

Write your name on the cover of the test booklet and nowhere else. Enclose this sheet with the booklet. Failure to follow these directions will cost you 1 point. The test has 100 points (to be scaled up to 160 points) and is scheduled to take 50 minutes. Therefore, expect to spend 1 minute for every 2 points. For example, a 10-point question should take 5 minutes. I cannot give extra time because of the class which follows yours.

1) (10 points) Answer EITHER Part A OR Part B.

A) Draw the Laffer Curve and explain why it takes that shape.

B) How can increasing a tax rate result in less revenue?

2) (12 points) For EITHER public goods OR inequitable distribution of wealth, define it. Then Explain why it is an ECONOMIC reason for government intervention.

3) (12 points) Answer EITHER Part A OR Part B.

A) If the inflation rate is expected to be 5% and turns out to be 3%, then what two groups of people gain? Explain how you know they gain.

B) Obviously, high unemployment causes less production, less income, less government tax revenue, and more government payments. What are two other problems caused by high unemployment? Explain how high unemployment causes them.

4) (14 points) Using the table to the right to calculate the marginal tax rate, total taxes paid, and the average tax rate if your taxable income was \$60,000. Show all work and BRIEFLY explain how you got the answers.

Income	Tax Rate
0 - 10,000	10%
10,001 - 50,000	20%
50,001 - 90,000	30%
> 90,000	40%

5) (16 points) Both the inflation rate and the unemployment rate have problems. There are difficulties in calculating them that cause the data to be misleading. For EITHER inflation OR unemployment rate, explain TWO problems which may cause them to be misleading.

6) (18 points) State the problem facing Social Security. For EITHER the “solution” in Part A OR the “solution” in Part B, explain how that proposal will reduce the problem with Social Security. Would you use it? Why or why not?

A) Eliminate the cap on salaries.

B) Raise the retirement age.

7) (18 points) Answer EITHER Part A OR Part B.

A) Draw a supply and demand diagram for a product facing a relatively flat, downward sloping demand curve, and a relatively steep supply curve. Add a tax and determine who pays most of the tax. Explain why the curve(s) moved as drawn and how you determined the tax incidence.

B) Draw a supply and demand diagram for a product which causes a positive externality. Prove that the amount of the good produced is not optimal from society’s point of view. Explain your logic. (There is no need to explain how you would solve the problem.)