INSTRUCTOR'S MANUAL

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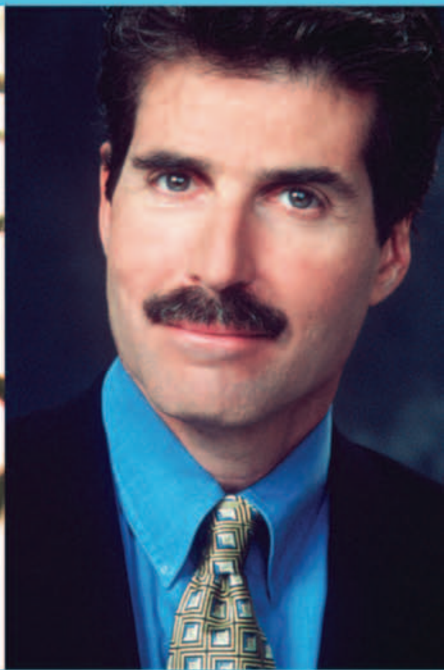

Teaching Tools for

MACROECONOMICS, Government and International Trade

from John Stossel

HIGH SCHOOL EDITION

Instructor's Manual to Accompany

Teaching Tools for MACROECONOMICS from JOHN STOSSEL

HIGH SCHOOL EDITION

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How to use the video clips effectively

This manual provides teachers with materials that will help them use the Stossel video clips more effectively in their classroom. The manual contains the following items for each clip:

(1) a list of the various concepts covered by the clip,
(2) a video description,
(3) the *Voluntary National Content Standards in Economics* that are covered,
(4) a preview question,
(5) discussion and analysis questions,
(6) an extension activity, and
(7) multiple-choice questions.

Many teachers will want to use the preview question to introduce the clip and focus the students on the major topic to be covered. Many preview questions encourage the students to share their opinions prior to viewing the video. After the video is shown, the discussion and analysis questions provide suggested focal points for additional discussion. The suggested answers help teachers bring up discussion points and are not designed to provide definitive answers to the questions. These questions may also be used to assess student understanding of the topics covered in the video clip. The extension activity can be used to reinforce the content of the clip. In some cases, this material is also appropriate for use as a homework assignment. Finally, the multiple-choice questions can be used to assess student understanding of the topic.

We believe that these video clips, along with selected use of materials from this manual, will help teachers enrich their classes and bring economic concepts more alive for their students.

Clip 1: Is life getting worse?
Length: 5:06

Concepts Illustrated:
Per capita GDP
Standard of living

Description:
This segment dispels the notion that life is worse or more difficult and risky today than in the past. The segment documents that most risks are greatly reduced from levels just a few years ago. Pollution levels and crime rates are down. Diseases such as diphtheria and rheumatic fever have virtually been eliminated while the flu, which killed 20 million people around 1918, has been contained. The type of work has changed from backbreaking farm labor to much easier means of employment. The fact is that America is the safest and most prosperous nation on Earth.

Voluntary National Content Standards in Economics

18. A nation's overall levels of income, employment, and prices are determined by the interaction of spending and production decisions made by all households, firms, government agencies, and others in the economy.

Preview Question:

"Is life in America better or worse than it was 100 years ago?"

Take a poll and ask a few students on each side to give reasons for their answers. Do not judge or direct their opinions.

Discussion and Analysis Questions:

1. Why do many people believe life is getting worse in America? (The media focus on problems such as crime, pollution, and poverty probably plays a role.)

2. How good were the good old days? (They were not very good. Throughout most of history, life has been "nasty, brutish, and short." In the United States 100 years ago, people died at earlier ages from infectious diseases that have now been conquered. The air and water were more polluted than today. Households did not have conveniences such as central heat, central plumbing, washing machines, or consumer electronics, to mention just a few items that many now take for granted.)

3. How is life better today? (Crime and pollution are down. Medical care is much better. Poverty is lower. Life expectancy is higher, and infant mortality is lower. Real wages are higher. Homes today have flush toilets, washers and driers, central heating and air conditioning, refrigerators, and dishwashers. Most people have color TVs, DVD and CD players, and cellular phones. The list could go on.)

Extension Activity: Wonderful Trends of the Past 100 Years

The following statistics are from Stephen Moore and Julian L. Simon, "The Greatest Century That Ever Was: 25 Miraculous Trends of the Past 100 Years," *Policy Analysis*, Cato Institute, Dec. 15, 1999. Stephen Moore was interviewed in the video. These statistics should make it clear to the students that life is much better today than it was 100 years ago.

25 WONDERFUL TRENDS OF THE 20TH CENTURY

TREND	1900-1920	1995-98
Life expectancy (years)	47	77
Infant mortality (deaths per 1,000 live births)	100	7
Deaths from infectious diseases (per 100,000 population)	700	50
Heart disease (age-adjusted deaths per 100,000 population)	307 (1950)	126
Per capita GDP (1998 dollars)	$4,800	$31,500
Manufacturing wage (1998 dollars)	$3.40	$12.50
Household assets (trillions of 1998 dollars)	$6 (1945)	$41
Poverty rate (percent of U.S. households)	40	13
Length of workweek (hours)	50	35
Agricultural workers (percent of workforce)	35	2.5
TV ownership (percent of U.S. households)	0	98
Homeownership (percent of U.S. households)	46	66
Electrification (percent of U.S. households)	8	99
Telephone calls (annual per capita calls)	40	2,300
Cars for transportation (percent of U.S. households)	1	91
Patents granted	25,000	150,000
High school completion (percent of adults)	22	88
Accidental deaths (per 100,000 population)	88	34
Wheat price (per bushel in hours of work)	4.1	0.2
Bachelor's degrees awarded to women (percent of degrees)	34	55
Black income (annual per capita, 1997 dollars)	$1,200	$12,400
Resident U.S. population (millions)	76	265
Air pollution (lead, micrograms per 100 cubic meters of air)	135 (1977)	4
Computer speed (millions of instructions per second)	0.02 (1976)	700
Computer ownership (percent of U.S. households)	1 (1980)	44

Questions for Discussion or Written Response

1. In your view, which three of the above statistics indicate the most important advancements? Why? (Answers will vary. The authors of the study say, "A central message of this study is that the fruits of a free society are prosperity, wealth, and better health.")

2. Are there any other statistics that you would want to see before concluding that life is better today?" If so, what would they be? (According to the study's authors, "there have been worrisome increases in family breakupS, abortions, illegitimate births, and teen suicide." Violent crime increased in the twentieth century before declining. You might ask the students for reasons that these trends occurred.)

3. Are there other improvements in life that are not included in these statistics? (There are many conveniences today that are not mentioned in these statistics. For example, ask your students how many of them have a DVD player, iPod, or TiVo.)

Multiple-Choice Questions:

1. Which of the following would be most appropriate for the measurement of differences in the average standard of living of people at different points in time?
   a. Nominal GDP.
   b. Real GDP.
   c. Nominal per capita GDP.
* d. Real per capita GDP.

2. As per capita GDP has risen over time in the United States and other countries, the
* a. life expectancy has increased.
   b. rate of illiteracy has increased.
   c. rate of infant mortality has increased.
   d. amount of leisure time has declined.

Is life getting worse?

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Questions for Discussion or Written Response

1. In your view, which three of the above statistics indicate the most important advancements? Why?
2. Are there any other statistics that you would want to see before concluding that life is better today? If so, what would they be?
3. Are there other improvements in life that are not included in these statistics?

Clip 2: Nominal values versus real values

Length: 2:45

Concepts Illustrated:
Adjusting nominal values for the effects of inflation
Real versus nominal figures

Description:

This segment clearly illustrates the error of comparing nominal (current) prices across time periods. Without adjusting for inflation, gas prices seem to be at their highest level. However, when adjusted for inflation, gas prices actually are lower than they were for most of the twentieth century. In addition, the segment brings out the point that a gallon of gas is cheaper than a gallon of ice cream or water. Some of the details of oil drilling and production are highlighted and compared to the relatively simple production processes of goods like water and ice cream.

Voluntary National Content Standards in Economics

18. A nation's overall levels of income, employment, and prices are determined by the interaction of spending and production decisions made by all households, firms, government agencies, and others in the economy.

19. Unemployment imposes costs on individuals and nations. Unexpected inflation imposes costs on many people and benefits some others because it arbitrarily redistributes purchasing power. Inflation can reduce the rate of growth of national living standards, because individuals and organizations use resources to protect themselves against the uncertainty of future prices.

Preview Question:

"Are gas prices higher today than in the past?"

Ask for a show of hands. Probably everyone will think "yes." Tell the students the video will provide the answer to the question, and the answer might not be as obvious as it seems.

Discussion and Analysis Questions:

1. What is the difference between a "real" and a "nominal" value? (A nominal value is in current dollars. A real value is adjusted for inflation.)

2. Why is the price of a gallon of gasoline lower today than 25 years ago? (When it is adjusted for inflation, the price of gasoline was higher in the past. In fact, the case can be made that gas prices today are lower than the prices of many other goods such as ice cream and water. People believe the price is higher because the media use nominal values to describe a more dramatic story.)

3. When making comparisons across time periods, why is it important to adjust for changes in the general level of prices? (The price of a good reflects the opportunity cost of obtaining the good. Changes in relative prices change the way resources are used because relative costs change. However, if the general level of prices has risen, nominal price changes may be a misleading indicator of what has happened to the relative price of a good. Even if the nominal price of a good has risen, its relative price might actually have changed in the opposite direction. It is important to compare GDP, income, and taxes in real values over time. Otherwise, we don't know what really happened. It may appear that people earn more during inflationary times, but that income doesn't necessarily buy more.)

Extension Activity: Nominal and Real Data

How can data from an earlier year be adjusted for changes in the general level of prices? This table shows the nominal price of a gallon of regular unleaded gasoline and data on the general level of prices as measured by the Consumer Price Index (CPI) for various years since 1973.

YEAR	NOMINAL PRICE OF GASOLINE	CPI (1982-84 = 100)
1973	$0.39	44.4
1980	$1.25	82.4
1990	$1.16	130.7
2000	$1.51	172.2
2005 (Nov.)	$2.34	197.6

The CPI is one measure of the general level of prices. Price and income data from an earlier year can be measured in terms of the price level of the later year by "inflating" the figure for the earlier year by the ratio of the CPI in the later year divided by the CPI of the earlier year. For example, the price of gasoline in 1973 can be measured in terms of the general level of prices in 2005 by multiplying the price of gasoline in 1973 ($0.39) by the ratio of the CPI in 2005 divided by the CPI in 1973. As the table shows, this ratio is 197.6 divided by 44.4, or 4.45. Multiplying the 4.45 times the $0.39 price of gasoline in 1973 yields $1.74. Thus, measured in 2005 prices, the real price of gasoline in 1973 was $1.74. Note that the 4.45 indicates that the general level of prices in November 2005 was 4.45 times the level of prices in 1973.

In economics "real" always means adjusted for differences in the general level of prices (i.e., inflation). Answer the following questions about the real price of gasoline during the 1973-2005 period:

1. Measured in terms of the general level of prices in November of 2005, derive the real price of a gallon of gasoline for the years 1980, 1990, and 2000. Show your work for each of these calculations.

