

AP Microeconomics Unit 6 - Market Failure and the Role of Government Practice Test

Question 1

The Ministry of Economics has determined that the production of firebolts creates pollution that costs society \$120 per firebolt to clean up. The private benefit of producing firebolts is \$80, and each firebolt can be purchased for \$80. Currently, 100 firebolts are being produced.

If these policymakers want to eliminate the market inefficiency created by the production of firebolts, which of the following should they do?

- A. prohibit the sale of firebolts
- B. increase firebolt production
- C. subsidize the production of firebolts
- D. prohibit the production of firebolts
- E. use cost-benefit analysis to evaluate different policies

Question 2

Which of the following must be true to maximize economic surplus in a market?

- A. All social costs and benefits are internalized by agents in the market.
- B. Marginal private cost equals marginal private benefit.
- C. All goods must be public goods.
- D. Quantity supplied equals quantity demanded.
- E. All goods must be common resources.

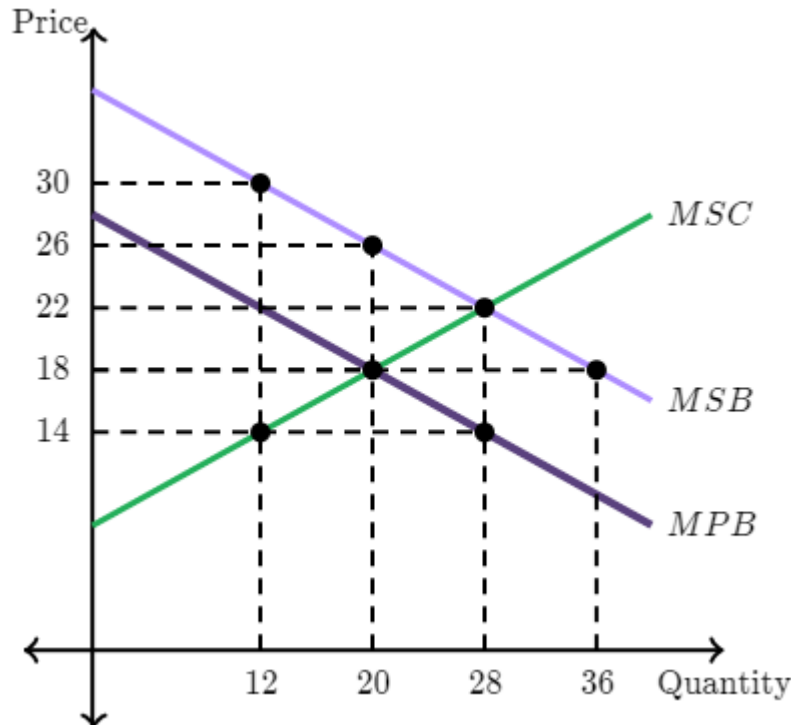
Question 3

Which of the following best describes when an agent manipulates an environment to achieve market power that serves no productive purpose?

- A. utility maximization
- B. profit-maximization
- C. rent-seeking
- D. benevolent dictatorship
- E. anchoring

Question 4

This graph shows the market for flazzles, including the marginal social benefit (MSB), marginal social cost (MSC), and marginal private benefit (MPB).



What is the socially optimal quantity, and what is the quantity that exists in equilibrium without regulation?

- A. Socially optimal: $Q = 28$; Without regulation: $Q = 28$
- B. Socially optimal: $Q = 20$; Without regulation: $Q = 12$
- C. Socially optimal: $Q = 28$; Without regulation: $Q = 12$
- D. Socially optimal: $Q = 28$; Without regulation: $Q = 20$
- E. Socially optimal: $Q = 20$; Without regulation: $Q = 36$

Question 5

Which of the following best describes where total surplus is maximized when an externality exists in a market?

- A. The quantity where marginal social cost equals marginal private benefit.
- B. The quantity where marginal social benefit equals marginal private cost.
- C. The quantity where marginal social cost is higher than marginal private cost
- D. The quantity where marginal social benefit is higher than marginal private benefit
- E. The quantity where marginal social cost equals marginal social benefit.

