

Learning Objectives

Chapter 10

In this chapter you will

Learn how social costs and benefits arise from private decision making
See why and how externalities can make market outcomes inefficient
See a graphical representation of the welfare loss associated with both positive and negative externalities
Examine how people can sometimes solve the problem of externalities on their own
Consider why private solutions to externalities sometimes do not work
Consider the role of taxes and subsidies in reducing externalities
Examine the various government policies aimed at solving the problem of externalities

You should be able to

Distinguish between a positive and a negative externality
Demonstrate why the optimal quantity and the market quantity differ in the presence of an externality
Define the Coase theorem
Explain how transaction costs may impede a private solution to an externality
Demonstrate the potential equality of a Pigovian tax and pollution permits
Graphically demonstrate the effect of a subsidy and a tax on reducing externalities
Explain the role of property rights in internalising externalities