   (1980: $\$1.25 \times \frac{197.6}{82.4} = \$2.99$

   (1990: $\$1.16 \times \frac{197.6}{130.7} = \$1.75$

   (2000: $\$1.51 \times \frac{197.6}{172.2} = \$1.73$)

2. Compared to 1980, have real gasoline prices risen? (No)

3. Compared to 1990 and 2000, have real gasoline prices risen? (Yes)

Multiple-Choice Questions:

1. Why is it important to use real rather than nominal figures when making comparisons of value across time periods?
   a. The real figures are a better measure of changes in the general level of prices.
   * b. The real figures are adjusted for changes in the general level of prices.
   c. The real figures reflect changes in the general level of prices as well as changes in purchasing power.
   d. The real figures adjust for changes in the level of interest rates.

2. In contrast with nominal values, real values refer to nominal values
   a. minus interest rates.
   b. minus personal income taxes.
   * c. corrected for price changes.
   d. corrected for depreciation.

Nominal values versus real values

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1. Measured in terms of the general level of prices in November of 2005, derive the real price of a gallon of gasoline for the years 1980, 1990, and 2000. Show your work for each of these calculations.

2. Compared to 1980, have real gasoline prices risen?

3. Compared to 1990 and 2000, have real gasoline prices risen?

Clip 3: Unemployment and labor mobility

DVD Clip: Laid off Steelworkers
Length: 2:57

Concepts Illustrated:
Labor markets
Regulation
Unemployment

Description:

Using the labor market in Youngstown, Ohio, as an example, the segment addresses resource mobility. After several steel mills closed, many workers were laid off, and unemployment grew to 25 percent. However, as new companies emerged, most of those workers found better, safer, and higher-paying jobs. While labor conditions were poor for several years, total employment in Youngstown eventually grew so that there were more jobs than before the steel mills closed.

The segment goes on to compare labor mobility in Europe and America. Generally, European labor market regulations make it more difficult for businesses to reduce employment. Perhaps surprising to some, such policies slow down resource movement, which leads to higher unemployment and depresses income growth. Resource mobility is more flexible in America so we have less unemployment, more rapid growth, and higher living standards.

Voluntary National Content Standards in Economics

4. People respond predictably to positive and negative incentives.

18. A nation's overall levels of income, employment, and prices are determined by the interaction of spending and production decisions made by all households, firms, government agencies, and others in the economy.

19. Unemployment imposes costs on individuals and nations. Unexpected inflation imposes costs on many people and benefits some others because it arbitrarily redistributes purchasing power. Inflation can reduce the rate of growth of national living standards, because individuals and organizations use resources to protect themselves against the uncertainty of future prices.

Preview Question:

"Would Americans be better off if the government made it more difficult for employers to lay off workers?"

Accept a variety of responses. Here are some relevant points to bring up:

- *Lay-offs impose serious burdens on the workers involved. No one looks forward to being dismissed from his or her job.*
- *Making it more difficult to dismiss workers may discourage employers from hiring them at all.*

Discussion and Analysis Questions:

1. Do all new jobs pay more than the jobs that disappeared? (While some new jobs pay less, most pay more. In addition, the work itself may be less physically difficult.) Do you think the news that new jobs often pay more is much consolation to workers who face lay-offs? Why? (No. Nobody looks forward to losing a job and having to find another. It is very stressful to think about paying the bills, getting new training, applying for new jobs, and so forth. It is understandable that the lay-offs hurt the people being dismissed.)

2. At year-end 2005, the unemployment rate in the United States was about 5 percent, compared to rates of near 10 percent in several European countries. Similar differentials have been present for a couple of decades. Why has the United States had persistently lower unemployment rates than major European nations? (Europe has thick layers of regulations that protect jobs and impose many expenses on employers such as long vacations and generous parental leave programs. As a result, employers are reluctant to hire new workers. New workers are expensive to hire and hard to fire.)

3. If regulations were passed in the United States that made it more difficult for employers to dismiss workers, how do you think this would influence the incentive for employers to hire additional workers? (Increasing the regulations regarding the dismissal of workers would discourage employers from hiring new workers.)

Extension Activity: Comparing Economic Freedom and Unemployment

Explain to the class that there is a correlation between nations that have high levels of economic freedom–limited government spending and lower taxes, secure property rights, low inflation, free trade, fewer business regulations–and positive economic outcomes including higher living standards and lower levels of unemployment.

The *Economic Freedom of the World Annual Report* published by the Fraser Institute ranks nations around the world in terms of their levels of economic freedom.

Ask the students to predict which of the nations in Table 1 would rank near the top in terms of economic freedom and which would rank near the bottom. Then ask the students to fill in the economic freedom ranking that is provided.

Next, ask the students to visit the *World Factbook* published by the CIA. This is a widely used website that contains a great deal of data on individual nations. It allows students to make many comparisons among nearly all the nations of the world. The *World Factbook* can be found at **www.cia.gov/cia/publications/factbook.** Ask the students to go to this website. Once there, they should enter the name of one of the countries in Table 1 and then click on "economy." Look up the unemployment rate and enter it into the last column on the right in Table 1.

When they are done, ask: What appears to be the correlation between high levels of economic freedom and the unemployment rate? (High ratings of economic freedom appear to be associated with low levels of unemployment. Low levels of economic freedom appear to be associated with high levels of unemployment.)

TABLE 1. ECONOMIC FREEDOM AND UNEMPLOYMENT

ECONOMIC FREEDOM RANK[1]	COUNTRY	UNEMPLOYMENT RATE
(1)	Hong Kong	(5.8%, 2005)
(2)	Singapore	(3.4%, 2005)
(3)	New Zealand	(4%, 2005)
(3)	United States	(5.1%, 2005)
(112)	Syria	(20%, 2002)
(115)	Russia	(7.6%, 2005)
(124)	Venezuela	(12.3%, 2005
(126)	Zimbabwe	(60%, 2005)

[1] *Economic Freedom of the World 2005 Annual Report,* Vancouver, B.C: Fraser Institute.

Multiple-Choice Questions:

1. The unemployment rate in the United States is
* a. lower than the rate in Germany and France.
   b. about the same as the rate in Germany and France.
   c. higher than the rate in Germany and France.
   d. lower than the rate in France but higher than the rate in Germany.

2. Increasing the regulations on hiring and firing workers provides employers with an incentive to
   a. increase employment.
* b. decrease employment.
   c. keep employment steady.
   d. support the expansion of unions.

Unemployment and labor mobility

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Unemployment and labor mobility

Extension Activity: Comparing Economic Freedom and Unemployment

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	Hong Kong	
	Singapore	
	New Zealand	
	United States	
	Syria	
	Russia	
	Venezuela	
	Zimbabwe	

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Clip 4: Government spending, jobs, and unemployment

DVD Clip: Broken Windows
Length: 2:40

Concepts Illustrated:
Expenditure multiplier
Fiscal policy
Wealth and living standards

Description:

John breaks several windows in an apartment to illustrate how jobs would be created by the destruction. Cleaning crews, window repairers, glass manufacturers, and many others would see an increase in demand for their services. At first glance it looks like the economy is helped because the destruction creates jobs and expands employment. But wait a minute—the destruction also destroys wealth and if the funds had not been spent repairing the damages, they would have been spent elsewhere. Therefore, destructive acts do not create jobs, they merely re-shuffle them. Furthermore, the destruction reduces wealth and the availability of goods and services for consumption.

Voluntary National Content Standards in Economics

4. People respond predictably to positive and negative incentives.

18. A nation's overall levels of income, employment, and prices are determined by the interaction of spending and production decisions made by all households, firms, government agencies, and others in the economy.

Preview Question:

"Does breaking windows create jobs?"

Accept a variety of responses. Here are some relevant points to bring up:

- *All choices involve a cost.*
- *Resources devoted to repairing broken windows have alternative uses.*

Discussion and Analysis Questions:

1. The "broken window fallacy" seems, on the surface, to make a lot of sense. Spending always ripples through the economy in this way. So why is the "broken window fallacy" called a "fallacy"? Let's imagine that the window owner was considering buying a new set of tires. Now these dollars are being used to repair the window. What is the opportunity cost of the window repair to the window owner? (The new set of tires.) Imagine that the window had not been broken and the window owner did not have to pay for the window repair. According to our example, what would he or she have purchased? (The new set of tires.) In what way would the window owner have been better off if his or her window had not been broken? (The window owner would have both an intact window and a new set of tires.) Remembering the ripple effect of spending, who besides the window owner was hurt financially when the window was broken? (In this case, the emphasis is on the economic activity that did not take place. The people involved in the production of tires would have been hurt. The tire salesperson was not paid to sell the tires, the tire installer was not paid to place the new tires on the car, the tire manufacturer was not paid to produce the tires, and so forth.)

2. Imagine that the repair to the broken window was to be paid for by government spending instead of private spending. Would this change the meaning of the "broken window fallacy"? (No. The government has alternate uses for its resources. Government spending on window repair is spending that cannot be used for other purposes such as lowering taxes or strengthening the armed forces.)

3. If a hurricane imposed great damage on both individuals and their property, would this create jobs? (It would create some kinds of jobs but it would destroy others. Overall, it would reduce wealth because people would have lost their property and some combination of private and government spending would be used to make repairs.)

Extension Activity: The Attack of September 11, 2001

Distribute the following handout to your class and ask the students to respond to the Question for Discussion.

September 11 and the Broken Window Fallacy

After the attacks on the World Trade Center on September 11, 2001, some well-meaning economists suggested that rebuilding New York City would stimulate billions of dollars of economic activity. Buildings would need to be repaired, new buildings would be built, subways would have to be repaired, and security systems would need to be improved. The economy was in a mild recession at the time. So in a sense, the attacks of September 11, 2001, were an economic "win" for the United States.

Question for Discussion

Were the events of September 11, 2001 good or bad for the U.S. economy? Did they expand employment in some industries? Did they expand overall employment? Be sure to keep in mind the "broken window fallacy."

(Resources used to rebuild parts of New York City were resources that could not be used for other purposes such as keeping taxes low, investing in improved transportation, and so forth. While employment in some industries [e.g. , construction and security] expanded, additional spending in these areas resulted in less spending in other areas. Thus, there is no reason to believe that there was an expansion in overall employment.)

Multiple-Choice Questions:

1. A hailstorm that breaks lots of windows in buildings is
   a. good for the economy because the spending on repairs will add new jobs to the economy.
   b. good for the economy because spending on the repairs will drive up the general level of prices.
   c. bad for the economy because the damage from the storm will be subtracted from this year's GDP.
   * d. bad for the economy because wealth was destroyed and more spending on repairs will result in less spending on other goods and services.

2. If the government levies $20 billion in taxes to finance additional spending on military weapons, the net impact on total employment will be
   a. a substantial increase in employment because the additional spending will create lots of jobs.
   b. a substantial decrease in employment because the higher taxes will destroy lots of jobs.
   * c. a small increase in employment because the higher taxes will reduce spending in other areas, which will tend to offset any jobs created by the government spending.
   d. a substantial increase in employment, but only if the additional spending leads to a larger budget deficit.

Government spending, jobs, and unemployment

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Question for Discussion

Were the events of September 11, 2001 good or bad for the U.S. economy? Did they expand employment in some industries? Did they expand overall employment? Be sure to keep in mind the "broken window fallacy."

