

Chapter 7 MULTIPLE-CHOICE QUESTIONS

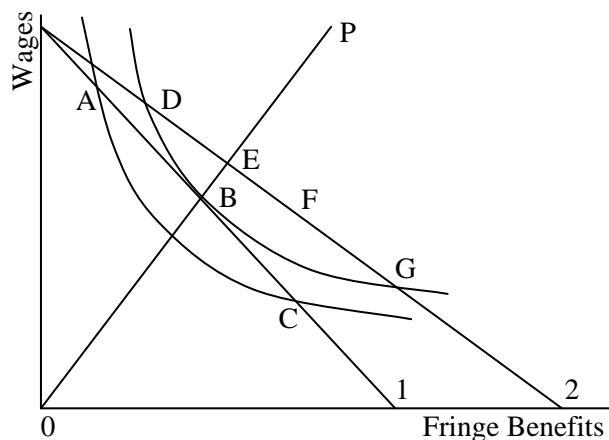
1. "Total compensation" includes:
 - a. Wages and salaries and all fringe benefits
 - b. Wages and salaries and public (legally mandated) fringe benefits only
 - c. Wages and salaries and private (nonmandatory) fringe benefits only
 - d. Wages and salaries and all fringe benefits net of all personal taxes
2. Fringe benefits currently account for approximately what percentage of total compensation?
 - a. 5% – 10%
 - b. 15% – 20%
 - c. 25% – 30%
 - d. 35% – 40%
3. As a percentage of benefits, the largest share goes to:
 - a. retirement and savings
 - b. insurance
 - c. paid leave
 - d. legally required benefits
4. The proportion of total compensation paid out as fringe benefits tends to be larger in:
 - a. high-paid industries compared to low-paid industries
 - b. service industries compared to manufacturing industries
 - c. white-collar occupations compared to blue-collar occupations
 - d. retail trade compared to transportation and public utilities
5. The share of fringe benefits in total employee compensation:
 - a. grew steadily in the 1960s and 1970s but has fallen since 1980
 - b. was unchanged in the 1960s and 1970s and has fallen since 1980
 - c. shrank in the 1960s and 1970s and has remained constant since then
 - d. grew steadily from 1960 through the mid-1990s
6. Which one of the following is *not* a valid explanation for why workers may prefer an extra dollar's worth of fringe benefits to an extra dollar's worth of cash?
 - a. workers may prefer to bind themselves against their own tendencies toward immediate gratification
 - b. certain fringe benefits effectively trade current taxes for future taxes
 - c. people generally prefer in-kind benefits to cash
 - d. certain fringe benefits are untaxed
7. Because there is a _____ marginal rate of substitution of fringe benefits for wages, a worker's wage-fringe indifference curves are typically _____:
 - a. diminishing; convex to the origin
 - b. constant; straight lines
 - c. diminishing; concave to the origin
 - d. negative; straight lines
8. The slope of a wage-fringe indifference curve reflects:
 - a. the overall utility level of a person
 - b. a worker's willingness to give up an extra dollar of wages in exchange for an extra dollar of fringe benefits
 - c. the firm's cost of paying an extra dollar of compensation as wages rather than fringe benefits
 - d. an increasing marginal rate of substitution of fringe benefits for cash

9. An individual wage-fringe isoprofit line shows:
- combinations of wages and fringe benefits that result in constant dollar values of total compensation
 - combinations of wages and fringe benefits that result in the same profit to the firm
 - the greatest possible profit attainable from a given level of fringe benefits
 - the greatest possible profit attainable from a given level of wages
10. The slope of a wage-fringe isoprofit curve reflects:
- the overall profitability of the firm
 - a worker's willingness to give up an extra dollar of wages in exchange for an extra dollar of fringe benefits
 - the relative "price" of fringe benefits compared to wages
 - an increasing marginal rate of substitution of fringe benefits for cash
11. The firm's wage-fringe isoprofit curve typically has a slope less than 1 (absolute value) because:
- fringe benefits confer tax advantages on workers
 - on average, it costs firms more to purchase fringe benefits than workers
 - the composition of fringe benefits may increase worker productivity
 - increasing the proportion of compensation received as fringe benefits reduces a firm's profit level
12. If a firm can offer fringe benefits worth more than one dollar for a one dollar reduction in wages:
- the wage-fringe isoprofit line will be upward-sloping
 - the wage-fringe isoprofit line will have a slope less than one in absolute value
 - the marginal rate of substitution between wages and fringe benefits will be greater than one at the wage-fringe optimum
 - as a proportion of total compensation, fringe benefits will likely exceed one half
13. The employer's share of the Social Security and Medicare components of the payroll tax has increased, from 6.13% in 1980 to its current rate of 7.65%. Because employers pay no payroll tax on many fringe benefits, this change in tax rates has effectively:
- reduced the "price" of fringe benefits, increasing the slope of the wage-fringe isoprofit line
 - increased the "price" of fringe benefits, increasing the slope of the wage-fringe isoprofit line
 - reduced the "price" of fringe benefits, reducing the slope of the wage-fringe isoprofit line
 - increased the "price" of fringe benefits, reducing the slope of the wage-fringe isoprofit line
14. The trend of fringe benefits as a percentage of total compensation can be partially explained by the fact that:
- tax reform has rendered many types of fringe benefits fully taxable
 - "in-kind" benefits restrict workers' consumption choices
 - the firm may be able to purchase fringe benefits more cheaply than workers
 - many types of fringe benefits are income inelastic
15. Fringe benefits will tend to be a greater proportion of total compensation, the:
- more income elastic are fringe benefits
 - more they increase worker turnover
 - lower the employer's share of the Social Security tax
 - less there are economies of scale in purchasing fringe benefits

