

File: Chapter 001 Thinking Like an Economist

Multiple Choice Questions

1. Economics is best defined as the study of:

- A. inflation, interest rates and the stock market.
- B. supply and demand.
- C. how people make choices in the face of scarcity and the implications of those choices for society as a whole.
- D. the financial concerns of businesses and individuals.

Ans: C

Difficulty: 01 Easy

Learning Objective: 01-01

Topic: Economics: Studying Choice in a World of Scarcity

Blooms: Remember

AACSB: Reflective Thinking

Feedback: Economics is the study of how people make choices under conditions of scarcity and the implications of those choices for society as a whole.

2. Economics is the study of:

- A. the financial concerns of businesses and individuals.
- B. the role of government in limiting the choices people make.
- C. choice in the face of limited resources.
- D. whether we will have enough resources in the future.

Ans: C

Difficulty: 01 Easy

Learning Objective: 01-01

Topic: Economics: Studying Choice in a World of Scarcity

Blooms: Remember

AACSB: Reflective Thinking

Feedback: Economics is the study of how people make choices under conditions of scarcity and the implications of those choices for society as a whole.

3. Economists recognize that because people have limited resources:

- A. government intervention is necessary.
- B. they have to make trade-offs.
- C. they will never be happy.
- D. our future is bleak.

Ans: B

Difficulty: 01 Easy

Learning Objective: 01-01

Topic: Economics: Studying Choice in a World of Scarcity

Blooms: Remember

AACSB: Reflective Thinking

Feedback: Economists recognize that the resources available to us are limited, so having more of one good thing means having less of another.

5. An implication of scarcity is that:
- A. people will never be happy.
 - B. making trade-offs becomes unnecessary as wealth increases.
 - C. some people will always be poor.
 - D. people must make trade-offs.

Ans: D

Difficulty: 01 Easy

Learning Objective: 01-01

Topic: Economics: Studying Choice in a World of Scarcity

Blooms: Remember

AACSB: Reflective Thinking

Feedback: Although we have boundless needs and wants, the resources available to us are limited. So having more of one thing means having less of another.

6. If all the world's resources were to magically increase one hundredfold, then:
- A. people would still have to make trade-offs.
 - B. economics would no longer be relevant.
 - C. scarcity would disappear.
 - D. trade-offs would become unnecessary.

Ans: A

Difficulty: 02 Medium

Learning Objective: 01-01

Topic: Economics: Studying Choice in a World of Scarcity

Blooms: Understand

AACSB: Reflective Thinking

Feedback: Economists assume that resources will always be scarce relative to people's wants.

8. Forest lives in complete isolation in Montana. He is self-sufficient and feeds himself through hunting, fishing, and farming. Which of the following statements about Forest is true?
- A. Forest has unlimited resources.
 - B. Forest is not required to make trade-offs because he is self-sufficient.
 - C. Forest has to make trade-offs.
 - D. Forest doesn't have to consider costs and benefits.

Ans: C

Difficulty: 01 Easy

Learning Objective: 01-01

Topic: Economics: Studying Choice in a World of Scarcity

Blooms: Understand

AACSB: Reflective Thinking

Feedback: Even if Forest is self-sufficient, he still has limited resources and unlimited wants. For example, he might want to have more than 24 hours in a day. Thus, he still has to make trade-offs.

10. Chris has a one-hour break between classes every Wednesday. Chris can either stay at the

library and study or go to the gym and work out. The decision Chris must make is:

A. not an economic problem because neither activity costs money.

B. not an economic problem because it's an hour that Chris has no matter what he does.

C. an economic problem because the tuition Chris pays covers the cost of both the gym and the library.

D. an economic problem because Chris has only one hour, and engaging in one activity means giving up the other.

Ans: D

Difficulty: 02 Medium

Learning Objective: 01-01

Topic: Economics: Studying Choice in a World of Scarcity

Blooms: Understand

AACSB: Reflective Thinking

Feedback: Chris has to make a trade-off: if Chris goes to the gym, Chris cannot also study and vice versa.

12. Whether studying the output of the U.S. economy or how many classes a student will take, a unifying concept is that:

A. wants are limited and resources are unlimited, so trade-offs are unnecessary.

B. wants are unlimited and resources are scarce, so trade-offs have to be made.

C. wants are limited and resources are unlimited, so trade-offs have to be made.

D. both wants and resources are unlimited.

Ans: B

Difficulty: 02 Medium

Learning Objective: 01-01

Topic: Economics: Studying Choice in a World of Scarcity

Blooms: Understand

AACSB: Reflective Thinking

Feedback: Although we have boundless needs and wants, the resources available to us are limited. So having more of one thing means having less of another.

13. The Cost-Benefit Principle indicates that an action should be taken if, and only if:

A. its benefits are positive.

B. its costs are small.

C. its benefits are a result of its costs.

D. its benefits exceed its costs.

Ans: D

Difficulty: 01 Easy

Learning Objective: 01-02

Topic: Economics: Applying the Cost-Benefit Principle

Blooms: Remember

AACSB: Reflective Thinking

Feedback: The Cost-Benefit Principle states that an action should be taken if, and only if, its benefits exceed its costs.

15. According to the Cost-Benefit Principle, you should spend an additional hour studying for an exam if, and only if,:

- A. the benefits of studying for an additional hour are really high.
- B. the benefits of studying for an additional hour exceed the costs of studying for an additional hour.
- C. the benefits of studying for an additional hour are higher for you than for anyone else in your class.
- D. you have time to study for an additional hour.

Ans: B

Difficulty: 02 Medium

Learning Objective: 01-02

Topic: Economics: Applying the Cost-Benefit Principle

Blooms: Understand

AACSB: Reflective Thinking

Feedback: The Cost-Benefit Principle states that an action should be taken if, and only if, its benefits exceed its costs.

17. According to the Cost-Benefit Principle, you should go see the latest Star Wars movie with your friends this week-end if:

- A. the benefits of seeing the movie are greater than the costs of seeing the movie.
- B. you really like Star Wars.
- C. you can afford to go to the movies.
- D. you have a free ticket.

Ans: A

Difficulty: 01 Easy

Learning Objective: 01-02

Topic: Applying the Cost-Benefit Principle

Blooms: Remember

AACSB: Reflective Thinking

Feedback: The Cost-Benefit Principle tells us that we should make choices by weighing the benefits of an action against its costs.

18. A rational person is someone:

- A. who does not have well-defined goals.
- B. with well-defined goals who tries to fulfill those goals as best as he or she can.
- C. who doesn't worry about costs and benefits.
- D. who only considers the financial benefits and financial costs of making a choice.

Ans: B

Difficulty: 01 Easy

Learning Objective: 01-02

Topic: Applying the Cost-Benefit Principle

Blooms: Remember

AACSB: Reflective Thinking

Feedback: A rational person is someone with well-defined goals who tries to fulfill those goals

as best he or she can.

19. Suppose the cost to Tim of a third glass of soda is zero because he's at a restaurant that gives free refills. According to the Cost-Benefit Principle Tim should:

- A. drink a third glass of soda.
- B. drink a third glass of soda if the benefit of doing so is positive.
- C. drink a third glass of soda if his benefit from drinking his second glass of soda was positive.
- D. not drink a third glass of soda.

Ans: B

Difficulty: 02 Medium

Learning Objective: 01-02

Topic: Applying the Cost-Benefit Principle

Blooms: Understand

AACSB: Reflective Thinking

Feedback: According to the Cost-Benefit Principle, an individual should take an action if, and only if, the benefits of taking the action are at least as great as the costs. In this case, since the cost of a third glass of soda is zero, Tim should drink a third glass as long as the benefit of doing so is positive.

20. Janie must choose to either mow the lawn or wash clothes. If she mows the lawn, she will earn \$30, and if she washes clothes, she will earn \$45. She dislikes both tasks equally and they both take the same amount of time. Janie will therefore choose to _____ because it generates a _____ economic surplus.

- A. mow the lawn; bigger
- B. wash clothes; bigger
- C. mow the law; smaller
- D. wash clothes; smaller

Ans: B

Difficulty: 02 Medium

Learning Objective: 01-02

Topic: Applying the Cost-Benefit Principle

Blooms: Understand

AACSB: Reflective Thinking

Feedback: Because both activities have the same cost (Janie's time and her dislike of the task), the activity with the greatest benefit will yield the greatest economic surplus.

21. Dean should play golf instead of preparing for tomorrow's exam in economics if:

- A. he is irrational.
- B. the benefit of golfing is greater than the benefit of studying.
- C. the economic surplus from playing golf is greater than the economic surplus from studying.
- D. Dean can play golf for free.

Ans: C

Difficulty: 01 Easy

Learning Objective: 01-02

Topic: Applying the Cost-Benefit Principle

Blooms: Apply

AACSB: Analytic

Feedback: People should choose actions that generate the largest possible economic surplus.

22. Larry was accepted at three different graduate schools, and must choose one. Elite U costs \$50,000 per year and did not offer Larry any financial aid. Larry values attending Elite U at \$60,000 per year. State College costs \$30,000 per year, and offered Larry an annual \$10,000 scholarship. Larry values attending State College at \$40,000 per year. NoName U costs \$20,000 per year, and offered Larry a full \$20,000 annual scholarship. Larry values attending NoName at \$15,000 per year. Larry's opportunity cost of attending Elite U is:

- A. \$70,000
- B. \$50,000
- C. \$20,000
- D. \$15,000

Ans: A

Difficulty: 03 Hard

Learning Objective: 01-02

Topic: Applying the Cost-Benefit Principle

Blooms: Apply

AACSB: Analytic

Feedback: If Larry attends Elite U, he not only has to pay \$50,000 in out-of-pocket expenses, but he also has to give up the value his next-best option. To determine the value of his next best option, note that the value to Larry from attending State College (net of tuition) is $\$40,000 - \$20,000 = \$20,000$. And, his value from attending NoName U (net of tuition) is $\$15,000 - 0 = \$15,000$. Since going to State College is his next best option, and his opportunity cost of going to Elite U is $\$50,000 + \$20,000 = \$70,000$.

23. Larry was accepted at three different graduate schools, and must choose one. Elite U costs \$50,000 per year and did not offer Larry any financial aid. Larry values attending Elite U at \$60,000 per year. State College costs \$30,000 per year, and offered Larry an annual \$10,000 scholarship. Larry values attending State College at \$40,000 per year. NoName U costs \$20,000 per year, and offered Larry a full \$20,000 annual scholarship. Larry values attending NoName at \$15,000 per year. Larry's opportunity cost of attending State College is:

- A. \$35,000
- B. \$30,000
- C. \$20,000
- D. \$15,000

Ans: A

Difficulty: 03 Hard

Learning Objective: 01-02

Topic: Applying the Cost-Benefit Principle

Blooms: Apply

AACSB: Analytic

Feedback: If Larry attends State College, he not only has to pay \$20,000 ($= \$30,000 - \$10,000$) in out-of-pocket expenses, but he also has to give up the value of his next-best option. To determine the value of his next best option, note that the value to Larry from attending Elite U

(net of tuition) is $\$60,000 - \$50,000 = \$10,000$. And, his value from attending NoName U (net of tuition) is $\$15,000 - 0 = \$15,000$. So going to NoName U is his next-best option, and his opportunity cost of going to State College is $\$20,000 + \$15,000 = \$35,000$.

24. Larry was accepted at three different graduate schools, and must choose one. Elite U costs $\$50,000$ per year and did not offer Larry any financial aid. Larry values attending Elite U at $\$60,000$ per year. State College costs $\$30,000$ per year, and offered Larry an annual $\$10,000$ scholarship. Larry values attending State College at $\$40,000$ per year. NoName U costs $\$20,000$ per year, and offered Larry a full $\$20,000$ annual scholarship. Larry values attending NoName at $\$15,000$ per year. Larry's opportunity cost of attending State NoName U is:

- A. $\$60,000$
- B. $\$30,000$
- C. $\$20,000$
- D. $\$15,000$

Ans: C

Difficulty: 03 Hard

Learning Objective: 01-02

Topic: Applying the Cost-Benefit Principle

Blooms: Apply

AACSB: Analytic

Feedback: If Larry attends NoName U, he will not have any out-of-pocket expenses, but he will still have to give up the value of his next-best option. To determine the value of his next best option, note that the value to Larry from attending Elite U (net of tuition) is $\$60,000 - \$50,000 = \$10,000$. And, his value from attending State College (net of tuition) is $\$40,000 - \$20,000 = \$20,000$. Thus, going to State College is his next-best option, and his opportunity cost of attending NoName U is $\$20,000$.