Clip 5: Stadiums, subsidies, and taxes

Length: 5:54

Concepts Illustrated:

Government spending
Political decision-making and special-interest issues
Public choice economics
Subsidies
Taxes

Description:

The segment uses the Chicago White Sox baseball stadium as an example. Jerry Reinsdorf, the majority owner of the White Sox, and former Illinois Governor James Thompson are interviewed; they describe the rationale and process involved to fund the new stadium. By using tax dollars, the stadium costs are reduced for the owners of sports teams. Since costs are reduced, owners are able to increase both player salaries and profitability. Another concept is that taxes are used to transfer income away from some and toward others. In this case, the stadium was funded by a motel/hotel tax. Therefore, taxes are collected from consumers who typically reside outside of Illinois and transferred to the citizens of Illinois, mostly to the sports team and its owners.

Voluntary National Content Standards in Economics

17. Costs of government policies sometimes exceed benefits. This may occur because of incentives facing voters, government officials, and government employees, because of actions by special interest groups that can impose costs on the general public, or because social goals other than economic efficiency are being pursued.

18. A nation's overall levels of income, employment, and prices are determined by the interaction of spending and production decisions made by all households, firms, government agencies, and others in the economy.

Preview Question:

"Do subsidies for sports stadiums create jobs and promote economic development?"

Ask for a show of hands–yes, no, and maybe. Ask a few students for the reasons for their opinions.

Discussion and Analysis Questions:

1. What are the benefits and opportunity costs of building a sports stadium? (The benefits include having a sports team, jobs from construction and use of the stadium, and community pride in a winning team such as the Chicago White Sox who won the 2005 World Series. The opportunity costs include jobs lost when consumers spend less because of higher taxes and/or the loss of government programs such as schools, highways, or health care that cannot be funded because the money was spent on the stadium.)

2. When the government builds a sports stadium, who wins and who loses? (The biggest winner is the owner or owners of the team. The players on the team are also winners. Fans who can afford tickets and enjoy the upgraded facility will benefit. Taxpayers who do not use the stadium are losers. Businesspeople with competing businesses are also losers. Government-subsidized sports stadiums generally help wealthy owners and players and hurt poor people and many other citizens who pay the taxes.)

3. If government-subsidized sports stadiums help the rich at the expense of the poor and do not create jobs, why do governments pay for them? (This question presents a good opportunity to discuss public choice economics. The cost of government policies can exceed the benefits. This is because special interests receive large benefits and work hard to get them. The costs are spread across the entire population and are small for each individual. Therefore, the public does not pay attention or more readily accepts the politicians' argument that a stadium creates jobs.)

Extension Activity: Government Decision-Making

This is a brief simulation that illustrates that every choice for government spending has an opportunity cost. There is no free lunch in government spending–just as there is no free lunch in private spending. Every choice has an opportunity cost, and too often that opportunity cost is ignored.

1. **Set up the situation.**

   The state government is considering a temporary half-cent increase in the sales tax to expand government programs. The tax is expected to raise $500,000,000 per year, and the governor and state legislature are considering the following choices:

   a. **New stadium**

   Build a new stadium for the professional football team that has threatened to move to another state. The new stadium would be a state-of-the-art facility with comfortable seats, skyboxes, extensive restrooms, and numerous food areas. Backers claim the construction will create many high-quality jobs.

   b. **"Education for the Future"**

   This is a plan to improve the public schools and improve student performance in math, reading, and science. Under this plan teacher salaries would increase, schools would get new facilities, and accountability for student performance would increase. Backers believe that improving the skills of future members of the workforce will attract businesses that will create high-quality jobs.

   c. **"Transportation Express"**

   This is a plan to create highways throughout the state and public transportation in urban areas. Backers believe that the improved transportation system will stimulate business development and make the state a more pleasant place in which to live. They also believe the construction will create many new jobs.

   d. **No new taxes**

   Some state legislators believe that the taxpayers should keep the money they earned and the sales tax should not be raised. They argue that lower taxes create incentives for people to work, spend, save, and invest. They argue, therefore, that more jobs will be created and living standards will be raised.

2. **Time to choose.**

   Write each alternative on a separate sheet of paper and spread the four sheets throughout the classroom. Have the students go to the sheet of paper with the program they support.

3. **Discuss the decision.**

   Have the students discuss their choices and encourage students who made different choices to be critical. The key here is not that one choice is better than the others but each decision has benefits and opportunity costs.

Finally, ask what choices members of the state legislature might make and why. Which special interests would support each program?

Multiple-Choice Questions:

1. Which of the following provides the most reasonable explanation for why sports teams lobby for high subsidies?
   a. Without the subsidies the teams would cease to exist.
   b. Subsidies promote the efficient use of resources.
   * c. Sports interests seek a redistribution of income favoring themselves.
   d. The subsidies reduce costs, which helps the poor.

2. Proponents of a $500,000,000 taxpayer-financed stadium for the new National League baseball team in Washington, D.C., argued that the spending would expand the local economy by several billion dollars. They were
   a. probably correct because such projects generally increase local income by three or four times the spending on the projects.
   b. probably incorrect because spending on such projects mostly replaces other types of spending.
   c. probably incorrect because the tax increase necessary to finance the project will reduce spending on other goods and services.
   * d. both b and c are correct.

Stadiums, subsidies, and taxes

Multiple-Choice Questions:

1. Which of the following provides the most reasonable explanation for why sports teams lobby for high subsidies?

   a. Without the subsidies the teams would cease to exist.
   b. Subsidies promote the efficient use of resources.
   c. Sports interests seek a redistribution of income favoring themselves.
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   b. probably incorrect because spending on such projects mostly replaces other types of spending.
   c. probably incorrect because the tax increase necessary to finance the project will reduce spending on other goods and services.
   d. both b and c are correct.

Clip 6: How much tax do the rich pay?

Length: 1:54

Concepts Illustrated:

Marginal tax rates
Progressive tax
Proportional tax
Regressive tax

Description:

The segment documents the proportion of federal personal income taxes paid by the wealthiest Americans. At the beginning of the clip, the Reverend Al Sharpton, former Democratic Presidential candidate, claims the top 1 percent of income earners pay less than 5 percent of total income taxes. He suggests they should pay 15 percent. The fact is that the top 1 percent of earners already pay 34 percent of the total federal personal income tax collected by the IRS. The top 5 percent pay over 50 percent of the total.

Voluntary National Content Standards in Economics

16. There is an economic role for government to play in a market economy whenever the benefits of a government policy outweigh its costs. Governments often provide for national defense, address environmental concerns, define and protect property rights, and attempt to make markets more competitive. Most government policies also redistribute income.

Preview Question:

"Do the rich pay their fair share of taxes?"

Elicit the views of the students on this question, and ask a few students to give reasons for their opinions.

Discussion and Analysis Questions:

1. According to the video, IRS statistics show the top 1 percent of income earners pay what percentage of all federal personal income taxes? (34 percent) What percentage of all federal personal income taxes do the richest 5 percent of earners pay? (50 percent)

2. Is the federal income tax progressive, proportional, or regressive? (The federal income tax is progressive; the higher one's income, the greater percentage of that income is paid in taxes.)

3. A marginal tax rate is the rate on additional income. The marginal tax rate for the federal income tax increases from 0 percent up to 35 percent on very high incomes. How do high marginal tax rates affect the incentives for people to work, save, invest, and earn? (High marginal tax rates reduce the incentive to work, earn, save, and invest. Higher marginal tax rates reduce after-tax income so people do not gain as much from higher incomes.)

Extension Activity: Income Levels and Tax Rates

The table below updates the figures in the video to 2003 and provides an opportunity for the students to see who really pays taxes. AGI is adjusted gross income, which is income after business expenses but before exemptions and deductions are taken.

	NUMBER OF RETURNS	AGI ($ MILLIONS)	INCOME TAXES PAID ($ MILLIONS)	GROUP'S SHARE OF TOTAL AGI (%)	GROUP'S SHARE OF INCOME TAXES (%)	INCOME SPLIT POINT	AVERAGE TAX RATE (%)
All taxpayers	128,609,786	6,287,586	747,939	100.00	100.00		11.9
Top 1%	1,286,098	1,054,567	256, 340	16.77	34.27	Above $295,495	24.31
Top 5%	6,430,489	1,960,676	406,597	31.18	54.36	Above $130,080	20.74
Top 10%	12,860,979	2,663,470	492,452	42.36	65.84	Above $94,891	18.49
Top 25%	32,152,447	4,078,227	627,380	64.86	83.88	Above $57,343	15.38
Top 50%	64,304,893	5,407,851	722,027	86.01	96.54	Above $29,019	13.35
Bottom 50%	64,304,893	879,735	25,912	13.99	3.46	Below $29,019	2.95

Sources: Internal Revenue Service, The Tax Foundation

Questions:

1. True, false, or uncertain and why? "The top 1 percent of taxpayers may pay 34 percent of federal personal income taxes, but they also earn more than 34 percent of the income." (False. They earn only 17 percent of AGI but pay 34 percent of federal income taxes.)

2. What percentage of federal personal income taxes does the bottom 50 percent of earners (people earning below $25,912) pay? (3.46 percent)

3. How does the average income tax rate of those in the bottom half of the income distribution compare with the average rate paid by the top 1 percent of earners? (The average rate for the bottom group is 2.95 percent compared to 24.31 percent for the top 1 percent.)

4. Is there a good reason why the poor pay less of their income in taxes than the rich? (Progressive taxes are based on the ability-to-pay theory of taxation. The poor may be sacrificing necessities rather than luxuries so their tax is lower.)

5. Do you think people whose income is in the lower half of all income pay any other taxes? (They may pay other taxes such as Social Security tax, state income tax, state and local sales taxes, and property tax. However, the rich pay more of these taxes also.)

Multiple-Choice Questions:

1. In 1980 the top 1 percent of earners paid 19.1 percent of the federal personal income tax. By 2003 the share of this tax collected from the top 1 percent of earners
   a. had declined to less than 15 percent.
   b. was still slightly less than 20 percent.
   c. had risen to approximately 22 percent.
   * d. had risen to approximately 34 percent.

2. The share of the federal personal income tax paid by the bottom half of earners is
   a. higher than the share paid by the top 1 percent of earners.
   b. about 10 percent of all income taxes paid.
   * c. less than 4 percent of all income taxes paid.
   d. both a and b are correct.

How much tax do the rich pay?

Multiple-Choice Questions:

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    a. had declined to less than 15 percent.
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    c. had risen to approximately 22 percent.
    d. had risen to approximately 34 percent.

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How much tax do the rich pay?

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Sources: Internal Revenue Service, The Tax Foundation

Questions:

1. True, false, or uncertain and why? "The top 1 percent of taxpayers may pay 34 percent of federal personal income taxes, but they also earn more than 34 percent of the income." (False. They earn only 17 percent of AGI but pay 34 percent of federal income taxes.)

2. What percentage of federal personal income taxes does the bottom 50 percent of earners (people earning below $25,912) pay? (3.46 percent)

3. How does the average income tax rate of those in the bottom half of the income distribution compare with the average rate paid by the top 1 percent of earners? (The average rate for the bottom group is 2.95 percent compared to 24.31 percent for the top 1 percent.)

