THE ECONOMY TODAY 13e

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YouTube READY

YouTube Title: "Front Fell Off"
http://www.youtube.com/watch?v=WcU4t6zRAKg&feature=related
Video Length: 2:02 minutes

The Economy Today **Chapter 28: Environmental Protection**
The Micro Economy Today **Chapter 14: Environmental Protection**
The Economy Today **Learning Objective 1: How markets encourage pollution**

Topics: Market Failure: External Costs
Key Terms: Negative Externalities, External Costs, Externalities in Production

Summary

This comedy skit is a mock interview of a "Senator Collins" who attempts to describe the oil spill disaster that occurred in 1991 when the Greek tanker *Kirki* lost its bow off the west coast of Australia. He details the account of the "front falling off" the tanker and the resulting 20,000 tons of crude that spilled into the ocean.

Economic Application

The term externalities refers to all costs or benefits of a market activity borne by a third party, that is, by someone other than the immediate producer or consumer. In production, these externalities may occur when a power plant burns high-sulfur coal or an oil tanker spills thousands of tons of oil and therefore damages the surrounding environment. The damage inflicted on the neighboring people, vegetation, and ecosystem is external to the cost calculations of the firm and are not reflected in the price of the products created by the firms. The behaviors of profit maximizers are guided by comparisons of revenues and costs, not by philanthropy, aesthetic concerns, or the welfare of fish.

Multiple-Choice Question

Which of the following is an example of an external cost associated with the oil production (including oil transportation) described in the YouTube mock interview?

a) The costs borne by the oil company to clean up the oil spill.
b) The increased price borne by oil consumers due to the 20,000 ton decreased supply of oil.
c) The costs borne by the oil tanker company to fix the bow of the boat.
d) The costs borne by West Australian fishers because of the die-off of the fish population caused by the oil spill.

Discussion Question

If a firm's price of its product did, in fact, include all external costs, how would this change production decisions?