25. Larry was accepted at three different graduate schools, and must choose one. Elite U costs $\$50,000$ per year and did not offer Larry any financial aid. Larry values attending Elite U at $\$60,000$ per year. State College costs $\$30,000$ per year, and offered Larry an annual $\$10,000$ scholarship. Larry values attending State College at $\$40,000$ per year. NoName U costs $\$20,000$ per year, and offered Larry a full $\$20,000$ annual scholarship. Larry values attending NoName at $\$15,000$ per year. Larry maximizes his economic surplus by attending:

- A. Elite U.
- B. State College.
- C. NoName U because he has a full scholarship there.
- D. NoName U because the annual cost is only $\$20,000$.

Ans: B

Difficulty: 03 Hard

Learning Objective: 01-02

Topic: Applying the Cost-Benefit Principle

Blooms: Analyze

AACSB: Analytic

Feedback: To determine what Larry should do, determine the value of each option *as if it were his only choice*. In this case, the value to Larry from attending Elite U (net of tuition) is $\$60,000 - \$50,000 = \$10,000$. His value from attending State College (net of tuition) is $\$40,000 - \$20,000$

= \$20,000. And, his value from attending NoName U (net of tuition) is $\$15,000 - 0 = \$15,000$. Thus, his economic surplus will be the highest if he attends State College.

26. Larry was accepted at three different graduate schools, and must choose one. Elite U costs \$50,000 per year and did not offer Larry any financial aid. Larry values attending Elite U at \$60,000 per year. State College costs \$30,000 per year, and offered Larry an annual \$10,000 scholarship. Larry values attending State College at \$40,000 per year. NoName U costs \$20,000 per year, and offered Larry a full \$20,000 annual scholarship. Larry values attending NoName at \$15,000 per year. What is Larry's economic surplus from attending State College instead of his next best alternative?

- A. \$40,000
- B. \$20,000
- C. \$10,000
- D. \$5,000

Ans: D

Difficulty: 03 Hard

Learning Objective: 01-02

Topic: Applying the Cost-Benefit Principle

Blooms: Evaluate

AACSB: Analytic

Feedback: The benefit to Larry of attending State College is \$40,000. His cost of attending State College includes both \$20,000 ($= \$30,000 - \$10,000$) in out-of-pocket expenses and the value of his next best alternative. To determine the value of this next best alternative, note that the value to Larry from attending Elite U (net of tuition) is $\$60,000 - \$50,000 = \$10,000$. And, his value from attending NoName U (net of tuition) is $\$15,000 - 0 = \$15,000$. Thus, his next best alternative is NoName U, and Larry's economic surplus from attending State College instead of NoName U is $\$40,000 - \$20,000 - \$15,000 = \$5,000$.

27. Jen spends her afternoon at the beach, paying \$1 to rent a beach umbrella and \$11 for food and drinks rather than spending an equal amount of money to go to a movie. Her opportunity cost of going to the beach is:

- A. the \$12 she spent on the umbrella, food and drinks.
- B. only \$0 because she would have spent \$12 to go to the movie.
- C. the value she places on seeing the movie.
- D. the value she places on seeing the movie plus the \$12 she spent on the umbrella, food and drinks.

Ans: C

Difficulty: 02 Medium

Learning Objective: 01-02

Topic: Applying the Cost-Benefit Principle

Blooms: Understand

AACSB: Reflective Thinking

Feedback: Opportunity cost is the value that must be foregone to undertake an activity. By going to the beach, Jen gives up the value she places on seeing the movie. We don't include the \$12 she spends at the beach because she also would have spent that money at the movies.

28. All else equal, relative to a person who earns minimum wage, a person who earns \$30 per hour has:

- A. a higher opportunity cost of working an additional hour.
- B. a higher opportunity cost of taking the day off work.
- C. a lower opportunity cost of driving farther to work.
- D. the same opportunity cost of spending time on leisure activities.

Ans: B

Difficulty: 02 Medium

Learning Objective: 01-02

Topic: Applying the Cost-Benefit Principle

Blooms: Understand

AACSB: Reflective Thinking

Feedback: All else equal, giving up a day of work “costs” the person who can earn \$30 per hour more than it does someone who earns the minimum wage.

29. The opportunity cost of an activity includes the value of:

- A. all of the alternatives that must be forgone.
- B. the next-best alternative that must be foregone.
- C. the least-best alternative that must be foregone.
- D. the chosen activity minus the value of the next-best alternative.

Ans: B

Difficulty: 01 Easy

Learning Objective: 01-02

Topic: Applying the Cost-Benefit Principle

Blooms: Remember

AACSB: Reflective Thinking

Feedback: The opportunity cost of an activity is not the total value of all possible activities that you could have pursued, but only the value of the one alternative you give up, which is presumably the next-best one.

30. Amy is thinking about going to the movies tonight. A movie ticket costs \$15, and she’ll have to cancel a \$20 dog-sitting job that she would have been willing to do for free. The opportunity to Amy cost of going to the movies is:

- A. \$5.
- B. \$15.
- C. \$20.
- D. \$35

Ans: D

Difficulty: 02 Medium

Learning Objective: 01-02

Topic: Applying the Cost-Benefit Principle

Blooms: Understand

AACSB: Reflective Thinking

Feedback: Opportunity cost includes both implicit costs and explicit costs. If she goes to the movies, Amy will give up the opportunity to earn \$20 plus the \$15 cost of the ticket.

31. The economic surplus of an action is:

- A. the benefit gained by taking an action.
- B. the difference the explicit and implicit costs of taking an action.
- C. the difference between the benefit and the cost of taking an action.
- D. the money a person has left over after taking an action.

Ans: C

Difficulty: 01 Easy

Learning Objective: 01-02

Topic: Applying the Cost-Benefit Principle

Blooms: Remember

AACSB: Reflective Thinking

Feedback: Economic surplus is defined as the benefit of an action minus its cost.

32. You are trying to decide whether to purchase the latest Harry Potter book online or borrow it from the library. There is no charge for borrowing a book from the library, but going to the library takes more time than ordering a book online. Regardless of how you get the book, its benefit to you is the same. If the cost of buying the book online is \$13, then you should:

- A. borrow the book from the library because you can get it from the library for free.
- B. borrow the book from the library if the cost of doing so (in terms of the extra time it takes) is less than \$13.
- C. borrow the book from the library if the cost of doing so (in terms of the extra time it takes) is greater than \$13.
- D. buy the book online because it takes less time.

Ans: B

Difficulty: 02 Medium

Learning Objective: 01-02

Topic: Applying the Cost-Benefit Principle

Blooms: Understand

AACSB: Reflective Thinking

Feedback: The benefit to you of borrowing the book from the library is the \$13 you save. Thus, you should borrow the book from the library if your cost of doing so is less than \$13.

33. Alex received a four-year scholarship to State U. that covered tuition and fees, room and board, and books and supplies. If Alex becomes a full-time student, then:

- A. attending State U. for four years is costless for Alex.
- B. Alex has no incentive to study hard while at State U.
- C. the opportunity cost of attending State U. includes the money Alex could have earned working for four years.
- D. the opportunity cost of attending State U. includes the sum of the benefits Alex would have had from attending each of the other schools to which he was admitted.

Ans: C

Difficulty: 02 Medium

Learning Objective: 01-02

Topic: Applying the Cost-Benefit Principle

Blooms: Understand

AACSB: Reflective Thinking

Feedback: Even though Alex has no out-of-pocket costs, by attending State U Alex would be giving up on 4 years worth of earnings.

34. Suppose Mary is willing to pay up to \$15,000 for a used Ford pick-up truck. If she buys one for \$12,000, her _____ would be _____.

A. benefit; \$12,000

B. cost; \$15,000

C. economic surplus; \$3,000

D. economic surplus; \$12,000

Ans: C

Difficulty: 02 Medium

Learning Objective: 01-02

Topic: Applying the Cost-Benefit Principle

Blooms: Understand

AACSB: Reflective Thinking

Feedback: Mary's benefit from owning the truck is \$15,000 and the cost is \$12,000, so her economic surplus is \$3,000.

35. If individuals are rational, they should choose actions that yield the:

A. largest total benefits.

B. smallest total costs.

C. smallest economic surplus.

D. largest economic surplus.

Ans: D

Difficulty: 01 Easy

Learning Objective: 01-02

Topic: Applying the Cost-Benefit Principle

Blooms: Remember

AACSB: Reflective Thinking

Feedback: Rational individuals should make decisions based on the Cost-Benefit Principle, which means taking those actions that yield the largest possible economic surplus.

36. Suppose the most you would be willing to pay for a plane ticket home is \$250. If you buy one for \$175, then your economic surplus is:

A. \$250.

B. \$175.

C. \$75.

D. \$0.

Ans: C

Difficulty: 02 Medium

Learning Objective: 01-02

Topic: Applying the Cost-Benefit Principle

Blooms: Understand

AACSB: Reflective Thinking

Feedback: The economic surplus of taking an action is its benefit minus its cost.

37. The Cost-Benefit Principle:

- A. fully captures how people choose between alternatives.
- B. provides an abstract model of a rational person should choose between alternatives.
- C. describes how people behave once they have enough education.
- D. provides little insight into how people actually chose between alternatives.

Ans: B

Difficulty: 01 Easy

Learning Objective: 01-02

Topic: Applying the Cost-Benefit Principle

Blooms: Remember

AACSB: Reflective Thinking

Feedback: The Cost-Benefit Principle is not intended to exactly capture all features of human behavior. It just says that a rational decision maker should weigh costs and benefits.

38. Economists believe the Cost-Benefit Principle is:

- A. a simple but useful model of how people should make choices.
- B. a comprehensive description all the factors that influence people's choices.
- C. an interesting intellectual exercise with little applicability to the real world.
- D. of little use to those who wish to learn how to make better decisions.

Ans: A

Difficulty: 01 Easy

Learning Objective: 01-02

Topic: Applying the Cost-Benefit Principle

Blooms: Remember

AACSB: Reflective Thinking

Feedback: The Cost-Benefit Principle is seen as a simple but useful model of how people should make choices.

39. The cost-benefit model used by economists is:

- A. unrealistic because it is too detailed and specific to apply to most situations.
- B. unrealistic because everyone can think of times when he or she violated the principle.
- C. useful because everyone follows it all of the time.
- D. useful because most people follow it most of the time.

Ans: D

Difficulty: 01 Easy

Learning Objective: 01-02

Topic: Applying the Cost-Benefit Principle

Blooms: Remember

AACSB: Reflective Thinking

Feedback: Most people make sensible decisions most of the time.

40. Economists use abstract models because:

- A. every economic situation is unique, so it is impossible to make generalizations.
- B. every economic situation is essentially the same, so specific details are unnecessary.
- C. they are useful for describing general patterns of behavior.
- D. computers have allowed economists to develop abstract models.

Ans: C

Difficulty: 01 Easy

Learning Objective: 01-02

Topic: Applying the Cost-Benefit Principle

Blooms: Remember

AACSB: Reflective Thinking

Feedback: Economic models focus on the critical features of human behavior.

41. The fact that most people make some decisions based on intuition rather than calculation is:

- A. irrational, because intuition is usually wrong.
- B. consistent with the cost-benefit model because calculating costs and benefits is irrational.
- C. consistent with the cost-benefit model because most people intuitively weigh costs and benefits.
- D. inconsistent with the cost-benefit model, but still rational.

Ans: C

Difficulty: 02 Understand

Learning Objective: 01-02

Topic: Applying the Cost-Benefit Principle

Blooms: Understand

AACSB: Reflective Thinking

Feedback: People weigh costs and benefits, even if they are not consciously aware that they are doing so.

42. Moe has a big exam tomorrow. He considered studying this evening, but decided to hang out with Curly instead. If neither activity involves any explicit costs, and Moe always chooses rationally, then it must be true that:

- A. the opportunity cost of studying is greater than the value Moe gets from spending time with Curly.
- B. the opportunity cost of studying is less than the value Moe gets from spending time with Curly.
- C. Moe gets more benefit from spending time with Curly than from studying.
- D. Moe gets less benefit from spending time with Curly than from studying.

Ans: C

Difficulty: 03 Hard

Learning Objective: 01-02

Topic: Applying the Cost-Benefit Principle

Blooms: Analyze

AACSB: Analytic

Feedback: If Moe rationally chooses to spend time with Curly, then his benefit of spending time with Curly must outweigh his cost. Given that neither activity involves any explicit costs, the opportunity cost of spending time with Curly equals the benefit of studying. Thus, if Moe rationally chooses to spend time with Curly, it must be the case that his benefit from spending

time with Curly is greater than his benefit from studying.

