

QUESTIONS OF TRUTH & CONSEQUENCE**Part I: Introduction to Contracts and Contracting Problems**

1. What is the nature of the firm? What constrains the growth of the firm? What promotes the growth of the firm?
2. Leasing does not occur in the case of elevators in an office building, while the furniture is often rented. Why?
3. Firms exist to produce; profits are a by-product and profitability is shown by rate of return on sales. TFU
4. What determines the boundary between the firm and the market process? Also, some people claim that the large-firm market share has been rising strongly because these firms are more efficient. Discuss this statement in the context of the boundary between the firm and market. What are the factors that might make large firms more efficient?
5. The market pricing mechanism allocates resources to the highest value users; however, the pricing mechanism is replaced by an individual who organizes factors of production by lowering costs. What are these costs, and why is there this difference in costs? Isn't the pricing mechanism efficient? Explain.
6. Consider the following problem: A shipment of furniture has been delivered from a factory to a retail store for the purpose of sale to the public.

Case 1: The owner of the factory also owns the furniture and the retail store. She pays the operator of the store a weekly salary in exchange for selling the merchandize.

Case 2: The owner of the factory and retail store are separate individuals. The owner of the retail store pays the owner of the factory for the furniture and then sells the merchandize to the public.

What are the advantages and disadvantages of the two different organizational structures?

7. Why do firms exist to the extent they do?
 - (i) what are the benefits of having firms (as opposed to market transactions)?
 - (ii) what are the costs of having firms (as opposed to market transactions)?
 - (iii) how can the firm's benefits be maximized relative to its costs?
8. As firms grow in size and complexity, new approaches of doing business have emerged, particularly in terms of new organization evolving. For example, downsizing and outsourcing. How is this consistent with Coase's view of the firm? Be specific in your analysis.
9. What are property rights? How do contracts affect property rights? What role do transaction costs play in property rights and contract structure? What function do

property rights, contract structure, and transaction costs have in the Coasian view of the firm? Be specific in your analysis.

Part II: Opportunistic Behavior

10. What is the contracting problem that causes termite companies to be bonded? How does the bond solve the problem? Is the termite company at risk because of the bond? Why?
11. Give five examples where economic agents are forced to post bonds because of potential opportunistic behavior.
12. Relate the case of GM and Fisher Body. How does this case compare to AOL and Time-Warner, IBM and Microsoft, or MCI and WorldCom (or older examples: NCR and AT&T or GM and EDS)?
13. The natural gas industry offers a number of examples of contracts conditioned by the threat of opportunistic behavior. What are they?
14. How do exclusive dealing and exclusive territories work together?
15. How does exclusive dealing differ from franchising?
16. What are the various forms of opportunistic behavior associated with natural gas? What contractual provisions are used to solve these problems?
17. Why would you expect oil tankers not to be owned by producers? Some are, like the Exxon Valdez. How can you explain this?
18. When you finance a car, you are forced to put some money down and then the finance company lends you the rest. Why? Will you have to put more money down (in percentage terms) on a used car or a new car? What about the down payment on a restored classic car?
19. What is the evidence concerning brand names in their use as a quality assuring mechanism?
20. On the basis of theory, which products do we expect to see brand named? Is theory consistent with fact?
21. IBM has a rather stringent approval system for new products. Before a software application written by an IBM programmer can become an IBM product, its quality and usefulness has to be evaluated and unanimously or near unanimously approved. As a result, many useful software tools developed by IBM have never been approved to be sold as IBM products. However, many of these programs were used internally. In contrast, in many small and medium companies, very little is needed in order to approve a new product. Would IBM do better by adopting more flexible approved procedures used by many younger companies? Explain

