AS/ECON 4070 3.0AF   Midterm Exam   Wednesday October 25 2006

time $=$ 50 minutes

Do **all 3** questions. All questions count equally.

1. What would be the incidence of a \$7 per unit excise tax on a product which is provided in a perfectly competitive market, for which the demand curve has the equation

$$Q^D = 120 - 5P^D$$

and for which the supply curve had the equation

$$Q_s = 2p_s - 20$$

where P^D is the price paid by demanders, p_s is the price received by suppliers, Q^D is the quantity demanded and Q_s is the quantity supplied?

2. What would be the incidence of a tax levied on all revenue earned by firms in the service sector in Canada? State as precisely as possible the assumptions that you are making.

continued over

3. The picture above shows the effects of a $1 tax on clothing, when the price of food is $1, and when the net–of–tax price of clothing is $1. Point A, at $(900, 900)$ is the consumption bundle which the person would choose if there were no tax. Point B at $(1600, 400)$ is on the same indifference curve as A, but is located where the slope of the indifference curve is $-1/2$.

State, as precisely as possible : (a) the person's compensated elasticity of demand for clothing ; (b) the compensating variation to the tax ; (c) the revenue the tax would collect if the person were compensated for the damage done by the tax; (d) the excess burden of the tax.

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end

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