Part 1: Multiple Choice (2.5 points each unless indicated, 62.5 points total)

1. _____ Which of the following is true regarding the size of U.S. transfer programs? Use current spending on these programs to measure size.
   a. TANF, EIC and Food Stamps are each larger than Social Security.
   b. TANF and EIC are each larger than Social Security. Food Stamps is a smaller program than Social Security.
   c. TANF, EIC and Food Stamps are, considered individually, each a smaller program than Social Security. Collectively (TANF + EIC + Food Stamps), the three programs are larger than Social Security.
   d. TANF, EIC and Food Stamps are, considered individually, each a smaller program than Social Security. Collectively (TANF + EIC + Food Stamps), the three programs are still smaller than Social Security.

2. _____ What is the “Supplemental Security Income” program?
   a. another name for traditional, old age, Social Security
   b. another name for AFDC
   c. proposed individual savings accounts. Payments into these accounts would be voluntary and would be in addition to (i.e. on top of) an individual’s regular Social Security taxes.
   d. proposed individual savings accounts. Payments into these accounts would be voluntary and would replace part of an individual’s regular Social Security taxes.
   e. a programs which gives payments to people based primarily on whether or not they are aged, blind, or disabled rather than just their income.

3. _____ Which of the following is true of unemployment insurance?
   a. Unemployment insurance is “experience rated”. The amount a firm pays for unemployment insurance increases if it has laid off a large % of workers in the past.
   b. The federal government mandates that firms above a certain size buy unemployment insurance. The insurance itself, however, is provided by private firms.
   c. Unemployment insurance premiums are collected as part of the payroll (FICA) tax. The unemployment insurance program is the “UI” part of the Social Security/Medicare trust.
   d. Unemployment insurance benefits are fixed. They do not vary as a worker’s (former) income changes.

4. _____ What is Medicaid?
   a. Sports drink for Doctors and other medical professionals.
   b. The primary government program designed to assist the aged (i.e. old) in getting access to medical care.
   c. The primary government program designed to assist the poor in getting access to medical care.
   d. A proposed new government program to provide a federally subsidized prescription drug benefit to seniors.
5. _______ Billy-Bob states; “It is so hard to be detached. Consider transfer programs as an example. Most people, I think, decide what they’d like to see in a transfer program like based on their situation in life. The rich don’t like lots of transfers, the poor do. I’m reading about a book, however, which recommends that, when deciding on transfer programs, we try to take the perspective of someone who doesn’t know what their place in society will be.” Who wrote the book Billy Bob is reading?
   a. Thomas Aquinas.
   c. Frederich Nietzsche
   d. John Rawls
   e. Joan Robinson
   f. Thorsten Veblan

6. Peggy Lee supports adopting a transfer and tax system which is designed to ensure (near) equal distribution of disposable income. Recently, two studies have been released. Indicate (✓) whether each study provides and argument supporting to Peggy Lee’s goals.

<table>
<thead>
<tr>
<th>What does the study do?</th>
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<tbody>
<tr>
<td>Conclusions/Results of Study</td>
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<tr>
<td>all people have fundamentally the same ability to receive utility from goods and services (i.e. all utility functions are the same or at least very similar)</td>
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<tr>
<td>In the long-run, people work as hard and smart as they want to work regardless of how much they keep per hour. Therefore, in the long-run, redistribution programs will not affect the amount the economy produces.</td>
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7. _______ Which of the following is true of Social Security in 2003? This is not asking what will happen to Social Security in the future or what Social Security was in the past.
   a. Social Security is currently 100% “pay-go”.
   b. Social Security is currently 75% “pay-go” and 25% pre-funded.
   c. Social Security is currently 50% “pay-go” and 50% pre-funded.
   d. Social Security is currently 25% “pay-go” and 75% pre-funded.
   e. Social Security is currently 100% pre-funded.

