ECON 224: Second Quiz
November 27, 2012

5 points for each question, total of 30 points.

1. The vertically integrated electricity utilities were unbundled into three segments: digestion, circulation, and defibrillation.

T  F  Explain: generation, transmission, distribution

2. In rate-base rate-of-return regulation (RoR), there is an incentive to “pad the rate base.”

T  F  Explain: In RoR, the average cost is calculated as variable cost plus a fair rate of return on the “rate base” of capital. The bigger the rate base, the higher the allowed price.

3. Unbundling is the same thing as structural separation.

T  F  Explain: Unbundling involves any separation of an industry into segments performing different functions. In structural separation, no company is allowed to do business in more than one segment.

4. In ruinous competition, firms lower their prices until one firm exits the market and a monopoly is all that is left.

T  F  Explain: Firms do lower their prices below AC, perhaps all the way to MC since that still brings in some revenue on the margin. But no firm ever exits because the fixed capital is a sunk cost and still has the most value in continuing to operate in the same industry.