

Common Sense Economics

Part III: Economic Progress and the Role of Government

Practice Test

1. A government fulfills a protective function when it
 - a. taxes some citizens in order to provide income transfers to others.
 - b. provides funds for flood control projects and builds highways.
 - c. prevents illegal seizure of private property.
 - d. established and enforces minimum wage laws.

2. Which of the following is the best example of a public good?
 - a. an amusement park like Disney World
 - b. a civic center owned and operated by the government
 - c. a state university
 - d. a regional flood control project

3. Which of the following is true?
 - a. If we want to get the most from our resources, the pricing of goods and allocation of investment should be decided by majority voting.
 - b. In a representative democracy, majority voting will assure that approved projects are productive.
 - c. There are good reasons to expect that majority voting will sometimes result in the approval of projects that are inefficient.
 - d. Private firms can force their customers to pay for products they produce, but the government cannot do so.

4. Which of the following is true?
 - a. Voters have a strong incentive to make well-informed choices when voting in state and federal elections.
 - b. The rational ignorance effect indicates that voters have very little incentive to be well informed when making political choices.
 - c. Political action is based on voluntary exchange and mutual agreement.
 - d. Policies favored by a majority will assure that resources are allocated efficiently.

5. When the government becomes more heavily involved in imposing regulations and taxes on some in order to provide favors to others
 - a. resources will move away from productive projects and toward counterproductive favor seeking activities.
 - b. the efficiency of resource use will improve.
 - c. per capita income levels will grow rapidly.
 - d. subsidies and targeted tax breaks favoring special interest groups will decline.

6. Measured in terms of the reduction in private sector output, what is the cost of taxing a dollar away from the private sector and transferring it to the government?
 - a. one dollar
 - b. less than one dollar, because the administration of and compliance with the tax laws creates jobs for people
 - c. less than a dollar, because of the excess burden resulting from the elimination of productive exchanges by the taxes
 - d. more than a dollar, because collection of the taxes requires resources that would otherwise be available for private sector production

7. Special-interest programs are highly attractive to vote-seeking politicians because
 - a. these programs are highly efficient and therefore they tend to enhance the general welfare of the populace.
 - b. members of special-interest groups favoring these programs are less likely to vote than the taxpayers who pay for them.
 - c. low-income recipients are the primary beneficiaries of special-interest programs.
 - d. members of special-interest groups favoring these programs feel strongly about them while most other voters will be uninformed on the issue.

8. Under a democratic representative government, legislators will have a strong incentive to support the positions of well-organized special-interest groups because
 - a. these positions will be efficient – they will generate more benefits than costs.
 - b. these position will be favored by the majority of voters.
 - c. the special-interest voters are likely to be uninformed, while others will feel strongly about an issue.
 - d. the special-interest voters will feel strongly about an issue, while others are likely to be uninformed.

9. Which of the following best explains why legislators often find debt financing more attractive than taxation?
 - a. The current cost of debt financing is less visible than taxation.
 - b. Debt financing exposes the current costs of government programs; taxes do not.
 - c. Debt financing reduces the attractiveness of special-interest spending.
 - d. Taxation allows politicians to supply voters with immediate benefits without having to impose a visible current cost.

10. Politicians have incentive to support special-interest groups at the expense of unorganized, widely dispersed groups (for example, taxpayers or consumers)
 - a. only when the benefits that accrue to the special-interest group exceed the costs imposed on others.
 - b. when nonspecial-interest voters are unconcerned or uninformed about the issue, and campaign funds are readily available from the special-interest group.
 - c. only if the government action is efficient.
 - d. only if the government action reduces the size of the budget deficit.

11. Which of the following explains why pork-barrel spending is often approved, even when the spending is inefficient?
 - a. Each representative has little incentive to oppose pork-barrel spending since the tax savings would accrue to taxpayers throughout the nation.
 - b. General opposition to pork-barrel spending by a legislator would make it more difficult for the legislator to arrange for pork-barrel projects that provide concentrated benefits for his or her district.
 - c. Logrolling increases the likelihood that pork-barrel projects will be approved.
 - d. All of the above are correct.

12. The difference between the national debt and a federal budget deficit is
 - a. nothing; the national debt and the budget deficit are the same thing.
 - b. the national debt is financed primarily through government bonds, while the deficit is financed through taxes.
 - c. the federal budget deficit represents the total amount of outstanding government debt while the national debt includes only the increase in the debt during the current year.
 - d. the national debt represents the cumulative effect of all previous budget deficits and surpluses, while the federal budget deficit reflects only the additions to the debt during the current year.