4. Is there a good reason why the poor pay less of their income in taxes than the rich? (Progressive taxes are based on the ability-to-pay theory of taxation. The poor may be sacrificing necessities rather than luxuries so their tax is lower.)

5. Do you think people whose income is in the lower half of all income pay any other taxes? (They may pay other taxes such as Social Security tax, state income tax, state and local sales taxes, and property tax. However, the rich pay more of these taxes also.)

Clip 7: Are boycotts of sweatshop products helpful?

Length: 5:50

Concepts Illustrated:
International trade
Labor markets
Minimum wage

Description:

The role of profits in business activity to import goods from cheaper, foreign countries is a general theme. The segment begins with scenes from various student protests regarding imported goods made by "sweatshops." As expressed during interviews with several students, their stated goals are to raise wages and improve conditions for the workers in foreign countries. They are implicitly calling for price controls either through artificially raising prices of the goods or implementing some kind of minimum wage for the workers. Either one would result in fewer goods being imported which would actually lower the wages and increase unemployment for the workers in the "sweatshops." The protestors claim foreign workers are being exploited. During interviews with representatives from foreign countries, quite the opposite story is depicted. Those countries and workers desire those jobs and would like to have more.

Voluntary National Content Standards in Economics

5. Voluntary exchange occurs only when all participating parties expect to gain. This is true for trade among individuals or organizations within a nation, and among individuals or organizations in different nations.

8. Prices send signals and provide incentives to buyers and sellers. When supply or demand changes, market prices adjust, affecting incentives.

13. Income for most people is determined by the market value of the productive resources they sell. What workers earn depends, primarily, on the market value of what they produce and how productive they are.

Preview Question:

"Would workers in poor countries be better off if Americans refused to buy items produced in sweatshops?"

Accept a variety of responses. Here are some relevant points to bring up:

- *Poor working conditions and low wages are relative to the countries involved.*
- *What is considered a low wage in the United States, a nation characterized by highly productive workers, is quite different from what is considered a low wage in Mexico, a nation characterized by less productive workers.*
- *Companies are not compelled to open factories in poor nations. They do it voluntarily and are usually welcomed by the people of the host nation.*

Discussion and Analysis Questions:

1. Some of the protesting students suggest that Americans should not buy products produced by companies that use "sweatshops." If Americans bought fewer products produced by firms in low-wage countries, how would the demand for workers in these countries be affected? (Demand for workers would decrease, and unemployment in poor countries would increase.)

2. According to the college students, do companies like Nike exploit their workers by paying low wages? (Yes. These companies pay low wages when the wages levels are compared to what is paid to U.S. workers.) According to the people who live in these countries, do companies like Nike exploit their workers by paying low wages? (No. People look forward to such companies opening. These companies often pay much higher wages and provide better working conditions when compared to what other local employers provide or when compared to work on local farms.)

3. If firms selling goods in the United States were required to pay the U.S. minimum wage to workers that they employ in low-wage countries like Mexico or India, would the workers in the low-wage countries be helped? Why or why not? (They would not be helped. The increase in wages would provide an incentive for these companies to leave places like Mexico and India. The net result would be less employment, more unemployment and a lower standard of living in these countries.)

Extension Activity: The Sweatshop Shortage

Distribute the following handout to your class and ask the students to respond to the Questions for Discussion.

The World Does Not Have Enough Sweatshops

Jeffrey Sachs is a well-known economist. A professor at Harvard for many years, he now has an appointment at Columbia University. Professor Sachs is deeply concerned about reducing world poverty and has written and spoken extensively on the subject.

In a recent book Professor Sachs writes that "the rich-world protesters . . . should support increased numbers of such jobs [because] the sweatshops are the first rung on the ladder out of extreme poverty." He goes on to say, "By now the anti-globalization movement should see that globalization, more than anything else, has reduced the numbers of extreme poor in India by 200 million and in China by 300 million since 1990." [1]

Professor Sachs suggests that sweatshops can help to reduce poverty. He suggests further that we don't have enough sweatshops! Why? Many nations around the world are hostile to companies that wish to open factories in their nations. Leaders in some nations–nations which became independent of colonial powers at a time when socialist ideas were popular–do not embrace the institutions of a free-market economy as the way out of poverty. India, for example, was leery of market reforms until the early 1990s. Also, many interest groups, including labor unions, are opposed to sweatshops.

Questions for Discussion

1. Who is Jeffrey Sachs? (He is a respected and well-known economist who has a deep interest in reducing world poverty.)

2. What do you think Professor Sachs means when he says that sweatshops are "the first rung on the ladder out of extreme poverty"? (He means that getting those first jobs is just the beginning. Economies are fluid. As people become wealthier, better educated, and more productive, they move on to better-paying jobs. He points to the reduction of poverty in nations such as China and India as examples.)

[1] *The End of Poverty: Economic Possibilities for Our Time,* by Jeffrey D. Sachs, Penguin Press, 2005.

Multiple-Choice Questions:

1. Why would workers be less well off if the firms paying the low wages were forced to leave the country by new government rules that required them to pay higher wages?
* a. The new wage rules would decrease the demand for labor and increase unemployment.
  b. The new wage rules would increase the demand for labor and increase unemployment.
  c. The new wage rules would decrease the demand for labor and decrease unemployment.
  d. The new wage rules would increase the demand for labor and decrease unemployment.

2. If Americans bought fewer products produced by firms in low-wage countries, there would be
* a. a reduction in the demand for labor and increased unemployment in low-wage countries.
  b. an increase in the demand for labor and increased unemployment in low-wage countries.
  c. a reduction in the demand for labor and decreased unemployment in low-wage countries.
  d. an increase in the demand for labor and decreased unemployment in low-wage countries.

Are boycotts of sweatshop products helpful?

Multiple-Choice Questions:

1. Why would workers be less well off if the firms paying the low wages were forced to leave the country by new government rules that required them to pay higher wages?

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   b. The new wage rules would increase the demand for labor and increase unemployment.
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[1.] *The End of Poverty: Economic Possibilities for Our Time,* by Jeffrey D. Sachs, Penguin Press, 2005.

Questions for Discussion

1. Who is Jeffrey Sachs?

2. What do you think Professor Sachs means when he says that sweatshops are "the first rung on the ladder out of extreme poverty"?

Clip 8: Does outsourcing cost American jobs?

Length: 5:33

Concepts Illustrated:
Employment
International trade

Description:

Lou Dobbs of CNN argues that outsourcing is bad and should be restricted. However, as some jobs are sent to foreign countries, labor resources are freed up to move to more productive areas. While the short-term consequences can be difficult, the long-term benefits often include better and higher-paying jobs for the displaced workers. The Levis factory in Powell, Tennessee, is used to illustrate the major point of the clip. When the plant closed because the jobs were sent to Mexico, the people who had worked there for 20 years became unemployed. Many of the workers from the Levis factory have found better jobs.

Voluntary National Content Standards in Economics

5. Voluntary exchange occurs only when all participating parties expect to gain. This is true for trade among individuals or organizations within a nation, and among individuals or organizations in different nations.

6. When individuals, regions, and nations specialize in what they can produce at the lowest cost and then trade with others, both production and consumption increase.

Preview Question:

"Would Americans be better off if outsourcing were prohibited?"

Accept a variety of responses. Here are some relevant points to bring up:

- *Outsourcing provides American consumers with less expensive goods and services.*
- *Outsourcing has short-term effects that are painful to workers.*
- *Outsourcing creates far more jobs than it destroys.*

Discussion and Analysis Questions:

1. According to Lou Dobbs, what is outsourcing doing to America? (He thinks that businesses that use cheap labor from other nations are destroying middle-class jobs.)

2. How do American consumers benefit from outsourcing? (Many consumer products such as textiles cost less.)

3. Why do business firms outsource certain activities? (Outsourcing allows businesses to save money and become more competitive.) What happens to businesses that outsource and become more competitive? (They make better products and eventually create new jobs.)

Extension Activity: How Could Outsourcing Produce More Jobs?

Distribute the following handout to your class and ask them to respond to the Questions for Discussion.

How Could Outsourcing Produce More Jobs?

A study done in 2004 by Professor Matthew J. Slaughter at Dartmouth University found that outsourcing is actually a way of increasing the number of American jobs. He found that employment increased not only for American firms

involved in outsourcing but also for their affiliates in other countries. While employment in foreign affiliates rose by 2.8 million jobs, employment in the U.S. parent firms rose even more –by 5.5 million jobs. In other words, for every one job outsourced, U.S. firms created nearly two jobs in the United States. Companies that outsource create far more domestic jobs than companies that do not.

Professor Slaughter's findings are surprising to some. Is this some statistical trick? How could jobs be created by outsourcing in the real world? Consider the case of a small manufacturer in Milwaukee, Wisconsin. Irv Jackson owns a factory that manufactures parts for large, earth-moving equipment.

Irv's customers started to tell him that his prices were too high. He protested. He was charging the same prices for his products as he did in previous years. His customers said that while that was true, Irv's competitors were charging even less. Irv's customers valued their relationship with his company. He had been a trustworthy supplier for many years. They encouraged him to consider outsourcing some of his manufacturing to China. This was all new to Irv. Like many Americans, he was skeptical that outsourcing could work.

Irv's business started to decline. He lost contracts. He laid off workers. He hated this. He'd always been proud of the number of jobs his business had created. He decided that he had to make a change. He contacted a manufacturer in China. He was stunned at the low prices charged by the Chinese company to produce some of the parts he wanted. He quickly made a deal and shifted some of his manufacturing to his new affiliate in China.

What happened? Irv's business was able to cut costs. Soon his bids were being accepted by more of his customers. His business expanded. As his business expanded, he hired more workers. Not only did he hire back most of the people who were laid off, he started hiring new workers.

All this took place over a period of a couple of years. There was no single event. No reporters sought out Irv to learn how he had gradually added new jobs due to outsourcing. Lou Dobbs never called to see how Irv was able to add new jobs in Milwaukee.

Questions for Discussion

1. What sort of business does Irv Jackson run? (Manufacturer of parts for earth-moving equipment.)

2. Why did Irv's business begin to decline? (He was losing contracts because his prices were no longer competitive.)

3. What did the decline in business mean for some of Irv's workers? (He had to lay off some employees.)

4. How did Irv's arrangements with a manufacturer in China help his business? (By outsourcing some of his manufacturing, he was able to offer more competitive prices. His business expanded, and soon he hired new workers to keep up.)

5. Why didn't Lou Dobbs call Irv Jackson? (Irv's success took place gradually. There was no one event to attract attention.)

Multiple-Choice Questions:

1. If businesses in the United States were prevented from outsourcing some jobs to low-wage countries, how would American consumers be affected?
   a. Consumers would pay less for some goods and services.
   b. Consumers would pay about the same for some goods and services.
   * c. Consumers would pay more for goods and services.
   d. Consumers would ignore any changes.

2. If labor-intensive textile products could be produced more cheaply in low-wage countries than in the United States, the United States would gain if it
   a. levied a tariff on the goods produced by the cheap foreign labor.
   b. subsidized the domestic textile industry so it could compete in international markets.
   * c. used its resources to produce other items while importing textiles from foreigners.
   d. levied a tax on the domestic textile products to penalize the industry for inefficiency.

Does outsourcing cost Americans jobs?