22. Show that vertically integration will not affect the degree of competition in perfectly functioning markets. Also, discuss conditions under which vertical integration may reduce competition and lead to market power.
23. Vertically integration can cause increased efficiency even in firms that are not vertically integrated. TFU
24. The goals of a merger can often be reached by internal growth or long-term contracts. TFU
25. How might joint ventures decrease competition? Increase competition?
26. Publishers of small daily newspapers usually own their own presses, but large book publishers normally contract their printing jobs to independent printers. What accounts for this difference in who owns the printing presses?
27. Firm producing output that requires the use of a capital asset will either lease/rent, own the equipment, or will jointly own the equipment with another firm. Explain when each method will be employed. Be specific in your explanation.
28. The parties to a long term contract have a mutual interest in designing a contract that maximizes its value to both parties. Explain the nature or incentive structure of these long term contracts along with potential problems that can arise. Be specific in your answers.
29. The primary reason for writing contracts is to protect against the hazards inherent to exchange where one or both parties have invested in reliance, or relationship-specific assets, in support of the transaction. Though contracts specify the obligations of the parties for the duration of the agreement, contracts do not attempt to specify all contingencies and provide provisions to accommodate future uncertainty by stipulating bonds for contract renegotiation. What is needed for invoking adjustment in the contracts? Describe and explain the nature of these provisions, and be specific in your explanations.
30. Timing and coordination of activities are critical in construction projects such as office towers or shopping malls. That is, coordinating the work of a large number of labor specialties over the course of a project is a complex task. At any point in time a number of these specialties will be simultaneously involved on the project and often the work of one cannot proceed until a phase of work has been completed by several others. At these stages, tasks must be strictly ordered for work to proceed. As a result, delays in a key task can have system-wide effects, hindering progress on a group of operators and forcing managers either to wait until the antecedent task has been completed or to uncover an alternative sequence of operation. Discuss how time and space considerations or “temporal specificities” affect the contracting practices employed in the construction industry. Be specific in your analysis.

31. The practice of payola in the music industry is well documented. For instance, the spread of “rock and roll” music is attributed to the practice of payola between record companies and disc jockeys. First, comment on this statement. Second, discuss the economic significance of the payola system. Compare it to the practice of drug companies paying doctors to “learn” about the uses of their drugs.
32. In order to enhance market share, some major airline companies offer travel agents commission override programs, which grant rebates if agents purchase large quantities or high fractions of their customers’ travel services from the airline. What are the efficiency implications existing, if any, for such contractual dealings between the major airline companies and travel agents?
33. In regards to the insurance industry, describe the nature of commission contracts offered through exclusive dealings contracts. Provide details and be specific in your analysis.

Part III: Shirking

34. In many settings, such as a university, it is hard to monitor workers. For instance, many business school professors shirk in the sense that they use the computer system, departmental secretaries and research assistants for private consulting or writing textbooks. Some business school deans have adopted a system of research budgets that are under the discretionary control of each faculty member. What are the costs and benefits of this approach to solving the contracting problem?
35. What does residual claimant status mean, as a contract condition what function does it perform, and when do we expect to see it?
36. Discuss the structure of royalties in the case of literary works. Specifically, what is the explanation of advances against royalties? Why do royalty rates often escalate with sales? When do we expect to see authors receiving lump-sum payments for their work?
37. Under what circumstances are commission sales not an efficient contract structure?
38. Describe the special services argument as it applies to automobile distribution.
39. In the California gold rush, income sharing as a way of reducing income variance and uncertainty was apparently important. What evidence exists to support this argument? However, a common rule allowed miners to keep large chunks of gold instead of putting them into the common pool. How can this be reconciled with the demand for income averaging?
40. Contrast the effect of having the royalty fee of a franchise paid as a function of franchisee profits as opposed to sales.
41. The McDonalds franchise sells hamburger patties to the franchise outlets. The purpose of this sale could be to monitor quality or it could be to extract a rental from the franchisee. In any

