

## **Additional Material for Final Exam**

### **EXTERNALITIES (Chapter 10)**

Know the definitions of an externality, internalizing an externality, Coase's Theorem, transaction costs, and a pollution tax (also called a Pigovian tax)

Be able to describe examples of positive and negative externalities

Be able to interpret the graphs of positive and negative externalities

Public solutions:

1. regulation
2. taxes and subsidies (also called Pigovian taxes)
3. tradable pollution permits

Private solutions:

1. moral codes and social sanctions
2. charities
3. relying on the self-interests of the relevant parties  
Coase's Theorem  
make sure that you can solve a Coase's Theorem problem (like the one we did in class)
4. contracts

Problems with private solutions:

1. transaction costs
2. bargaining breaks down
3. too many people affected (difficult to coordinate private bargaining)

Be able to *compare and contrast* the private and public solutions, focusing on the advantages and disadvantages of each