

The Coasian Analysis of Externalities: Some Conceptual Difficulties

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Abstract

This paper is concerned with two distinct issues flowing from Coase's analysis of externalities and of how courts deal with them. The first issue relates to the domain of validity of the Coase Theorem. It is argued in the paper that if non-pecuniary considerations are brought into the analysis then it can no longer be claimed that the outcome will be efficient regardless of liability assignments. In other words, it is contended in the paper that the validity of the Coase Theorem is crucially dependent on neglect of non-pecuniary considerations from the analysis. From this it follows that if in a context non-pecuniary considerations are important, the use of the Coasean logic can be quite misleading. As in the context of externalities affecting the environment the non-pecuniary considerations tend to be particularly important, different liability assignments can have very different implications for environmental degradation.

The second issue relates to whether the two ideas of efficient allocation of resources being attained through bargaining in a world of zero transaction costs and individualized efficient court decisions are compatible with each other. One implication of individualized efficient court decisions is that it could not be the case that liability assignments are well-defined. In each case, whether the injurer will bear the harm or the victim is contingent on the facts of the case and the requirements of efficiency. Individualized efficient court decisions consequently imply that it could not be the case that law makes injurers liable and also that it could not be the case that law makes injurers not liable. But then the very basis on which bargaining could take place in a world of zero transaction costs disappears. It is argued in the paper that the individualized efficient court decisions not only make the liability assignments ambiguous but also introduce strategic manipulability in the system with its attendant costs.

Keywords: Non-Pecuniary Considerations; Domain of Validity of the Coase Theorem; Coasian Logic and Environmental Issues; Individualized Efficient Court Decisions; Strategic Manipulability of the Efficient Court Decisions.

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