- event, do you think that McDonalds sells the hamburgers at marginal cost? Even if they do not sell at marginal cost, are total joint profits of the franchisor and franchisee less as a consequence?
42. Give the facts of the Chicken Delight franchise. What were the peculiar aspects? The court ruled against Chicken Delight, which seems to have led to its demise. However, was it likely to survive anyway?
 43. How do the problems of adverse selection and moral hazard apply to health insurance? Would you expect consumers with health insurance to be more likely to take brand named drugs?
 44. Evaluate the following statement: "Tie-ins are indirect form of discrimination. Therefore, they always tend to reduce competition and economic efficiency."
 45. Firms belonging to trade association always reduce competition. TFU
 46. Unlike specialty stores, department stores sell a wide variety of products to a single group of customers, and are often especially interested in maintaining reputation for customer service. How might this affect the design of incentive compensation for salespeople at the department store compared to salespeople at specialty outlets?
 47. University faculty members have excellent reputations for doing research, but their teaching is dreadful. The university is considering incentive compensation for professors in order to improve their teaching after complaints from students. What considerations are important for the university in measuring and rewarding teaching performance?
 48. Every university offers tenure (lifetime employment) to faculty whose performance meets some criteria. A recent academic study investigated the relationship between the probability that a junior faculty member is given tenure, and the salary level that the university pays to junior professors in that department. Do you predict that departments that are less likely to give tenure pay junior professors lower or higher salaries? What about tenure faculty salaries? Why?
 49. Tournament theory has been used to explain the size of wage differentials between different levels of management in the company. When should these wage differentials be quite large? How should these differentials be related to the type of industry in which the firm is located?
 50. KBG international employs 40 marketing associates. It is expected that within a year, one of the marketing associates will be promoted to rank of a senior associate. The job responsibilities of the senior associate are exactly the same as those of marketing associates. However, a senior associate has a 25% larger cubical than other marketing people, she also receives a 25% greater base salary, a 25% bigger desk, and even her chair is 25% bigger. In this firm, workers are paid straight salary; the only reward for good performance is promotion to senior associate level. Suppose the worker with the most sales over the next twelve months is promoted. The incentive effects of the tournament

- are greatest when: (1) each worker knows only his sales number and does not learn sales of co-workers until the end of the sales period; (2) all marketing associates are of the same ability; and (3) a typical sales is relatively small so that each marketing associate works on hundreds of unrelated sales every year. Are the above factors essential for maximizing incentives in tournaments?
51. Many firms have begun to hire temporary workers from agencies or workers on a project basis as independent contractors. Why do you think this trend is occurring? What are the benefits of hiring independent contractors? What are the costs?
 52. Discuss the differences and similarities between outsourcing and franchising?
 53. General Motors' new Saturn car line was a completely new design that was built by a specially-recruited workforce in a new factory constructed specifically for the Saturn. To market the new car, which GM hoped would help it lean to become competitive again on the world scale, it set up separate dealerships and announced that the sales people in these organizations would not be paid on a commission basis, as is common in the industry. Instead, they were to be salaried. What might be the advantage of this pay policy?
 54. Professional team sports such as football, basketball, and hockey appoint captains to monitor the effort levels of the team members. The captain answers to the coach, who answers to the general manager, who answers to the team owner(s). When the team performs poorly by continuously losing games, the coach is generally the one who gets fired (and sometimes the general manager gets fired). Why is the captain not fired or replaced by another team member? Also, why are most shirking members on the team not fired or fined for not exerting effort?
 55. The franchisor usually receives a franchise fee along with a percentage of sales from the franchisee outlet. The franchisee has incentive to chisel rents from the franchise contract. Explain the various ways in which the franchisee will attempt to do this and what methods the franchisor employs to prevent this. Be specific in your answers.
 56. Uniqueness of brand names or trademarks merely identifies the owner of a product, in the sense of defining property rights, without creating or implying any market power. Explain this statement, and be specific in your analysis.
 57. In a franchising contract between a franchisor and a franchisee, an important distinction exists between pre-contract and post-contract arrangement. Explain what these distinctions and potential problems, if any, that are likely to exist. Be specific in your analysis.
 58. Explain the different models of how termination laws can affect franchising contracts between the franchisor and the franchisee. Be specific in your analysis.

59. Explain the differences, if any exist, between exclusive dealing contracts, franchise contracts, and exclusive territory contracts. What are the advantages and disadvantages of each type of contract. Be specific in your analysis.
60. The alcoholic beverage market is characterized by a three-tier distribution network, where the brewery sells its product to a franchised wholesaler who in turn sells beer to retail outlet. Discuss the contractual relationship between the different parties, and any potential problems that are likely to occur. Be specific in your analysis.