Multiple-Choice Questions:

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What happened? Irv's business was able to cut costs. Soon his bids were being accepted by more of his customers. His business expanded. As his business expanded, he hired more workers. Not only did he hire back most of the people who were laid off, he started hiring new workers.

All this took place over a period of a couple of years. There was no single event. No reporters sought out Irv to learn how he had gradually added new jobs due to outsourcing. Lou Dobbs never called to see how Irv was able to add new jobs in Milwaukee.

Questions for Discussion

1. What sort of business does Irv Jackson run? (Manufacturer of parts for earth-moving equipment.)

2. Why did Irv's business begin to decline? (He was losing contracts because his prices were no longer competitive.)

3. What did the decline in business mean for some of Irv's workers? (He had to lay off some employees.)

4. How did Irv's arrangements with a manufacturer in China help his business? (By outsourcing some of his manufacturing, he was able to offer more competitive prices. His business expanded, and soon he hired new workers to keep up.)

5. Why didn't Lou Dobbs call Irv Jackson? (Irv's success took place gradually. There was no one event to attract attention.)

Clip 9: Economic freedom and prosperity

DVD Clip: The Role of Freedom in Prosperity

Length: 2:16

Concepts Illustrated:
Economic freedom
Economic growth
Sources of prosperity

Description:

A single point is made in this segment. When economic freedom and liberty are allowed to flourish, economic growth and prosperity follow. The clip compares and contrasts places where government planning predominates (India, North Korea, Syria, and Haiti) against places where there is relatively little government planning (United States, Hong Kong, Switzerland, and New Zealand). The countries with government planning are poorer and less desirable places to live.

Voluntary National Content Standards in Economics

10. Institutions evolve in market economies to help individuals and groups accomplish their goals. Banks, labor unions, corporations, legal systems, and not-for-profit organizations are examples of important institutions. A different kind of institution, clearly defined and well enforced property rights, is essential to a market economy.

Preview Question:

"Why do some countries prosper while others are poor?"

Ask the students for their opinions and list them without comment. At the end of the lesson, discuss the keys to economic freedom and compare them to the students' original ideas.

Discussion and Analysis Questions:

1. "Economic freedom is present when private property is protected; when people are free to compete; and when resources, goods, and services are allocated by voluntary exchange and market prices rather than by government." Does this statement provide an accurate definition of economic freedom? Why or why not? (It is a good definition because people have the freedom to make economic decisions without being limited by a lot of government regulations. In addition, government promotes economic freedom by enforcing order, and contracts, and protecting private property.)

2. How does the growth rate of economies with more economic freedom compare with those that are less free? (There is a very strong correlation between increased economic freedom and the growth rate of a nation's economy. In most cases, the higher the degree of economic freedom, the higher the rate of growth of real GDP.)

3. Why would economic freedom increase economic prosperity? (Economic freedom encourages people to take risks and develop better goods and services and encourages firms to discover lower-cost methods of producing those goods and services. Economic freedom makes it easier and quicker to go into business, invest or train for new jobs, and make choices in the labor market.)

Extension Activity: Economic Freedom, Prosperity, and the Quality of Life

Most high school economics textbooks do not mention the importance of economic freedom to prosperity or even define the term. This activity provides some ideas on how to correct this deficiency. All statistics in the activity are from James Gwartney and Robert Lawson with Erik Gartzke, *Economic Freedom of the World, 2005 Annual Report*, Fraser Institute, 2005.

1. Help the students understand what economic freedom is. According to Gwartney, Lawson, and Gartzke, economic freedom rests on four cornerstones, which are:
   - Personal choice rather than collective choice;
   - Voluntary exchange coordinated by markets rather than allocation through the political process;
   - Freedom to enter and compete in markets; and
   - Protection of persons and their property from aggressive acts by others.

   Economic freedom can also be defined by what governments do and do not do. To promote economic freedom, governments should:
   - Establish an evenhanded legal system;
   - Protect individuals and their property from people using violence, coercion, and fraud to seize things that do not belong to them;
   - Facilitate access to sound money; and
   - Provide an infrastructure for voluntary exchange and the operation of markets.

   To promote economic freedom, governments should restrain from:
   - Taking actions that interfere with personal choice, voluntary exchange, and the freedom to compete in the labor and product markets;
   - Increasing taxes and government expenditures;
   - Increasing government regulations on the cjoices that businesses and people' can make; and
   - Limiting access into occupations and business activities.

2. What difference does economic freedom make? Ask the students to examine the statistics below and make conclusions based on them. These statistics compare eight characteristics of nations that score in the top fifth in economic freedom with nations that score in the bottom fifth. The differences should dramatically illustrate the difference that economic freedom makes in a nation's standard of living and quality of life.

Economic Freedom Index

Characteristic	Top Fifth	Bottom Fifth
Per capita GDP	$25,062	$2,409
Economic growth rate	2.5%	.6%
Investment per capita	$4,903	$195
Unemployment rate	5.2%	13%
Life expectancy	77.7 yrs.	52.5 yrs.
Income level of poorest 10%	$6,451	$1,185
Adult literacy	96.4%	65.3%
Access to improved water	97.0%	70.9%

Source: James Gwartney and Robert Lawson with Erik Gartzke, *Economic Freedom of the World, 2005 Annual Report*, Fraser Institute, 2005.

3. Research project. Have the students compare the top 10 nations in the Economic Freedom Index (EFI) with the bottom 10 nations. Have the students look at factors such as per capita GDP, life expectancy, infant mortality, economic growth rate, adult literacy, unemployment rate, and inflation rate. A good online source for research is the *CIA Factbook*, available at **http://www.cia.gov/cia/publications/factbook/**. Have each student select a nation to research and report to the class. Then make generalizations about countries with high economic freedom and low economic freedom.

TOP 10 COUNTRIES AND BOTTOM 10 COUNTRIES

TOP 10			BOTTOM 10		
NATION	**EFI**	**PER CAPITA GDP**	**NATION**	**EFI**	**PER CAPITA GDP**
Hong Kong	8.7		Gabon	5.1	
Singapore	8.5		Central African Rep.	4.9	
New Zealand	8.2		Congo, Rep. of	4.8	
Switzerland	8.2		Algeria	4.6	
United States	8.2		Burundi	4.5	
United Kingdom	8.1		Guinea-Bissau	4.5	
Canada	8.0		Congo, Dem. Rep.	4.3	
Ireland	7.9		Venezuela	4.3	
Australia	7.8		Zimbabwe	3.3	
Estonia	7.8		Myanmar	2.8	

Source: James Gwartney and Robert Lawson with Erik Gartzke, *Economic Freedom of the World, 2005 Annual Report*, Fraser Institute, 2005.

Multiple-Choice Questions:

1. Why do political instability and insecure property rights retard economic growth?
   a. Fear that private property will be confiscated substantially reduces the incentive to invest and create wealth.
   b. When property rights are insecure, foreign investors are reluctant to invest in the country.
   c. Savings will tend to flow out of a country if individuals fear their property is insecure.
   * d. All of the above are reasons.

2. On average, countries that have a larger degree of economic freedom tend to have
   a. higher per capita income levels but slower rates of economic growth than countries with less economic freedom.
   b. lower per capita income levels but more rapid rates of economic growth than countries with less economic freedom.
   * c. both higher per capita income levels and more rapid rates of economic growth than countries with less economic freedom.
   d. both lower per capita income levels and slower rates of economic growth than countries with less economic freedom.

Economic freedom and prosperity

Multiple-Choice Questions:

1. Why do political instability and insecure property rights retard economic growth?

   a. Fear that private property will be confiscated substantially reduces the incentive to invest and create wealth.

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Economic freedom and prosperity

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Economic freedom and prosperity

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Singapore	8.5		Central African Rep.	4.9	
New Zealand	8.2		Congo, Rep. of	4.8	
Switzerland	8.2		Algeria	4.6	
United States	8.2		Burundi	4.5	
United Kingdom	8.1		Guinea-Bissau	4.5	
Canada	8.0		Congo, Dem. Rep.	4.3	
Ireland	7.9		Venezuela	4.3	
Australia	7.8		Zimbabwe	3.3	
Estonia	7.8		Myanmar	2.8	

Source: James Gwartney and Robert Lawson with Erik Gartzke, *Economic Freedom of the World, 2005 Annual Report*, Fraser Institute, 2005.

Clip 10: Institutions, growth, and freedom

DVD Clip: Economic freedom in the U.S., India and Hong Kong

Length: 11:04

Concepts Illustrated:

Economic growth

Secondary effects

Sources of prosperity

Description:

The segment compares and contrasts the ease with which businesses operate in each of the three countries. The freedom of firms to innovate and create new goods is a key source of economic growth and prosperity. In India, which is dominated by socialist policies, it is very difficult to open a new business, and existing businesses find conditions to be restrictive and burdensome. The United States has the reputation of being a free market country, but the government is still heavily involved in many business aspects, and the policies can be barriers to innovation. Hong Kong is arguably the country with the most economic freedom. As John illustrates, a simple form is all one needs to open a new business. Several entrepreneurs are interviewed to describe their experiences in the U.S., India and Hong Kong.

Voluntary National Content Standards in Economics

10. Institutions evolve in market economics to help individuals and groups accomplish their goals. Banks, labor unions, corporations, legal systems, and not-for-profit organizations are examples of important institutions. A different kind of institution, clearly defined and well enforced property rights, is essential to a market economy.

14. Entrepreneurs are people who take the risks of organizing productive resources to make goods and services. Profit is an important incentive that leads entrepreneurs to accept the risks of business failure.

Preview Question:

"Should just anyone be allowed to open a business? Are regulations needed to protect workers and consumers?"

Accept a variety of responses. Here are some relevant points to bring up:

- *Regulations on businesses and high tax rates may be well intentioned, but they have secondary effects of discouraging enterprise and self-reliance.*
- *Some nations with large populations and no natural resources have become wealthy while other nations with small populations and many natural resources remain poor.*
- *Wealth is associated with high levels of economic freedom.*

Discussion and Analysis Questions:

1. People often think poverty in some nations is the result of overpopulation. Why does this seem like a weak explanation? (India is a large and densely populated country and it is relatively poor. In contrast, Hong Kong is one of the world's most densely populated countries and it is rich. Population size and density does not seem to be the critical variable in explaining why some nations are rich. Several nations in the world have large and dense populations and are rich. Japan and Singapore are additional examples.)

2. Hong Kong does not have a democracy, and yet Milton Friedman says that it was freedom in Hong Kong that allowed it to become wealthy. What sort of freedom is he referring to? (He is referring to economic freedom. For example, entrepreneurs have the freedom to easily start businesses in Hong Kong.)

3. Why has the lack of a government safety net encouraged economic expansion in Hong Kong? (People in Hong Kong know that the government provides only a minimal safety net. This encourages them to depend on themselves and their own creativity. Entrepreneurs are more willing to take business risks. Many of these businesses are successful.)

4. What does the experience of Hong Kong suggest about the need for government regulations to protect consumers and workers? (It raises doubts about such regulations. Places like Hong Kong that have limited regulations prosper. Places like India that have many regulations are poor.)

Extension Activity: Mystery Nations

Distribute the handout "Mystery Nations" to the class. Ask the students to read the characteristics of each nation and predict whether the nation is rich or poor. Then distribute the handout "Mystery Nations Revealed." Discuss the identities of the nations. Finally, discuss how high levels of economic freedom explain why some nations are rich while other nations are poor.