43. If one fails to account for implicit costs in decision making, then applying the cost-benefit rule will be flawed because:

- A. the benefits will be overstated.
- B. the costs will be understated.
- C. the benefits will be understated.
- D. the costs will be overstated.

Ans: B

Difficulty: 02 Understand

Learning Objective: 01-03

Topic: Three Important Decision Pitfalls

Blooms: Understand

AACSB: Reflective Thinking

Feedback: The full cost of an action includes both implicit and out-of-pocket costs.

44. Your classmates from the University of Chicago are planning to go to Miami for spring break, and you are undecided about whether you should go with them. The round-trip airfares are \$600, but you have a frequent-flyer coupon worth \$500 that you could use to pay part of the airfare. All other costs for the vacation are exactly \$900. The most you would be willing to pay for the trip is \$1400. Your only alternative use for your frequent-flyer coupon is for your trip to Atlanta two weeks after the break to attend your sister's graduation, which your parents are forcing you to attend. The Chicago-Atlanta round-trip airfares are \$450. If you do not use the frequent-flyer coupon to fly to Miami, should you go to Miami?

- A. Yes, your benefit is more than your cost.
- B. No, your benefit is less than your cost.
- C. Yes, your benefit is equal to your cost.
- D. No, because there are no benefits in the trip.

Ans: B

Difficulty: 03 Hard

Learning Objective: 01-03

Topic: Three Important Decision Pitfalls

Blooms: Evaluate

AACSB: Analytic

Feedback: If you don't use your frequent-flyer coupon, your total cost is $\$600 + \$900 = \$1500$, but your benefit is only \$1400.

45. Your classmates from the University of Chicago are planning to go to Miami for spring break, and you are undecided about whether you should go with them. The round-trip airfares are \$600, but you have a frequent-flyer coupon worth \$500 that you could use to pay part of the airfare. All other costs for the vacation are exactly \$900. The most you would be willing to pay for the trip is \$1400. Your only alternative use for your frequent-flyer coupon is for your trip to Atlanta two weeks after the break to attend your sister's graduation, which your parents are forcing you to attend. The Chicago-Atlanta round-trip airfares are \$450. What is the opportunity cost of using the coupon for the Miami trip?

- A. \$100
- B. \$450
- C. \$500
- D. \$550

Ans: B

Difficulty: 02 Medium

Learning Objective: 01-03

Topic: Three Important Decision Pitfalls

Blooms: Understand

AACSB: Reflective Thinking

Feedback: If you use the coupon for the Miami trip, then you lose the value of using it to go to Atlanta.

46. Your classmates from the University of Chicago are planning to go to Miami for spring break, and you are undecided about whether you should go with them. The round-trip airfares are \$600, but you have a frequent-flyer coupon worth \$500 that you could use to pay part of the airfare. All other costs for the vacation are exactly \$900. The most you would be willing to pay for the trip is \$1400. Your only alternative use for your frequent-flyer coupon is for your trip to Atlanta two weeks after the break to attend your sister's graduation, which your parents are forcing you to attend. The Chicago-Atlanta round-trip airfares are \$450. Should you use the frequent flyer coupon to go to Miami?

- A. Yes, your benefit is more than your cost.
- B. No, your benefit is less than your cost.
- C. Yes, your benefit is equal to your cost.
- D. No, because there are no benefits in the trip.

Ans: B

Difficulty: 03 Hard

Learning Objective: 01-03

Topic: Three Important Decision Pitfalls

Blooms: Evaluate

AACSB: Analytic

Feedback: If you use the frequent flyer coupon to go to Miami, your out-of-pocket expenses would be \$1000, and you would give up the ability to save \$450 to go to Atlanta. Thus, the total cost of using the frequent flyer coupon to go to Miami would be \$1450, which is higher than your willingness to pay.

47. Your classmates from the University of Chicago are planning to go to Miami for spring break, and you are undecided about whether you should go with them. The round-trip airfares are \$600, but you have a frequent-flyer coupon worth \$500 that you could use to pay part of the airfare. All other costs for the vacation are exactly \$900. The most you would be willing to pay for the trip is \$1400. Your only alternative use for your frequent-flyer coupon is for your trip to Atlanta two weeks after the break to attend your sister's graduation, which your parents are forcing you to attend. The Chicago-Atlanta round-trip airfares are \$450. If the Chicago-Atlanta round-trip air fare were \$350, should you use the coupon to go to Miami?

- A. No, your economic surplus would be $-\$50$.
- B. No, your economic surplus would be $-\$100$.

- C. Yes, your economic surplus would be \$50.
- D. Yes, your economic surplus would be \$400.

Ans: C

Difficulty: 03 Hard

Learning Objective: 01-03

Topic: Three Important Decision Pitfalls

Blooms: Evaluate

AACSB: Analytic

Feedback: If you use the frequent flyer coupon to go to Miami, your out-of-pocket expenses would be \$1000 and the opportunity cost of using the coupon would be \$350. Thus, the total cost of using the frequent flyer coupon to go to Miami would be \$1350, which is \$50 less than your willingness to pay.

48. Pat earns \$25,000 per year (after taxes), and Pat's spouse, Chris, earns \$35,000 (after taxes). They have two pre-school-aged children. Childcare for their children costs \$12,000 per year. Given that Chris doesn't want to stay home with the kids, regardless of what Pat does, Pat should stay home with the kids if, and only if, the value of Pat spending more time with the kids is greater than:

- A. \$37,000 per year.
- B. \$25,000 per year.
- C. \$13,000 per year.
- D. \$12,000 per year.

Ans: C

Difficulty: 03 Hard

Learning Objective: 01-03

Topic: Three Important Decision Pitfalls

Blooms: Analyze

AACSB: Analytic

Feedback: The benefit of staying Pat home with the kids is the \$12,000 per year saved on childcare plus the value of Pat spending more time with the kids. The cost of Pat staying home with the kids is \$25,000 in foregone earnings. Thus, weighing costs and benefits, Pat should stay home with the kids if, and only if, the value of Pat spending more time with the kids is greater than \$13,000 per year.

50. You paid \$35 for a ticket (which is non-refundable) to see SPAM, a local rock band, in concert on Saturday. Assume that \$35 is the most you would have been willing to pay for a ticket. Your boss called, and she is looking for someone to cover a shift on Saturday at the same time as the concert. You would have to work 4 hours and she would pay you \$11/hr. The psychic cost to you of working is \$2/hr. Should you go to the concert instead of working Saturday?

- A. Yes, the benefit of going to the concert is more than the cost.
- B. No, the benefit of going to the concert is less than the cost.
- C. Yes, the benefit of going to the concert is equal to the cost.
- D. No, because there are no benefits of going to the concert.

Ans: B

Difficulty: 03 Hard

Learning Objective: 01-03

Topic: Three Important Decision Pitfalls

Blooms: Evaluate

AACSB: Analytic

Feedback: The fact that you were willing to pay up to \$35 to go to the concert indicates that the benefit to you of going to the concert is \$35. The cost of going to the concert is the foregone value of working, which is $4 \times (\$11 - \$2)$ or \$36. [Note that we do not factor in the cost of the ticket since it's a sunk cost.] Since the benefit of going to the concert is less than the cost, you should not go to the concert.

51. You paid \$35 for a ticket (which is non-refundable) to see SPAM, a local rock band, in concert on Saturday. Assume that \$35 is the most you would have been willing to pay for a ticket. Your boss called, and she is looking for someone to cover a shift on Saturday at the same time as the concert. You would have to work 4 hours and she would pay you \$11/hr. The psychic cost to you of working is \$2/hr. What is the opportunity cost of going to the concert?

- A. \$1
- B. \$9
- C. \$35
- D. \$36

Ans: D

Difficulty: 02 Medium

Learning Objective: 01-03

Topic: Three Important Decision Pitfalls

Blooms: Understand

AACSB: Reflective Thinking

Feedback: The cost of going to the concert is the foregone value of working, which is $4 \times (\$11 - \$2)$ or \$36. [Note that we do not factor in the cost of the ticket since it's a sunk cost.]

52. You paid \$35 for a ticket (which is non-refundable) to see SPAM, a local rock band, in concert on Saturday. Assume that \$35 is the most you would have been willing to pay for a ticket. Your boss called, and she is looking for someone to cover a shift on Saturday at the same time as the concert. You would have to work 4 hours and she would pay you \$11/hr. The psychic cost to you of working is \$2/hr. What is your opportunity cost of going to work on Saturday?

- A. \$0
- B. \$9
- C. \$35
- D. \$36

Ans: C

Difficulty: 02 Medium

Learning Objective: 01-03

Topic: Three Important Decision Pitfalls

Blooms: Understand

AACSB: Reflective Thinking

Feedback: By going to work, you give up attending the concert, which you value at \$35.

53. You paid \$35 for a ticket (which is non-refundable) to see SPAM, a local rock band, in concert on Saturday. Assume that \$35 is the most you would have been willing to pay for a ticket. Your boss called, and she is looking for someone to cover a shift on Saturday at the same time as the concert. You would have to work 4 hours and she would pay you \$11/hr. The psychic cost to you of working is \$2/hr. Your economic surplus from going to work instead of seeing SPAM on Saturday is:

- A. \$0
- B. \$1
- C. \$35
- D. \$36

Ans: B

Difficulty: 03 Hard

Learning Objective: 01-03

Topic: Three Important Decision Pitfalls

Blooms: Apply

AACSB: Analytic

Feedback: The benefit of working is $4 \times (\$11 - \$2)$ or \$36. The cost of working is the value you place on going to the concert or \$35 (since this is the most you would have been willing to pay for a ticket). Note that we do not factor in the cost of the ticket since it's a sunk cost. Subtracting the cost of working from the benefit of working, we see that the economic surplus of working is \$1.

54. Matt has decided to purchase his textbooks for the semester. His options are to purchase the books online with next day delivery at a cost of \$175, or to drive to campus tomorrow to buy the books at the university bookstore at a cost of \$170. Last week he drove to campus to buy a concert ticket because they offered 25 percent off the regular price of \$16. The benefit to Matt of buying his books at the university bookstore instead of online is:

- A. \$5
- B. \$9
- C. \$170
- D. \$175

Ans: A

Difficulty: 02 Medium

Learning Objective: 01-03

Topic: Three Important Decision Pitfalls

Blooms: Understand

AACSB: Reflective Thinking

Feedback: Matt saves \$5 by purchasing the books at the university bookstore.

55. Matt has decided to purchase his textbooks for the semester. His options are to purchase the books online with next day delivery at a cost of \$175, or to drive to campus tomorrow to buy the books at the university bookstore at a cost of \$170. Last week he drove to campus to buy a concert ticket because they offered 25 percent off the regular price of \$16. The benefit to Matt of driving to campus to buy the concert ticket last week was:

- A. \$2
- B. \$4
- C. \$9
- D. \$16

Ans: B

Difficulty: 02 Medium

Learning Objective: 01-03

Topic: Three Important Decision Pitfalls

Blooms: Understand

AACSB: Reflective Thinking

Feedback: Matt saved \$4 (25% of \$16) by driving to campus to buy the ticket.

56. Matt has decided to purchase his textbooks for the semester. His options are to purchase the books online with next day delivery at a cost of \$175, or to drive to campus tomorrow to buy the books at the university bookstore at a cost of \$170. Last week he drove to campus to buy a concert ticket because they offered 25 percent off the regular price of \$16. Given that driving to campus to buy the concert ticket was rational for Matt, Matt should:

- A. not drive to campus to buy the books because the \$5 he would save is only two percent of the cost of the books, and that is much less than the 25 percent he saved on the concert ticket.
- B. drive to campus to buy the books because the books are cheaper at the bookstore than online.
- C. drive to campus to buy the books because the \$5 he would save is more than he saved by driving to campus to buy the concert ticket.
- D. not drive to campus to buy the books because the cost of gas and his time must certainly be more than the \$5 he would save.

Ans: C

Difficulty: 03 Hard

Learning Objective: 01-03

Topic: Three Important Decision Pitfalls

Blooms: Evaluate

AACSB: Analytic

Feedback: Because Matt was willing to drive to campus to save \$4 last week, we can assume that the cost of driving to campus is no more than \$4, so he should be willing to drive to campus to save \$5.

