Should property law matter for the economic analysis of property rights?

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Abstract: In this paper, I develop an epistemological comparison of the traditional economic analysis of property rights and the newly emerging legal institutionalist approach. In 2015, there was a debate between Geoffrey Hodgson and Daniel Cole, on the one side, and Douglas Allen and Yoram Barzel, on the other, focusing on the way that property law is treated in the economic analysis of property rights (EAPR). Hodgson claimed that EAPR reduces law to spontaneity, private ordering and custom and conceives only instrumental approach to it by economic agents. He argued that this account leads to ignore the fact that law consists of state backed legal rules with certain level of legitimacy, relation to morality and norms of agents and can imply their specific economic functions like collateralization. EAPR authors interpreted the criticism as being purely semantic, implicitly connecting its more substantial implication to potential mis-appreciation of main EAPR insights. This led to a status quo which limited the possible benefits accrued from the debate for the progress in the economic research on property rights. It is argued here that a distinction between explanans and explanandum has to be introduced comparing the two approaches on different levels. I show how this allows us to overcome the status quo and conceptualize an approach to property rights that draws on both EAPR and its criticism.

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But unless both advocates and critics carefully acknowledge that terms are being used in different ways, the non-semantic issues become lost behind a smokescreen.

Geoffrey Hodgson (2015b)

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1. Introduction

In 2015 Geoffrey Hodgson (2015a) mounted a criticism of a strand of new institutional economics, the economic analysis of property rights (EAPR), for its lack of recognition of property law. This problem was already recognized to the degree that in the *Handbook of Law and Economics* Lueck and Miceli (2007: 187) state that “the economic analysis of property law is substantially less well developed than the economic analysis of contract law or tort law.... The economics of property rights, however, is well developed but mostly without a focus on property law...[and] much of the economics of property rights literature remains ignorant of property law. Similarly, property law scholarship often is ignorant of economics.” In the past three decades, during which EAPR developed and produced its well known contributions it has been criticised for this problem mostly by legal scholars (Merrill & Smith, 2001b and Fitzpatrick, 2006) and some economists (Cole & Grossman 2002, Arruñada 2012). Peculiarly, Hodgson’s criticism was the one draw the attention of EAPR authors who thought it deserved an answer.

Hodgson’s criticism was made from a standpoint that can be understood as broadly legal institutionalist (IAPR) (Deakin et al 2017). It went in the similar direction as previously mentioned authors insisting that EAPR analytic framework is unable to account for what property legally speaking is. Hodgson drew upon the criticisms made by his predecessors. He reiterated the point made by Cole & Grossman (2002) that proponents of EAPR did not recognize the difference between legal institution of property and pre-legal fact of possession. He also paralleled the argument originated by Merrill and Smith (2001b) and reinforced by Arruñada (2012) in arguing that property can only be understood as based on *in rem* rights instead of *in personam* rights that we generally find in contracts. But what made Hodgson’s criticism particularly powerful was the fact that it reconstructed how this inability lead EAPR towards an account of law that reduces it to spontaneity (Hodgson 2015a: 4), private ordering (Hodgson 2015a: 4, 18) and custom (Hodgson 2015a: 3-9). This reconstruction drew extensively upon his understanding of different paradigms in history of economic thought and in particular, the change of approach to motivation for economic behaviour that has occurred. (Hodgson 2015a: 12-17) Appreciation for this change that emerged practically at the same time while EAPR authors were producing their main contributions allowed Hodgson to notice that they operated on the basis of presuppositions about motivation that have in the meantime been abandoned.

Possibly the most persuasive aspect of his criticism consisted in showing the way in which this new understanding of motivation was particularly sensitive of legal institutions.

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2 Their insights have been collected in Barzel (1997), Allen & Lueck (1995) and for an earlier collection see Furubotn and Pejovich (1972)

