

# CONTENTS OF VOLUME 1

Introduction to the Series	v
Contents of the Handbook	vii
Preface	xi
<b>PART I: Primary Elements of the Legal System</b>	<b>1</b>
<i>Chapter 1</i>	
Contract Law	
<b>BENJAMIN E. HERMALIN, AVERY W. KATZ, AND RICHARD CRASWELL</b>	<b>3</b>
1. Introduction	7
1.1. The economic motive for contracts	7
1.2. Law & economics issues in contracting	13
1.3. What this chapter is not	17
1.4. Organization of the chapter	18
2. Freedom of contract	18
2.1. Freedom of contract defined	19
2.2. The economic case for freedom of contract	21
2.3. The economic case against freedom of contract	30
2.4. Other arguments for regulating private contracts	46
2.5. Legal doctrines regulating freedom of contract	48
3. Formation of contracts	57
3.1. Pre-contractual behavior	58
3.2. Avoiding miscommunication	61
3.3. Legal doctrines addressing contract formation	62
4. Interpretation of contracts: contractual incompleteness	68
4.1. Modeling incomplete contracts	68
4.2. The sources of contractual incompleteness	75
4.3. Consequences of contractual incompleteness	80
4.4. Legal doctrines addressing contractual incompleteness	86
4.5. Overall assessment of the law of contract interpretation	99
5. Enforcement of contracts	99
5.1. General issues in enforcement	99
5.2. Monetary damages for breach of contract	102
5.3. Complications in determining monetary damages	115
5.4. Private enforcement of contracts	120
5.5. Other law bearing on contract enforcement	126

6. Conclusions	127
References	128
<i>Chapter 2</i>	
Liability for Accidents	
STEVEN SHAVELL	139
1. Introduction	142
Part A: Central theory of liability	142
2. Incentives	143
2.1. Unilateral accidents and levels of care	143
2.2. Bilateral accidents and levels of care	144
2.3. Unilateral accidents, levels of care, and levels of activity	146
2.4. Bilateral accidents, levels of care, and levels of activity	147
3. Risk-bearing and insurance	147
3.1. First-best solution to the accident problem	148
3.2. The accident problem given liability but in the absence of insurance	148
3.3. The accident problem given liability in the presence of insurance	149
4. Administrative costs	151
4.1. Volume of suit	151
4.2. Level of care and volume of suit	153
4.3. Comments	154
4.4. Strict liability and negligence	155
Part B: Extensions	156
5. Liability of firms	156
5.1. Victims are strangers	156
5.2. Victims are consumers	157
6. Aspects of the negligence determination	158
6.1. Differences among injurers	159
6.2. Imperfect assessment of care by courts	159
6.3. Imperfect ability to control care by injurers	160
6.4. Errors in the calculation of due care	160
7. Causation	161
7.1. Strict liability	161
7.2. Negligence rule	162
7.3. Uncertainty over causation	162
7.4. Proximate causation	163
8. The magnitude of liability: damages	164
8.1. Basic theory: strict liability	164
8.2. Basic theory: negligence rule	165
8.3. Difficulty in estimating harm	166
8.4. Punitive damages	166
8.5. Accuracy of damages and legal costs	167

9. Multiple injurers	167
9.1. Strict liability	168
9.2. Negligence rule	168
10. The judgment-proof problem	168
10.1. Incentives to engage in harmful activities	169
10.2. Incentives to take care	169
10.3. Incentives to purchase liability insurance	170
10.4. Policies to ameliorate the judgment-proof problem	170
11. Vicarious liability	171
12. Nonpecuniary harm	173
12.1. Incentives in the risk-neutral case	173
12.2. Incentives and insurance in the risk-averse case: fines as a supplement to liability	173
Part C: Methods of controlling risk	175
13. Liability versus other methods of controlling risk	175
13.1. Methods of control	175
13.2. Comparison	175
13.3. Resolution of externalities through bargaining by affected parties	178
14. Conclusion	179
References	179

### Chapter 3

#### Property Law

DEAN LUECK AND THOMAS J. MICELI	183
1. Introduction	186
1.1. Property rights and property law	186
1.2. Property rights, transaction costs, and the Coase Theorem	187
1.3. The impact of transaction costs: when does law matter?	189
1.4. Outline of chapter	189
2. Basic property rights models	190
2.1. Open access	191
2.2. Private property rights	192
2.3. Common property rights	194
2.4. State property rights	196
2.5. Mixed property rights and complex assets	198
3. The origin of property rights	200
3.1. First possession	200
3.2. Claiming the asset	202
3.3. The rule of capture for asset flows	204
3.4. First possession in law	204
3.5. Alternatives: auctions, bureaucracy, politics, and violence	208
4. The evolution of property rights	209
4.1. The Demsetz thesis	209

