

# Conceptual Foundations of Property Rights: Some key issues

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# General perspectives

1. Property rights are social constructions
2. There is no unique answer to the question of the design of property rights regimes
3. Property rights regimes must be based on recognition of limits of markets
  1. Coase and DeSoto are wrong
4. Rights of individuals are different than the rights of corporations

# Chicago School of Law and Economics

- Saw legal institutes as basis of market economy
- Focused on efficiency
- Assumed that clearly defining property rights would result in efficiency
  - Competitive markets lead to economic efficiency
  - Strong presumption that markets are competitive
    - Even when there is a single firm

# The critique

- Even with competition, markets are not in general efficient
  - Free contracting does not result in efficiency, because contracts between two parties affect their
- Coase conjecture is wrong, whenever there is imperfect information or transactions costs
- Distributional issues cannot be separated out from efficiency issues
- Markets often are not competitive
- For the same reasons that contracts/markets can never be complete, it is impossible to fully define property rights

# The alternative framework

- Law is concerned with equity as well as efficiency
  - Many institutions are created to maintain inequities, not to enhance efficiency
- Regulations help correct market failures
  - Pollution
  - Incomplete contracting—specifying defaults
  - Reducing externalities on third parties

# Immediate implications

- Responsibilities as well as rights
- Rights are always circumscribed and limited
  - Both rights to income and rights of control
- Never possible ex ante to specify all rights
  - Defined over time by cases
  - Evolutionary process
    - But no reason to believe that evolution by itself has any optimality properties (contrary to Hayek)
    - Political Coase theorem is especially wrong
  - Never tabula rosa—always some initial assignment, so typically attempts to define property rights represent a reassignment of rights
  - Explains why legal transplants won't work

– Key question is how political/legal system corrects “mistakes”

- In context of rapid changing environment mistakes may happen more frequently and easily
- May be more important to invest in avoiding mistakes (human fallibility)
- And in investing more in error-correction systems
- *Different degrees of flexibility and adaptability may be optimal in different economies*

# Political Economy

- Security of property rights matters
- But security of property rights depends on legitimacy
- Legitimacy depends in part on how property was acquired
- But there is a need to draw a line upon the past
  - How can this be done in a way which restores legitimacy to property rights?

# Ex ante vs. ex post regulatory frameworks

- High transaction costs of ex post system
- Typically intertwine compensation with incentives—mistake
- Greater rigidity of ex ante system

# Independence

- Should mean particular decisions are based on the law, not on wealth or political connections
- But the *law* should itself be determined by a political process
- But legitimacy of the outcomes of that political process will depend on the legitimacy of the political process itself