
Incidence - Lecture 1

1. Incidence of Commodity Taxation: Heating Oil

Consider the heating oil market in New England. Demand is

$$Q^D = 300 - 40P$$

and supply is

$$Q^S = 20P$$

where P is dollars per gallon and Q is thousands of gallons.

- (a) Compute the market equilibrium (price and quantity).
- (b) Now suppose a per-gallon tax of $t = \$3$ is imposed on heating oil. Compute the new equilibrium price paid by consumers P^C , the price received by producers P^S , and the traded quantity.
- (c) Explain the incidence of the tax and the intuition.