Part IV: Pricing

61. Block booking in the movie industry seems to have resulted from a measurement problem. Explain.
62. Describe the contracting problems in the petroleum coke industry paying special attention to the issue of contract price and price renegotiation.
63. Is it uncommon to see real estate sales contracts that pay an increasing commission rate to the agent as the sales price increases. Why? In what kinds of circumstances involving real property would you expect to see such a contract?
64. Long term contracts involve estimates of future prices. When those estimates prove to be wrong, the contracting parties often renegotiate price. Why? Give some examples.
65. Why did GM ultimately buy Fisher Body?
66. Take-or-pay contracts are a price mechanism that is intended to mitigate opportunistic behavior. Explain the use of TOP contracts in natural gas and in petroleum coke.
67. What is the theory and evidence concerning the use of resale price maintenance as a cartel device?
68. What is basing point pricing? How might it be used to create a cartel?
69. What is it about IPTAY (the athletic booster club) that causes Clemson University to raise more money from high intensity demanders than could be raised from them by simply selling the best seats to the highest bidder?
70. Describe the optimal contract structure for a shopping mall.
71. Why do wholesalers not sell to the public at wholesale prices?
72. Would a manufacturer ever want its product to be sold as a loss-leader?
73. After the University of Miami won the national football championship in 1982, there was serious discussion about removing seats from the Orange Bowl because the stadium was

- too big. Georgia Tech did actually remove 10,000 seats a couple of years ago. How does this make any sense?
74. Offer an explanation of Sam's Wholesale Warehouse.
 75. Recently, in order to better align interests of paving contractors and the motoring public, states and municipalities have begun to allow road construction contracts that contain incentive for early completion and penalties for delays. Should the paving employees be compensated on the same factors (ignoring issues of unionization of workers)? the highway administration? why or why not?
 76. Hewlett Packard is a company with over 100,000 employees and businesses ranging from measuring equipment to computers and printers. Every year different businesses within HP buy tens of thousands of computers and printers. Should HP equip its employees with HP computers or should they purchase computers from someone else? Discuss what a sensible internal pricing policy is.
 77. Retail price maintenance is always initiated by dealers rather than producers. TFU
 78. Explain the "free rider" justification for RPM. Under what industry conditions would favor it?
 79. In general, the natural gas industry is characterized by long-term contracts (averaging fifteen to twenty years in length) between the gas-producer and the pipeline-owner; thus, locked into a bilateral monopoly relationship. Discuss the details of this bilateral monopoly relationship and potential problems and remedies from exogenous changes in market conditions. Be specific in regards to the structure of the contract.
 80. Many department stores usually have a high number of salespersons available for service in the cosmetics department relative to the clothing or other departments. Why do these large stores adopt this strategy? What theory best explains this phenomena?
 81. Manufactures often impose vertical restrictions that limit intra-brand competition by retailers. Why would the manufacturer do this? Competition is supposed to be good? What is the nature of this argument? Be specific in your analysis.
 82. Retail price maintenance (RPM) is the practice by which manufacturers attempt to control the prices at which their products are resold by dealers and distributors to the customers. The uses of RPM have different welfare implications. What are they? How do they differ? Be specific in your analysis.
 83. Corning Glass Works contracts required wholesalers conduct business only with retailers that openly agreed to RPM agreements and not with those that had not signed RPM agreements. The Federal Trade Commission (FTC) challenged these boycott provisions in Corning's contracts with wholesalers. Analyze Corning's use of RPM, and describe

FTC's case against Corning. Is Corning's use of RPM consistent with economic theories of RPM? Be specific in your analysis.

84. In agriculture, landowners and farmers differ in incentives with various contracts and contractual structures. Also, uncertainty is a crucial component in the formal contract. Describe the various contract types between landowners and farmers. Explain the source of transaction costs which determine the optimal contract design- with emphasis on production, measurement costs, input use/sharing, output share and input/output share.

Part V: Measurement

85. Describe the efficiency of the DeBeers marketing arrangement.
86. List and briefly discuss the various means available to consumers to assure product quality.
87. In the real estate market, homeowners will, once having made the decision to sell their home, spend resources fixing and painting their homes without knowing the potential buyer's true preferences. Why fix and paint the house before selling the home when it will not likely suit the tastes of the buyer? Explain the economics behind this occurrence. Be specific in your analysis.
88. The claim is that Holstein steers are the only breed sold at auction for veal. (Veal is cow meat that is light in color and especially tender.) Presumably this is because their stomachs bloat immediately when they first eat grass, and grass turns cow meat from veal to beef. Assume that this is true. How can we know that the Holstein steers bought at auction are slaughtered for veal?
89. In the horse racing industry, most races are called claiming races. That is, every horse in the race is up for sale at a price stated in advance and one that is the same for all horses in the race. Explain this phenomenon.
90. In the grocery store, oranges are often sold loose or already packaged. Which oranges cost more by the pound or, in other words, if I were to give you one pound of either loose or packaged oranges, which would you choose? Discuss this issue in detail.

