Chapter 12 # 1: What are the benefits and costs to having a property right in information as opposed to a communal right?

The benefits to property right in information is that it incentivizes those who produce information (such as researchers) to create / gather more information. This, however, discourages the dissemination of information. On the other hand, communal rights to information encourage dissemination of information but may discourage the gathering of information.

Chapter 12 #2: Why are buyers of antiques not required to tell the seller of the true value of the item?

If a person were forced to divulge information about antiques, his incentive to gain the information in the first place would be greatly diminished, and we would have suboptimal exploration.

Chapter 12 #3: Why is the seller of a house required to notify the buyer of latent defects?

The economic answer is that in general, the person has a property right to information when it is costly to gain such information, but the person does not have a property right and therefore cannot take advantage of his information when the information is obtained at very low cost.

In terms of latent defects, the seller of a house is obligated to tell the future buyer about its latent defects since the seller is likely to know them as a by-product of ownership (that is, no extra cost is involved in obtaining the information). Forcing the disclosure in this case is unlikely to reduce the amount of information gathered by the seller. Furthermore, it would be costly for the buyer on his/her own to discover the defects before purchase. Even worse, with multiple potential buyers incurring costs to collect such information, the costs would be too much.

Chapter 12 #4: What are the cost and benefits of a patent system?

The main cost is that the holder of the patent is granted a monopoly. Therefore, the supply of the patented item will be less than optimal.

The main benefit is that patents incentivizes innovators to invent at the optimal level given that they can adequately capture the return on their inventions.

In the absence of patents, transaction costs would be excessively high since dissemination of information to the appropriate parties and monitoring the terms of the contracts made would be too expensive. Therefore, patents take away those transaction costs.

Chapter 12 #5: Why are trademarks a property right? Why are trademarks for as long as the company is in business and not just for twenty years as patents are?

Trademarks are property rights because their owners gain value from them as the owners maintain a certain level of quality. They are useful to the extent that they distinguish one company's products (or services) from another.

Without trademark protection, others will have an incentive to provide shoddier but cheaper to produce goods and then pretend that they are selling the trademarked items. If there are no trademarks, buyers will have to rely on more costly methods such as inspection of the item and/or establishment of long-term relationships with sellers.

Therefore, the quality control that trademarked goods uphold makes it so that trademarks are respected as long as the company is in business.

Chapter 12 # 6: Why does Paul Newman have the property right to his name?

Because having the property right on his name allows him to administer it as he sees fit. Any other solution would involve high transaction costs. If his name were a communal right, the value of his name would fall a lot and in the end it would be discredited. Having the right to disallow others from using the name doesn't work either because he would have to go about contracting with other people to not use his name. This means that an enormous amount of transacting would have to be undertaken.

Chapter 12 #7: Should rap groups be allowed to include phrases from other singers' recordings without compensation?

Phrases in singers' recordings cannot be trademarked because doing so would make the trademark too encompassing. Their lines are used ordinarily in many circumstances.

Chapter 12 # 8: Should telephone directories be copyrighted or should one company be allowed to copy the phone directory of another company without charge? A publisher could include phone people and phone numbers to catch those who copy directly from its phone book.

If there were no copyright, there would be no incentive to go through the trouble to get together all the information for the phonebook. In other words, phonebooks should be protected for the same reason there is a copyright on regular books. It's an original work piece that should be protected by the law. Gathering all the information is not trivial. If there is no copyright, after the first phonebook provider all the rest would just free ride on the first one. Moreover, if the law gives Paul Newman the property right to his picture for advertising, even if the allocation is incorrect, it is easily remedied. If the law mistakenly provides a communal right to his picture, it cannot be remedied.

Chapter 13 #1: When is the harm-benefit distinction meaningful?

When there are transaction costs and the efficient outcome is determined, then the appropriate allocation of entitlements is obvious and the harm-benefit distinction becomes relevant.

Chapter 13 # 2: Why do economic markets tend to use carrots, while pollution and traffic safety use sticks.

Markets use carrots, i.e. restitution for benefit, because in a market scenario we have people transacting with each other. So they know each other when benefits are exchanged. If we had liability for not transacting, then the transaction costs would be excessive because we don't know who we would have transacted with.

In case of traffic and pollution safety, the government sets the efficient outcome and punishes for deviations (by holding the deviator liable). The persons harmed come out and reveal themselves. Using restitution would involve too large transaction costs as people that follow the rule come up and ask for their reward. <u>But deviating from the rules is much less common than abiding by the rules</u>.

Chapter 13 #3: Why do long-run entry and exit decisions affect our choice regarding punishment and reward?

