7. Which of the following policy options is/are usually cost-effective?
   a. A pollution tax or charge.
   b. Cap and trade programs.
   c. An emissions standard in which all sources are required to reduce their pollution by the same percentage.
   d. All of the above
   e. a and b only

8. Which of the following is the best description of a cap-and-trade system?
   a. Under a cap-and-trade system, polluters are allowed to emit the pollution that they want to as long as they inform the government in advance.
   b. Under a cap-and-trade system, polluters pay a fee to the government for each unit of pollution that they emit, thus creating a double dividend.
   c. Under a cap-and-trade system, the government sets a cap on pollution and then the government pays traders a unit subsidy when they reduce their pollution below the cap.
   d. Under a cap-and-trade system, there is no strict limit on the amount of pollution a business can emit since a polluter can emit more than its initial limit as long as it buys rights from other polluters, who must then reduce their pollution below their initial limit.
   e. Under a cap-and-trade system, all the polluters that trade in a geographic region are required to reduce their emissions to the rate set by the cap.

9. Transaction costs are prevalent throughout the economy. Which of the following statements about transaction costs is/are correct?
   a. Lawyers’ fees and fees paid to courts are two examples of transaction costs.
   b. Government should weigh potential transaction costs when deciding whether to address an inefficiency created by an externality.
   c. Liability rules always lead to efficient outcomes because under this approach transaction costs are eliminated
   d. a, b and c
   e. a and b
10. Which of the following statements is/are correct?

a. Product charges, in which a pollution fee is paid for each unit produced, are always better than emissions charges because they are easier to implement.

b. It is never possible to achieve a socially efficient outcomes through regulations because regulations are inflexible.

c. The term “stock pollutants” refers to pollutants that accumulate over time because the emissions load exceeds the environment’s absorptive capacity.

d. A cost-effective allocation is socially optimal, maximizing the net benefits to society.

e. All of the above are true.

11. Which of the following is a correct statement about Ronald Coase and the “Coase theorem”?

a. Coase showed that externalities can be addressed efficiently through the use of a tax.

b. Coase showed that cap-and-trade is an economically efficient way to address an externality.

c. Coase argued that the private allocation of public goods would be inefficient, justifying government provision of things like parks and defense.

d. Coase proved that externalities lead to inefficient outcomes since they do not maximize social net benefits.

e. Coase showed that it is possible to efficiently address an externality through negotiation and side payments.
12. The figure above represents a situation in which a firm supplies a good Q. The firm’s marginal cost is labeled $MC_P$ and the firm receives the price $P=3$. Production of Q leads to an external cost of $1$ per unit (MEC) on a nearby community resulting in the marginal cost to society curve, $MC_S$.

Which of the following statements is/are correct?

a. Relative to the market equilibrium where $Q=4$ thousand, the affected community could be made better off by paying the firm to reduce its production to the 2 thousand.

b. The firm would be better off if it paid the affected community for the right to increase its production from 2 thousand units to the profit-maximizing level, 4 thousand.

c. Because the price is $3$ and the MEC is only $1$, it is not possible for the affected community to pay the firm to reduce its production.

d. If the firm were required to compensate the affected community for any external costs that the community suffers, no production would occur.

e. All of the above are true