

2. The effects of a tariff on imported kumquats can be divided into the following categories: tariff revenues received by the treasury (\$8 million); increased use of resources to produce more kumquats domestically (\$6 million); the value of reduced consumption by domestic consumers (\$13 million); and increased profits received by domestic kumquat growers (\$5 million). A CBA from the national perspective would find costs of the tariff equal to \$19 million—the sum of the costs of increased domestic production and forgone domestic consumption (\$6 million + \$13 million). The increased profits received by domestic kumquat growers and the tariff revenues received by the treasury simply reflect higher prices paid by domestic consumers on the kumquats that they continue to consume and, hence, count as neither benefits nor costs. Thus, the net benefits of the tariff are negative (–\$19 million). Consequently, the CBA would recommend against adoption of the tariff.

- a) Assuming the agriculture department views kumquat growers as its primary constituency, how would it calculate net benefits if it behaves as if it is a spender?**
- b) Assuming the treasury department behaves as if it is a guardian, how would it calculate net benefits if it believes that domestic growers pay profit taxes at an average rate of 20 percent?**

2.a. If the agriculture department behaved as if it were a "spender," then the benefits would probably be:

- \$5 million domestic grower profits ("constituents")
- \$8 million tariff revenue (income from foreigners)

Total benefits: \$13 million

Costs would be \$13 million (reduced consumption)

Net benefits: \$0 million.

A spender might treat the additional resources devoted to domestic kumquat production (\$6 million) as a cost (if the resources go to non-constituents) or as a benefit (if the recipients are their constituents, such as labour). Either would be okay. However, the description of the question implies that the growers are the primary constituents, thus we would lean towards the view that a spender would not treat the \$6 million as a benefit.

If the agriculture department behaved as if it were a "spender," then it might consider the increased prices paid by domestic consumers as a cost. However, again we would argue that the growers are the primary constituency and, therefore, a spender would probably ignore the increased prices paid by domestic consumers. For this reason, a "spender" might also ignore the \$13 million loss in consumption benefits.

2.b. If the treasury department behaved as if it were a "guardian," then it would count only the costs and benefits accruing to the government. If so, benefits would equal \$9 million (\$8 million in tariff revenue and \$1 million = 20% x \$5 million in profits tax) and costs would be zero, so that net benefits would equal \$9 million.