Mystery Nations[1]

Predict which of the following nations are rich and which are poor:

Country A
- Size: Three-tenths the size of the United States
- Population: About 40 million (small for a nation this size)
- Natural Resources: Rich resources with fertile land, lead, zinc, tin, copper, iron ore, oil, uranium

Is this nation likely to be rich or poor?

Country B
- Size: About the size of California
- Population: Over 127 million
- Natural Resources: Fish, no mineral resources

Is this nation likely to be rich or poor?

Country C
- Size: Twice the size of California
- Population: Large population of 128 million
- Natural Resources: Vast resources including oil, tin, iron ore, coal, limestone, lead, zinc, natural gas

Is this nation likely to be rich or poor?

Country D
- Size: 1.8 times the size of the United States.
- Population: 143 million
- Natural Resources: Vast resources with major deposits of oil, natural gas, coal, many strategic minerals, vast timber supplies

Is this nation likely to be rich or poor?

Country E
- Size: 3.5 times bigger than Washington, D.C.
- Population: 4 million
- Natural Resources: Fish, deepwater port

Is this nation likely to be rich or poor?

[1] The source of statistics for this exercise is the *CIA World Factbook* available at **www.cia.gov/cia/publications/factbook**.

Mystery Nations Revealed

Country A: Argentina

Population: 39,537,943
Per capita GDP: $13,600 (2005)
Life expectancy: 75.91 years
Literacy rate (age 15 and over can read and write): 97.1%
Infant mortality: 15.18 deaths/1,000 live births

Country B: Japan

Population: 127,417,244
Per capita GDP: $30,400 (2005)
Life expectancy: 81.15 years
Literacy rate (age 15 and over can read and write): 99%
Infant mortality: 3.26 deaths/1,000 live births

Country C: Nigeria

Population: 128,771,988
Per capita GDP: $1,000 (2005)
Life expectancy: 46.74 years
Literacy rate (age 15 and over can read and write): 68%
Infant mortality: 98.8 deaths/1,000 live births

Country D: Russia

Population: 143,420,309
Per capita GDP: $10,700 (2005)
Life expectancy: 67.1 years
Literacy rate (age 15 and over can read and write): 99.6%
Infant mortality: 15.39 deaths/1,000 live births

Country E: Singapore

Population: 4,425,720
Per capita GDP: $29,700 (2005)
Life expectancy: 81.62 years
Literacy rate (age 15 and over can read and write): 92.5%
Infant mortality: 2.29 deaths/1,000 live births

What are the characteristics of nations that have produced wealth? These nations have a common set of institutions[2] that provides a stable environment which rewards the activities of entrepreneurs. These factors include:

- Limited size of government in terms of expenditures, taxes, and state-run enterprises,
- Stable legal structure which has an independent system of justice and secure protection of property rights,
- Low levels of inflation and access to sound money,
- Freedom to trade internationally, and
- Limited government regulation of financial institutions, labor markets, and business.

[2] *Economic Freedom of the World, 2005 Annual Report*, Fraser Institute, 2005.

Multiple-Choice Questions:

1. High levels of economic freedom in places such as Hong Kong tend to result in
   a. low levels of per capita income.
   b. modest levels of per capita income.
* c. high levels of per capita income.
   d. modest but consistent levels of per capita income.

2. The historically low levels of economic freedom in places such as India tend to result in
* a. low levels of per capita income.
   b. modest levels of per capita income.
   c. high levels of per capita income.
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Institutions, growth, and freedom

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Institutions, growth, and freedom

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Clip 11: Property rights, eminent domain, and the role of government

DVD Clip: Eminent Domain in New Rochelle

Length: 4:19

Concepts Illustrated:

Protection of property rights

Role of government

Description:

Property rights and their enforcement are the major themes of this segment. Eminent domain is the ability of the government to take private land for public use. Using a neighborhood in New Rochelle, New York, as an example, the segment documents the local government forcing people out of their homes because it feels the land is better served in another capacity. Interviews with the mayor and a group of residents bring out both sides of the debate.

Voluntary National Content Standards in Economics

5. Voluntary exchange occurs only when all participating parties expect to gain. This is true for trade among individuals or organizations within a nation, and among individuals or organizations in different nations.

16. There is an economic role for government to play in a market economy whenever the benefits of a government policy outweigh its costs. Governments often provide for national defense, address environmental concerns, define and protect property rights, and attempt to make markets more competitive. Most government policies also redistribute income.

17. Costs of government policies sometimes exceed benefits. This may occur because of incentives facing voters, government officials, and government employees, because of actions by special-interest groups that can impose costs on the general public, or because social goals other than economic efficiency are being pursued.

Preview Question:

"Should political officials be able to take property from some private owners and transfer it to others if they think that will promote the public good?"

Accept a variety of responses. Here are some relevant points to bring up:

- *Private ownership of property is a fundamental right in a market economy.*
- *Private property rights provide an incentive for people to save, invest, innovate, exchange, and care for property.*
- *When resources are privately owned, users will have to pay the opportunity cost of the resource if they want to use it.*
- *Private ownership is a key factor in promoting economic growth.*

Discussion and Analysis Questions:

1. Traditionally, how has eminent domain been used in the United States? (Eminent domain was intended to make it possible for the government to undertake projects like road construction, bridges, and parks that provide widespread benefits for the general public.) What is the argument being used to defend the taking of homes in New Rochelle? (The argument is that the neighborhood is blighted. Transferring ownership will result in economic development.)

2. How do business owners normally acquire property they wish to develop? (They negotiate with the property owners to see if a voluntary agreement can be reached. Business owners normally have to compensate homeowners in a way that is agreeable to both parties.)

3. Why might the traditional way of obtaining land for development–compensating property owners at an agreed-upon price–be superior to using eminent domain? (Both parties, homeowners and developers, would reach a mutually acceptable agreement. Using eminent domain means the government must use force. Business owners do not have to consider the wishes of the property owners. This creates winners and losers.)

Extension Activity: Was Justice O'Connor Right?

Distribute the following handout to your class and ask them to respond to the Questions for Discussion.

Was Justice O'Connor Right?

In a market economy, individuals and businesses–not the government–own most of the resources. Private property ownership means that individuals can benefit from the ownership of their property, including their labor. Private ownership means that people and businesses are able to obtain, use, and transfer property as they see fit. Private property rights provide an incentive for people to save, invest, innovate, exchange, and care for property. Private ownership is a key factor in promoting economic growth. There are numerous examples of the benefits of private ownership:

- Private ownership provides incentives for people to take care of their property because it can gain in value. For example, people take better care of their own homes than rental apartments. People take better care of cars they own than cars they rent.

- The threat that private property may be taken without the consent of the owner discourages people from investing in their property including homes and businesses, or even their own education. Business owners in nations such as Cuba and North Korea that do not respect private property have little incentive to start and manage businesses. Why bother? The government could nationalize their business at any time.

- The threat that private property may be taken without the consent of the owner discourages people from saving and investing. Individuals who live in nations such as Argentina that have a history of nationalizing savings held in local banks have little incentive to save and invest. Why bother? The government could nationalize their savings at any time.

- Private property owners must have confidence that the courts will protect their rights or they will not make productive use of their property. In some countries legally operating businesses are taken over by the police or military and turned over to other owners. If the courts do not defend individual private ownership rights against the police or military, where can an individual turn? Nowhere. This arbitrary taking of property discourages people from starting businesses or to running them well.

In the 2005 case of *Kelo v. City of New London*, the Supreme Court ruled that it was proper for private property to be taken for the use of a private company. Justice Sandra Day O'Connor disagreed with this controversial opinion. She argued that if the decision stands, "Nothing is to prevent the State from replacing any Motel 6 with a Ritz-Carlton, any home with a shopping mall, or any farm with a factory."

Questions for Discussion

1. In a market economy, who owns most of the property? (Individuals and businesses.)

2. What is private property ownership? (People and businesses are free to benefit from the ownership of their property. They can obtain, use, and transfer property as they see fit.

3. What are the main advantages of private ownership of property? (Property rights encourage investment, innovation, exchange, care of property, and economic growth.)

4. What was the ruling in the case of *Kelo v. City of New London*? (The Supreme Court ruled that it was permissible for the government to take private property from some owners and transfer it to others who they believe would do a better job of developing the property.)

5. Why did Justice O'Connor disagree with this ruling? (She argued that nothing could now prevent the government from taking property from some owners, such as homeowners, and transferring it to other owners, such as businesses that offer to develop the property in a different way.)

Multiple-Choice Questions:

1. Eminent domain is the ability of government to
   a. levy property taxes.
   b. enforce contracts.
* c. take private land for public use.
   d. take public land for private use.

2. Voluntary transfer of property is what sort of "game"?
* a. Win-win game.
   b. Win-lose game.
   c. Hide-and-seek game.
   d. Mystery game.

Property rights, eminent domain, and the role of government

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Property rights, eminent domain, and the role of government

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5. Why did Justice O'Connor disagree with this ruling? (She argued that nothing could now prevent the government from taking property from some owners, such as homeowners, and transferring it to other owners, such as businesses that offer to develop the property in a different way.)

Clip 12: Is government too big?

Length: 4:56

Concepts Illustrated:
Fiscal policy
Size and growth of government
Taxes

Description:

The overriding theme of this video clip is that taxes are high and are placed on numerous goods in order to fund all of the projects in which government is currently involved. The segment begins by documenting some of the goods and services that government is involved in that most people probably don't realize. Examples include product inspections, subsidies for TV and radio, railroads, and subways. By using a roofing worker in St. Louis as an example, many of the taxes that average Americans pay are illustrated. The taxes include sales tax, electricity tax, personal property tax, gas tax, and payroll tax. In aggregate, Americans pay more in taxes than they do for food, clothing, and shelter combined.

Voluntary National Content Standards in Economics

16. There is an economic role for government to play in a market economy whenever the benefits of a government policy outweigh its costs. Governments often provide for national defense, address environmental concerns, define and protect property rights, and attempt to make markets more competitive. Most government policies also redistribute income.

17. Costs of government policies sometimes exceed benefits. This may occur because of incentives facing voters, government officials, and government employees, because of actions by special-interest groups that can impose costs on the general public, or because social goals other than economic efficiency are being pursued.

Preview Question:

"Make a list of all the taxes you pay."

Combine the students' lists to make one class list. Here are some examples of taxes:

- *Federal, state, and local income taxes*
- *Federal Social Security tax*
- *Federal, state, and local excise taxes (such as on gasoline)*
- *State and local sales taxes*
- *Property tax*
- *Driver's license fee*

When the lesson is finished, add to the list.

Discussion and Analysis Questions:

1. How long do Americans work to pay taxes; how long do they work to pay themselves? (The average American works four months to pay taxes and eight months to pay for his or her own purchases. It is May before the tax burden is paid off.)

2. Why do politicians have an incentive to conceal the cost of taxes? (People want something for nothing, and hiding taxes makes it less likely that people will know the true cost of government. In the words of Jean-Baptiste Colbert, finance minister to Louis XIV of France, "the art of taxation consists of so plucking the goose as to obtain the largest amount of feathers with the least amount of hissing."