3 Indeed, Hodgson’s mapping of different strands in history of economic thought and particularly institutionalism necessary to understand the present discussion is refreshing as unlike in most cases where economic arguments are presented with little methodological reflection, the problems with property appear to be rooted in controversies that are at least a century old (some of them being already clear in the work of Hohfeld in the first decades of XX century)
Instead of being reduced to spontaneity and custom they could now be considered as state backed legal rules with certain level of legitimacy (Hodgson 2015a: 5, 15-17), relation to morality and norms of agents (Hodgson 2015a: 4-5) and can be recognized in their specific economic functions like collateralization (Hodgson 2015a: 7, 18). Hodgson (2015a:12-14) forcefully showed how EAPR retains an uncritical reliance upon rational utility maximiser that considers law only instrumentally. For EAPR law is only relevant in as much a particular level of enforcement makes actors follow (or not follow) the rules. This gets to be analysed as a set of relevant transaction costs in the context of use and trade over valuable resources. Hodgson pledged for a much more complex world in which agents go against their own order of preferences on the basis of morality (Hodgson 2015a: 15), law is not enacted only on the basis of obedience in fear of enforcement but acceptance of its legitimacy (Hodgson 2015a: 15-17) and is able to influence the cost setting relevant for economic actors in ways beyond the costs of transacting.

Beyond a number of substantive arguments that will be tackled below, EAPR proponents reacted to Hodgson’s claims by interpreting them primarily as a demand for semantic clarification (Barzel 2015: 720, Allen 2015: 713). Thus they deemed these claims to be of limited impact and without ability to put EAPR analytical standpoint into question in an essential manner. In his further response, Hodgson went on to underline why his criticism should not be taken as purely semantic and to characterise the epistemic standpoint of EAPR as nominalist (Hodgson 2015b: 743). To contrast it, he argued for an anti-nominalist position thus showing unreconcilable differences between the two ways of approaching economic analysis and warning about all that gets to be left out of the scope of analysis if one goes in the nominalist direction in approaching institutions.

Importantly, these arguments appeared not to put in question the significance of EAPR analytical framework as far as its models provide insights about the phenomena related to interaction of individuals with law. Indeed, both Hodgson (2015a) and the precedent critics (Cole & Grossman 2002, Merrill & Smith 2001b, Arruñada 2012, Fitzpartick 2006) show respect for the advances made by EAPR and are explicit in their intention not to put those into question. In turn, the nominalist proponents of EAPR are left comfortable in their intention to use the analytical framework that is deficient in its conceptualization of property law as long as it accrues further insights about the phenomena related to interaction of individuals with law (that will be generally accepted). After everything has been said and done, one gets the impression that there is more to the legal institutional criticism of EAPR. It seems clear that the criticism offers an alternative analytical framework with many benefits, but the discussion somehow makes it difficult to appreciate and incorporate them towards a more powerful approach. The issue seems to be framed as trade-off between accepting EAPR findings and demand for change of its analytic framework.

From an external standpoint, this ending of the debate in a kind of analytic status quo is highly non-satisfactory. It leaves us not so far from where we were before. It does bring some clarification as to the differences between the two approaches. Still these seem to imply the existence of an impasse instead of any decisive insight how to proceed in approaching property in an institutional analysis.
In the following sections, this apparent outcome of the debate is taken as a sign that there is a further need for a systematic clarification in comparison between EAPR and IAPR. According to the arguments made here, the lack of clarity is particularly present when it comes to explanatory power of the two approaches and the area of their overlapping. On that basis, I will try to show how a further inquiry can lead us to a more conclusive and beneficial outcome than the status quo. To achieve this, in the second section, a reconstruction of the problem of whether defining property has only semantic implications for analysis will be supplemented by a meta-theoretic framework. This framework focuses to the object and goal of explanation of institutionalist approach to property. Once the two approaches are reconstructed, the mentioned framework will be utilized to inquire on how the apparent status quo can be overcome. I will try to show how IAPR is able to integrate the findings of EAPR. This ability of IAPR does away with previously explained trade-off that appeared to be unavoidable. In other words, we can liberate ourselves from the necessity to either base the criticism of EAPR in a miss-appreciation of its findings or accept that the EAPR analytical framework has to change. Instead, integrative capacity of IAPR sheds light on the manner in which the change of the framework towards more sensitivity with regards to property law can build upon the EAPR findings themselves. The goal is to explain how IAPR is able to play the role of not only an encompassing approach but also of an approach that looks at the object of explanation in a synthetic manner and tackles issues related to EAPR findings that were previously left out as they did not seem to be related.