57. Matt has decided to purchase his textbooks for the semester. His options are to purchase the books online with next day delivery at a cost of \$175, or to drive to campus tomorrow to buy the books at the university bookstore at a cost of \$170. Last week he drove to campus to buy a concert ticket because they offered 25 percent off the regular price of \$16. Assume the minimum that Matt would be willing to accept to drive to campus is equal to the \$4 he saved on the concert ticket. What would his economic surplus be if he bought his textbooks at the university bookstore rather than online?

- A. \$5
- B. \$1
- C. \$50

D. \$20

Ans: B

Difficulty: 03 Hard

Learning Objective: 01-03

Topic: Three Important Decision Pitfalls

Blooms: Apply

AACSB: Analytic

Feedback: If he bought his textbooks at the university bookstore instead of online, Matt would save \$5, but the cost of driving to campus would be \$4, so his economic surplus would be \$1.

58. The marginal benefit of an activity is the:

A. same as the total benefit of an activity.

B. total benefit of an activity divided by the level of the activity.

C. extra benefit associated with an extra unit of the activity.

D. total benefit associated with an extra unit of the activity.

Ans: C

Difficulty: 01 Easy

Learning Objective: 01-03

Topic: Three Important Decision Pitfalls

Blooms: Remember

AACSB: Reflective Thinking

Feedback: Marginal benefit is the increase in total benefit that results from carrying out one additional unit of an activity.

60. Suppose the total benefit of watching 1 baseball game is 100, the total benefit of watching 2 games is 120, and the total benefit of watching 3 games is 125. In this case, the marginal benefit of watching the 3rd game is:

A. 125

B. 5

C. 41.67

D. 375

Ans: B

Difficulty: 02 Medium

Learning Objective: 01-03

Topic: Three Important Decision Pitfalls

Blooms: Understand

AACSB: Reflective Thinking

Feedback: Marginal benefit is the increase in total benefit that results from a carrying out one additional unit of an activity. By watching the 3rd game, total benefit increases from 120 to 125, so the marginal benefit is 5.

61. The extra benefit that results from carrying out one additional unit of an activity is the _____ of the activity.

A. marginal benefit

B. total benefit

- C. average benefit
- D. economic benefit

Ans: A

Difficulty: 01 Easy

Learning Objective: 01-03

Topic: Three Important Decision Pitfalls

Blooms: Remember

AACSB: Reflective Thinking

Feedback: Marginal benefit is the additional benefit of carrying out one additional unit of an activity.

62. The marginal cost of an activity is the:

- A. change in the total cost of the activity that results from carrying out an additional unit of the activity.
- B. the total cost of the activity divided by the change in the level of the activity.
- C. the total cost of the activity divided by the level of the activity.
- D. change in the level of the activity divided by the change in the cost of the activity.

Ans: A

Difficulty: 01 Easy

Learning Objective: 01-03

Topic: Three Important Decision Pitfalls

Blooms: Remember

AACSB: Reflective Thinking

Feedback: Marginal cost is the additional cost of carrying out an additional unit of an activity.

63. The extra cost that results from carrying out one additional unit of an activity is the _____ of the activity.

- A. marginal benefit
- B. marginal cost
- C. reservation cost
- D. opportunity cost.

Ans: B

Difficulty: 01 Easy

Learning Objective: 01-03

Topic: Three Important Decision Pitfalls

Blooms: Remember

AACSB: Reflective Thinking

Feedback: Marginal cost is the additional cost of carrying out one additional unit of an activity.

64. Dividing the total cost of n units of an activity by n reveals the:

- A. average benefit.
- B. marginal cost.
- C. units per cost.
- D. average cost.

Ans: D

Difficulty: 01 Easy

Learning Objective: 01-03

Topic: Three Important Decision Pitfalls

Blooms: Remember

AACSB: Reflective Thinking

Feedback: Average cost is the total cost of undertaking n units of an activity divided by n .

65. For the Fall semester, you had to pay a nonrefundable fee of \$600 for your meal plan, which gives you up to 150 meals. If you eat all of the meals, your average cost for a meal is:

- A. \$6.
- B. \$5.
- C. \$4.
- D. \$0.25.

Ans: C

Difficulty: 02 Medium

Learning Objective: 01-03

Topic: Three Important Decision Pitfalls

Blooms: Understand

AACSB: Reflective Thinking

Feedback: To find the average cost, divide the total cost by the number of meals. Here, $\$600/150 = \4 .

66. For the Fall semester, you had to pay a nonrefundable fee of \$600 for your meal plan, which gives you up to 150 meals. If you eat 100 meals, your average cost for a meal is:

- A. \$6.
- B. \$5.
- C. \$4.
- D. \$0.25.

Ans: A

Difficulty: 02 Medium

Learning Objective: 01-03

Topic: Three Important Decision Pitfalls

Blooms: Understand

AACSB: Reflective Thinking

Feedback: To find the average cost, divide the total cost by the number of meals. Here, $\$600/100 = \6 .

67. For the Fall semester, you had to pay a nonrefundable fee of \$600 for your meal plan, which gives you up to 150 meals. If you eat 100 meals, your marginal cost of the 100th meal is:

- A. \$6.
- B. \$4.
- C. \$0.25.
- D. \$0.

Ans: D

Difficulty: 02 Medium

Learning Objective: 01-03

Topic: Three Important Decision Pitfalls

Blooms: Understand

AACSB: Reflective Thinking

Feedback: The non-refundable \$600 you paid for your meal plan is a sunk cost; no matter how many meals you eat up to 150, your marginal cost is 0.

68. The average benefit of n units of an activity is the:

- A. total benefit of n units divided by n .
- B. n divided by the total benefit of n units.
- C. n times the total benefit of n units.
- D. extra benefit from carrying out one additional unit of the activity.

Ans: A

Difficulty: 01 Easy

Learning Objective: 01-03

Topic: Three Important Decision Pitfalls

Blooms: Remember

AACSB: Reflective Thinking

Feedback: Any average is the total divided by the number of units.

69. You save \$10 on gas every week because you take the bus to school. You have class 5 days a week. What is your average benefit per day of taking the bus to school?

- A. \$10
- B. \$5
- C. \$2
- D. \$0

Answer: C

Difficulty: 02 Medium

Learning Objective: 01-03

Topic: Three Important Decision Pitfalls

Blooms: Understand

AACSB: Reflective Thinking

Feedback: Your average benefit per day is your total benefit, \$10, divided by the number of days you take the bus, 5. So your average benefit per day is \$2.

70. Your scholarship depends on your maintaining a 3.5 cumulative GPA. Your GPA for last semester was 3.6, which brought your cumulative GPA down. What must be true?

- A. Last semester's grades were higher than your overall GPA.
- B. Last semester's grades were lower than your overall GPA.
- C. If this semester's grades are the same as last semester's, your overall GPA will stay the same.
- D. If this semester's grades are the same as last semester's, you might lose your scholarship.

Ans: B

Difficulty: 03 Hard

Learning Objective: 01-03

Topic: Three Important Decision Pitfalls

Blooms: Analyze

AACSB: Analytic

Feedback: When an average is falling, it must be true that the last unit included is less than the average over all prior units.

71. Refer to the table below. The average cost of 4 units of this activity is:

Units of Activity	Total Cost	Total Benefit
0	\$0	\$0
1	\$30	\$100
2	\$40	\$160
3	\$60	\$190
4	\$100	\$210
5	\$150	\$220
6	\$210	\$225

- A. \$20
- B. \$25
- C. \$30
- D. \$40

Ans: B

Difficulty: 02 Medium

Learning Objective: 01-03

Topic: Three Important Decision Pitfalls

Blooms: Understand

AACSB: Reflective Thinking

Feedback: Total cost is \$100, so dividing by 4 gives \$25.

72. Refer to the table below. The marginal cost of the 3rd unit of this activity is:

Units of Activity	Total Cost	Total Benefit
0	\$0	\$0
1	\$30	\$100
2	\$40	\$160
3	\$60	\$190
4	\$100	\$210
5	\$150	\$220
6	\$210	\$225

- A. \$30
- B. \$25
- C. \$20
- D. \$10

Ans: C

Difficulty: 02 Medium

Learning Objective: 01-03

Topic: Three Important Decision Pitfalls

Blooms: Understand

AACSB: Reflective Thinking

Feedback: Total cost increases from \$40 to \$60 when you go from 2 to 3 units, so the marginal cost of the 3rd unit is \$20.

73. Refer to the table below. The average benefit of 2 units of activity is:

Units of Activity	Total Cost	Total Benefit
0	\$0	\$0
1	\$30	\$100
2	\$40	\$160
3	\$60	\$190
4	\$100	\$210
5	\$150	\$220
6	\$210	\$225

A. \$80

B. \$60

C. \$40

D. \$20

Ans: A

Difficulty: 02 Medium

Learning Objective: 01-03

Topic: Three Important Decision Pitfalls

Blooms: Understand

AACSB: Reflective Thinking

Feedback: Total benefit is \$160, so dividing by 2 gives \$80.

74. Refer to the table below. The marginal benefit of the 5th unit of activity is:

Units of Activity	Total Cost	Total Benefit
0	\$0	\$0
1	\$30	\$100
2	\$40	\$160
3	\$60	\$190
4	\$100	\$210
5	\$150	\$220
6	\$210	\$225

A. \$50

B. \$44

C. \$10

D. \$5

Ans: C

Difficulty: 02 Medium

Learning Objective: 01-03

Topic: Three Important Decision Pitfalls

Blooms: Understand

AACSB: Reflective Thinking

Feedback: Total benefit increases from \$210 to \$220 when you go from 4 to 5 units, so the marginal benefit of the 5th unit is \$10.

75. Refer to the table below. According to the Cost-Benefit Principle, how many units of this activity should be carried out?

Units of Activity	Total Cost	Total Benefit
0	\$0	\$0
1	\$30	\$100
2	\$40	\$160
3	\$60	\$190
4	\$100	\$210
5	\$150	\$220
6	\$210	\$225

A. 1

B. 3

C. 4

D. 6

Ans: B

Difficulty: 03 Hard

Learning Objective: 01-03

Topic: Three Important Decision Pitfalls

Blooms: Evaluate

AACSB: Analytic

Feedback: Three units of the activity provide a net benefit (total benefit - total cost) of \$130, which is the highest of all the options given. Also, note that marginal benefit is greater than marginal cost for the first three units, but marginal benefit is less than marginal cost for units 4, 5 and 6.

76. Refer to the table below. The average cost of 5 units of activity is:

Units of Activity	Total Cost	Total Benefit
0	\$0	\$0
1	\$2	\$12
2	\$6	\$22
3	\$12	\$30

4	\$20	\$36
5	\$30	\$40
6	\$42	\$42
7	\$56	\$43

- A. \$4
- B. \$6
- C. \$8
- D. \$10

Ans: B

Difficulty: 02 Medium

Learning Objective: 01-03

Topic: Three Important Decision Pitfalls

Blooms: Understand

AACSB: Reflective Thinking

Feedback: Average cost is the total cost divided by the number of units. Here $\$30/5 = \6 .

77. Refer to the table below. The marginal cost of the 4th unit of activity is:

Units of Activity	Total Cost	Total Benefit
0	\$0	\$0
1	\$2	\$12
2	\$6	\$22
3	\$12	\$30
4	\$20	\$36
5	\$30	\$40
6	\$42	\$42
7	\$56	\$43

- A. \$5
- B. \$6
- C. \$8
- D. \$10

Ans: C

Difficulty: 02 Medium

Learning Objective: 01-03

Topic: Three Important Decision Pitfalls

Blooms: Understand

AACSB: Reflective Thinking

Feedback: Total cost increases from \$12 to \$20 when you go from 3 to 4 units, so the marginal cost of the 4th unit is \$8.

78. Refer to the table below. The average benefit of 4 units of activity is:

Units of Activity	Total Cost	Total Benefit
0	\$0	\$0

1	\$2	\$12
2	\$6	\$22
3	\$12	\$30
4	\$20	\$36
5	\$30	\$40
6	\$42	\$42
7	\$56	\$43

- A. \$4
- B. \$5
- C. \$9
- D. \$10

Ans: C

Difficulty: 02 Medium

Learning Objective: 01-03

Topic: Three Important Decision Pitfalls

Blooms: Understand

AACSB: Reflective Thinking

Feedback: Average benefit is total benefit divided by the number of units. Here $\$36/4=\9 .