13. Transfer payments are
 - a. payments made to individuals who are employed by the government.
 - b. payments made to individuals who provide goods and services to the government.
 - c. transfers of income from taxpayers to recipients who do not provide related services for the payments.
 - d. omitted from the government expenditure figures.

14. The effectiveness of government antipoverty programs is reduced because they
 - a. crowd out private/charitable efforts by families, individuals, churches and charitable organizations.
 - b. encourage young people to stay in school and postpone having children.
 - c. provide strong incentives for the poor to advance their education and secure full-time jobs.
 - d. provide individuals with strong incentives to earn, learn and invest.

15. The increase in transfer payments initiated by the War on Poverty during the latter half of the 1960s resulted in
 - a. a steady reduction in the poverty rate throughout the next two decades.
 - b. a more equal distribution of income.
 - c. fewer single-parent families because a married couple receives benefits twice as large as a single-parent family.
 - d. little change in the official poverty rate in the decades that followed.

16. Which of the following will increase the likelihood a person will experience periods of poverty?
- completing high school rather than dropping out
 - getting married before having a child
 - having a child as a teenage single parent
 - maintaining full-time employment
17. Central planning is an ineffective method to organize an economy because
- most central planners are less intelligent than business entrepreneurs in market economies.
 - central planners cannot possibly obtain all the information necessary to allocate resources efficiently.
 - central planners do not respond predictably to incentives.
 - central planners have inadequate funding to meet the needs of their constituents.
18. Which of the following will reduce the effectiveness of centralized economic planning?
- The central planners will be unable to maintain sufficient information for a sound economic plan in a world of dynamic change.
 - The central planners spending the funds of taxpayers will make poorer investment choices than investors spending their own money.
 - The choices of the central planners will be influenced by political, rather than economic, considerations.
 - All of the above.
19. From the viewpoint of economic efficiency, does representative democracy do a good job of handling special-interest issues?
- Yes, special-interest groups are unable to benefit from government action unless they can convince the majority of voters that their position is sound.
 - No, legislators can often derive political gain from the support of special-interest projects that are inefficient.
 - Yes, the power of special interests is curtailed when decisions are made legislatively.
 - No, actions favored by well-organized special-interest groups are often rejected even when they would promote economic progress.
20. When decentralized governmental units operate independently and compete with each other, governments will attract residents and expand their tax base when
- they increase their tax rates.
 - they provide residents with fewer government services.
 - they provide residents with desired services at an attractive tax cost.
 - they discontinue desired government services in order to keep taxes low.

21. The U.S. constitution prohibits government from imposing tariffs and quotas that restrict _____. The authors of Common Sense Economics would also apply this prohibition to _____. (Fill in the blanks)
- a. exports; imports
 - b. imports; exports
 - c. budget deficits; budget surpluses
 - d. budget surpluses; budget deficits
22. If a three-fourths majority of both houses of the U.S. Congress was required for approval of a spending project, economic analysis indicates that
- a. federal spending would increase sharply from the current level.
 - b. the political power of special-interest groups would increase.
 - c. inefficient government spending programs would expand.
 - d. the power of special interests would be curtailed and federal spending reduced.
23. A special-interest issue generates substantial personal benefits
- a. for all voters.
 - b. for the majority of voters.
 - c. for the vast overwhelming number of voters, but small personal costs are imposed on a small minority of voters.
 - d. for a small minority of voters, but small personal costs are imposed on the vast overwhelming number of voters.
24. The political structure that is most consistent with economic growth and progress is
- a. rule by the majority.
 - b. a dictatorship.
 - c. limited government, protection of individuals from aggression by others, and decentralized political decision-making.
 - d. centralization of power in the hands of an elected legislature and a president or prime minister.
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ANSWER KEY 1 THROUGH 24

1. (c), 2. (d), 3. (c), 4. (b), 5. (a), 6. (d), 7. (d), 8. (d), 9. (a), 10. (b), 11. (d), 12. (d)
13. (c), 14. (a), 15. (d), 16. (c), 17. (b), 18. (d), 19. (b), 20. (c), 21. (a), 22. (d)
23. (d), 24. (c)