The article "The Problem of Externality" by Carl J. explores the concept of externalities and their connection to transaction costs. It highlights the divergence between private and social costs when externalities are present, leading to market inefficiencies that require government intervention or the creation of new markets. The author emphasizes that transaction costs are the key driver behind externalities, as they prevent the internalization of side effects through bargaining. The paper examines two contrasting approaches to externalities: the modern welfare theory based on general equilibrium analysis and the Coase theorem view. While the former focuses on evaluating economic performance against optimal solutions, the latter suggests that the presence of externalities is not easily identifiable when considering bargaining and side payments. The author then analyzes the nature of transaction costs, arguing that existing classifications are inadequate and proposes a new categorization specifically for externalities. The article also criticizes the concept of externalities as a normative judgment, rather than a proven market failure, suggesting that the government may not be better equipped to handle externalities than the market. Finally, the paper explores the relationship between the Coase theory and the Pigou tradition, challenging the common misconception that the former advocates for minimal government intervention, while the latter supports government intervention through taxation. The author concludes that the Pigou tradition, in its pure form, actually suggests no government intervention, while the Coase analysis, taking into account individual wealth maximization, offers a more nuanced perspective on the role of government in addressing externalities.