

“Since monopolies make super-normal profits, would it be a good idea to tax them?”

Introduction

Thesis: It would usually not be a good idea to tax monopolies because, firstly, it would not improve efficiency and, secondly, the incidence of the tax on consumers can exceed 100%. However, in some cases – for instance when the tax on consumers will not exceed 100% – the government can use an ad valorem tax to maximize government revenue.

Body

- Because monopolies raise prices above competitive levels ($P > MC$), they are not Pareto Efficient (define term). (explain this with a diagram)
- Compare this to competitive markets.
- However, a tax on monopolies would not improve this. Other government interventions such as price ceilings could be more helpful for this.

- However, what if the government just wants to impose a tax to get more government revenue?
- Then, it could lead to bad consequences for the consumer because the effective incidence of the tax can exceed 100%. (explain this with a diagram)

- However, in some markets this problem might not arise (the incidence of the tax would not be so large). And, because monopolies make a lot of profit, it would then be smart for a government to tax them as this would create a lot of government revenue.
- The government should do this by imposing an ad valorem tax because this would maximize government revenue. (explain this with a diagram)

Conclusion