16. Which of the following is *not* a cause of fringe benefit growth?
- Tax advantages to the employer
 - Efficiency considerations
 - Economies of scale
 - Fringe benefits are income inelastic

Questions 17 – 21 refer to the diagram below. All points along the ray OP reflect a constant proportion of wages to fringe benefits.

17. The shape of the indifference curves reflects:
- a diminishing marginal rate of substitution of fringe benefits for wages
 - increased utility as fringe benefits are substituted for wages along an indifference curve
 - increased utility as wages are substituted for fringe benefits along an indifference curve
 - an increasing marginal rate of substitution of fringe benefits for wages



18. Given isoprofit line 1, this worker's wage-fringe optimum is given by point:
- A
 - B
 - C
 - D
19. Suppose some development rotates the isoprofit line outward, to line 2. If history is a guide, we would expect this worker's new wage-fringe optimum to be at point:
- D
 - E
 - F
 - G
20. Which one of the following events could *not* have caused a shift from isoprofit line 1 to line 2?
- The employer's share of the payroll tax rate has increased and the limits expanded
 - Firms structured fringe benefits so as to increase worker productivity
 - The government began to subject some fringe benefits to the personal income tax
 - Insurance companies offered group discounts for medical and disability coverage
21. If the isoprofit line shifts from line 1 to line 2, then:
- to maintain profit level 2, the firm must provide more fringe benefits and reduce wages
 - to maintain profit level 2, the firm must reduce fringe benefits and raise wages
 - as the firm moves from line 1 to line 2, it could provide more fringe benefits while paying the same wage rate
 - providing more fringe benefits would reduce the firm's profit
22. One view of the firm is that stockholders hire managers who, in turn, hire workers. Maximum profits are earned by satisfying the customer. The two principal-agent relationships illustrated in this view are:
- manager-stockholder; worker-manager
 - stockholder-manager; customer-manager
 - manager-stockholder; manager-worker
 - stockholder-manager; manager-worker

23. The principal-agent problem arises primarily because:
 - a. principals and agents work in a team, leading to free-rider problems
 - b. principals and agents have common interests
 - c. principals pursue some of their own objectives that may conflict with the objectives of the agents
 - d. agents pursue some of their own objectives that may conflict with the objectives of the principals
24. Which one of the following best represents the principal-agent problem in the employer-employee relationship?
 - a. An employee works during a paid lunch hour in order to leave work one hour early
 - b. An employer fails to provide safety goggles to a worker as required by occupational safety and health legislation
 - c. a worker leaves work early without permission
 - d. A worker opts for early retirement in response to the firm's incentive plan
25. Compensation paid in proportion to the value of sales best describes:
 - a. piece rates
 - b. commissions
 - c. time rates
 - d. bonuses
26. Which of the following best exemplifies a piece-rate compensation scheme?
 - a. Jose's pay is proportional to the number of wiring harnesses he assembles each day
 - b. Carla's pay is proportional to the value of her sales at the dress shop each month
 - c. Stan's pay is proportional to the number of his textbooks sold each year
 - d. Louise's pay is proportional to the number of hours she works each month
27. Royalties would most likely be received by a(n):
 - a. art dealer
 - b. factory worker
 - c. used car dealer
 - d. author
28. For employers, the chief advantage of royalties and commissions is that these pay policies:
 - a. promote teamwork and cooperation
 - b. increase turnover
 - c. reduce shirking where work effort is costly to observe
 - d. reduce income variability
29. Salaried workers can be considered "quasi-fixed resources" in that:
 - a. production is largely independent of the firm's use of salaried workers
 - b. federal work rules limit the ability of firms to fire salaried workers
 - c. their work hours typically are fixed
 - d. raises or promotions may be used to reduce shirking
30. Raises and promotions are used by employers as a device to:
 - a. reduce shirking by salaried workers
 - b. transform labor from a quasi-fixed to a variable resource
 - c. reduce turnover by hourly workers
 - d. reduce free-riding by teams of workers
31. In a work environment in which teamwork is highly valued, pay is more likely to be received as:
 - a. piece work
 - b. commissions
 - c. time rates
 - d. royalties