3. "I think business should shoulder a larger share of the tax burden." When politicians make statements like this, what are they trying to do? (They are trying to make people believe that businesses and not consumers will pay the cost of government. However, business taxes are passed on to consumers and employees in the form of higher prices, lower wages, or less employment if taxes cause some businesses to close.)

Extension Activity: What Is a Good Tax?

Taxes should be evaluated beyond whether they are high or low. In this activity the students will provide a report card on key taxes. The criteria for grades are:

1. **Equity or Fairness**
   People differ on what "fairness" is. Most people agree that regressive taxes that tax the poor at a higher rate than the rich are not fair. Some people believe a fair tax is a progressive tax, which taxes the rich at a higher percentage than the poor. Progressive taxes are based on the idea that the rich have a greater ability to pay than the poor. Others favor a flat or proportional tax, which taxes everyone at the same rate. Finally, some people believe taxes should be based on the benefits people receive from the government program. When the students grade equity, they should defend their position on what grounds they believe the tax is fair or unfair.

2. **Simplicity**
   A tax should be simple. Taxpayers should understand what they must pay and why. It should be easy to calculate the tax owed. Increased complexity causes people to make mistakes, promotes cheating, and builds resentment.

3. **Neutrality**
   A good tax is neutral on the economy and does not interfere with the efficient allocation of resources. If a tax discourages people's incentives to work, save, and invest, the tax is not neutral. If the tax favors some groups over others, the tax is not neutral.

4. **Revenue Productivity**
   A good tax collects enough revenue to fund the government program it is designed to pay for. Also, it should not cost a lot to administer the tax because high administrative costs will leave less money to fund the program.

After explaining these criteria of a good tax to the students, have them grade some of the more important taxes in the United States. After they have graded the taxes, discuss the reasons for their grades to help them understand taxes better. You may wish to add taxes to this list.

TAX REPORT CARD

TAX	EQUITY	SIMPLICITY	NEUTRALITY PRODUCTIVITY	REVENUE	TOTAL GRADE
Federal income tax					
Social Security tax					
State sales tax					
Gasoline excise tax					
Sin taxes (cigarettes, alcohol)					
Property tax					

Grading Key: The grade is not as important as the reasoning behind it. Following are some points to bring up as you discuss the taxes:

Federal Income Tax

Equity–Progressive

Simplicity–Complex with complicated deductions, rates, and calculations

Neutrality–The high marginal rates for the wealthy could hurt incentives to work, save, and invest.

Revenue Productivity–Brings in the most revenue of all federal taxes

Social Security Tax

Equity–Proportional and then regressive because it is paid on income up to a determined limit

Simplicity–Simple payroll tax

Neutrality–Does not affect the economy but may affect individual saving

Revenue Productivity–Does not bring in enough revenue to pay future benefits

State Sales Tax

Equity–Most are regressive because the rich save more of their money rather than buy goods; exempting food from the tax makes it less regressive

Simplicity–Simple because it's added on to purchases and collected from businesses

Neutrality–Incentive to reduce consumption

Revenue Productivity–Does not fluctuate as much as income taxes

Gasoline Excise Tax

Equity–Regressive

Simplicity–Simple and hidden

Neutrality–Provides an incentive to use less gas

Revenue Productivity–Produces most revenue for highway construction and mass transit

Sin Taxes

Equity–Regressive

Simplicity–Simple and hidden

Neutrality–Provide an incentive to buy less of the products taxed

Revenue Productivity–Produce significant, but not great, revenue

Property Tax

Equity–Proportional

Simplicity–Complex and depends on assessments of a property's value

Neutrality–Creates an incentive not to improve one's property

Revenue Productivity–Revenue does not increase as much as with income tax because assessments lag behind increases in income and property value.

Multiple-Choice Questions:

1. Total government spending (federal, state, and local) sums to approximately
   a. 10 percent of the U.S. economy.
   b. 20 percent of the U.S. economy.
   * c. 33 percent of the U.S. economy.
   d. 50 percent of the U.S. economy.

2. During the last 40 years, the composition of federal spending has
   a. been virtually unchanged, but federal spending as a share of GDP has declined substantially.
   b. been virtually unchanged, but federal spending as a share of GDP has increased sharply.
   * c. shifted away from national defense and toward spending on income transfers and health care.
   d. shifted away from health care and income transfers and toward spending on national defense.

Is government too big?

Multiple-Choice Questions:

1. Total government spending (federal, state, and local) sums to approximately

    a. 10 percent of the U.S. economy.
    b. 20 percent of the U.S. economy.
    c. 33 percent of the U.S. economy.
    d. 50 percent of the U.S. economy.

2. During the last 40 years, the composition of federal spending has

    a. been virtually unchanged, but federal spending as a share of GDP has declined substantially.
    b. been virtually unchanged, but federal spending as a share of GDP has increased sharply.
    c. shifted away from national defense and toward spending on income transfers and health care.
    d. shifted away from health care and income transfers and toward spending on national defense.

Is government too big?

What Is a Good Tax?

TAX REPORT CARD

TAX	EQUITY	SIMPLICITY	NEUTRALITY PRODUCTIVITY	REVENUE	TOTAL GRADE
Federal income tax					
Social Security tax					
State sales tax					
Gasoline excise tax					
Sin taxes (cigarettes, alcohol)					
Property tax					

Clip 13: Size and growth of government

DVD Clip: Government Growth
Length: 1:47

Concepts Illustrated:
Role of government
Size and growth of government

Description:

The segment discusses and uses an enlightening graphic image to document the size and growth of the U.S. government since 1800. Despite politicians' claims to reduce spending, government spending has increased dramatically since the mid-1930s. In the early 1800s, government costs averaged about $20 per person per year. Until World War II, the average was less than $500. Today the average is about $10,000 per year. The fundamental roles of government such as protecting rights and defending the country are identified toward the end of the clip.

Voluntary National Content Standards in Economics

16. There is an economic role for government to play in a market economy whenever the benefits of a government policy outweigh its costs. Governments often provide for national defense, address environmental concerns, define and protect property rights, and attempt to make markets more competitive. Most government policies also redistribute income.

17. Costs of government policies sometimes exceed benefits. This may occur because of incentives facing voters, government officials, and government employees, because of actions by special interest groups that can impose costs on the general public, or because social goals other than economic efficiency are being pursued.

Preview Question:

"How large should government be? Is it bigger today than during earlier periods of American history?"

Accept a variety of responses. Here are some relevant points to bring up:

- *Government is larger today than in the past as is the nation's population.*
- *Growth of government, however, has outpaced population growth.*
- *The federal government today provides many goods and services that were once the responsibility of individuals and households.*

Discussion and Analysis Questions:

1. According to Tibor Machan, what is the role of government? (To protect individual rights and protect the nation from foreign attack.)

2. John Stossel says that Thomas Jefferson warned that "the natural progress of things is for government to gain and liberty to yield." What do you suppose Jefferson meant by that? (As government grows, it takes over responsibilities once reserved for individuals and families. Some see this as an intrusion into personal lives and private business affairs.)

3. When government provides more goods and services and is more heavily involved in regulation, it is easier for special interest groups to gain favors from the government. How might this happen? (When government increases its regulations of the health-care industry, for example, many special interests representing physicians, nurses, hospitals, nursing homes, insurance providers, and pharmaceutical drug companies have strong incentives to attempt to influence government policy and spending in ways that help them. A more limited federal role would provide incentives to the health-care industry to seek profits by competing successfully in the health-care marketplace rather than by seeking to influence government policy.)

Extension Activity: Federal Spending over Time

Distribute the following handout to the class. Ask the students to determine if the federal government was running a surplus or a deficit for each year. They should write the amount of the surplus or deficit in the column farthest to the right. Then they should complete the Questions for Discussion.

FEDERAL RECEIPTS, OUTLAYS (BILLIONS OF DOLLARS)[1]

FISCAL YEAR	RECEIPTS	SPENDING	SURPLUS (+) OR DEFICIT (-)
1950	39.4	42.6	(-3.1)
1960	92.5	92.2	(+0.3)
1970	192.8	195.6	(-2.8)
1980	517.1	590.9	(-73.8)
1990	1,032.0	1,253.1	(-221.1)
2000	2,025.2	1,789.1	(+236.2)
2005 (est.)	2,052.8	2,479.4	(-426.6)

[1] *Economic Report of the President: 2005 Report,* Spreadsheet Tables: Table B-78- Federal Receipts, Outlays, Surplus or Deficit, 1939-2006.

Questions for Discussion

1. How would you characterize the levels of federal spending since 1950? (Government spending has increased dramatically over these years.)
2. In how many of these years has the federal government run a deficit? (In five of seven of these years: 1950, 1970, 1980, 1990, and 2005)
3. Are the federal deficits getting larger or smaller? (The most recent deficits are very large; in 2005 the estimated deficit was over $400 billion.)
4. Why might running such large deficits be a problem? (Large deficits will mean higher future taxes in order to pay the interest on the larger amount of outstanding debt. The additional borrowing to finance the deficits may also lead to higher interest rates than would otherwise be present.)
5. What would elected officials in the federal government have to do to reduce federal spending? (They would have to cut or eliminate several federal programs.)

Multiple-Choice Questions:

1. In 1789 the U.S. government cost about $20 per person, adjusted for inflation. Today the government costs about
   a. $100 per person.
   b. $500 per person.
   c. $5,000 per person.
   * d. $10,000 per person.

2. Some economists argue that the government should play a limited role in the economy. What is the role of government in a free market economy?
   * a. Provide for national defense and protection of individual rights.
   b. Provide for national defense and the health care of citizens.
   c. Provide for national defense, the health care of citizens, and the protection of the environment.
   d. Provide for the national health, education, and welfare of all citizens.

Size and growth of government

Multiple-Choice Questions:

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   a. $100 per person.
   b. $500 per person.
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Size and growth of government

Federal Spending over Time

Determine if the federal government was running a surplus or a deficit for each year. Write the amount of the surplus or deficit in the column farthest to the right.

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Questions for Discussion

1. How would you characterize the levels of federal spending since 1950?
2. In how many of these years has the federal government run a deficit?
3. Are the federal deficits getting larger or smaller?
4. Why might running such large deficits be a problem?
5. What would elected officials in the federal government have to do to reduce federal spending?

Clip 14: Pork barrel spending

Length: 4:26

Concepts Illustrated:
Collective decision-making
Special interests and political power
Voting and economic efficiency

Description:

Voting behavior and collective decision-making are the two major concepts addressed in this segment. By using the example of a proposed $200 million bridge in Ketchikan, Alaska, the segment illustrates the behavior of special interests in obtaining government funding for projects that benefit a small number of people. The irony of the situation is that most of the local residents seem to be opposed to the bridge. Even so, the Alaska Congressman is pursuing the funding. This is an excellent illustration of the economics of collective decision-making in action.

Voluntary National Standards in Economics

16. There is an economic role for government to play in a market economy whenever the benefits of a government policy outweigh its costs. Governments often provide for national defense, address environmental concerns, define and protect property rights, and attempt to make markets more competitive. Most government policies also redistribute income.

17. Costs of government policies sometimes exceed benefits. This may occur because of incentives facing voters, government officials, and government employees, because of actions by special-interest groups that can impose costs on the general public, or because social goals other than economic efficiency are being pursued.

