

The University of Calgary
Department of Economics
Economics 611 (06) Course Topic 2
Winter 2008

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Reading Course: Topics in Regulatory Economics

Outline: The course will consider government policies towards regulation and liberalisation of network industries. We will consider recent developments in the theory of regulation and the design of regulatory policies in industries where unfettered competition is deemed inappropriate, e.g. because technological considerations render supply by one or few firms optimal. We will look at complications that arise because regulators have limited knowledge of the industry that they regulate. We examine how best to introduce competition into such industries, where appropriate.

The course is mainly based on the survey article by Armstrong and Sappington, "Recent developments in the theory of regulation." Two relevant books for the course are: Laffont and Tirole (1993), *A Theory of Incentives in Procurement and Regulation*, MIT Press. Newbery (1999), *Privatization, Restructuring, and Regulation of Network Industries*, MIT Press.

Requirement: Four problem sets (40%) and an original term paper of 15-25 pages (60%).

Reading List:

1) INTRODUCTION: WHY AND HOW TO REGULATE?

Laffont and Tirole (1993) "A Theory of Incentives in Procurement and Regulation", MIT Press,
Introductory chapter (pp.1-35).

2) OPTIMAL REGULATION

Armstrong and Sappington, 2004, "Recent Developments in the Theory of Regulation",

Paragraphs 2.1.1-2.1.3

Baron D., 1989, *Design of Regulatory Mechanisms and Institutions*, in R. Schmalensee and R.D.

Willig eds.: The Handbook of Industrial Organization, Elsevier North-Holland.

Laffont and Tirole: pp.1-35 and paragraphs, 2.2-2.4, B2.1.1

3) COMPETITION AND REGULATION

Armstrong, C. Doyle, and J. Vickers, "The Access Pricing Problem: A Synthesis", Journal of Industrial Economics, 44, 1996, 131-150.

Armstrong and Sappington, 2004, "Recent Developments in the Theory of Regulation",

Paragraphs 4.1, 4.2, 5

Dana and Spier (1994) "Designing a Private Industry: Government Auctions with Endogenous

Market Structure", Journal of Public Economics 53, pp. 127-47

Laffont and Tirole, paragraphs 7.2, 7.3

4) REGULATION IN A DYNAMIC SETTING

Armstrong and Sappington, 2004, "Recent Developments in the Theory of Regulation",

Paragraphs 2.2.2, 2.3

Baron D., 1989, Design of Regulatory Mechanisms and Institutions, in R. Schmalensee and R.D.

Willig eds.: The Handbook of Industrial Organization, Elsevier North-Holland.

Laffont and Tirole 1993 "A Theory of Incentives in Procurement and Regulation", MIT Press,

1.10, 9.1, 9.2, 10.1-10.3.

5) PRACTICAL REGULATION

Armstrong and Sappington, 2004, "Recent Developments in the Theory of Regulation"

Paragraphs 3.1, 3.2

ADDITIONAL READINGS (optional)

General interest readings on Regulation

Crew, M.A. and Kleindorfer (2002) "Regulatory Economics: Twenty Years of progress?",

Journal of regulatory Economics, 21(1) 5-22

Laffont J-J., 1994, "The new economics of regulation ten years after",

Econometrica, vol. 62, n°

3, 507-537.

Vogelsang, I. (2002) "Incentive Regulation and Competition in Public Utility Markets: A 20-year

Perspective", *Journal of Regulatory Economics*, 22(1) 5-27

Textbooks on Regulatory Economics

Armstrong, Cowan and Vickers (1994) "Regulatory Reform: Economic Analysis and British Experience", MIT Press

Laffont and Tirole (1993) "A Theory of Incentives in Procurement and Regulation", MIT Press

Newberry (2000) "Privatization, Restructuring, and Regulation of Network Utilities", MIT Press

Shleifer and Vishny (1998) "The Grabbing Hand: Government Pathologies and Their Cures", MIT Press

Spulber (1989) "Regulation and Markets", MIT Press

Vickers and Yarrow (1988) "Privatization: An Economic Analysis", Harvard University Press

Viscusi, Vernon and Harrington (2000) "Economics of Regulation and Antitrust - 3rd Edition", MIT Press

Monopoly Regulation

Baron and Besanko (1984) "Regulation, Asymmetric Information, and Auditing", *RAND Journal of Economics* 15 (4), pp. 447-70

Baron and Myerson (1982) "Regulating a Monopolist with Unknown Costs", *Econometrica* 50, pp. 911-30

Braeutigam, R, 1989, Optimal policies for natural monopoly, in R. Schmalensee and R.D. Willig eds.: *The Handbook of Industrial Organization*, Elsevier North-Holland.

Calzolari, "Incentive Regulation of Multinational Enterprises" *International Economic Review*, 2004 45:1

Che, Y.K. (1995) "Revolving Doors and the Optimal Tolerance for Agency Collusion", *RAND Journal of Economics*, 26(3) 378-397

Laffont and Martimort (2002) "The Theory of Incentives: The Principal-Agent Model", Princeton Univ. Press, Chapter 2-3

Laffont and Tirole (1986) "Using Cost Information to Regulate Firms", *Journal of Political Economy* 94, pp. 614-41

Laffont, J.J. and J. Tirole (1988) "The Dynamic of Incentive Contracts", *Econometrica* 56(5) 1153-1176

Laffont, J.J. and J. Tirole (1990) "Adverse Selection and Renegotiation in Procurement", *Review of Economics Studies* 57(4) 597-626

Laffont, J.J. and J. Tirole (1991) "The Politics of Government Decision Making: A Theory of Regulatory Capture", *Quarterly Journal of Economics*, 106(4) 1089-1127

Loeb, M. and W. Magat (1979) "A Decentralized Method for Utility Regulation", *Journal of Law and Economics*, 22(2) 399-404

Riordan, M.H. and D.E.M. Sappington (1988) "Optimal Contracts with Public ex-post Information", *Journal of Economic Theory* 45(1) 189-199

Schleifer, 1998, "State versus Private Ownership", *Journal of Economic Perspectives*.
 Regulation and Competition

Auriol and Laffont (1992) "Regulation by Duopoly", *Journal of Economics and Management Strategy* 1 (3), pp. 507-33

Bulow and Roberts (1989) "The Simple Economics of Optimal Auctions," *Journal of Political Economy* 97 (5), pp. 1060-90.

Klemperer (2002) "What Really Matters in Auction Design", *Journal of Economic Perspectives* 16 (1), pp. 169-89

Shleifer (1985) "A Theory of Yardstick Competition", *Rand Journal of Economics* 16 (3), pp. 319-27

Access Pricing

Armstrong, M. (2002), "The Theory of Access Pricing and Interconnection," in M.E. Cave, et al.(eds.) *Handbook of Telecommunications Economics Vol.1*, North-Holland: 295-384

Laffont and Tirole (1994) "Access Pricing and Competition", *European Economic Review* 38, pp. 1673-710