Question 6

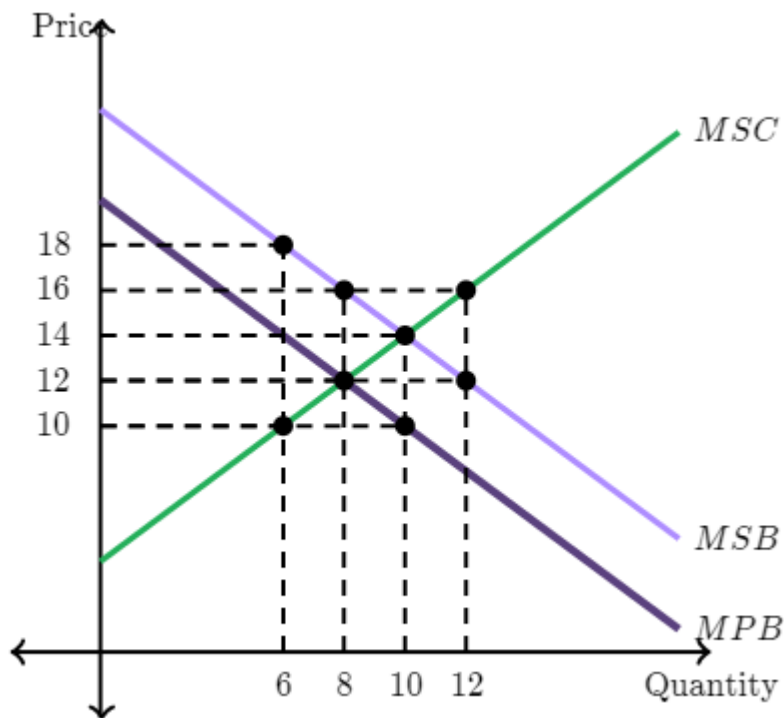
The production of good B creates negative externalities, but there are no externalities in the consumption of good B.

What must be true at the market equilibrium for good B if the market is not regulated?

- A. Marginal private cost is greater than marginal social cost
- B. Marginal social benefit is less than marginal social cost
- C. Marginal social cost equals marginal social benefit.
- D. Marginal social benefit is greater than marginal private benefit
- E. Marginal social cost is less than marginal private benefit

Question 7

This graph shows the marginal social cost (MSC), marginal private benefit (MPB), and the marginal social benefit (MSB) associated with the market for snizzles.



If the government wants to intervene in this market, which of the following policies most likely leads to the optimal quantity being sold in this market?

- A. A price ceiling of \$16
- B. A per-unit subsidy of \$4 per unit.
- C. A price floor of \$10
- D. A per-unit tax of \$4 per unit.
- E. A price floor of \$14

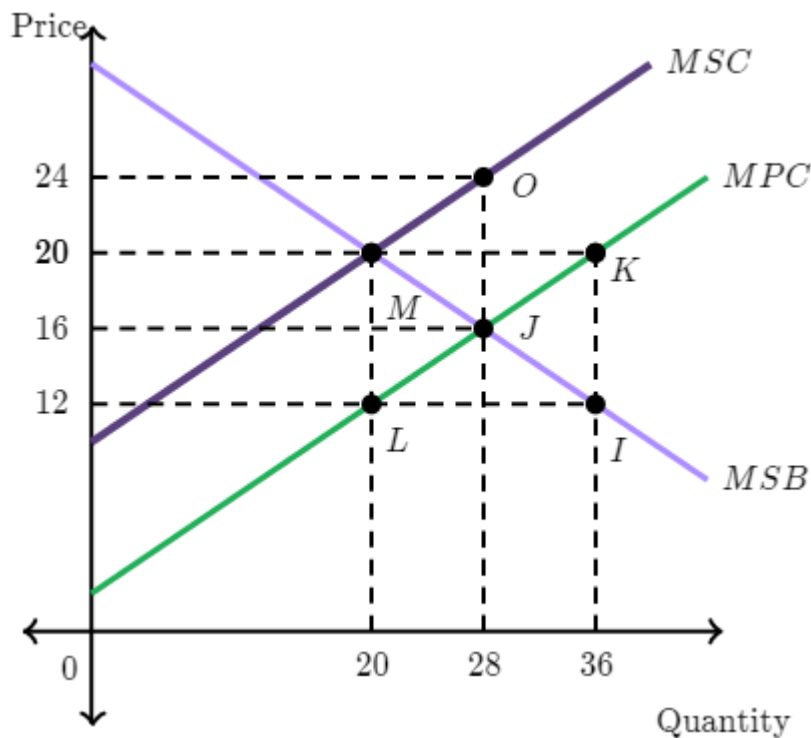
Question 8

Which of the following best describes why lump-sum taxes on producers don't eliminate deadweight loss in the short run in a market with a negative externality?

