1.26 Government Intervention: Indirect Taxes, Subsidies and Price Controls: 30-minute Pack

Total Marks

AQA 7136 · Calculators not allowed · about 30 minutes

Name: _____ Date: ____ / ____ / _____

Answer all questions in full sentences where required. Show working for calculations. Draw diagrams where asked and label axes and shifts. Time guidance 30 minutes.

1 Evaluate the view that an ad valorem tax on single-use plastic bags is the most effective government intervention to correct the negative externality of plastic pollution in a national retail market.

(Total for Question 1 is 15 marks)

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2 Explain briefly two advantages of using price controls (maximum or minimum prices) as a policy tool compared with quantity controls or tradable permits in the short run.

(Total for Question 2 is 5 marks)

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Mark scheme · 1.26 Government Intervention: Indirect Taxes, Subsidies and Price Controls: 30-minute Pack

Question 1

Level 1 Basic identification of effects of an ad valorem tax, limited analysis. May include an attempted diagram and simple statements about higher price reducing quantity. Little evaluation or alternative policy comparison. **1-5**

Level 2 Clear analysis of how an ad valorem tax changes prices and quantities, discussion of behavioural responses and tax incidence, and some comparison with alternatives. Some use of diagrams and relevant evidence, with limited evaluation of strengths and weaknesses. **6-10**

Level 3 Comprehensive analysis including well-labelled diagrams, discussion of incidence, elasticities, likely behavioural change, administrative and enforcement costs, distributional impacts, and detailed comparison with bans, subsidies or producer responsibility schemes. Balanced evaluation with a supported judgement on overall effectiveness in correcting the externality. **11-15**

Indicative content:

- ad valorem tax mechanism: percentage levy increases consumer price, reduces quantity demanded and internalises external cost
- diagram: supply curve shifted up proportionally producing higher price and lower quantity, label consumer and producer prices and tax wedge
- incidence: depends on elasticities, may reduce demand significantly if demand elastic, hence reduce pollution
- behavioural responses: potential for reuse, switching to alternatives, or avoidance and black markets for untaxed suppliers
- administration and enforcement: collecting percentage tax at point of sale may be simpler than item taxes but requires monitoring and compliance costs
- measurement problem: tax corrects only at point of sale and may not reflect full social cost per unit if external cost not well known
- alternatives: ban can eliminate use but may encourage substitution to other materials with own costs; subsidies for reusables encourage positive behaviour but cost government money; producer responsibility schemes shift cost to producers and may incentivise redesign
- distributional effects: tax may be regressive on low-income consumers but revenue could be recycled to mitigate impact
- market distortions and unintended consequences: potential for increased use of other single-use items or businesses relocating sales, and enforcement loopholes
- conclusion: weigh speed, effectiveness, political feasibility and administrative cost to reach supported judgement whether ad valorem tax is most effective compared with alternatives

Question 2

identifies advantage 1 such as simplicity and speed of implementation **M1**

explains simplicity: price controls can be set quickly and are easy for consumers and firms to understand compared with setting up permit markets **A1**

identifies advantage 2 such as immediate distributional impact or protection of consumers/producers **M1**

explains how price ceilings protect consumers in crisis or price floors protect producers' incomes without needing complex trading systems **A1**

gives a short caveat or realistic limitation such as risk of shortages/surpluses requiring further policies **B1**

Answer: Advantages: price controls are simple and fast to implement, and can provide immediate consumer or producer protection; however they risk shortages or surpluses and may need complementary measures.

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