8. _______ Who is getting a better deal (rate of return) from the Social Security taxes they paid, someone who retired in 1995 or someone who will retire in 2010? Assume both people earn(ed) the average income for their time period and age group.
   a. The person who retired in 1995 got a better deal (rate of return).
   b. The both get (approximately) the same rate or return. Social Security won’t be bankrupt yet and both earn(ed) the average income for their time period and age group.
   c. The person who will retire in 2010 will get a better deal (rate of return).
9. Batte Guyana is considering a national pension system. It wants to ensure 1) the elderly have minimum standards of living, 2) income distribution among the elderly is relatively equal, 4) those retiring in the distant future will have adequate benefits, 5) there are good work incentives, and 5) there are high investment levels. Indicate (√) which system is better for each criteria.

<table>
<thead>
<tr>
<th>Issue</th>
<th>Defined Benefits</th>
<th>Defined Contributions</th>
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<th>Pre-Funded</th>
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<td>high levels of investment</td>
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10. What is the retirement age under Social Security? Check (√) one box per row.

<table>
<thead>
<tr>
<th>Issue</th>
<th>59</th>
<th>62</th>
<th>65</th>
<th>67</th>
<th>70</th>
<th>73</th>
</tr>
</thead>
<tbody>
<tr>
<td>Earliest one can currently collect some Social Security</td>
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<tr>
<td>Earliest one will be able to collect full Social Security benefits in the future (2020)</td>
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11. _____ Steve expects to retire and be eligible to collect Social Security sometime around 2050. Assuming no changes are made to the current Social Security system. How much will Steve receive in Social Security benefits?

a. 100% of the benefits promised to him
b. ≅ 65% of the benefits promised to him
c. ≅ 35% of the benefits promised to him
d. 0% of the benefits promised to him
12. _____ Your text referred to Social Security’s “Substitution effect”. What is this “Substitution effect”?
   a. people shopping for jobs in which they can contribute to a system with individual retirement accounts instead of Social Security
   b. people favoring interest income over “earned income” because interest income is not subject to Social Security taxes
   c. people saving less, i.e. decreasing their private savings, because they believe social security will be there for them in the future
   d. people saving more, i.e. increasing their private savings, because they do not believe social security will be there for them in the future
   e. lower GDP as people retire earlier (i.e. work less) because of the existence of Social Security

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14 – 16 Match each type of transfer program with the appropriate graph below. Some answers may be used more than once. Use G if the answer is “none of the above”.

14. _____ AFDC
15. _____ EIC
16. _____ a Negative Income Tax

G. none of the above
17 - 20. Match each type of transfer program with the appropriate Budget Line. Some answers may be used more than once. Use Q if the answer is “none of the above”.

17. ____ a program giving an individual a payment in kind rather than cash

18. ____ AFDC

19. ____ EIC

20. ____ a Negative Income Tax

Q. none of the above
Exam 3: Part 2

(Same) Code Name: __________________________

Part B: Answer 1 of the following 2 questions (37.5 points)

B1. It is 2004 and little has changed regarding Social Security except that we have a new president, Georgiana Shrub. President Shrub proposes that 1/5 of each individual’s Social Security taxes will go into a private account in their name. The individual will be able to choose which mutual fund (at or above a certain safety rating) to invest their 1/5 in. The rest of their Social Security taxes are used the same way as in the past. A person’s benefits will be \( \frac{4}{5} \times \) their regular social security benefits + they can draw down whatever has accumulated in their private account as they please.

a. Explain how this plan (relative to the current system) will affect the benefits different groups (ages, income, etc.) of future retirees receive. Who gains and who loses and why?
   - the rich versus the poor
   - men (on average) versus women (on average)
   - the generation just entering the work force versus the generation soon to be retiring

b. Explain how and why his plan affects national savings? Is this a good thing? Why?

c. Does his plan change the fundamental nature (or mission) of the Social Security program? If so, in what ways? By how much (i.e. is the entire system changed or just parts of it?)

d. How does this plan affect the financial viability of the Social Security system? Explain your answer.

B2. You have been asked by President Bush and the Congress to devise a method for “saving Social Security”, i.e. restoring it to long-term financial stability, without introducing private individual accounts.

- Explain your plan and how it restores Social Security to long-term financial stability.
- How does your plan change Social Security and who gains and who loses from it?