- A. They don't alter marginal cost.
- B. They don't reduce a firm's profit.
- C. They change a firm's choice of output.
- D. They alter the demand for the good.
- E. They are too difficult to impose.

Question 9

The marginal social cost (MSC), marginal private cost (MPC), and marginal social benefit (MSB) associated with the production of a good are shown in this graph.



What is the socially optimal price and quantity in this market?

- A. $P = \$16, Q = 28$
- B. $P = \$20, Q = 36$
- C. $P = \$12, Q = 20$
- D. $P = \$20, Q = 20$
- E. $P = \$28, Q = 24$

Question 10

Because no private provider was willing to do so, the city of Montrose has decided to provide emergency room services free of charge. However, a doctor can only see one patient at a time.

What kind of good is the emergency room service in Montrose?

- A. private good
- B. artificially scarce
- C. common resource
- D. oligopoly
- E. public good

Question 11

What kinds of goods are excludable?

- A. Only public goods
- B. Private goods and artificially scarce goods
- C. Only private goods
- D. Common resources and public goods
- E. Public goods and private goods

Question 12

Which of the following best defines the free rider problem?

- A. When goods are nonexcludable, people have no incentive to pay for their production
- B. When production of a good creates costs that are not considered by producers
- C. When consumption of a good creates benefits that are not considered by consumers
- D. When goods are non-rival, they tend to be overconsumed
- E. When the political or social environment is changed to extract more profit without contributing any additional benefit

Question 13

Which of the following government policies would address the problem of overuse of a common resource?

- A. remove property rights to the resource
- B. create a licensing system to limit access
- C. subsidize the resource
- D. make it non-rival in consumption
- E. allow free access to anyone who wants to use it

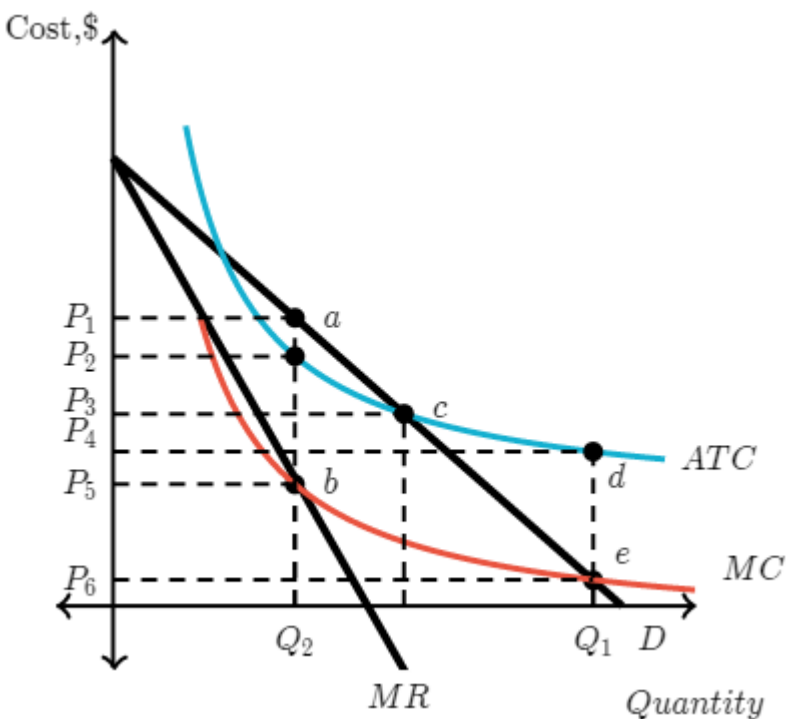
Question 14

Which of the following policy interventions will theoretically reduce the deadweight loss generated by a monopoly?

- A. a per-unit tax on the monopolist
- B. a binding price floor on the monopolist
- C. a lump-sum subsidy to the monopolist
- D. a lump-sum tax on the monopolist
- E. a per-unit subsidy to the monopolist

Question 15

This graph shows the average total cost (ATC), marginal cost (MC), demand (D), and marginal revenue (MR) for a natural monopoly.