32. A simple income-leisure model might predict that salaried workers would work fewer hours than hourly workers. In fact the opposite seems to be true, in part because:
- raises and promotions are “won” on the basis of productivity rankings
 - firms typically offer raises and promotions solely on the basis of seniority
 - of the principle-agent problem
 - salaried work is an example of a deferred compensation scheme
33. The effectiveness of profit-sharing plans may be diminished because:
- potential free-rider problems render such plans ineffective in all but the largest firms
 - profit-sharing is a type of deferred payment scheme
 - the plans are tied to group performance, so the link between profit-sharing and worker productivity is not always clear-cut
 - there is no means by which greater work effort can be translated into greater compensation for a worker
34. Team bonuses:
- solve the free-rider problem associated with individual bonuses
 - create a principal-agent problem by channeling effort toward team performance at the expense of individual performance
 - typically comprise a large percentage of the total compensation of middle managers, but almost none of the total pay of top executives
 - work best when targeted at relatively small groups of employees
35. In some instances, profit sharing may not be a very effective tool for raising worker productivity because of the:
- free-rider problem
 - principal-agent problem
 - retirement problem
 - tax and accounting rules that cause economic profit to differ from accounting profit
36. The free-rider problem is most likely to arise in:
- small groups
 - firms that tie bonuses to individual performance
 - a profit-sharing plan
 - firms that use piece rates
37. A stock option will have value to a worker if:
- the firm’s stock price is expected to rise
 - the firm’s stock price is expected to fall
 - the “grant price” of the stock is expected to exceed its market price
 - none of the above
38. Tournament pay:
- reduces profits because of the excessive pay to chief executive officers implied by such plans
 - may help to rationalize why some ineffective senior executives continue to be employed by a firm
 - explains why “hostile” corporate takeovers occur
 - explains why chief executive officers typically serve long periods at the top of their companies

39. Raises and promotions may be viewed as a form of:
- profit-sharing
 - commissions and royalties
 - piece rate pay
 - tournament pay
40. Compared to their counterparts in other developed countries, CEOs in the U. S. are paid:
- considerably less
 - about the same
 - considerably more
 - a greater percentage of their compensation in the form of straight salary
41. A firm might choose to pay its employees a wage higher than that which would clear the market because:
- the higher wage raises the opportunity cost of shirking
 - the higher wage may shift the labor demand curve to the left
 - the firm will have higher turnover, allowing new workers to invigorate the work place
 - the higher wage solves the free-rider problem

Questions 42 and 43 refer to the following information. Suppose a “fully effective” worker can produce 20 units per hour in a particular firm. The firm’s wage-productivity relationship is given by the table below:

42.	If the actual wage is \$7, the wage cost per effective unit of labor is:		<u>Wage</u>	<u>Output per Worker</u>
			\$10	20
a.	\$3.50	c.	9	20
b.	\$10.00	d.	8	16
			7	10

43. This firm’s efficiency wage rate is:
- \$7.00
 - \$8.00
 - \$9.00
 - \$10.00
44. According to efficiency wage models, the firm’s profits will increase whenever the wage causes:
- worker productivity to increase by a larger proportion than the wage increase
 - worker productivity to increase
 - worker turnover to fall
 - worker nutrition to increase
45. One implication of efficiency wage models is that:
- firms pay wages below the market-clearing rate
 - an excess supply of labor may be created
 - an excess demand for labor may be created
 - CEO contracts will contain golden parachute clauses
46. Which one of the following is *not* typically offered as an explanation for efficiency wages?
- An employer will not pay a wage that exceeds the market rate
 - A higher wage may reduce turnover
 - A higher wage may allow lower income workers to afford better nutrition that increases their stamina
 - The higher wage may be perceived by workers as raising the opportunity cost of shirking

47. Efficiency wage models are often criticized because:
- a. other pay-for-performance plans could serve as a substitute for an efficiency wage
 - b. employees could be required to post a forfeitable bond instead
 - c. shirking could be reduced by deferred compensation plans
 - d. all of the above
48. Labor market efficiency requires that each worker be allocated to:
- a. the job offering the highest wage available
 - b. the job offering the best fringe benefits available
 - c. his or her optimal job
 - d. his or her optimal job, and that each firm implements its optimal compensation package