In the long-run, damage prevention can also be achieved by exit of factories or residents from the area or by one or the other not entering the area in the first place. When there is some punishment mechanism in place, we may find that less-than-optimal number of firms have been started and have remained opened (or the production level is in the sub-optimal level) since many of these firms add on the punishment to their costs. On the other hand, rewards involve *extremely high transaction costs (from assuring that the 'positive' deed was actually done to monitoring that its maintenance is upheld).*

Chapter 13 #4: Why do negative externalities create clear guidelines concerning punishment (you should be punished for deviation from efficiency), while positive externalities create less clear guidelines (it is not clear that you should be rewarded for acting efficiently)?

In terms of the creation of negative externalities, we know who is producing such externalities and can clearly disincentivize such activities by punishing the production of negative externalities when caught. However, rewarding positive externalities poses many issues. For one, if an individual has an intrinsic incentive to make such an externality, then the act, itself, is the reward and therefore we should not need to reward the individual (and hence, procure more costs) to reach the efficient outcome.

Furthermore, collecting information about who created such externalities poses high transaction costs. This follows from the argument that we would need to find those who create positive externalities.

Chapter 13 #5: In *Rylands v. Fletcher*, 3 HL 330 (1868), the defendants had dammed an area covering an old abandoned coal mine to create a water mill. The coal mine had not been completely blocked off, and consequently, the water drained into the abandoned mine and into adjacent mines directly connected to the old mine. The adjacent mines were still operating and the plaintiff sued for damages. Who should be liable?

In this situation, we run through an analysis to determine the efficient outcome and how it affects future behavior. A cost-benefit analysis can be conducted. We know that if we make the owners of the abandoned coal mine liable, we would make the owners of abandoned coal mines make sure that their mines are completely blocked off. On the other hand, if the defendants who dammed the area are made liable, then parties who plan to dam areas will need to spend much more to make sure that all parts of abandoned coal mines are properly sealed. Because of this high transaction cost, it seems to be more efficient to instead make the abandoned coal mines liable because it will be much cheaper for them to do so.

Chapter 13 #6: If your neighbor's house needed a paint job, why couldn't you collect from the neighbor if you decided to paint her house on your own?

First of all, your neighbor may not have wanted his house painted. Secondly, any compensation for painting a neighbor's house without the consent of the neighbor would *incentivize people in the future to look for different activities that they think they could do in order to be compensated for their work without even asking the property owner. These people may act as their own judges of what should be done and will end up doing what they deem are much-needed activities.*

On the other hand, if the neighbor really wanted his/her house painted, he/she would have made arrangements to have it painted. Hence, if unarranged painting of the house is compensated, then this will result to more than optimal number of house paintings and number of people trying to paint other people's houses.

Chapter 14 #1: If the government takes your property, it must compensate you. But if through regulation it diminishes the value of your property by an equivalent amount, the government does not have to compensate you. Why? As always, only use economic arguments, not legal ones.

Compensation for regulation would not create incentives for greater efficiency (for the present and the future) because regulation has (or is presumed to have) already achieved the efficiency goal since it reduces negative externalities down to the optimal level. Furthermore, compensation would involve unnecessary court costs in order to transfer wealth as well as other transaction costs in determining the value of the losses.

In contrast, compensating for physical taking of property involves much lower transaction costs. The particular properties taken are legally transferred to the state so the additional transaction cost of paying for the transfer is relatively minor.

Chapter 14 #2: Under what circumstances should the government compensate for regulation? Explain.

The government should compensate for regulation if the property procures positive externalities as in the case of landmarks. Regulations should not reduce any incentives to provide such properties with positive externalities.

Furthermore, there should be compensation if government regulation is inefficient as in the case of Averne Bay Construction Company v. Thatcher, 15 N.E. 2d 587 (1938) found in page 125 of the textbook. In this situation, the zoning regulation did not make sense for the location's characteristics.

Chapter 14 #3: Why are we more inclined to compensate for positive externalities than for negative externalities?

We are more inclined to compensate for positive externalities because we want to motivate the creation of such externalities. Compensating negative externalities only result to a transfer and does not lead to an efficient outcome as no incentives are made to reach efficiency.

Chapter 14 #4: Even when there are positive externalities, compensating for regulation is problematic. Explain.

A system of compensation does involve considerable administrative costs, even in the case of positive externalities. The government will have to evaluate how much to compensate property owners and, at the same time, determine who should be compensated. Therefore, one must weigh the costs against the long-run misallocation costs under a system of regulation without compensation.