

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 12-point question should take 6 minutes. I cannot give extra time because some students have a class after your class.

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

A) When you buy a used car, why isn't it counted as investment when calculating GDP? Why is the car dealer's profits part of GDP?

B) When we calculate NI from NDP, we add or subtract a few items. What are TWO of those items? Why do we add or subtract them?

2) (12 points) For EITHER public goods OR providing a legal system, explain why it is an economic reason for government.

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

A) Use the table to the right to find the marginal tax rate, the total taxes paid, and the average tax rate for a person earning \$100,000. Show all work and if there is no work, then explain how you came up with your answer.

B) How can raising the tax rate result in less tax revenue?

Explain the economic reason and give a numerical example of an excise tax on hats.

Income	Tax rate
\$0 - \$30,000	10%
\$30,000 - \$90,000	20%
\$90,000 - \$150,000	30%
>\$150,000	40%

4) (14 points) Answer EITHER Part A OR Part B.

A) If the inflation rate is correctly anticipated, then what are the two costs caused by high inflation? Explain how high inflation causes them

B) We use the inflation rate to measure the increase in prices. There are several problems with doing this calculation. Explain two of them.

5) (16 points) Answer EITHER Part A OR Part B.

A) Suppose the expected inflation at the start of the year was 15%. The price level at the start of the year was 400. At the end of the year the price level was 440. How much was the inflation rate? Show all work. Who was hurt by this inflation? Explain your logic mentioning two types of people in your explanation.

B) Suppose an economy had 500 people of working age. 270 people have jobs. 30 people do not have jobs and are looking for a job. 20 people do not have jobs, but have quit looking for a job. The remaining 180 people are not employed and are not looking for a job because they are a stay-at-home parent. Calculate the labor force participation rate and the unemployment rate. Show all work and briefly explain why you chose the numbers you used.

6) (18 points) For EITHER negative externalities OR positive externalities. Define them and give an example. Use a supply and demand to prove the market will not produce the socially optimal quantity of the product in your example. Explain how economists feel the problem should be fixed **without drawing** the solution on the graph. Explain why that solution works.

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

A) What is the problem facing Social Security? How would reducing the Social Security benefits reduce the problem? Would you reduce the Social Security benefits if you were in Congress? Why or why not?

B) What is the problem facing Social Security? How would raising the cap on taxable income reduce the problem? Would you raise the cap on income subject to the Social Security tax if you were in Congress? Why or why not?