79. Refer to the table below. The marginal benefit of the 6th unit of activity is:

Units of Activity	Total Cost	Total Benefit
0	\$0	\$0
1	\$2	\$12
2	\$6	\$22
3	\$12	\$30
4	\$20	\$36
5	\$30	\$40
6	\$42	\$42
7	\$56	\$43

- A. \$1
- B. \$2
- C. \$4
- D. \$7

Ans: B

Difficulty: 02 Medium

Learning Objective: 01-03

Topic: Three Important Decision Pitfalls

Blooms: Understand

AACSB: Reflective Thinking

Feedback: Total benefit increases from 40 to 42 when you go from 5 to 6 units, so the marginal benefit of the 6th unit is \$2.

80. Refer to the table below. According to the Cost-Benefit Principle, how many units of this activity should be carried out?

Units of Activity	Total Cost	Total Benefit
0	\$0	\$0
1	\$2	\$12
2	\$6	\$22
3	\$12	\$30
4	\$20	\$36
5	\$30	\$40
6	\$42	\$42
7	\$56	\$43

- A. 2
- B. 3
- C. 4
- D. 5

Ans: B

Difficulty: 03 Hard

Learning Objective: 01-03

Topic: Three Important Decision Pitfalls

Blooms: Evaluate

AACSB: Analytic

Feedback: Three units of this activity provide a net benefit (total benefit - total cost) of \$18, which is the highest of all the options given. Also, note that marginal benefit is greater than marginal cost for the first three units, but marginal benefit is less than marginal cost for units 4, 5, 6 and 7.

81. The table below shows how total donations, average donations, total labor costs and average labor costs vary depending on the number of employees State U hires for its fundraising activities.

Number of Employees	Total Donations	Average Donations	Total Labor Costs	Average Labor Costs
1	\$30,000			\$8,000
2	\$42,426		\$17,000	
3		\$17,321	\$27,000	
4	\$60,000			\$9,500
5		\$13,416	\$50,000	

The total value of donations raised by three employees is:

- A. \$43,899.
- B. \$45,000.

C. \$48,911.

D. \$51,963.

Ans: D

Difficulty: 03 Hard

Learning Objective: 01-03

Topic: Three Important Decision Pitfalls

Blooms: Apply

AACSB: Analytic

Feedback: With three employees, average donations are \$17,321. Total donations equal average donations times the number of employees, or \$51,963 ($= \$17,321 \times 3$).

82. The table below shows how total donations, average donations, total labor costs and average labor costs vary depending on the number of employees State U hires for its fundraising activities.

Number of Employees	Total Donations	Average Donations	Total Labor Costs	Average Labor Costs
1	\$30,000			\$8,000
2	\$42,426		\$17,000	
3		\$17,321	\$27,000	
4	\$60,000			\$9,500
5		\$13,416	\$50,000	

The total labor cost with 4 employees is:

A. \$21,500.

B. \$22,000.

C. \$38,000.

D. \$43,121.

Ans: C

Difficulty: 03 Hard

Learning Objective: 01-03

Topic: Three Important Decision Pitfalls

Blooms: Apply

AACSB: Analytic

Feedback: With 4 employees, average labor costs are \$9,500. Total labor costs equal average labor costs times the number of employees or \$38,000 ($\$9,500 \times 4$).

83. The table below shows how total donations, average donations, total labor costs and average labor costs vary depending on the number of employees State U hires for its fundraising activities.

Number of Employees	Total Donations	Average Donations	Total Labor Costs	Average Labor Costs
1	\$30,000			\$8,000
2	\$42,426		\$17,000	
3		\$17,321	\$27,000	
4	\$60,000			\$9,500

5		\$13,416	\$50,000	
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The President of State U decides to hire fundraising employees as long as their average benefit exceeds their average cost. This results in _____ employees being hired and a net benefit (total donations minus total labor costs) of _____.

- A. 5; \$17,080
- B. 5; \$67,080
- C. 4; \$60,000
- D. 4; \$22,000

Ans: A

Difficulty: 03 Hard

Learning Objective: 01-03

Topic: Three Important Decision Pitfalls

Blooms: Analyze

AACSB: Analytic

Feedback: Average benefit exceeds average costs for all 5 employees, so 5 employees will be hired. With 5 employees, total donations are \$67,080 and total costs are \$50,000, so the net benefit is \$17,080 (= \$67,080 - \$50,000).

84. The table below shows how total donations, average donations, total labor costs and average labor costs vary depending on the number of employees State U hires for its fundraising activities.

Number of Employees	Total Donations	Average Donations	Total Labor Costs	Average Labor Costs
1	\$30,000			\$8,000
2	\$42,426		\$17,000	
3		\$17,321	\$27,000	
4	\$60,000			\$9,500
5		\$13,416	\$50,000	

The marginal benefit (in terms of extra donations) of the 2nd employee is:

- A. \$42,426.
- B. \$21,213.
- C. \$12,426.
- D. \$11,337.

Ans: C

Difficulty: 02 Medium

Learning Objective: 01-03

Topic: Three Important Decision Pitfalls

Blooms: Understand

AACSB: Reflective Thinking

Feedback: When the number of employees increases from 1 to 2, total donations increase by \$12,426

85. The table below shows how total donations, average donations, total labor costs and average

labor costs vary depending on the number of employees State U hires for its fundraising activities.

Number of Employees	Total Donations	Average Donations	Total Labor Costs	Average Labor Costs
1	\$30,000			\$8,000
2	\$42,426		\$17,000	
3		\$17,321	\$27,000	
4	\$60,000			\$9,500
5		\$13,416	\$50,000	

The marginal cost of the 4th employee is:

- A. \$9,500.
- B. \$10,750.
- C. \$11,000.
- D. \$13,000.

Ans: C

Difficulty: 03 Hard

Learning Objective: 01-03

Topic: Three Important Decision Pitfalls

Blooms: Apply

AACSB: Analytic

Feedback: The total cost of 4 employees is \$38,000 (= \$9,500 × 4). Thus, when the number of employees increases from 3 to 4, total labor costs increase by \$11,000 (= \$38,000 - \$27,000).

86. The table below shows how total donations, average donations, total labor costs and average labor costs vary depending on the number of employees State U hires for its fundraising activities.

Number of Employees	Total Donations	Average Donations	Total Labor Costs	Average Labor Costs
1	\$30,000			\$8,000
2	\$42,426		\$17,000	
3		\$17,321	\$27,000	
4	\$60,000			\$9,500
5		\$13,416	\$50,000	

The Chair of the Economics Department at State U says that fundraising employees should be hired as long as their marginal benefit exceeds their marginal cost. If the University follows this advice, then _____ employee(s) will be hired, and the net benefit (total donations minus total labor costs) will be _____.

- A. 1; \$22,000
- B. 2; \$25,426
- C. 3; \$25,426
- D. 2; \$3,476

Ans: B

Difficulty: 03 Hard

Learning Objective: 01-03

Topic: Three Important Decision Pitfalls

Blooms: Analyze

AACSB: Analytic

Feedback: The marginal benefit of the 2nd employee (\$12,426) exceeds its marginal cost (\$9,000), but the marginal benefit of the 3rd employee (\$9,537) is less than its marginal cost (\$10,000). Thus, the University should hire 2 employees, and the net benefit will be \$25,426 (= \$42,426 - 9,000).

87. The table below shows how total donations, average donations, total labor costs and average labor costs vary depending on the number of employees State U hires for its fundraising activities.

Number of Employees	Total Donations	Average Donations	Total Labor Costs	Average Labor Costs
1	\$30,000			\$8,000
2	\$42,426		\$17,000	
3		\$17,321	\$27,000	
4	\$60,000			\$9,500
5		\$13,416	\$50,000	

The net benefit of hiring fundraisers is largest when _____ employees are hired.

- A. 4
- B. 3
- C. 2
- D. 1

Ans: C

Difficulty: 03 Hard

Learning Objective: 01-03

Topic: Three Important Decision Pitfalls

Blooms: Analyze

AACSB: Analytic

Feedback: When more than 2 employees are hired, their marginal cost exceeds their marginal benefit.

88. Ginger bought a phone that came with a \$10 rebate. Ginger should fill out and mail in the rebate form if:

- A. the opportunity cost of the time and trouble of sending in the rebate form is less than \$10.
- B. the opportunity cost of the time and trouble of sending in the rebate form is more than \$10.
- C. she would have bought the phone without the rebate, and so sending in the rebate form involves no opportunity cost.
- D. Ginger's surplus from purchasing the phone was less than \$10.

Ans: A

Difficulty: 02 Medium

Learning Objective: 01-03

Topic: Three Important Decision Pitfalls

Blooms: Understand

AACSB: Reflective Thinking

Feedback: Ginger should disregard the sunk cost of the phone and consider only the marginal benefit of receiving the rebate with the marginal cost of sending in the form.

89. Tony notes that an electronics store is offering a flat \$20 off all prices in the store. Tony reasons that if he wants to buy something with a price of \$50, then it is a good offer, but if he wants to buy something with a price of \$500, then it is not a good offer. This is an example of:

- A. inconsistent reasoning; saving \$20 is saving \$20.
- B. the proper application of the Cost-Benefit Principle.
- C. rational choice because saving 40% is better than saving 4%.
- D. inconsistent reasoning because prices are sunk costs.

Ans: A

Difficulty: 02 Medium

Learning Objective: 01-03

Topic: Three Important Decision Pitfalls

Blooms: Understand

AACSB: Reflective Thinking

Feedback: In applying the Cost-Benefit Principle, it is a common decision pitfall to consider proportions rather than the amount saved.

90. Suppose a retail store was offering 10% off list prices on all goods. The benefit of the 10% savings is:

- A. unrelated to the list price of the good.
- B. negatively related to the list price of the good.
- C. positively related to the list price of the good.
- D. zero since costs and benefits shouldn't be measured proportionally.

Ans: C

Difficulty: 02 Medium

Learning Objective: 01-03

Topic: Three Important Decision Pitfalls

Blooms: Understand

AACSB: Reflective Thinking

Feedback: The higher is the list price, the more you save.

91. A firm pays Pam \$40 per hour to assemble personal computers. Each day, Pam can assemble 4 computers if she works 1 hour, 7 computers if she works 2 hours, 9 computers if she works 3 hours, and 10 computers if she works 4 hours. Pam cannot work more than 4 hours day. Each computer consists of a motherboard, a hard drive, a case, a monitor, a keyboard, and a mouse. The total cost of these parts is \$600 per computer. What is the marginal cost of producing the computers that Pam can assemble during her 3rd hour of work?

- A. \$5,400
- B. \$5,520
- C. \$1,200

D. \$1,240

Ans: D

Difficulty: 03 Hard

Learning Objective: 01-03

Topic: Three Important Decision Pitfalls

Blooms: Apply

AACSB: Analytic

Feedback: Pam produces 2 additional computers in her 3rd hour. The cost of the parts for these computers is \$1,200 ($= 2 \times \600). In addition, the firm has to pay Pam \$40 for that hour. Thus, the marginal cost of producing the computers that Pam can assemble in her 3rd hour is \$1,240.

92. A firm pays Pam \$40 per hour to assemble personal computers. Each day, Pam can assemble 4 computers if she works 1 hour, 7 computers if she works 2 hours, 9 computers if she works 3 hours, and 10 computers if she works 4 hours. Pam cannot work more than 4 hours day. Each computer consists of a motherboard, a hard drive, a case, a monitor, a keyboard, and a mouse. The total cost of these parts is \$600 per computer. What is the marginal cost of producing the computers that Pam can assemble during her 2nd hour of work?

A. \$1,800

B. \$1,840

C. \$4,200

D. \$4,280

Ans: B

Difficulty: 03 Hard

Learning Objective: 01-03

Topic: Three Important Decision Pitfalls

Blooms: Apply

AACSB: Analytic

Feedback: Pam produces 3 additional computers in her 2nd hour. The cost of the parts for these computers is \$1,800 ($= 3 \times \600). In addition, the firm has to pay Pam \$40 for that hour. Thus, the marginal cost of producing the computers that Pam can assemble in her 2nd hour is \$1,840.

93. A firm pays Pam \$40 per hour to assemble personal computers. Each day, Pam can assemble 4 computers if she works 1 hour, 7 computers if she works 2 hours, 9 computers if she works 3 hours, and 10 computers if she works 4 hours. Pam cannot work more than 4 hours day. Each computer consists of a motherboard, a hard drive, a case, a monitor, a keyboard, and a mouse. The total cost of these parts is \$600 per computer. If the firm sells each computer for \$625, then how many hours a day should the firm employ Pam to maximize its net benefit from her employment?