Part VI: Legal Protection

91. What contracting problems are at play in the dumping of garbage?
92. Discuss the application of the Coase Theorem in the following settings: coastal development, restaurant smoking, depletion of timber in south Georgia (U.S.), upstate South Carolina, and the Amazon rain forests.

93. An increase in the number of officials in a basketball game will result in more fouls committed. True or false? Explain. “Invention follows innovation, but the two processes use quite different resources and may have differing incentives.” First, comment on this statement. Second, discuss the economic significance of innovation and inventions.
94. “Patent system can be worthwhile if induced innovations are important, and if the reward from patents do speed them up.” First, comment on this statement. Second, discuss the economic significance of innovation and inventions.
95. “Positive aspects of technological change are complicated, but normative aspects are quite simple.” First, comment on this statement. Second, discuss the economic significance of innovation and inventions.
96. Explain how the “free rider” problem may cause the rate of innovation to be too low. Also, will this cause the number of innovations to slow down?
97. Explain the role and value of the patent system, and how it relates to the development of “prospects.” Also, discuss the effects of patent-related problems and solutions on patent system.
98. Explain the effects of the patent system on the pricing of the patented idea(s) and patent licenses on future patents. Along with the benefits and costs, discuss the relationship, if any exists, between cross licenses, patent pools and grant backs, and what distinguishes them from ordinary licenses. Lastly, how does the patent law enforce the exclusiveness of patented products?
99. Explain the nature and scope of copyright laws. What are some of the exceptions to the copyright laws? How are copyright holders affected by the presence of photocopy machines, and what remedies are available to them? Also, how do, if at all, do publishers behave in the pricing of copyright material in the presence of photocopying. Finally, is there any difference between copyrighted printed material and prerecorded video cassettes?
100. Discuss the benefits and costs of trademark law. Do trademark laws cover brand names? What role, if any, do counterfeit goods have on trademark products? Is there a price difference between trademark products and counterfeit products? Finally, what are the welfare implications of counterfeit goods?
101. A problem encountered in the private sector is measurement. That is, in every exchange, both the seller and the buyer will require some verification of the measurements of exchanged goods: the seller to assure himself he is not giving up too much, the buyer to assure himself he is not receiving too little. Explain how quality of enforcement and the effectiveness of laws affect the overall welfare of the parties involved in the exchange. Is public law enforcement a necessary element of gains from trade?
102. Marriage is a universal phenomenon; however, with third party involvement. Specifically, (1) the state is directly involved in the contract’s creation and dissolution, and; (2) the

state establishes a set of fixed rules that define property within the contract. Using theory of contracts, explain some of the potential problems that may arise without state intervention in marriage. Also, explain how state intervention in marriage contract can overcome these problems.

103. Homesteading, like common-property resource, causes farmers to rush to the land in an effort to preempt other potential farmers and, in the process, dissipate the value of the land. Alternatively, homesteading policy was employed by the state as the formation and protection of property rights. Explain how contracting structure through homesteading policy resolves the above puzzling result. Be specific in your explanation.

