

WILFRID LAURIER UNIVERSITY
Waterloo, Ontario

Session: Winter 2008
Economics 310U
Economic Analysis of Law

Name: _____
ID#: _____
Section: _____

Instructor: Azim Essaji

Number of Pages: Cover page plus five (5) question pages

Time Allowed: 2 Hours

Aids: Dictionaries, Translation Dictionaries, Non-programmable, non-graphing calculator

The doors of the examination room will be opened approximately 10 minutes before the start of the examination. Candidates will be permitted to enter the examination room quietly up to one half hour after the scheduled start of the exam. Candidates arriving late will not be allowed any extra time.

Candidates must not begin the examination or attempt to read the examination questions until instructed to do so.

Candidates once having entered, may not leave the exam room before completing and submitting the exam unless accompanied by a Proctor. Candidates are not permitted to submit their examination and leave the examination room until 1 hour after the examination has begun, and in no case before their attendance has been taken. In no case may a candidate leave the room temporarily, for any reason, until 30 minutes after the start of the examination. In order that remaining candidates are not disrupted, candidates must remain seated and may not leave the examination room during the last 15 minutes of the examination session.

At the close of the examination period, candidates must stop writing immediately. The Presiding Officer may seize the papers of candidates who fail to observe this requirement, and a penalty may be imposed at the discretion of the instructor. Candidates must submit all their work, according to the instructions of the Presiding Officer, including all materials and a copy of the examination paper with their name and student ID number written on it. Unused examination booklets may not be taken from the examination room.

A candidate who leaves before the examination is over must hand in all completed and attempted work, notes made during the exam, and a copy of the examination paper with their name and student ID number on it.

Talk or any form of communication between candidates is absolutely forbidden. No information of any kind is to be written on the question paper or on scrap paper for the purpose of assisting other candidates. Responses to questions must not be done in an exaggerated way or in a manner that will involve transmission of information to others.

Candidates must remain seated during the examination period. A candidate needing to speak to the proctor (e.g. to ask for additional supplies or to request permission to leave the examination room for any reason) should so indicate by raising his or her hand.

Questions concerning possible errors, ambiguities or omissions in the examination paper must be directed to the proctor who will investigate them through the proper channels. The proctor is not permitted to answer questions other than those concerning the examination paper.

Candidates must not use or attempt to use any improper source of information. No candidates for an examination may bring into the examination room any books, notes or other material containing information pertaining to the examination unless the examiner has given instructions that such material will be allowed and this instruction is specified on the examination paper. Any item brought into the examination room is subject to inspection.

No briefcases, backpacks or other bags and carriers may be brought to the desk site where the candidate is writing the examination. These bags should be left outside the examination room. If books, notes etc. cannot be left outside the examination room, they must be put at the front of the examination room in a place designated by the proctor before a candidate takes a seat. Candidates are advised not to bring valuables to the examination room.

No electronic or communication devices will be allowed in the examination room, including cell phones, blackberries, pagers, etc. Calculators are not allowed unless specified by the instructor and indicated on the examination paper. Only non programmable models authorized by the instructor will be allowed. It is the candidate's responsibility to ascertain whether the use of calculators is permitted, and, if it is, whether any restrictions are imposed on the types of calculators that may be brought to the examination.

Translation dictionaries (e.g. English French) or other dictionaries, (thesaurus, definitions, technical) are not allowed unless specified by the instructor and indicated on the examination paper. Electronic dictionaries are never allowed.

Except for bottled water, no food or drink is allowed in the examination room. Candidates with health problems that warrant relaxation of this regulation should provide medical documentation to the presiding officer prior to the beginning of the examination. Such students should restrict themselves to those items and packaging that will least distract other examinees.

Candidates are expected to write their examinations in an honest and straightforward manner. Where there are reasonable grounds for believing a violation of exam protocol has occurred, the candidate will be subject to the disciplinary procedures and sanctions according to the University Calendar.

Only currently registered students will be permitted to write the final exam.

Examinations conducted at Wilfrid University will be bound by WLU regulations, regardless of where the candidate is registered.

Approved by Senate (Oct. 27/2003)

Total Marks: 120

Part A: Please answer BOTH of the following two questions. Each question is worth 20 marks. Please remember: this is a course in the Economic Analysis of Law. Consider economic rationales in answering the questions below.

Question A1

Suppose an accident causes \$100 worth of harm to the victim. The injurer is the only one who can take precautions to avoid the accident. The probability of the accident occurring is given by:

$$p(x) = \frac{10}{10x + 10},$$

where x is the injurer's level of precaution. Each unit of precaution costs \$1, i.e., $w = 1$.

Note that,

$$p'(x) = -\frac{100}{(10x + 10)^2}.$$

Suppose that it costs \$800 for the victim to bring suit, \$800 for the injurer to defend the suit, and that the suit costs the legal system \$500.

- (a) (4 marks) Assuming that the victim does not bring suit, what level of precaution will the injurer undertake?
- (b) (5 marks) If the victim does bring suit, what level of precaution will the injurer undertake?
- (c) (1 mark) Will the victim bring suit?
- (d) (10 marks) What is the total social cost of bringing the suit? Is it efficient to bring the suit?

