Public Finance - Sample Exam 2018

IES CUNI, SS 2018

Name:

Instructions:

- You have 80 minutes to finish the test.

- You can obtain up to 60 points from this exam. Points awarded for each exercise are given in parentheses.

- In Part 1 (multiple choice questions), only one answer is correct.

- In Part 2 (true or false), when the statement is false, always explain why.

- In Part 3, answer the questions briefly, but precisely—a long answer does not imply a high score, a precise one does. When asked to draw a diagram, always draw a diagram and label the axes.

Part 1 - Multiple choice questions (3 points each, 15 in total)

1. Which of the following welfare functions is called Rawlsian?

    a) $W = \sum_{i=1}^{N} U_i$

    b) $W = \frac{1}{N} \sum_{i=1}^{N} U_i$

    c) $W = \min\{U_i\}$

    d) $W = \prod_{i=1}^{N} U_i$

2. Which of the following cannot be considered a pure public good?

    a) national defense

    b) clean air

    c) parking spaces

    d) a lighthouse

3. A pecuniary externality occurs when the actions of an economic actor:

   a) cause a positive effect on other economic actors.

   b) produce pollution.

   c) have a direct negative effect on other economic actors.

   d) cause a change in market prices.

4. The majority voting equilibrium exists if:

   a) there is a cyclical pattern in the voting system

   b) there are only single-peaked preferences

   c) the transitivity condition holds

   d) the median voter has the same preferences as the mean voter

5. The issue that people behave differently when they handle public funds than when they handle their private funds can be best described by the term:

   a) the principal-agent problem

   b) the intensive vs. extensive margin problem

   c) the scope insensitivity problem

   d) the free-rider problem

Part 2 - True or false? (2 points each, 10 in total)

For the following statements, decide whether they are true (T) or false (F). When (and only when) they are false, explain why. Answers without a correct explanation will not receive any points.

1. The lump sum tax maximizes the deadweight loss.

   T / F

2. In the Czech Republic, property taxes are collected fully by the central government and then redistributed to the local governments.

   T / F

3. A utilitarian social planner with full information will not be completely egalitarian.

   T / F

4. The Coase theorem postulates that even if there are well-defined property rights and costless bargaining, the problem of externalities cannot be solved by the market agents themselves.

   T / F

5. The excise tax is a tax levied on the earnings of corporations.

   T / F

Part 3 - Open ended questions (5 points each, 25 in total)

1. Use your own words and a real-world example to explain the problem of *dependency on question wording* in contingent valuation surveys. List and briefly explain at least two other problems commonly encountered in contingent valuation surveys.

2. What are Pigouvian taxes? State and explain a real-world example of a problem that could be solved using Pigouvian taxes. Why are optimal Pigouvian taxes sometimes hard to calculate?

3. What are the main reasons why economists think that decentralization of power may be beneficial to society? What could local governments do better than central governments? On the other hand, at what could the local governments be worse than central governments?

4. Briefly explain the problem of moral hazard in the insurance market. What effect does moral hazard likely have on the price of private insurance?

5. Describe the concept of specific egalitarianism. According to your opinion, should this concept be used in practice? For what type of goods or services? Why, or why not?