Part VII: Common Access Property Rights

104. The positive externalities of shopping malls are well known. Alternatively, the shopping mall can also be interpreted as common-property resource problem. The argument applies to selling activity. Consumers are like fish, out there waiting to be hooked. Manufacturers and retailers use real resources to convert people from potential customers (free fish) into actual customers (captured fish). The customer is of no value to the seller until he is captured. The selling effort of each firm will raise the costs of its competitors, and, if the firms fail to take this into account, they will collectively overspend on selling (i.e., over fishing). Explain what institutional arrangement can be implemented to solving this “over fishing” problem for mutual benefits. Also, are there any problems or conflicts associated with implementing institutional arrangement? Can customers (fish) do anything to affect or be affected by the institutional arrangements? Finally, can the firms do anything to affect or be affected by the institutional arrangements?
105. Explain the nature of the population problem. How is the population problem related to “the tragedy of the commons”? Also provide solutions, if any exists, to this problem.
106. In macroeconomics, government expenditure can be viewed as either “worthless/non-competing” or “useful/competing” with private expenditure. How does the functioning or operation of the lighthouse fit/lie in this framework? Provide the arguments for lighthouses. Be specific in your explanations.
107. Coase (1937) indicates the existence of the firm because the use of pricing mechanism is costly; that is, a nexus of contract between various inputs at a single location to produce output. Similarly, financial exchange market is made up of nexus of internal and external contracts to produce prices. In addition, the exchange develops an elaborate structure to economize on “search and information costs, bargaining and decision costs, policing and enforcement costs.” Explain how price quotes incorporate property rights. Be specific in your explanation and analysis.
108. The New York Stock Exchange is an institution that “makes a market” in financial securities, specifically, the common stock of certain corporations. Not all corporations

have stock that trades on the NYSE, and the stock of companies that is traded on the NYSE may be bought and sold in other markets. First, does the NYSE concern itself with the fact that other markets trade in the same securities that it does; should it concern itself? Second, how does the NYSE limit the number of securities that are traded there and why does it do so?

ADDENDA

Part I: Introduction to Contracts and Contracting Problems

109. The church, although not often thought of as such, is a firm designed to produce religious goods. Like other firms it must meet its payroll, pay its creditors, plan for future contingencies, and act on a host of other day-to-day decisions. A church's ability to survive requires an organizational form that is best able to produce a given amount of output. First, compare and contrast Coasian approach of the firm to the church. Second, explain how the decision-making process (i.e., property rights distributed among members) will, if at all, affect on the organizational structure of the church. Lastly, using theory of contracts, explain the different payment schemes, if any, for clergy and what effect does this have on productivity and growth of the church.
110. All marriage contracts are entered into with the promise, and most with the intention, to deliver a lifetime stream of spousal services. These services are peculiar in that their value is crucially dependent on the attitude with which they are delivered and received. In reliance on the promise of these services, each party invests in assets specific to the marriage and foregoes other opportunities both for marriage and for other activities. First, explain what are the "specific assets" in a marriage, and what, if any, are their costs and benefits? Second, why enter into long-term contract of marriage given future uncertainty? Third, is the marriage contract arguably flawed and if so, how?

Part II: Opportunistic Behavior

111. Insurance firms, when offering policies to prospective customers, face two problems. First, the purchase of insurance decreases the incentive of the insured party to engage in activities that reduce the likelihood that a loss occurs. Second, the probability that a loss will occur differs across individuals. These are traditional problems of moral hazard and adverse selection. Discuss the ways in which contract structure can resolve or solve these problems. Also, analyze the effects, if any, on social welfare when both problems are present simultaneously.
112. In the past, couples' inability to procreate had to be accepted as regrettable but unalterable; however, today new possibilities exist for infertile parents. For instance, surrogate motherhood, where the surrogate mother conceives a child with the sperm of the infertile wife's husband and, upon birth, relinquishes the child to the natural father and his wife. Specifically, in a surrogate contract is initiated by an infertile wife, who will have

no genetic link to the child, and her husband, who contributes sperm. The surrogate mother contributes both the egg and womb. First, explain how the above contractual arrangement can be analyzed from a Coasian approach to the theory of the firm. Second, what, if any, are pre- and post-contractual problems likely to exist and what, if any, provisions can be incorporated to eliminate them.

Part III: Shirking

113. What determines the boundary between the firm and the market process? Where does franchise fit into this framework? Be specific in your analysis and explanation.
114. Commonly, a manufacturer distributes output before knowing demand and thus risks making more than its independent retailers can sell. That is, despite its best forecasting effort, a manufacturer may produce and sell to its independent retailers more output than they can subsequently resell. If retailers anticipate this possibility ex-ante, they reduce the wholesale price they will pay the manufacturer to reflect the decrease in profitability due to surplus merchandise. First, describe the contract structure between the manufacturer and the retailers. Second, what options, if any, does the manufacturer have that minimizes the cost of unsold inventory.
115. There is some evidence that franchising is becoming less common in the fast-food industry. While hard data are hard to come by, it is rumored that the major franchisors are buying back many of their outlets. Moreover, there is a trend for franchised outlets to be bought up by corporate holding companies separate from the franchisor. Why might this be happening? Is this phenomenon consistent with the claim that franchisors are buying back their stores?

