

Law and Economics
Session 7
Property Law 1

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- Topics:
 - 1 Environmental law
 - 2 Health/safety regulation
 - 3 Taxation
 - 4 International law
 - 5 Corporate law/governance
 - 6 Bankruptcy law
 - 7 Antitrust
 - 8 Regulation of natural monopoly
 - 9 Employment law
 - 10 Antidiscrimination law
 - 11 Family Law
 - 12 Trusts and Estates
 - 13 Evidence

- Property:
 - A bundle of rights an owner exercises over a specified resource, such as the right to own, transform and transfer.
- Often, property rights are ambiguous.
- In a sense, property rights are what the courts are expected to rule in the event of a dispute.

- Why should there be property rights?
- Why should governments protect them?
- Do property rights matter?
 - That is, do property rights allocations have “efficiency” consequences?

- What can be owned privately and what should be owned publicly?
- What may owners do with their property?
- How to compensate for the violation of property right?

Why have property rights?

- Efficient Exchange.
- Efficient utilization of resources
 - “Tragedy of commons”. Open pastures, open fisheries
 - Illustration: Suppose two herdsmen raise cattle on a common pasture. Each cattle brings \$5 if there are two cattle raised; \$3 if there are three cattle raised; \$2 if there are four raised (Diminishing returns).
 - Suppose each herdsman puts either 1 or 2 cattle on the commons.
- Protection of property right discourages reallocational efforts, which are not productive.
- Lack of government protection of property rights entails “private enforcement efforts.” Why are private enforcement less efficient? Public good feature of “enforcement.”

One Property Right: The Right to Resell

- Yes for many goods
- No for many others
 - Examples?
 - Inalienable goods.

- Search costs
- Information costs
- Incomplete contracts
- Endowment effect
- Wealth constraints

TABLE 4.3
Factors Affecting Transaction Costs

Lower Transaction Costs	Higher Transaction Costs
1. Standardized good or service	1. Unique good or service
2. Clear, simple rights	2. Uncertain, complex rights
3. Few parties	3. Many parties
4. Friendly parties	4. Hostile parties
5. Familiar parties	5. Unfamiliar parties
6. Reasonable behavior	6. Unreasonable behavior
7. Instantaneous exchange	7. Delayed exchange
8. No contingencies	8. Numerous contingencies
9. Low costs of monitoring	9. High costs of monitoring
10. Cheap punishments	10. Costly punishments

“Theorems” for what the law should do

- What should the law do in light of the failure of the Coase Theorem with transaction costs?
- “Normative Coase Theorem”:
 - “Law should facilitate voluntary bargaining.”
- “Normative Hobbes Theorem”:
 - “Law should minimize the harm resulting from the failure of voluntary bargaining.”
- Why the government should publish private information about companies, for example.

Remedies for property rights violations

- **Damages:** Compensatory monetary damages for the wrongs inflicted.
 - If you trampled my crops, you pay the monetary value of the harm
 - How to set damages for trespassing?
- **Injunction:**
 - Court order “enjoining” the defendant to stop violation.
- What should be the rule if someone steals a family heirloom?

Example: Laundry and Electric Company

- Facts: E pollutes L, destroying L's profit of \$200. Without pollution, E and L would earn respectively \$1000 and \$300. The pollution can be prevented by installation of scrubbers by E at the cost of \$500 or by installation of filters by L at the cost of \$100.
- Socially efficient outcome.
- Outcomes under:
 - No remedy (with and without bargaining)
 - Damages for pollution (with and without bargaining)
 - Injunctions to prevent pollution (with or without bargaining)
- When bargaining is impossible, legal incentives can reduce efficiency.

Role of Transaction Costs

- With no transaction costs:
 - Injunctions/Damages doesn't matter
- High transaction costs:
 - In this case, no remedy was best, but damages was preferred to injunction
- Low/medium transaction costs:
 - Injunction is preferred because it gives the parties clear positions from which to bargain.

Sriracha Sauce Case

- A Southern California city has declared the factory that produces the popular Sriracha hot sauce a public nuisance.
- The Irwindale City Council's action Wednesday night gives the factory 90 days to make changes to stop the spicy odors that prompted complaints from some residents last fall. Declaring a public nuisance will allow city officials to enter the factory and make changes if the odors persist after the deadline. . . .
- Irwindale sued Huy Fong Foods last October, asking a judge to halt production at the company's factory, saying residents downwind complained that fumes from the grinding of red hot chili peppers was stinging their eyes and giving them headaches and coughing fits.
- In November a judge ordered the company to stop producing the annoying odors, but by then the annual pepper-grinding season, which runs from August through October, had ended.
- In the meantime, several residents complained that the smell was persisting as Huy Fong Foods workers continued to bottle the popular hot sauce that is a staple in Asian restaurants and homes. Data provided by the AQMD showed the majority of complaints came from four households.

Public vs. Private Ownership

- Earlier we saw that private ownership of the commons was preferred to common ownership.
- In general:
 - private goods should be privately owned
 - public goods should be publicly owned
- In particular:
 - Nonrival goods should be publicly owned

Rights of Use for Personal Property

- Usually rights of use to owned property should be unrestricted.
 - In the absence of externalities, broadening rights of use expands the owner's choice set without imposing costs on others.
- With externalities, use rights may be restricted
 - E.g., a loud drum set.

What about redistribution?

- As we saw in the section on wealth effects, assignment property rights can be seen as an allocation of wealth. Why not reassign property rights from the wealthy to the poor?
- In general, a redistributive goal can be better served by tax/subsidy policies.

Solve Rancher-Farmer Dilemma with other doctrines?

- Contract?
- Tort?
- Criminal Law?

The distinction between contract and property

- Contractual obligations are made between two individuals.
- Property obligations run with the land.