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Quiz#5 (Semester 1/2019) EE312 Static general equilibrium

Suppose that the economy starts from a competitive equilibrium. Then, the government imposes a *unit tax* on firm. That is, firm must give up a fraction of its output to the government. Suppose the tax rate is "t". Discuss the following questions

a) How does the new government policy affect firm's employment decision? Why? Compare the outcome with that would have happened if firm is instead taxed with the lump-sum method.
b) Use the demand and supply diagram, show the effect of government tax's policy on the competitive equilibrium.