![Stockholm University logo]

Department of Economics

Course name:	**Law & Economics 1**
Course code:	**EC2105**
Type of exam:	**Retake exam**
Examiner:	**Lars Vahtrik**
Number of credits:	**7,5 credits**
Date of exam:	**Saturday 28 March 2020**
Examination time:	**3 hours (12:00- 15.00)**

Explain notions/concepts and symbols. If you think that a question is vaguely formulated, specify the conditions used for solving it. Only legible exams will be marked. You may use your books, notes and calculator.

The exam consists of 4 questions. Each question is worth 25 points, 100 points in total. For the grade E 45 points are required, for D 50 points, C 60 points, B 75 points and A 90 points.

Question 4 is a credit question. If you have handed in assignments during the course you may choose to answer this question anyway if you aim at a higher score. Note that in this case only the score on the exam will be counted regardless of your score on the assignments!

Your results will be made available on your Ladok account (www.student.ladok.se)
within 15 working days from the date of the examination.

Good luck!

Question 1

a) A thief (B) has stolen a jacket from a student (A). B later sells the jacket to a person (C) who has no knowledge of that it is stolen. A later sees C wearing his jacket and calls the police who arrests C. C explains that C has bought the jacket from B and even shows a receipt, although B's name is false. Please discuss from an economic perspective whether the law should protect A or C in the current situation. **(10p)**

b) One of the consequences for A when the jacket was stolen was that A had a USB-stick with the latest version of A's essay on it in one of the pockets. A had a back-up copy, but it still was many hours of work that disappeared when the jacket was stolen and A had to rewrite large parts of the essay. A also got a cold from being forced to wear A's spring jacket instead of a warm winter jacket in January. When B finally was tracked down and brought to court to be punished for the theft, A also sued for damages. Please discuss whether B should be liable to pay any damages to A for the injuries A suffered. **(10 p)**

c) A asks the lawyer for a fee estimate for handling the dispute with B. The lawyer asks if A wants to pay an hourly fee, fixed fee or a contingency fee. Discuss the pros and cons with the different fee structures. **(5p)**

Question 2

Consider an investor and an entrepreneur that can enter a business relationship where the investor invests 200 and where the joint profit of the investment amounts to 100 each in case the entrepreneur performs. In case the entrepreneur breaches the contract the investor gets -200 and the entrepreneur gets 200 (without damages). In addition our investor can make an additional investment with a third party of 180. If the entrepreneur performs our investor will increase the profit from 100 to 120 by making the extra investment and our entrepreneur still recieves 100. In case of breach the extra investment yields a payoff of -380 to the investor and 200 to the entrepreneur (without a contract). Will a naïve use of expectation damages give the investor optimal incentives to invest in reliance? Explain and show, with the help of relevant calculations, how a correct interpretation of perfect expectation damages can solve the problem of optimal reliance in this case. Explain (words only, no numbers) why no damages will create incentives for optimal reliance. **(25p)**

Question 3

Consider a very primitive society without a state that can protect property rights. The ability to guard your property rights will then solely depend on your private military strength. Unfortunately military strength reduces the amount of resources available to productive efforts. Explain thouroughly, using game theory and efficiency arguments, why two different groups may want to establish a social contract to create a government that enforces property rights even though that means that they have to pay taxes.

Assume food production is 20 for each group with all resources allocated to food production. With a private army you can steal 10 units of food from the other group. The oppurtunity cost of a private army is assumed to be 4 units of food. Also assume that you need a private army to be able to steal. The cost to the government of an army will also be 4 units of food and taxes need to be raised to finance that army. Assume that enforcement means perfect damages in case of theft.   **(25p)**

Question 4 (Credit question)

Consider Hart and More's example with the chef, the skipper and the tycoon. Explain the setup in the example and discuss the consequences of different allocations of ownership of the yacht for the incentives to make relation specific investments that increase the value of the cruise.   **(25 p)**