Question A2

Suppose an accident causes \$2,000 worth of harm to the victim. The injurer and the victim can both take precautions to avoid the accident. The probability

of the accident occurring is denoted by

$$p(x, y) = \frac{5}{x + 10} + \frac{5}{y + 10}$$

where x represents the units of precaution taken by the injurer and y denotes the precautions taken by the victim. Each unit of precaution costs \$1, i.e. $w = 1$ and $r = 1$.

Note that the partial derivatives of $p(x, y)$ are

$$\frac{\partial p(x, y)}{\partial x} = -\frac{5}{(x + 10)^2}$$

and,

$$\frac{\partial p(x, y)}{\partial y} = -\frac{5}{(y + 10)^2}$$

- (a) (3 marks) What are the socially-optimal levels of precaution?
- (b) (6 marks) Will the rule of negligence yield optimal precaution levels? Assume that the court sets the injurer's threshold level of precaution at $\bar{x} = 40$.
- (c) (6 marks) Will the rule of contributory negligence yield optimal precaution levels? Assume that the court sets the victim's threshold level of precaution at the socially optimal level, y^* , the injurer's optimal level of precaution at x^* , but the court miscalculates the damages and awards \$3,645 if the injury occurs.
- (d) (5 marks) Which scenario, (b) or (c), yields the less efficient outcome?

Part B: Please complete FOUR (4) of the following SIX (6) questions. Each question is worth 20 marks. Please remember: this is a course in the Economic Analysis of Law. Consider economic rationales in answering the questions below.

Question B1

Calabresi and Melamed said: "When there are obstacles to cooperation, the more efficient remedy is the award of compensatory money damages.... When there are few obstacles to cooperation, the more efficient remedy is the award of

an injunction against the defendant's interference with the plaintiff's property." Explain what this means and why it should be true.

Question B2

Farmer Joe switches from growing corn to raising pigs. The result is a terrible smell and serious water pollution problems in the nearby river; this water pollution reduces the yields at nearby farms. Neighbouring residents complain about the smell and reduced yields, but Joe insists that the pork operation is more profitable than growing corn (or any other crop). The Ministry of the Environment refuses to intervene, claiming that smells and pollution are a normal consequence of farming. Pam brings a lawsuit on behalf of herself and 20 other farmers, complaining of interference in the use and enjoyment of their land. They ask for an injunction preventing Joe from discharging pig manure onto his land where it can give rise to smells and river pollution. Assume that Joe's increased profits are greater than the cumulative losses suffered by the nearby farms.

(a) (10 marks) From an efficiency perspective, should the courts protect Pam and her fellow farmers' right to be free of pollution?

(b) (10 marks) If Pam and her fellow farmers win, what are the merits of granting an injunction, as requested by the plaintiffs, versus allowing them to collect damages?

Question B3

Consider the following fact scenario, based on *Jones v. Star Credit Corp.* (NY, 1969).

On August 31, 1965, the Joneses, a poor, semi-literate couple agreed to buy a home freezer unit from Star Credit Corp. for \$900, after a visit from Star Credit's salesman. With the addition of credit charges, credit life insurance, credit property insurance and the sales tax, the purchase price totalled \$1,234.80. The Joneses paid back \$619.88 before suing to have the court declare that they had fulfilled their end of the contract (i.e., they asked the court to relieve them of continued payments on the contract). Star Credit claims that with credit charges, the Joneses still owe it \$819.81. What is uncontested

is that the maximum retail value of a new home freezer like that of the Joneses is approximately \$300.

(a) (6 marks) Suppose that in August 1965, Star Credit was well-known in the Joneses neighbourhood as being a front for organized crime, and that refusal to contract with Star Credit could have dire consequences. Should the Joneses now be relieved of the outstanding balance on the contract?

(b) (14 marks) Suppose that Star Credit is a legitimate business, and there was no threat to the Joneses, implicit or otherwise, when the contract was signed. Should the Joneses case succeed, nonetheless? Is it relevant that poor people like the Joneses would not have had access to credit from banks, credit cards or department store credit in 1965?

Question B4

Consider the fact scenario from *Outson v. Zurowski*.

Outson was induced by Zurowski to enter into a pyramid scheme. The pyramid scheme involved a contribution of \$2,200 to an “investment board” by the participant, followed by the recruitment of eight additional individuals. Once the scheme was completed, the participant would receive \$17,600.

Zurowski had participated in two such schemes before. He signed a contract with Outson, that if Outson invested in the pyramid scheme, he would protect their investment, i.e., give them back their \$2,200 if the scheme ended before completion. Note though, that the creation and participation in pyramid schemes was (and still is) prohibited by the Criminal Code. It appears that Zurowski was aware that the scheme was illegal, but at the time the contract was signed, Outson was not.

Just after Outson invested in the scheme, adverse publicity and police investigations of pyramid schemes led Zurowski to shut down the scheme. Outson sued to recover his \$2,200. In his defence, Zurowski argued that participating in a pyramid scheme was illegal according to the Criminal Code, and thus the contract between him and Outson was illegal; accordingly, he claimed the contract was unenforceable.

Suppose you were the judge in this case. How would you rule? Would your answer change if it Outson was aware from the outset that the scheme was illegal?

Question B5

Evaluate the claim that minimum wage laws are inefficient.

Question B6

Evaluate the claim that anti-discrimination legislation is inefficient.

Section C: Bonus Questions (1 mark each)

1. Name the federal Minister of Justice.
2. Name the Attorney-General of Ontario.
3. Name one of the justices on the Supreme Court of Canada.
4. How many women are there on the Supreme Court of Canada?

END