Part IV: Pricing

116. PET one gallon milk sells for \$2.89 at The Pantry, \$3.25 at Eckard's, \$2.45 at Bi-Lo and \$2.59 at Winn-Dixie. Why is the "law of one price" not at work? Is the milk industry perfectly competitive or price discriminating market? What explains the difference in the prices charged by the different stores? Be specific in your answers.
117. Video Only publicly advertises that consumers should shop around and then come to Video Only to buy at the lowest price. How do larger, more well-known stores compete with discount stores that sell the same product for less? What are the contracting issues at hand? Are there any remedies?
118. Many different "options" are available in a particular model of new cars. Some are "mandatory options" where the buyer has no control in purchasing, while some are "optional options" where the buyer has full freedom to choose. As a result, separate pricing and block pricing co-exist in the market and their occurrences differ widely for different models and different options. First, under what conditions will separate pricing be more profitable than bundling and when will bundling be more profitable than separate

pricing profitable? Second, why do manufacturers label as options the features that make up the bundled product?

119. There is a movement in automobile retailing toward non-negotiable prices. There is also some indication that automobile manufacturers may be opening company stores, that is, outlets that they directly own as opposed to franchised dealerships. What might be the cause of these phenomena? Are they possibly related? Do you think that these trends will survive and thrive?

Part V: Measurement

120. The buying and selling of babies is illegal. However, couples (either married or unmarried) or eligible singles wishing to have children can adopt. The market for adoption is characterized by the presence of public and state-licensed private agencies that manage the process by which babies and older children are first given up for adoption and then allocated by means of some agency-determined ordering to persons who have paid to the agency a fixed or income-adjusted fee. First, comment on the role of government in regulating in the market for adoption. Second, using theory of contracts, explain some of the potential problems that may arise during pre- and post-contracting period. Also, what remedies or provisions are available that may eliminate or minimize the nature of the problem.
121. “Since the mid-70s there has been a decline in the quality of service in many retailing industries with the diffusion of discount-type retailing and growing use of part-time workers. The decline in the quality of retail service in a period when women’s time is becoming more valuable appears paradoxical.” First, comment on the statement. Second, explain how contracting can be a way of resolving this paradox.
122. With a rise of two-earner household, the allocation of shopping responsibilities has changed. That is, the increase in the relative earnings of women has resulted in a rise in males shopping. How have manufacturers and retailers adjusted to this phenomena in the way they sell their products? Discuss the economic of contracting arrangement between the manufacturer and retailers.
123. In every exchange, both the seller and the buyer will require some verification of the measurements of exchanged goods: the seller to assure himself he is not giving up too much, the buyer to assure himself he is not receiving too little. For instance, consumers will exchange money for goods if they perceive what they receive to be more valuable than what they give up. Quite often, measurement is costly at time of purchase. What arrangements can firms make/engage in to assure product quality. Discuss the nature of contractual issues, and be specific in your explanations.
124. In most job markets the employer is not sure of a potential candidate’s productive capabilities at the time of hiring nor immediately after hiring. Similarly, the job candidate is not sure about the treatment likely to be received from his/her future employer. First, what is the contractual nature of this problem between employee and employer. Second, what actions can be undertaken by both parties to remedy this problem.

125. “In equilibrium, the price premium yields the competitive rate of return on the investment made to establish and maintain reputation. It is not a barrier to entry; it is simply another cost of doing business. A firm has an incentive to preserve quality as long as the present value of premium exceeds the opportunity cost, which is the present value of the short-run profits from lowering quality.” Explain this statement.
126. Explain how the use of non-salvageable capital investment or “conspicuous” specific asset expenditure affects the price charged for high-quality products compared to low-quality products. Also, what role do these expenditures have on the information or non-information content in advertising, and how does that affect the frequency and intensity of advertisements.
127. Explain the effects of manufacturers’ recalling of their products from the market. Specifically, during post-recall, how do consumers, competitors, and the market react to the recalling of the products. Does the issue of fault or no-fault affect the manufacturer? Finally, what actions are undertaken by the manufacturer to restore confidence in the product’s reputation?