

DISCUSSION QUESTION

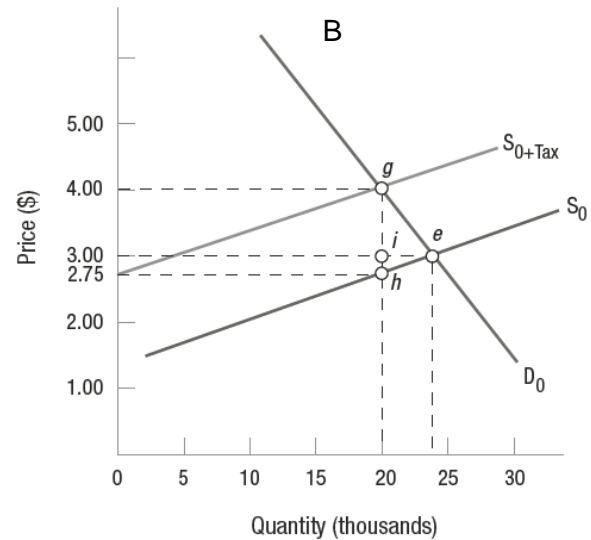
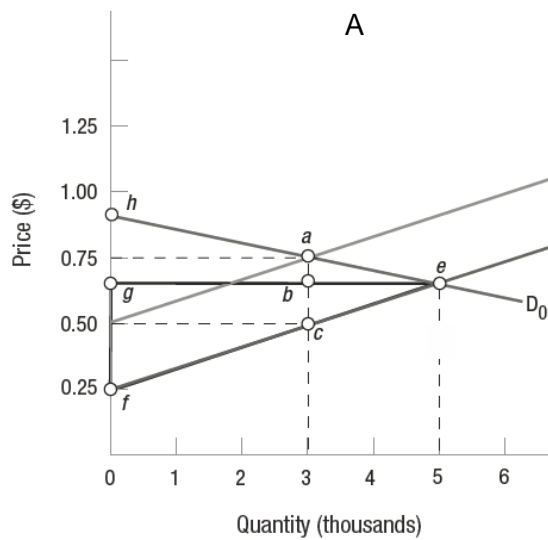
Name:
Instructor:
Course:

How is the lottery similar to a regressive tax? How is it different?

PEER GROUP PROBLEM SOLVING

Name:
Instructor:
Course:

The graphs below show the effects of a tax in two different markets, A and B.



- Which market is relatively demand elastic and which market is relatively demand inelastic?
- Identify the deadweight loss in each market (list the points). Calculate the deadweight loss. In which market is the deadweight loss the greatest? Why?

IN-CLASS EXPERIMENT / ACTIVE EXERCISE

Divide students into three groups. Assign group each a type of tax: progressive, flat, or regressive. Ask each group to explain the tax to the other two groups and provide a real-world example.

SOLUTIONS AND INSTRUCTOR NOTES

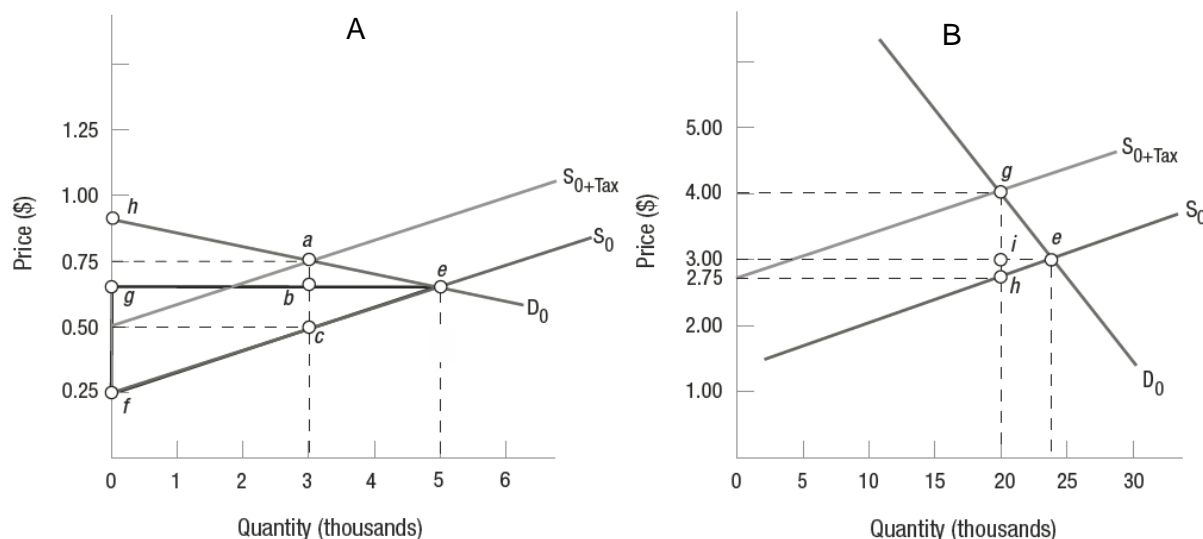
Discussion Question

How is the lottery similar to a regressive tax? How is it different?

Studies have shown that low-income people spend a larger proportion of their income on lottery tickets than do higher-income people. In this way it resembles a regressive tax. It is fundamentally different in that the purchase of a lottery ticket is voluntary while the payment of a tax is not.

Peer Group Problem Solving

The graphs below show the effects of a tax in two different markets, A and B.



- a) Which market is relatively demand elastic and which market is relatively demand inelastic?

Graph A is relatively demand elastic. The deadweight loss is represented by the triangle with points a – c – e. The deadweight loss is equal to 250.

Graph B is relatively demand inelastic. The deadweight loss is represented by the triangle with points g – h – e. The deadweight loss is equal to 500.

- b) Identify the deadweight loss in each market (list the points). Calculate the deadweight loss. In which market is the deadweight loss the greatest? Why?

When demand is inelastic, consumers are not as price-sensitive so changes in price result in relatively less change in demand. As a result, sellers can pass on more of the

tax burden in the form of higher prices. Overall, due to the smaller effect of a price change on quantity demanded, the deadweight loss will be lower in the relatively inelastic market.

In-Class Experiment / Active Exercise

Divide students into three groups. Assign group each a type of tax: progressive, flat, or regressive. Ask each group to explain the tax to the other two groups and provide a real-world example.

Examples will vary.

Progressive tax: tax rate rises in percentage of income as income increases

Flat tax: tax rate is a constant proportion of one's income

Regressive tax: tax rate falls in percentage of income as income increases

For more in-class experiment and active learning ideas, visit www.econedactive.com.