

**EC337 – Economic Analysis of Legal Issues  
Spring 2013, Boston University**

Instructor: Jeremy Smith

**Second Mid-term Practice Test**

Monday, March 18, 2013

This is a 38-minute test. There is a total of 38 points allocated across two questions. Use the number of points allocated to each part as a suggestion for how long to spend on that part. I recommend that you attempt all parts before using more time than is suggested for any one part. If you complete some parts in less than the suggested time, use your extra time to revisit parts you may have had trouble with the first time through and to check your work.

Please read the questions carefully and write your answers in the blue booklets provided. Please follow my instructions at all times.

You only need to identify yourself with your BU ID on the blue booklets. You may keep this question sheet when the exam is over.

1. [25 points total, 5 parts] Ivan will be hosting an event at his home on Saturday. On the preceding Wednesday, a pipe at his home breaks. If the pipe is not fixed, he will have to cancel the event, which will cause him to miss out on \$1200 in certain profit. He calls Joe, who is the only plumber available. Ivan and Joe enter a contract that states that Joe will fix the pipe on Saturday morning and Ivan will pay Joe \$500. On Friday, Qiao offers Joe \$1500 to fix her hot tub on Saturday. If Joe accepts this offer, he will have to breach his contract with Ivan.

a) [4 points] Is it efficient for the contract between Ivan and Joe to be breached? Explain briefly.

b) [5 points] Assume that Joe knows that courts always employ the “expectancy” remedy rule when a breach of contract is found, and that Joe and all courts know exactly how much profit Ivan stands to earn from hosting the event. Will Joe decide to breach the contract? Explain briefly.

c) [5 points] Assume instead that Joe knows that courts always employ the “expectancy” remedy rule when a breach of contract is found, but that Joe also knows that Ivan will lie to the court and be able to convince them that he stands to earn \$2000 in certain profit from the event. Will Joe decide to breach the contract? Explain briefly.

d) [5 points] Suppose instead that, on Friday afternoon, Ivan learns that Joe has agreed to fix Qiao’s hot tub on Saturday, and that Joe will hence breach his contract with Ivan. Ivan manages to get the case brought in front of the court immediately. Assume that the court orders specific performance. Will Ivan’s event be held as planned on Saturday? Explain.

e) [6 points] Go back to assuming that Joe knows that courts always employ the “expectancy” remedy rule when a breach of contract is found, and that Joe and all courts know exactly how much profit Ivan stands to earn from hosting the event. However, suppose that it is common knowledge that an emergency plumbing service becomes available that can fix pipes (but not hot tubs) at a cost of \$900 at any time. Just considering Ivan and Joe, now is it efficient for the contract between them to be breached? Will Joe decide to breach? Explain.

2. [13 points total, 4 parts] Suppose that a band called Elastica records an album that bears a suspicious stylistic resemblance to an earlier album by a band called Wire. Before Elastica's album, Wire was earning \$800,000 per year in sales of its own album, and will continue to do so indefinitely if Elastica's album is not released. If, on the other hand, Elastica's album is released, each band will earn \$300,000 per year in sales indefinitely.

a) [4 points] Briefly state the fundamental trade-off that is faced when deciding on the strength of intellectual property protections.

b) [2 points] In the present case of Elastica and Wire, what is the efficient outcome? Why?

Suppose that Wire sues Elastica for copyright infringement.

c) [3 points] Will efficiency be achieved if the court orders Elastica to compensate Wire for the damage caused by releasing their album? Explain.

d) [4 points] Will efficiency be achieved if, instead, the court upholds Elastica's right to release their album and be free of any liability to Wire? Explain.