
(A) too much of the good at too high a price.
(B) too much of the good at too low a price.
(C) too little of the good at too low a price.
(D) too little of the good at too high a price.
(E) the right amount of the good at the correct price.

Use the supply and demand graph below to answer questions 9, 10 and 11. In the graph, B is the current equilibrium level of output of this product, and A is the optimal level of output from society’s perspective. S is the original supply curve without a tax, and $S_1$ is the new supply curve.

9. This graph indicates that there are
(A) spillover benefits from the production of this product.
(B) spillover costs from the production of this product.
(C) too few resources devoted to the production of the product.
(D) positive externalities from the production of the product.
(E) no spillover costs or benefits associated with the production of the good.

10. One solution to this externality problem is to
(A) give consumers a subsidy of the amount FG.
(B) give producers a subsidy of the amount AB.
(C) tax producers by the amount DE.
(D) tax consumers by the amount EF.
(E) tax consumers by the amount DG.

11. If the government corrects this externality problem with a tax so that all the costs are included in the cost of production, then the product price will be
(A) A.
(B) D.
(C) E.
(D) F.
(E) G.
Use the supply and demand graph below to answer questions 12, 13 and 14. In the graph, A represents the current equilibrium level of output of this product, and B represents the optimal level of output from society’s perspective.

12. This supply and demand graph indicates that there are  
   (A) spillover benefits from the production of this product.  
   (B) spillover costs from the production of this product.  
   (C) too many resources devoted to the production of this product.  
   (D) negative externalities from the production of this product.  
   (E) no spillover costs or benefits to society.

13. Assume the government decides to correct this externality by providing a subsidy to producers. This can be demonstrated as a  
   (A) shift in the demand curve from $D_1$ to D.  
   (B) shift in the supply curve from $S$ to $S_1$.  
   (C) shift in the supply curve from $S_1$ to $S$.  
   (D) shift in both the demand curve from D to $D_1$ and the supply curve from $S_1$ to $S$.  
   (E) shift in both the demand curve from $D_1$ to D and the supply curve from $S$ to $S_1$.

14. The amount of the subsidy to be given to correct this externality problem is  
   (A) AB.  (B) BC.  (C) EF.  
   (D) GH.  (E) AC.

15. Which of the following best summarizes most economists’ position on allocating resources to control pollution?  
   (A) All forms of air and water pollution should be eliminated.  
   (B) Government policies to reduce pollution have zero opportunity costs.  
   (C) Pollution should be reduced to the point where the marginal social cost of pollution control equals the marginal social benefit of pollution control.  
   (D) Pollution should be reduced to the point where the total social cost of pollution control equals the total social benefit of pollution control.  
   (E) Pollution should be reduced to the point where the average social cost of pollution control equals the average social benefit of pollution control.

16. Public-choice theory is based on the idea that  
   (A) self-interest motivates participants only in the private sector of the economy.  
   (B) self-interest motivates participants only in the public sector of the economy.  
   (C) self-interest motivates participants in both the public and private sectors of the economy.  
   (D) the interests of society are the main interest of participants in the public sector of the economy.  
   (E) the interests of society are the main interest of participants in the private sector of the economy.
17. With which of the following statements would advocates of public-choice theory agree?
   I. Government leaders usually consider the public interest over special interests.
   II. Because of the median-voter hypothesis, there is not much difference in the views of candidates running for office.
   III. Most voters are well informed about candidates for office.
   (A) I only
   (B) II only
   (C) III only
   (D) II and III only
   (E) I, II, and III

18. Government may attempt to reduce income inequality by doing which of the following?
   I. Provide transfer payments to the poor
   II. Directly influence market prices, such as establishing a minimum wage
   III. Tax high-income earners at a higher rate than low-income earners
   (A) I only
   (B) II only
   (C) III only
   (D) I and II only
   (E) I, II, and III

19. Which of the following is the best example of a tax based on the ability-to-pay theory of taxation?
   (A) Sales tax
   (B) Property tax
   (C) Excise tax on gasoline
   (D) Federal income tax
   (E) Highway tolls

20. In which of the following taxes is the benefits-received principle of taxation most evident?
   (A) Corporation income tax
   (B) Personal income tax
   (C) Excise tax on gasoline
   (D) Inheritance taxes
   (E) Progressive tax rates

21. Which of the following taxes is considered regressive?
   (A) Sales tax
   (B) Personal income tax
   (C) Corporation income tax
   (D) Federal estate tax
   (E) Inheritance taxes

22. An excise tax will generate the most revenue for government if
   (A) demand is unit elastic.
   (B) demand is elastic.
   (C) demand is inelastic.
   (D) supply is inelastic.
   (E) supply is perfectly elastic.

23. “The President’s proposal to increase the federal tax on gasoline is intended to reduce the amount of gasoline purchased and raise more revenue.” The second goal would be best served (and the first goal least served) if the demand for gasoline were which of the following?
   (A) Unit elastic
   (B) Relatively elastic
   (C) Relatively inelastic
   (D) Perfectly inelastic
   (E) Decreased by the tax
24. A motel owner is upset that the scenic view provided by the neighboring wooded property will be destroyed because the property’s owner plans to cut and sell the trees to a commercial lumber company. The Coase Theorem suggests that this dispute could be resolved by
   (A) a law passed by the government.
   (B) a zoning ordinance against commercial lumbering.
   (C) the owners themselves.
   (D) a government fine for cutting trees.
   (E) an environmental campaign against altering wildlife habitat.

25. If the government increases the amount of government insurance on bank deposits, this action would
   (A) increase the probability of adverse selection.
   (B) lessen the probability of adverse selection.
   (C) increase the probability of a moral-hazard problem.
   (D) lessen the probability of a moral hazard problem.
   (E) eliminate the probability of adverse selection or moral hazard.