A. 1 hour

B. 2 hours

C. 3 hours

D. 4 hours

Ans: C

Difficulty: 03 Hard

Learning Objective: 01-03

Topic: Three Important Decision Pitfalls

Blooms: Analyze

AACSB: Analytic

Feedback: The marginal benefit of the first hour of work is greater than its marginal cost. That is, the marginal cost of the first hour is \$2,440 (= \$2,400 for parts + \$40 for labor), and the marginal benefit is \$2,500 (= 4 × \$625). Marginal benefit is also greater than marginal cost for the 2nd and 3rd hours of work. For the 4th hour of work, however, marginal benefit is less than marginal cost. Thus, the firm should employ Pam for 3 hours a day.

94. A firm pays Pam \$40 per hour to assemble personal computers. Each day, Pam can assemble 4 computers if she works 1 hour, 7 computers if she works 2 hours, 9 computers if she works 3 hours, and 10 computers if she works 4 hours. Pam cannot work more than 4 hours day. Each computer consists of a motherboard, a hard drive, a case, a monitor, a keyboard, and a mouse. The total cost of these parts is \$600 per computer. If the firm sells each computer for \$650, then how many hours a day should the firm employ Pam to maximize its net benefit from her employment?

- A. 1 hour
- B. 2 hours
- C. 3 hours
- D. 4 hours

Answer: D

Difficulty: 03 Hard

Learning Objective: 01-03

Topic: Three Important Decision Pitfalls

Blooms: Analyze

AACSB: Analytic

Feedback: The marginal benefit of the first hour of work is greater than the marginal cost. That is, the marginal cost of the first hour is \$2,440 (= \$2,400 for parts + \$40 for labor), and the marginal benefit is \$2,600 (= 4 × \$650). Marginal benefit is also greater than or equal to marginal cost for the 2nd, 3rd and 4th hours of work. Thus, the firm should employ Pam for 4 hours.

95. A firm pays Pam \$40 per hour to assemble personal computers. Each day, Pam can assemble 4 computers if she works 1 hour, 7 computers if she works 2 hours, 9 computers if she works 3 hours, and 10 computers if she works 4 hours. Pam cannot work more than 4 hours day. Each computer consists of a motherboard, a hard drive, a case, a monitor, a keyboard, and a mouse. The total cost of these parts is \$600 per computer. If Jane works for 6 hours she can rent out 9 apartments, and if she works for 7 hours she can rent out 12 apartments. The marginal benefit of Jane's 7th hour of work equals:

- A. 12 apartments
- B. 9 apartments
- C. 3 apartments
- D. 1 apartment

Ans: C

Difficulty: 03 Hard

Learning Objective: 01-03

Topic: Three Important Decision Pitfalls

Blooms: Apply
AACSB: Analytic

Feedback: Marginal benefit is the increase in total benefit that results from carrying out one additional unit of an activity.

96. The following table shows the relationship between the speed of a computer's CPU and its benefits and costs. Assume that all other features of the computer are the same (that is, CPU speed is the only source of variation), and only the CPU speeds listed below are available for purchase.

CPU GHz	Total Benefit	Marginal Benefit	Total Cost	Marginal Cost
2.0	\$1,000		\$900	
2.5	\$1,400			\$100
3.0		\$300	\$1,200	
3.5	\$1,900		\$1,500	
4.0	\$2,000			\$400

The marginal benefit of upgrading from a 2.0GHz computer to a 2.5GHz computer is:

- A. \$1,400.
- B. \$1,000.
- C. \$400.
- D. \$100.

Ans: C

Difficulty: 02 Medium

Learning Objective: 01-03

Topic: Three Important Decision Pitfalls

Blooms: Understand

AACSB: Reflective Thinking

Feedback: Going from a 2.0GHz to a 2.5GHz computer increases total benefit from \$1,000 to \$1,400, so the marginal benefit is \$400.

97. The following table shows the relationship between the speed of a computer's CPU and its benefits and costs. Assume that all other features of the computer are the same (that is, CPU speed is the only source of variation), and only the CPU speeds listed below are available for purchase.

CPU GHz	Total Benefit	Marginal Benefit	Total Cost	Marginal Cost
2.0	\$1,000		\$900	
2.5	\$1,400			\$100
3.0		\$300	\$1,200	
3.5	\$1,900		\$1,500	
4.0	\$2,000			\$400

The total benefit of a 3.0GHz computer is:

- A. \$300.

- B. \$900.
- C. \$1,700.
- D. \$1,650.

Ans: C

Difficulty: 02 Medium

Learning Objective: 01-03

Topic: Three Important Decision Pitfalls

Blooms: Understand

AACSB: Reflective Thinking

Feedback: To find total benefit of a 3.0GHz computer, add the marginal benefit of a 3.0GHz computer to the total benefit of 2.5GHz computer.

98. The following table shows the relationship between the speed of a computer's CPU and its benefits and costs. Assume that all other features of the computer are the same (that is, CPU speed is the only source of variation), and only the CPU speeds listed below are available for purchase.

CPU GHz	Total Benefit	Marginal Benefit	Total Cost	Marginal Cost
2.0	\$1,000		\$900	
2.5	\$1,400			\$100
3.0		\$300	\$1,200	
3.5	\$1,900		\$1,500	
4.0	\$2,000			\$400

The total cost of a 2.5GHz computer is:

- A. \$1,000.
- B. \$900.
- C. \$200.
- D. \$100.

Ans: A

Difficulty: 02 Medium

Learning Objective: 01-03

Topic: Three Important Decision Pitfalls

Blooms: Understand

AACSB: Reflective Thinking

Feedback: To find the total cost of a 2.5GHz computer, add the marginal cost of a 2.5GHz computer to the total cost of a 2.0GHz computer.

99. The following table shows the relationship between the speed of a computer's CPU and its benefits and costs. Assume that all other features of the computer are the same (that is, CPU speed is the only source of variation), and only the CPU speeds listed below are available for purchase.

CPU GHz	Total Benefit	Marginal Benefit	Total Cost	Marginal Cost
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2.0	\$1,000		\$900	
2.5	\$1,400			\$100
3.0		\$300	\$1,200	
3.5	\$1,900		\$1,500	
4.0	\$2,000			\$400

The marginal cost of upgrading from a 2.5GHz to 3.0GHz computer is:

- A. \$400.
- B. \$300.
- C. \$200.
- D. \$100.

Ans: C

Difficulty: 03 Hard

Learning Objective: 01-03

Topic: Three Important Decision Pitfalls

Blooms: Apply

AACSB: Analytic

Feedback: The total cost of a 2.5GHz computer is \$1000 (= \$900 + \$100). Thus, going from a 2.5GHz to a 3.0GHz computer increases total cost from \$1,000 to \$1,200, meaning that marginal cost is \$200.

100. The following table shows the relationship between the speed of a computer's CPU and its benefits and costs. Assume that all other features of the computer are the same (that is, CPU speed is the only source of variation), and only the CPU speeds listed below are available for purchase.

CPU GHz	Total Benefit	Marginal Benefit	Total Cost	Marginal Cost
2.0	\$1,000		\$900	
2.5	\$1,400			\$100
3.0		\$300	\$1,200	
3.5	\$1,900		\$1,500	
4.0	\$2,000			\$400

Application of the Cost-Benefit Principle would lead one to purchase a _____ computer.

- A. 2.0GHz
- B. 2.5GHz
- C. 3.0GHz
- D. 4.0GHz

Ans: C

Difficulty: 03 Hard

Learning Objective: 01-03

Topic: Three Important Decision Pitfalls

Blooms: Analyze

AACSB: Analytic

Feedback: At 3.0GHz and below, marginal benefit is greater than its marginal cost. But for 3.5GHz and above, marginal benefit is less than marginal cost. So, a 3.0GHz computer should be purchased.

101. The following table shows the relationship between the speed of a computer's CPU and its benefits and costs. Assume that all other features of the computer are the same (that is, CPU speed is the only source of variation), and only the CPU speeds listed below are available for purchase.

CPU GHz	Total Benefit	Marginal Benefit	Total Cost	Marginal Cost
2.0	\$1,000		\$900	
2.5	\$1,400			\$100
3.0		\$300	\$1,200	
3.5	\$1,900		\$1,500	
4.0	\$2,000			\$400

Choosing a 3.5GHz computer would be irrational because:

- A. its marginal benefit is less than its marginal cost.
- B. its marginal benefit is equal to its marginal cost.
- C. it is impossible to tell the difference compared to a 3.0GHz computer.
- D. its marginal benefit is greater than its marginal cost.

Ans: A

Difficulty: 03 Hard

Learning Objective: 01-03

Topic: Three Important Decision Pitfalls

Blooms: Analyze

AACSB: Analytic

Feedback: The marginal benefit of a 3.5GHz computer is \$200 ($=\$1,900 - \$1,700$), and its marginal cost is \$300 ($=\$1,500 - \$1,200$). Thus, its marginal benefit is less than its marginal cost.

102. Jack has a ticket to see Daughtry for which he paid \$30 yesterday. He takes an unpaid day off from work to get ready for the concert. When he arrives at the concert, five different people offer him \$70 for his ticket. Jack decides to keep his ticket. At the time he makes this decision, his opportunity cost of seeing Daughtry is:

- A. \$30 plus his forgone earnings.
- B. \$40.
- C. \$70.
- D. \$70 plus his forgone earnings.

Ans: C

Difficulty: 02 Medium

Learning Objective: 01-03

Topic: Three Important Decision Pitfalls

Blooms: Understand

AACSB: Reflective Thinking

Feedback: At the time he makes his decision, the ticket price and the lost day's pay are sunk

costs. Keeping the ticket requires sacrificing the \$70 he was offered for it.

103. Jody has purchased a non-refundable \$75 ticket to attend a Miley Cyrus concert on Friday night. Subsequently, she is asked to go to out dinner at no expense to her. If she uses cost-benefit analysis to choose between going to the concert and going out to dinner, the opportunity cost of going out to dinner should include:

- A. only the entertainment value of the concert.
- B. the cost of the ticket plus the entertainment value of the concert.
- C. only the cost of concert ticket.
- D. neither the cost of the ticket nor the entertainment value of the concert.

Ans: A

Difficulty: 02 Medium

Learning Objective: 01-03

Topic: Three Important Decision Pitfalls

Blooms: Understand

AACSB: Reflective Thinking

Feedback: The price of the non-refundable ticket is a sunk cost, so the only thing that Jody should include in calculating the opportunity cost of going out to dinner, is the entertainment value of the concert.

104. You won a free ticket to see the latest Star Trek movie this Friday night (which you can costlessly resell for its face value of \$15). Your favorite band is also performing on Friday and is your only alternative activity. Friday is your last chance to see either the movie or the band. Tickets to see your favorite band cost \$30, and on any given day, you would be willing to pay as much as \$50 for a ticket. Based on this information, what is your opportunity cost of going to see the Star Trek movie on Friday?

- A. \$0
- B. \$30
- C. \$35
- D. \$50

Ans: C

Difficulty: 02 Medium

Learning Objective: 01-03

Topic: Three Important Decision Pitfalls

Blooms: Understand

AACSB: Reflective Thinking

Feedback: The opportunity cost of seeing the movie is the economic surplus you give up by not seeing your favorite band ($\$50 - \$30 = \$20$) plus the \$15 you could have received by selling your movie ticket.

105. You want to buy a TV that regularly costs \$250. You can either buy the TV from a nearby store or from a store that's downtown. Relative to going to the nearby store, driving downtown involves additional time and gas. The downtown store, however, has a 10% off sale this week. Last week you drove downtown to save \$20 on some concert tickets, a 15% savings. Should you

drive downtown to buy the TV?

- A. Yes, because you will save 10%, which is better than nothing.
- B. No, because you will save more than \$20.
- C. Yes, because you will save more than \$20.
- D. No, because you will only save 10%, which is less than 15%.

Ans: C

Difficulty: 03 Hard

Learning Objective: 01-03

Topic: Three Important Decision Pitfalls

Blooms: Analyze

AACSB: Analytic

Feedback: The information indicates that you are willing to drive downtown to save \$20, so you should also be willing to drive downtown to save \$25.

106. The table below shows the relationship between the number of times you get your car washed each month and your total monthly benefit from car washes. Each car wash costs \$15.

Number of Car Washes Per Month	Total Monthly Benefit from Car Washes
0	\$0
1	\$20
2	\$36
3	\$48
4	\$56
5	\$60



What's the average benefit of 4 car washes per month?

- A. \$14
- B. \$12
- C. \$8
- D. \$4

Ans: A

Difficulty: 03 Hard

Learning Objective: 01-03

Topic: Three Important Decision Pitfalls

Blooms: Apply

AACSB: Analytic

Feedback: The average benefit of undertaking n units of an activity is the total benefit of undertaking n units divided by n . Thus, in the case, the average benefit is \$14 ($=\$56/4$).