Preview Question:

"Why do elected officials vote for pork barrel projects, spending projects they know are not efficient?"

Accept a variety of responses. Here are some relevant points to bring up:
- *Pork barrel projects are widely regarded as ones with little or no real economic value.*
- *Members of Congress wish to please local constituents.*
- *One way that elected officials serve constituents is by bringing federal spending projects to local states and districts.*

Discussion and Analysis Questions:

1. From the viewpoint of economic efficiency, does pork barrel spending make sense? (No. It rarely creates sustainable jobs or worthwhile improvements. The "Bridge to Nowhere" is a good example. It will create very few sustainable jobs and, given the small population, will do little to stimulate other productive activities. The "celebration of the peanut" is another example of spending that has nothing to do with making the economy more efficient.)

2. During the last decade, the number of pork barrel spending projects has increased from 2,000 to 14,000. Why are they so popular with elected officials? (Pork barrel spending helps politicians bring federal dollars home to benefit local interest groups. These groups, in turn, are likely to vote in support of the official at election time.)

3. Some economists argue that a supra-majority, a two-thirds majority, for example, should be required for approval of spending projects at the federal level. Do you think this is a good idea? Why or why not? (The students might note that such a change in rules would make it far more difficult for members of Congress to vote for pork barrel projects.)

Extension Activity: Milking Voters on the Farm

Distribute the following handout to your class and ask them to respond to the Questions for Discussion.

Milking Voters on the Farm

The Milk Income Loss Contract (MILC) program is a subsidy program intended to help dairy farmers. Under the program dairy farmers receive a federal subsidy whenever the price of milk in Boston falls below $16.94 per hundredweight. The subsidy is applied to the first 2.4 million pounds of milk produced. This is roughly the annual production of a herd of 140 dairy cows. Most dairy farms in Wisconsin have about 75 cows. Wisconsin has 15,000 dairy farmers. In 2002 Wisconsin dairy farmers received $413 million in subsidies from the MILC program.

Questions for Discussion

1. Who benefits from the MILC program? (Many of Wisconsin's 15,000 dairy farmers stand to benefit. In 2002 Wisconsin dairy farmers received millions of dollars in additional income as a result of the MILC program.)

2. Do people in other states derive much benefit from the MILC program? (Not much. Wisconsin and California are the largest dairy-producing states.)

3. If you knew that your taxes would increase by a few cents because Wisconsin dairy farmers have a subsidy, would you vigorously protest the action to your members of Congress? (Probably not. The protest would not seem to be worth your effort.)

4. Do you think that Wisconsin dairy farmers are likely to vote for Members of Congress who support the MILC program? (Yes. Wisconsin dairy farmers have a strong financial interest in wishing to keep the MILC program.)

5. Imagine that Representative Lisa Olson is a newly elected member of Congress. Her district is in the heart of Wisconsin's dairy land. She thinks that she can do a great deal of good for the people in her district and hopes to serve them for many years. She prides herself on being a fiscal conservative and dislikes what many people call "pork barrel" spending programs. Do you think Representative Olson will vote in favor of the MILC program? (She will almost certainly vote to continue the MILC program because she wants to be reelected to office. The MILC program is of great interest to many of her constituents–people who will watch carefully to see how she votes on this program. Representative Olson also knows that the cost of the MILC program is spread out in such a way that it is hardly detectable to other taxpayers.)

Multiple-Choice Questions:

1. The term "pork barrel spending" refers to
   a. government spending programs financed with user charges.
   b. favors exchanged between elected officials to gain mutual support of legislation.
   * c. spending of questionable economic value financed by federal taxes even though it will benefit only people in a local area.
   d. spending for basic national defense projects such as increased salaries for people serving in the armed forces.

2. Why is legislation such as the bill to build the bridge in Ketchikan, Alaska, passed when most everyone knows that it is "pork"?
   * a. The benefits are concentrated among constituents in a part of Alaska while the costs are spread out over millions of taxpayers.
   b. The benefits are diffused to millions of taxpayers and the costs are concentrated among special-interest groups.
   c. Such legislation will create permanent jobs and expand the local economy.
   d. When it comes to federal spending, members of Congress often ignore the interests of their home districts.

Pork barrel spending

Multiple-Choice Questions:

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Pork barrel spending

Milking Voters on the Farm

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Questions for Discussion

1. Who benefits from the MILC program?

2. Do people in other states derive much benefit from the MILC program?

3. If you knew that your taxes would increase by a few cents because Wisconsin dairy farmers have a subsidy, would you vigorously protest the action to your Members of Congress?

4. Do you think that Wisconsin dairy farmers are likely to vote for members of Congress who support the MILC program?

5. Imagine that Representative Lisa Olson is a newly elected member of Congress. Her district is in the heart of Wisconsin's dairy land. She thinks that she can do a great deal of good for the people in her district and hopes to serve them for many years. She prides herself on being a fiscal conservative and dislikes what many people call "pork barrel" spending programs. Do you think Representative Olson will vote in favor of the MILC program?

Clip 15: Competition and efficiency of government

DVD Clip: Jersey City Water Department
Length: 2:11

Concepts Illustrated:
Cost efficiency
Government versus private-sector firms
Privatization
Role of profit and loss

Description:

Through the example of city water in Jersey City, New Jersey, private versus public production is the theme of the segment. When the water was administered by the city, the pipes were rusted, the water failed tests, and the price was rising. Since the contract was placed with a private company, the water is cleaner and the price is falling.

Voluntary National Content Standards in Economics

14. Entrepreneurs are people who take the risks of organizing productive resources to make goods and services. Profit is an important incentive that leads entrepreneurs to accept the risks of business failure.

16. There is an economic role for government to play in a market economy whenever the benefits of a government policy outweigh its costs. Governments often provide for national defense, address environmental concerns, define and protect property rights, and attempt to make markets more competitive. Most government policies also redistribute income.

17. Costs of government policies sometimes exceed benefits. This may occur because of incentives facing voters, government officials, and government employees, because of actions by special interest groups that can impose costs on the general public, or because social goals other than economic efficiency are being pursued.

Preview Question:

"Do the firms and agencies that produce government goods and services have strong incentives to produce efficiently?"

Accept a variety of responses. Here are some relevant points to bring up:

- *Producers in government do not face competition in the same way that producers in the private sector do.*
- *Producers in the private sector seek to earn a profit.*
- *The desire to earn a profit provides a strong incentive to produce efficiently.*

Discussion and Analysis Questions:

1. What usually happens to government agencies that produce inefficiently? (Not much. Often funding continues for the program regardless of a lack of efficiency.)

2. Do people providing government goods and services face the same incentives as people who work in the private sector? (No. Funding of government programs often continues even if the programs are inefficient. Government agencies rarely go out of business.)

3. What incentives do producers in the private sector confront that encourage them to provide goods and services at the lowest possible price? (Businesses in the private sector face competition. Entrepreneurs have to figure out how to keep costs low so that they can earn a profit. If they cannot earn a profit, they go out of business.)

Extension Activity: What Should the Role of Government Be in Providing Goods and Services?

Distribute the following handout to your class. Ask the students to read the information which follows and then complete the chart.

The Role of Government in Producing Goods and Services

Almost all of the things we consume are produced by the private sector. Clothing, houses, apartments, books, cars, tools, airplanes, medicine–nearly everything is produced by people in private business. But government produces some goods and services.

Why does government produce some things and not others? Most of the time, when individuals purchase something, they receive the benefits. But some goods and services are different. It is these differences that may result in some goods and services being produced by government. Here are three questions to consider when deciding whether a good or service should be produced by government or by the private sector.

1. Does the good or service convey benefits to both payers and nonpayers? When individuals can obtain goods and services without paying for them, this is called a "free-rider" problem.

2. Is it impossible to exclude nonpayers from receiving the benefits?

3. Does the good or service allow for shared consumption or will one person's consumption of a good or service reduce its usefulness to others?

On the table below, identify and explain whether the goods and services should be provided by government or by the private sector.

GOOD OR SERVICE	PRIVATE? PUBLIC?	WHY? CAN NONPAYERS BE EXCLUDED? DOES CONSUMPTION BY ONE REDUCE USEFULNESS FOR ANOTHER?
A spring-break Caribbean cruise	(Private)	(It is easy to exclude nonpayers. If spring-breakers could obtain cruises whether they paid or not, there would be no incentive for business to produce them.)
Police protection	(Public)	(When police patrol a neighborhood, all the neighbors benefit. It is difficult to exclude nonpayers. Consumption by one neighbor does not diminish consumption by another.)
Flood control	(Public)	(It is difficult to exclude nonpayers from benefiting. Consumption by one household does not diminish consumption by another.)
i-Pods	(Private)	(It is easy to exclude nonpayers. If consumers could use i-Pods whether they paid or not, there would be no incentive for business to produce them.)
Armed forces	(Public)	(It is difficult to exclude nonpayers. Consumption by one citizen does not diminish consumption by another.)
Apartments	(Private)	(It is easy to exclude nonpayers. If renters could obtain apartments whether they paid rent or not, there would be no incentive for business to produce them.)

Multiple-Choice Questions:

1. Which of the following best explains why managers of government agencies have little incentive to be efficient?
   * a. Public-sector managers have little fear of going out of business.
   b. Public-sector managers face fierce competition.
   c. Voters can easily detect if government is acting inefficiently.
   d. Elected officials face incentives that reward day-to-day oversight of public-sector managers.

2. What incentive do private-sector producers have that encourages them to provide goods and services at the lowest possible price?
   a. Desire to earn the praise of government officials.
   b. Desire to help the community.
   c. Desire to increase cooperation.
   * d. Desire to earn a profit.

Competition and efficiency of government

Multiple-Choice Questions:

1. Which of the following best explains why managers of government agencies have little incentive to be efficient?

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   b. Public-sector managers face fierce competition.
   c. Voters can easily detect if government is acting inefficiently.
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   a. Desire to earn the praise of government officials.
   b. Desire to help the community.
   c. Desire to increase cooperation.
   d. Desire to earn a profit.

Competition and efficiency of government

What Should the Role of Government Be in Providing Goods and Services?

Almost all of the things we consume are produced by the private sector. Clothing, houses, apartments, books, cars, tools, airplanes, medicine–nearly everything is produced by people in private business. But government produces some goods and services.

Why does government produce some things and not others? Most of the time, when individuals purchase something, they receive the benefits. But some goods and services are different. It is these differences that may result in some goods and services being produced by government. Here are three questions to consider when deciding whether a good or service should be produced by government or by the private sector.

1. Does the good or service convey benefits to both payers and nonpayers? When individuals can obtain goods and services without paying for them, this is called a "free-rider" problem.

2. Is it impossible to exclude nonpayers from receiving the benefits?

3. Does the good or service allow for shared consumption or will one person's consumption of a good or service reduce its usefulness to others?

On the table below, identify and explain whether the goods and services should be provided by government or by the private sector.

GOOD OR SERVICE	PRIVATE? PUBLIC?	WHY? CAN NONPAYERS BE EXCLUDED? DOES CONSUMPTION BY ONE REDUCE USEFULNESS FOR ANOTHER?
A spring-break Caribbean cruise		
Police protection		
Flood control		
i-Pods		
Armed forces		
Apartments		