

**ADVANCED SUBSIDIARY GCE
ECONOMICS**

Market Failure and Government Intervention

WEDNESDAY 4 JUNE 2008

2882

Afternoon
Time: 1 hour

Additional materials (enclosed): Designated Answer Booklet 2882/AB

Additional materials (required):
None



INSTRUCTIONS TO CANDIDATES

- Write your name in capital letters, your Centre Number and Candidate Number in the spaces provided on the Answer Booklet.
- Read each question carefully and make sure you know what you have to do before starting your answer.
- Answer **all** the questions.
- Write all your answers in the separate Answer Booklet provided.
- The space should be sufficient for your answers but if you require more space use the lined pages at the end of the Answer Booklet and number your answers carefully.

INFORMATION FOR CANDIDATES

- The number of marks for each question is given in brackets [] at the end of each question or part question.
- The total number of marks for this paper is **45**.
- The quality of your written communication will be taken into account in marking your answer to the question labelled with an asterisk (*).

This document consists of **4** printed pages.

Answer **all** parts of this question in the accompanying answer booklet.

Smoking and negative externalities

Governments around the world accept that cigarettes are a demerit good and that smoking creates many negative externalities. For this reason, governments intervene in an attempt to correct this example of market failure.

One possible solution to the problem of negative externalities is to use regulation backed up by the threat of fines. The following article considers one recent example of regulation – the banning of smoking in workplaces, pubs and clubs. 5

‘Britain gives up smoking’

Smoking will be banned in all workplaces, pubs and clubs from next year after an historic vote in the House of Commons. MPs voted for a total ban after last minute appeals from health campaigners ended months of argument over the issue. 10

Patricia Hewitt, the Health Secretary, said that the law would ban smoking in “virtually every enclosed public place and workplace.” This would save thousands of lives a year, including those of many non-smokers who have to breathe in cigarette smoke from others. Peter Hollins, director-general of the British Heart Foundation, said “The vote is a landmark victory for the public health of this country and it will save the lives of many people across the UK”. In addition, if some people manage to give up smoking as a result of the ban, then experts suggest that this will save the National Health Service (NHS) many millions of pounds every year. 15

Fines will be used to ensure that the law is followed. Premises which fail to display ‘no smoking’ signs will be given on the spot fines of £200, whilst organisations which fail to stop people smoking in banned areas could be fined up to £2500. 20

Many problems remain with the enforcement of the law. For example, smoking will be permitted in private cars but banned for both taxi drivers and their passengers. Likewise there is some confusion as to how the ban will be applied to sports grounds – if a sports ground has a roof which is closed, then smoking will be banned, but if the roof is open, then smoking will be permitted. 25

Nevertheless, whilst the finer details of the ban are still being worked out, many public health campaigners welcome this new law as being a significant step forward.

Adapted from *The Times*, 15 & 16 February, 2006.

- (a) (i) Explain what is meant by the term 'social cost'. [2]
- (ii) Identify **one** example of a private cost arising from smoking. Explain why this is a private cost. [3]
- (b) (i) Identify **one** example of a negative externality arising from smoking. Explain why this is a negative externality. [3]
- (ii) Using a diagram, explain why negative externalities give rise to the problem of market failure. [10]
- (c) "Governments around the world accept that cigarettes are a demerit good" (line 1).
- (i) Explain what is meant by the term 'demerit good'. [2]
- (ii) Using an example, explain how the provision of greater information can correct the market failure arising from demerit goods. [3]
- (d) Regulation and minimum price controls are possible solutions to the market failure arising from negative externalities.
- (i) State and explain **two** advantages of using regulation to correct market failure. [4]
- (ii) Comment on the effectiveness of introducing a minimum price control as a solution to the negative externalities resulting from smoking. [6]
- *e)** Another solution to negative externalities is that of taxation. Discuss the effectiveness of taxation in correcting the market failure arising from negative externalities. [12]

[Total: 45 marks]

Copyright Acknowledgements:

Text: Adapted from Philip Webster and David Charter, *Britain gives up smoking*, The Times, 15 February, 2006; David Charter, *When is a ban not a ban? When the smoke can escape through the roof*, The Times, 16 February, 2006.

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