4.2. Empirical studies	210
4.3. The theory of rights evolution and variation	211
4.4. The mechanism of rights changes	212
5. Voluntary transfers of property	214
5.1. Protection of ownership and market exchange	214
5.2. Leases	217
5.3. Inheritance of land	223
6. Involuntary transfers of property	224
6.1. Adverse possession	224
6.2. The mistaken improver problem	226
6.3. Partition of real estate	228
6.4. Theft	228
7. Land use conflicts: externalities and property	229
7.1. A model of externalities in the short and long run	229
7.2. The Pigovian tax-subsidy approach	231
7.3. The property rule–liability rule framework	231
7.4. The law of trespass and nuisance	233
7.5. Zoning, covenants, and common law control	235
8. Public property and public use of private property	236
8.1. The optimal scale of ownership	236
8.2. The public trust doctrine	237
8.3. Eminent domain and regulatory takings	238
9. Inalienability of property rights	245
10. Conclusion	249
Acknowledgements	249
References	249

## Chapter 4

### Litigation

KATHRYN E. SPIER	259
1. Introduction	262
2. Basic framework	263
2.1. The decision to litigate	264
2.2. Out-of-court settlement	268
3. Topics	282
3.1. Accuracy	282
3.2. Evidence	285
3.3. Sequential litigation	292
3.4. Allocating the costs of litigation	300
3.5. Negative expected value (NEV) claims and “frivolous litigation”	305
3.6. Contingent fees	307
3.7. Tribunals	312

3.8. Multiparty litigation	318
3.9. Additional topics	324
4. Conclusion	333
References	334

*Chapter 5*

Empirical Study of the Civil Justice System

DANIEL P. KESSLER AND DANIEL L. RUBINFELD	343
---	-----

1. Introduction	345
2. Contract law	346
2.1. Introduction	346
2.2. The effects of contract law versus non-contractual relations	347
2.3. The effects of voluntary, or default rules of contract law	348
2.4. The effects of mandatory rules of contract law	350
3. Torts	351
3.1. Introduction	351
3.2. Medical malpractice	352
3.3. Auto accidents	358
3.4. Products liability	361
3.5. Punitive damages	363
3.6. Mass torts	366
4. Property	367
4.1. Introduction	367
4.2. The development of private property	368
4.3. Shared ownership	370
4.4. Property rights versus liability rules	370
4.5. Consequences for efficiency and economic growth of poorly defined/enforced property rights	372
5. The litigation process	373
5.1. Introduction: the costs of litigation	373
5.2. The chronology of a legal suit	374
5.3. Forum and law choice	375
5.4. Pre-trial	378
5.5. Settlement	381
5.6. Trial	383
5.7. Appeal	386
5.8. Alternatives to litigation: arbitration and mediation	387
5.9. Fee-shifting	389
5.10. Class actions	390
Acknowledgements	390
References	391

*Chapter 6*

## The Theory of Public Enforcement of Law

A. MITCHELL POLINSKY AND STEVEN SHAVELL	403
1. Introduction	405
2. Why public enforcement rather than private enforcement?	406
3. The general problem of public law enforcement	406
Part A: Basic theory when enforcement is certain	407
4. Monetary sanctions	407
5. Nonmonetary sanctions	409
6. Combined sanctions	411
Part B: Basic theory when enforcement is uncertain	412
7. Monetary sanctions	413
7.1. The risk-neutral case	413
7.2. The risk-averse case	414
8. Nonmonetary sanctions	417
8.1. The risk-neutral case	417
8.2. The risk-averse case	418
8.3. The risk-preferring case	419
9. Combined sanctions	419
Part C: Basic theory summarized and compared to practice	420
10. Summary of the basic theory	420
11. Theory versus practice	420
Part D: Extensions of the basic theory	422
12. Accidental harms	422
13. Precautions	424
14. Activity level	425
15. Errors	427
16. Costs of imposing fines	430
17. General enforcement	431
18. Marginal deterrence	432
19. Principal–agent relationship	434
20. Settlements	435
21. Self-reporting	437
22. Repeat offenders	438
23. Imperfect knowledge about the probability and magnitude of sanctions	439
24. Corruption	440
25. Incapacitation	443
26. Costly observation of wealth	444
27. Social norms	446
28. Fairness	447
29. Conclusion	449
References	450

*Chapter 7*

Empirical Study of Criminal Punishment

STEVEN D. LEVITT AND THOMAS J. MILES	455
1. Introduction	457
2. Basic theory: economic v. criminologic	458
2.1. The economic model of crime	458
2.2. Criminological approaches	460
3. Empirical tests of the economic model of crime	462
3.1. Challenges to empirical testing of the economic model	462
3.2. Data sources	463
3.3. Testing the economic model using the scale of policing	466
3.4. Testing the economic model using the scale of imprisonment	470
3.5. Testing the economic model using capital punishment	474
3.6. Testing the economic model using victim precautions	476
4. Empirical study of particular aspects of the criminal enforcement system	478
4.1. Challenges to empirical study of the criminal enforcement system	478
4.2. Policing strategies	479
4.3. Prosecution of offenses	480
4.4. Sentencing	484
4.5. Incarceration strategies	487
4.6. Post-release	488
5. Conclusion	489
References	489