What is necessary for this firm to be willing to produce the allocatively efficient quantity?

- A. No intervention is necessary.
- B. a price floor of P_1 and a lump-sum tax of P_1abP_5
- C. There is no allocatively efficient quantity for this firm.
- D. a regulated price of P_3

E. a price ceiling of P_6 and a lump-sum subsidy of P_4deP_6

Question 16

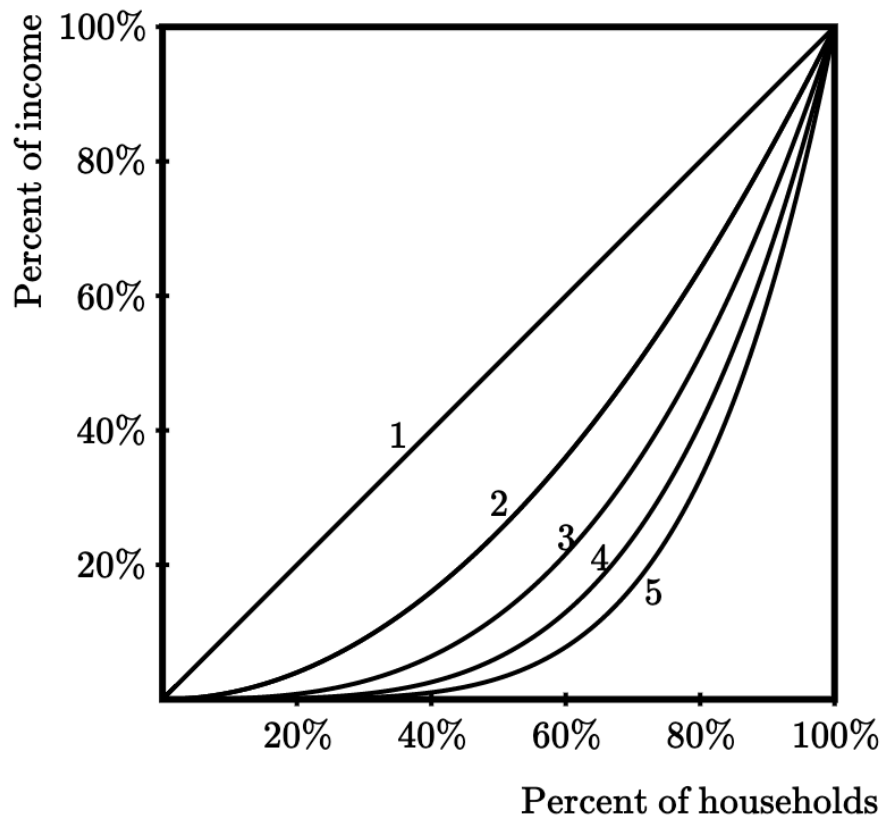
The government of Hamsterville implements a series of laws as a form of antitrust policy.

What is the government most likely trying to do?

- A. limit the ability of firms to create or protect monopoly power
- B. reduce the double counting of output in calculating national income
- C. limit the provision of public goods
- D. reduce income inequality between groups
- E. increase economies of scale

Question 17

This graph shows the Lorenz curves for five countries.



Which country has the least income inequality?

- A. Country 5

- B. Country 1
- C. Country 2
- D. Country 4
- E. Country 3

Question 18

What happens to the Gini coefficient and the Lorenz curve if an economy implements a progressive tax structure?

- A. The Gini coefficient decreases, the Lorenz curve moves farther away from the line of equality.
- B. The Gini coefficient decreases; the Lorenz curve is unaffected
- C. The Gini coefficient increases, the Lorenz curve moves farther away from the line of equality.
- D. The Gini coefficient is unaffected, the Lorenz curve moves closer to the line of equality.
- E. The Gini coefficient decreases; the Lorenz curve moves closer to the line of equality.

Question 19

What does it mean if a country has a Gini coefficient of 0?

- A. everyone has the same income
- B. one person earns all income
- C. everyone has the same wealth
- D. one person holds all wealth
- E. the economy is growing

Answer Key

1. E
2. A
3. C
4. D
5. E
6. B
7. B
8. A
9. D
10. C
11. B
12. A
13. B
14. E
15. E
16. A
17. B
18. E
19. A