107. The table below shows the relationship between the number of times you get your car washed each month and your total monthly benefit from car washes. Each car wash costs \$15.

Number of	Total Monthly
-----------	---------------

Car Washes Per Month	Benefit from Car Washes
0	\$0
1	\$20
2	\$36
3	\$48
4	\$56
5	\$60



What is the marginal cost of the 5th car wash each month?

- A. \$15
- B. \$14
- C. \$12
- D. \$4

Ans: A

Difficulty: 02 Medium

Learning Objective: 01-03

Topic: Three Important Decision Pitfalls

Blooms: Understand

AACSB: Reflective Thinking

Feedback: Each car wash costs \$15, so the marginal cost of a car wash is always \$15.

108. The table below shows the relationship between the number of times you get your car washed each month and your total monthly benefit from car washes. Each car wash costs \$15.

Number of Car Washes Per Month	Total Monthly Benefit from Car Washes
0	\$0
1	\$20
2	\$36
3	\$48
4	\$56
5	\$60



What is the marginal benefit of the 3rd car wash each month?

- A. \$4
- B. \$12
- C. \$16
- D. \$48

Ans: B

Difficulty: 02 Medium

Learning Objective: 01-03

Topic: Three Important Decision Pitfalls

Blooms: Understand

AACSB: Reflective Thinking

Feedback: Going from 2 to 3 car washes increases total benefit from \$36 to \$48, so the marginal benefit of the 3rd car wash is \$12.

109. The table below shows the relationship between the number of times you get your car washed each month and your total monthly benefit from car washes. Each car wash costs \$15.

Number of Car Washes Per Month	Total Monthly Benefit from Car Washes
0	\$0
1	\$20
2	\$36
3	\$48
4	\$56
5	\$60

How many times a month should you get your car washed?

A. 1

B. 2

C. 3

D. 4

Ans: B

Difficulty: 03 Hard

Learning Objective: 01-03

Topic: Three Important Decision Pitfalls

Blooms: Evaluate

AACSB: Analytic

Feedback: The marginal cost of a car wash is always \$15. The marginal benefit of the 1st car wash is \$20, the marginal benefit of 2nd is \$16, the marginal benefit of the 3rd is \$12, the marginal benefit of the 4th is \$8, and the marginal benefit of the 5th is \$4. Thus, marginal benefit is less than marginal cost after the second car wash.

110. Frank owns an apple farm and plans to spend 4 hours today picking apples. The number of apples he can pick per hour depends on the total number of hours he spends working in either the east orchard or the west orchard in the manner shown in the table below.

Hours in East Orchard	Number of Apples Per Hour	Hours in West Orchard	Number of Apples Per Hour
1	40	1	10
2	32	2	10
3	25	3	10
4	20	4	10

If Frank spends 2 hours picking apples in the east orchard and 2 hours picking apples in the west orchard, how many apples in total will Frank be able to pick today?

- A. 21
- B. 42
- C. 84
- D. 92

Ans: C

Difficulty: 03 Hard

Learning Objective: 01-03

Topic: Three Important Decision Pitfalls

Blooms: Apply

AACSB: Analytic

Feedback: Frank will be able to pick 64 ($= 2 \times 32$) apples in the east orchard and 20 ($= 2 \times 10$) apples in the West orchard, or 84 apples in total.

111. Frank owns an apple farm and plans to spend 4 hours today picking apples. The number of apples he can pick per hour depends on the total number of hours he spends working in either the east orchard or the west orchard in the manner shown in the table below.

Hours in East Orchard	Number of Apples Per Hour	Hours in West Orchard	Number of Apples Per Hour
1	40	1	10
2	32	2	10
3	25	3	10
4	20	4	10

What is the opportunity cost to Frank of spending an additional hour picking apples in the East orchard?

- A. 10 apples
- B. 20 apples
- C. 30 apples
- D. 40 apples

Ans: A

Difficulty: 02 Medium

Learning Objective: 01-03

Topic: Three Important Decision Pitfalls

Blooms: Understand

AACSB: Reflective Thinking

Feedback: If Frank spends an additional hour in the east orchard, he has to spend 1 less hour in the west orchard, during which time he could have picked 10 apples.

112. Frank owns an apple farm and plans to spend 4 hours today picking apples. The number of apples he can pick per hour depends on the total number of hours he spends working in either the east orchard or the west orchard in the manner shown in the table below.

Hours in East	Number of Apples Per	Hours in West	Number of Apples Per
---------------	----------------------	---------------	----------------------

Orchard	Hour	Orchard	Hour
1	40	1	10
2	32	2	10
3	25	3	10
4	20	4	10

What is the marginal benefit to Frank of the 2nd hour he spends picking in the east orchard?

- A. 8 apples
- B. 24 apples
- C. 32 apples
- D. 64 apples

Ans: B

Difficulty: 03 Hard

Learning Objective: 01-03

Topic: Three Important Decision Pitfalls

Blooms: Apply

AACSB: Analytic

Feedback: If Frank spends 1 hour in the east orchard he can pick 40 apples. If he spends 2 hours in the east orchard, he can pick 64 (= 32 × 2) apples. Thus, the marginal benefit of the 2nd hour he spends picking in the east orchard is 24 (= 64 - 40).

113. Frank owns an apple farm and plans to spend 4 hours today picking apples. The number of apples he can pick per hour depends on the total number of hours he spends working in either the east orchard or the west orchard in the manner shown in the table below.

Hours in East Orchard	Number of Apples Per Hour	Hours in West Orchard	Number of Apples Per Hour
1	40	1	10
2	32	2	10
3	25	3	10
4	20	4	10

How should Frank divide his time between the east and the west orchard?

- A. He should spend all 4 hours in the east orchard.
- B. He should spend 3 hours in the east orchard and 1 hour in the west orchard.
- C. He should spend 2 hours in east orchard and 2 hours in the west orchard.
- D. He should spend 1 hour in the east orchard and 3 hours in the west orchard.

Ans: B

Difficulty: 03 Hard

Learning Objective: 01-03

Topic: Three Important Decision Pitfalls

Blooms: Analyze

AACSB: Analytic

Feedback: The marginal cost to Frank of spending an additional hour in the east orchard is always 10 apples. His marginal benefit of spending the first hour in the west orchard is 40

apples; his marginal benefit of the 2nd hour is 24 apples ($= (32 \times 2) - 40$); his marginal benefit of the 3rd hour is 11 apples ($= (25 \times 3) - (32 \times 2)$); and his marginal benefit of the 4th hour is 5 apples ($= (20 \times 4) - (25 \times 3)$). So the marginal benefit of the 1st, 2nd and 3rd hour in the east orchard is greater than its marginal cost. But, the marginal benefit of the 4th hour is less than its marginal cost.

114. Positive economic principles are those that:

- A. are always correct.
- B. are influenced by political ideology.
- C. indicate how people should behave.
- D. predict how people will behave.

Ans: D

Difficulty: 01 Easy

Learning Objective:

Topic: Normative Economics Versus Positive Economics

Blooms: Remember

AACSB: Reflective Thinking

Feedback: By definition, positive economic principles predict how people will behave, and normative economic principles indicate how they should behave.

115. One thing that distinguishes normative economic principles from positive economic principles is that:

- A. normative principles are pessimistic and positive principles are optimistic.
- B. normative principles reflect social norms, and positive principles reflect universal truths.
- C. normative principles tell us how people should behave, and positive principles tell us how people will behave.
- D. normative principles tell us how people will behave, and positive principles tell us how people should behave.

Ans: C

Difficulty: 01 Easy

Learning Objective:

Topic: Normative Economics Versus Positive Economics

Blooms: Remember

AACSB: Reflective Thinking

Feedback: Normative economic principles describe how people should behave; positive economic principles predict how they will behave.

116 . Normative economic principles are concerned with how people _____ make decisions while positive economic principles are concerned with how people _____ make decisions.

- A. do; should
- B. should; do
- C. in power; in ordinary life
- D. in ordinary life; in power

Ans: B

Difficulty: 01 Easy

Learning Objective:

Topic: Normative Economics Versus Positive Economics

Blooms: Remember

AACSB: Reflective Thinking

Feedback: Normative economic principles describe how people should behave; positive economic principles predict how they will behave.

117. An editorial in the paper argues that a person only should be allowed to attend school if the marginal cost of educating that person is less than the marginal benefit of educating that person.

The writer's reasoning is an application of:

- A. positive economics.
- B. negative economics.
- C. normative economics.
- D. economic naturalism.

Ans: C

Difficulty: 02 Medium

Learning Objective:

Topic: Normative Economics Versus Positive Economics

Blooms: Understand

AACSB: Reflective Thinking

Feedback: Normative economic principles describe how people should behave; positive economic principles predict how they will behave. The editorial includes the word "should".

118. The Cost-Benefit Principle predicts that a person:

- A. is more likely to take an action if its cost increases.
- B. is more likely to take an action if its benefit increases.
- C. should take an action if its cost increases.
- D. should take an action if its benefit increases.

Ans: B

Difficulty: 01 Easy

Learning Objective:

Topic: Normative Economics Versus Positive Economics

Blooms: Remember

AACSB: Reflective Thinking

Feedback: Although the Cost-Benefit Principle is a normative economic principle, it also predicts that people will be more likely to take an action when its benefit rises, and less likely to take an action when its cost rises.

119. The Cost-Benefit Principle is:

- A. not an economic principle.
- B. neither a positive nor a normative economic principle.
- C. a positive economic principle.
- D. a normative economic principle.

Ans: C

Difficulty: 01 Easy

Learning Objective:

Topic: Normative Economics Versus Positive Economics

Blooms: Remember

AACSB: Reflective Thinking

Feedback: The Cost-Benefit Principle states how people *should* behave. Thus, it is a normative economic principle.

120. The Cost-Benefit Principle predicts that people will be less likely to smoke if the government:

- A. increases taxes on smoking-cessation devices such as nicotine patches.
- B. increases taxes on cigarettes, effectively raising the price.
- C. subsidizes hospitals treating lung disease.
- D. invests more money in cancer research.

Ans: B

Difficulty: 02 Medium

Learning Objective:

Topic: Normative Economics Versus Positive Economics

Blooms: Understand

AACSB: Reflective Thinking

Feedback: The Cost-Benefit Principle predicts that a person is more likely to take an action if its benefit rises, and less likely to do something if its cost rises.

121. The Cost-Benefit Principle predicts that:

- A. no one will perform volunteer services.
- B. people will always take the highest-paying job they are offered.
- C. benefits are more important than costs in making a decision.
- D. people will tend to do more of something when its benefits are greater.

Ans: D

Difficulty: 01 Easy

Learning Objective:

Topic: Normative Economics Versus Positive Economics

Blooms: Remember

AACSB: Reflective Thinking

Feedback: The Cost-Benefit Principle predicts that a person will be more likely to take an action when its benefit rises, and less likely to take an action when its cost rises.

122. Microeconomics differs from macroeconomics in that microeconomics focuses on:

- A. the performance of the entire economy.
- B. issues such as inflation, unemployment and economic growth.
- C. the choices made by individuals the implications of those choices.
- D. government policies designed improve the performance of the national economy.

Ans: C

Difficulty: 01 Easy

Learning Objective:

Topic: Economics: Micro and Macro

Blooms: Remember

AACSB: Reflective Thinking

Feedback: Microeconomics is the study of individual choice under scarcity and its implications

for the behavior of prices and quantities in individual markets.

123. Macroeconomics differs from microeconomics in that macroeconomics focuses on:

- A. individual choices and group behavior in individual markets.
- B. the performance of national economies and ways to improve that performance.
- C. production in specific markets.
- D. prices in specific markets.

Ans: B

Difficulty: 01 Easy

Learning Objective:

Topic: Economics: Micro and Macro

Blooms: Remember

AACSB: Reflective Thinking

Feedback: Macroeconomics is the study of the performance of national economies and the policies that governments use to try to improve that performance.

124. The study of individual choice and its implications for the behavior of prices and quantities in individual markets is:

- A. microeconomics.
- B. a normative economic principle.
- C. the Scarcity Principle.
- D. macroeconomics.

Ans: A

Difficulty: 01 Easy

Learning Objective:

Topic: Economics: Micro and Macro

Blooms: Remember

AACSB: Reflective Thinking

Feedback: Microeconomics is the study of individual choice under scarcity and its implications for the behavior of prices and quantities in individual markets.