PART II: Additional Areas of the Legal System 497

*Chapter 8*

Environmental Law

RICHARD L. REVESZ AND ROBERT N. STAVINS	499
1. Introduction	502
2. Setting goals and targets: the ends of environmental policy	504
2.1. Normative issues and analysis	505
2.2. Positive issues and analysis	526
3. Choosing instruments: the means of environmental policy	534
3.1. Normative issues and analysis	535
3.2. Positive issues and analysis	558
4. Allocation of responsibility across levels of government	564
4.1. Positive review of responsibility of levels of government	564
4.2. Normative review of allocation of regulatory responsibility	565
5. Conclusions	570
Acknowledgements	571
References	571

*Chapter 9*

## Regulation of Health, Safety, and Environmental Risks

W. KIP VISCUSI	591
1. The rise of risk regulation	593
2. Model of risky decisions	595
3. Sources of market failure	598
3.1. Imperfect perception of risk	598
3.2. Irrational behavior and addiction	602
3.3. Externalities	604
3.4. Modes of intervention	606
4. Hazard warnings and risk communication policies	609
4.1. Principles for hazard warnings	609
4.2. Responses to multiple information sources	610
4.3. A brief history of warnings	611
5. Risk assessment	612
5.1. Objectives	612
5.2. EPA risk assessment practices	614
6. Valuing the benefits of regulation	617
6.1. Risk valuation	617
6.2. Contingent valuation and survey methods	623
7. Benefit-cost analysis	626
8. Risk-risk analysis	633
8.1. Health effects	633
9. The enforcement and performance of government regulations	637
10. Conclusion	638
Acknowledgements	639
References	639

*Chapter 10*

## Taxation

LOUIS KAPLOW	647
1. Introduction	651
2. Framework	652
2.1. Purposes of taxation	652
2.2. Integrated view	652
2.3. Social objective	656
3. Optimal income taxation	658
3.1. Model	658
3.2. Linear income tax	660
3.3. Two-bracket income tax	663
3.4. Nonlinear income tax	664
3.5. Elaboration	669



4. Commodity taxation	670
4.1. Model	672
4.2. Analysis	673
4.3. Qualifications	675
4.4. Ramsey taxation	676
5. Other types of taxation	678
5.1. Capital taxation	678
5.2. Transfer (estate and gift) taxation	684
5.3. Social security taxation	686
5.4. State and local taxation	687
5.5. International taxation	688
6. Taxation and transfer payments	689
6.1. Optimal transfers	690
6.2. Categorical assistance	691
6.3. Work inducements	693
6.4. Cash versus in-kind transfers	694
7. Taxation and public goods	695
7.1. Distributive incidence and optimal redistribution	695
7.2. Distribution and distortion	697
7.3. Benefit taxation	700
8. Corrective taxation	701
8.1. Pigouvian taxes and subsidies	701
8.2. Choice of instruments	702
8.3. Distribution and distortion	704
9. Additional dynamic issues	705
9.1. Inflation	705
9.2. Risk-bearing	707
9.3. Transitions and capital levies	709
9.4. Capital gains	711
9.5. Human capital	712
9.6. Lifetime horizon	714
9.7. Budget deficits and intergenerational redistribution	716
10. Unit of taxation	717
10.1. Framework	717
10.2. Intrafamily sharing	718
10.3. Economies of scale	719
10.4. Altruism	720
10.5. Children	721
10.6. Incentives	722
11. Tax administration and enforcement	724
11.1. Choice of tax systems	725
11.2. Optimal administration and enforcement	726
11.3. Elasticity of taxable income	729

12. Additional features of tax systems	730
12.1. Tax base	730
12.2. Forms of consumption taxation	733
13. Tax equity	735
13.1. Welfarism	735
13.2. Choice of social welfare function	737
13.3. Other normative criteria	738
14. Conclusion	740
Acknowledgements	740
References	741

### *Chapter 11*

#### International Law

ALAN O. SYKES	757
1. Introduction	759
2. Legal background	760
3. Economic aspects of international law	761
3.1. States as rational actors	762
3.2. The economics of customary international law and "soft" law	763
3.3. The economics of treaties and other international agreements	766
3.4. The interface between domestic and international law	778
4. Security issues in international law	781
4.1. International alliances	781
4.2. The laws of war	784
5. International trade law	786
5.1. Trade policy, trade externalities and trade agreements	786
5.2. The legal architecture of world trade and its lessons for international law	789
5.3. Miscellaneous trade issues	804
6. International investment law	810
7. International antitrust	813
8. Human rights law	815
9. Conflicts of law	816
10. The international commons: the example of fisheries	818
11. Conclusion	821
Acknowledgements	822
References	822
Author Index of Volume 1	I-1
Subject Index of Volume 1	I-29