125. Which branch of economics is most likely to study differences in countries' growth rates?

- A. microeconomics
- B. normative economics
- C. macroeconomics
- D. experimental economics

Ans: C

Difficulty: 01 Easy

Learning Objective:

Topic: Economics: Micro and Macro

Blooms: Remember

AACSB: Reflective Thinking

Feedback: Macroeconomics is the study of the performance of national economies and the policies that governments use to try to improve that performance.

126. Which of the following would *not* be studied in microeconomics?

- A. How individual firms decide how much to produce.
- B. Whether to study or watch TV tonight.
- C. How an early freeze in California will affect the price of fruit.
- D. Whether the federal budget should be balanced.

Ans: D

Difficulty: 02 Medium

Learning Objective:

Topic: Economics: Micro and Macro

Blooms: Understand

AACSB: Reflective Thinking

Feedback: The federal budget is a topic related to the performance of the national economy, and therefore is a macroeconomic topic. The other issues relate to individual choices and individual markets, and so are microeconomic topics.

127. Which of the following would *not* be studied in macroeconomics?

- A. The causes of the Great Depression.
- B. The growth rate of the US economy.
- C. How a sharp increase in gasoline prices is likely to affect SUV sales.
- D. The impact of government spending on the economy.

Ans: C

Difficulty: 02 Medium

Learning Objective:

Topic: Economics: Micro and Macro

Blooms: Understand

AACSB: Reflective Thinking

Feedback: Macroeconomics is the study of the performance of national economies and the policies that governments use to try to improve that performance. SUV sales are directly related to individuals' choices about what to consume, and so are a microeconomic topic.

128. By convention, there are two major divisions of economics, called:

- A. marginal benefit and marginal cost.
- B. reservation price and opportunity cost.
- C. microeconomics and macroeconomics.
- D. rational economics and irrational economics.

Ans: C

Difficulty: 01 Easy

Learning Objective:

Topic: Economics: Micro and Macro

Blooms: Remember

AACSB: Reflective Thinking

Feedback: The two main categories of economic study are macroeconomics and

microeconomics.

129. A study that deals with the salaries of university professors would be considered:

- A. macroeconomics
- B. microeconomics
- C. economic naturalism
- D. real economics

Ans: B

Difficulty: 01 Easy

Learning Objective:

Topic: Economics: Micro and Macro

Blooms: Remember

AACSB: Reflective Thinking

Feedback: The study of individual markets, such as the market for professors, is part of microeconomics.

131. In deciding how many guitars to buy for his shop before the Christmas season, Mark is making a(n) _____ decision.

- A. microeconomic
- B. macroeconomic
- C. normative
- D. irrational

Ans: A

Difficulty: 01 Easy

Learning Objective:

Topic: Economics: Micro and Macro

Blooms: Remember

AACSB: Reflective Thinking

Feedback: Microeconomics focuses on individual choices.

132. A study of the impact of various government policies on economic growth would be considered:

- A. microeconomics.
- B. macroeconomics.
- C. government economics.
- D. marginal economics.

Ans: B

Difficulty: 01 Easy

Learning Objective:

Topic: Economics: Micro and Macro

Blooms: Remember

AACSB: Reflective Thinking

Feedback: Macroeconomics is the study of the performance of national economies and the policies that governments use to try to improve that performance.

133. The field of economics that would be most concerned with a recent fall in interest rates is:

- A. microeconomics.
- B. macroeconomics.
- C. economic naturalism.
- D. marginal economics.

Ans: B

Difficulty: 01 Easy

Learning Objective:

Topic: Economics: Micro and Macro

Blooms: Remember

AACSB: Reflective Thinking

Feedback: Macroeconomics focuses on overall national economic growth and factors that affect the overall economy such as the impact of changing interest rates on total spending in the economy.

134. An economic naturalist is someone who:

- A. uses economic arguments to protect the environment.
- B. has an innate talent for using economic concepts.
- C. applies economic insights to understand everyday life.
- D. studies the process of natural selection in a cost-benefit framework.

Ans: C

Difficulty: 01 Easy

Learning Objective:

Topic: Economic Naturalism

Blooms: Remember

AACSB: Reflective Thinking

Feedback: An economic naturalist is someone who uses insights from economics to make sense of observations from everyday life.

135. With ATMs, it is possible to retrieve cash from the bank at any time. One hundred years ago, one could only get cash from the bank during business hours, say, 9 am to 3 pm. The present availability of 24-hour service has arisen because:

- A. flexibility was not valued 100 years ago.
- B. it was impossible to provide 24-hour service 100 years ago.
- C. the cost of providing 24-hour service is much lower today.
- D. government forced banks to become more convenient.

Ans: C

Difficulty: 02 Medium

Learning Objective:

Topic: Economic Naturalism

Blooms: Understand

AACSB: Reflective Thinking

Feedback: According to the Cost-Benefit Principle, since the cost of providing 24-hour service

has fallen (due to technological innovations such as ATMs), we would expect more banks to provide 24-hour service now than 100 years ago.

136. The number of US households with access to the Internet is growing rapidly. Compared to 50 years ago, one would predict that when considering a major purchase, people today will gather:

- A. less information because the Internet has lowered the cost of gathering information.
- B. less information because the Internet has increased the benefit of gathering information.
- C. more information because the Internet has lowered the cost of gathering information.
- D. more information because the Internet has increased the cost of gathering information.

Ans: C

Difficulty: 02 Medium

Learning Objective:

Topic: Economic Naturalism

Blooms: Understand

AACSB: Reflective Thinking

Feedback: According to the Cost-Benefit Principle, since the cost of gathering information has fallen, we would expect people today to gather more information today compared to 50 years ago.

137. Every time you go to the grocery store, you try to wait in the shortest line. But the lines always seem to be roughly the same length. Why?

- A. Random chance equalizes the length of the lines.
- B. Other people are trying to choose the shortest line too.
- C. The cashiers work at the same speed.
- D. The cashiers do not have an incentive to work faster.

Ans: B

Difficulty: 01 Easy

Learning Objective:

Topic: Economic Naturalism

Blooms: Remember

AACSB: Reflective Thinking

Feedback: According to the Cost-Benefit Principle, we would expect people to try to wait in the shortest line (where the time cost of waiting is the lowest). So, if one line happens to be shorter than the others, customers will quickly join that line.

139. Suppose there are two parallel highways between two cities with approximately equal traffic. What would you expect to happen if the state began charging tolls to drive on one of those highways?

- A. More drivers would drive on the non-toll road, making the toll road less congested.
- B. More drivers would drive on the toll road making the non-toll road less congested.
- C. Traffic would remain evenly divided between the two roads as drivers continuously sought the less-congested route.
- D. Traffic would decrease on both roads.

Ans: A

Difficulty: 01 Easy

Learning Objective: 01-02

Topic: Applying the Cost-Benefit Principle

Blooms: Remember

AACSB: Reflective Thinking

Feedback: According to the Cost-Benefit Principle, in response to higher costs on the toll road, we would expect fewer people to use the toll road.

140. During times of high unemployment, colleges often observe an increase in enrollment even if tuition remains unchanged. Why?

- A. Students go to college even when the net benefit is negative.
- B. The opportunity cost of attending college is lower when unemployment is high.
- C. The opportunity cost of attending college is higher when unemployment is high.
- D. The benefit of attending college is lower because college graduates are less likely to find jobs.

Ans: B

Difficulty: 02 Medium

Learning Objective:

Topic: Economic Naturalism

Blooms: Understand

AACSB: Reflective Thinking

Feedback: According to the Cost-Benefit Principle, if we observe more people going to college, then it is likely because either the benefit of going to college has gone up, or the cost of going to college has gone down. An increase in the unemployment rate lowers the opportunity cost of going to college because individuals who otherwise might have preferred to work, will be less able to find jobs.

141. The last time gas prices increased drastically, sales of large Sport Utility Vehicles (SUVs) fell. Why?

- A. Higher gas prices lowered the benefit of driving an SUV.
- B. Higher gas prices increased the benefit of driving an SUV.
- C. Higher gas prices increased the cost of driving a SUV.
- D. Higher gas prices lowered the cost of driving a SUV.

Ans: C

Difficulty: 02 Medium

Learning Objective:

Topic: Economic Naturalism

Blooms: Understand

AACSB: Reflective Thinking

Feedback: According to the Cost-Benefit Principle, an increase in gas prices will increase the cost of driving an SUV, leading fewer people to purchase them.

142. Due to the fact that Curly used his frequent flyer miles to fly to visit Moe, Curly told Moe that it didn't cost him anything to visit. Is Curly correct?

- A. Yes, because Curly's frequent flyer miles made the trip free.
- B. Yes, because Curly could stay at Moe's house for free.
- C. No, because Curly could have used his frequent flyer miles to go somewhere else instead.
- D. No, because Curly had to pay for earlier trips in order to earn the frequent flyer miles.

Ans: C

Difficulty: 02 Medium

Learning Objective: 01-03

Topic: Three Important Decision Pitfalls

Blooms: Understand

AACSB: Reflective Thinking

Feedback: Curly gave up something of value (a different trip using his frequent flyer miles) to visit Moe.

143. Pat can either drive to work, which takes half an hour and uses \$1.50 worth of gas, or take the bus, which takes an hour and costs \$1.00. How should Pat get to work?

A. Pat should take the bus because it costs \$0.50 less than driving.

B. Pat should drive because it saves half an hour relative to taking the bus.

C. Pat should drive if saving half an hour is worth \$0.50 or more.

D. Pat should take the bus if saving half an hour is worth \$0.50 or more.

Ans: C

Difficulty: 03 Hard

Learning Objective: 01-02

Topic: Applying the Cost-Benefit Principle

Blooms: Analyze

AACSB: Analytic

Feedback: According to the Cost-Benefit Principle, Pat should drive if the marginal benefit of driving (saving half an hour) is greater than its marginal cost (\$0.50).

144. You have two options for how to spend the afternoon. You can either go see a movie with your roommate or work as a tutor for the Math Department. From experience, you know that going to see a movie gives you \$20 worth of enjoyment, and with your student discount, a movie ticket only costs \$12. If you spend the afternoon working as a math tutor, you will get paid \$45. On a typical day, you wouldn't be willing to spend the afternoon working as a math tutor for less than \$35. What is your opportunity cost of seeing a movie this afternoon?

A. \$8

B. \$12

C. \$22

D. \$57

Ans: B

Difficulty: 03 Hard

Learning Objective: 01-03

Topic: Three Important Decision Pitfalls

Blooms: Apply

AACSB: Analytic

Feedback: The opportunity cost of seeing the movie is the \$12 you pay for a ticket, plus the foregone \$10 in economic surplus you would have received from working as a tutor.

145. You have two options for how to spend the afternoon. You can either go see a movie with your roommate or work as a tutor for the Math Department. From experience, you know that going to see a movie gives you \$20 worth of enjoyment, and with your student discount, a movie

ticket only costs \$12. If you spend the afternoon working as a math tutor, you will get paid \$45. On a typical day, you wouldn't be willing to spend the afternoon working as a math tutor for less than \$35. What is your economic surplus from working as a math tutor instead of going to the movies?

- A. \$8
- B. \$2
- C. \$22
- D. \$57

Ans: B

Difficulty: 03 Hard

Learning Objective: 01-03

Topic: Three Important Decision Pitfalls

Blooms: Apply

AACSB: Analytic

Feedback: The benefit of spending the afternoon working as a math tutor is \$10. The cost of spending the afternoon working as a math tutor is the \$8 in economic surplus you would have received by going to the movies. Thus, your economic surplus from working as a math tutor instead of going to the movies is \$2.

146. You have two options for how to spend the afternoon. You can either go see a movie with your roommate or work as a tutor for the Math Department. From experience, you know that going to see a movie gives you \$20 worth of enjoyment, and with your student discount, a movie ticket only costs \$12. If you spend the afternoon working as a math tutor, you will get paid \$45. On a typical day, you wouldn't be willing to spend the afternoon working as a math tutor for less than \$35. Should you go see a movie or work as a math tutor?

- A. You should work as a math tutor.
- B. You should go to the movies.
- C. You should do neither
- D. Both options are equally good.

Ans: A

Difficulty: 03 Hard

Learning Objective: 01-03

Topic: Three Important Decision Pitfalls

Blooms: Evaluate

AACSB: Analytic

Feedback: To determine your best choice, calculate the value of each option as if it were your only choice. In this case, your economic surplus from going to the movies would be \$8 (= \$20 - \$12) and your economic surplus from working as a math tutor would be \$10 (= \$45 - \$35). Thus, your economic surplus would be higher if you worked as a math tutor.