2. Should the thousand flowers be left to bloom?

2.1 The criticism

Hodgson’s (2015a: 9f) case against EAPR is primarily focused on the definition of property rights that its proponents utilize in analysis. The crucial issue is whether the fact of control and possession can be defined as a right or not. As Hodgson (2015b: 733) notices, with regards to this definition one should have in mind that there are slight differences between EAPR authors. Also, as Cole and Grossman (2002) show, this problem is not contained only within boundaries of EAPR, but seems to be much more pervasive as it is implicit in analytical frameworks of a wide range of economic approaches. Maybe the most illustrative are the examples of (a) Heyne’s textbook stating that “firms do in fact have rights to discharge obnoxious substances into the air, as proved by the fact that they do it openly and are not fined. They have both actual and legal ‘rights to pollute’” (Heyne 2000: 334) and (b) Buchanan and Tullock’s (1966) analysis presuming that “the polluter holds the right, and that the only option available to those harmed by the pollution is to purchase the entitlement from the polluter through voluntary collective action or some tax and subsidy scheme adopted pursuant to a rule of unanimity.” In addition, Hodgson (2016: 42) also notices that this way of approaching property was originally present in arguments by Ludwig Von Mises (1949). It
has deeper roots in the socialist calculus debate.  

In any case, when it comes to EAPR proponents, this habit of defining pre-legal facts independent of any normativity as rights becomes quite apparent. For example, Alchian (1965) defined private property rights in terms of assignments of the ability to choose the use of goods (without affecting the property of other persons). Later, Alchian (1977: 238) defined these rights in relation to “the probability that [owner’s] decision about demarcated uses of the resource will determine the use.” In the same vein, Barzel (1997: 394) defined property as “an individual’s net valuation, in expected terms, of the ability to directly consume the services of the asset, or to consume it indirectly through exchange.” As he underlines “[the] key word is ability: the definition is concerned not with what people are legally entitled to do but with what they believe they can do.” Barzel is also famous for his distinction between economic and legal property rights. According to him (Barzel 1997: 3) the term “property rights” carries two distinct meanings in the economic literature: “One . . . is essentially the ability to enjoy a piece of property. The other, much more prevalent and much older, is essentially what the state assigns to a person. He decides to designate the first ‘economic property rights’ and the second ‘legal (property) rights’.” Later Barzel goes on to explain that “economic rights are the end (that is, what people ultimately seek), whereas legal rights are the means to achieve the end. Legal rights play a primarily supporting role...” Finally, Allen (2014: 4) claims that in his view “Following others, economic property rights are defined as the ability to freely exercise a choice.”

Hodgson (2015a: 11) rightly notices this general intuition can be interpreted to stem out from the standpoint adopted by property-right economists according to whom the ‘structure of property rights’ refers primarily to a set of constraints upon, and incentives and disincentives for, specific individual behaviours. This diagnosis rings a bell in the argument put forward recently by Di Robillant and Syed (forthcoming) that a deeper issue in L&E approach to property has to do with the habit of omitting of the legal-architectural issues (what property is) related to property law and rushing into substantial issues (how property emerges and what incentive structure it implies) that involve cost analysis.

Hodgson’s criticism of this way of approaching property is summarized in the following passage:

When von Mises and Alchian referred to property they reduced it simply to the fact of possession or control. Likewise, when Barzel and Allen refer to ‘economic rights’ they simply mean possession or control. My objection to these accounts is illustrated by the case of a thief who manages to steal an item and retain control of it. According to von Mises and Alchian, this would become the thief’s ‘property’.

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4 Indeed, the historical roots of misunderstanding concerning property law involve complexities that deserve attention in their own right. While Hodgson provides useful remarks from the side of history of economic thought, Merill and Smith discuss extensively the elements from history of legal thought.
According to Barzel and Allen, the thief would have established an ‘economic right’ to the stolen goods. (Hodgson 2015b: 736)

According to Hodgson, the general problem of this approach is that by using the concept of right for a pre-legal fact, it concentrates on possession, downplaying the issue of legitimate legal rights. As he reminds us, “possession is foremost a relation between a person and a thing [which] does not amount to legal ownership [while] ... the term ‘property’ should be reserved for cases of institutionalized possession with legal mechanisms of adjudication and enforcement.” These mechanisms are [inseparable from and incomprehensible without a distinction between] “...multiple different types of possible right that can be either the right to use a tangible or intangible asset (usus), the right to appropriate the returns from the asset (usus fructus), the right to change a good in substance or location (abusus), the right to the capital derived from the use of the good as collateral, the right to sell a good (alienation), and several other rights or limitations or a combination of those.” (Hohfeld 1919; Honore 1961, Hodgson 2015a: 7) Thus, to put it in terms of previously introduced distinction, a valid approach to substantial issues related to property can only be established if clarity is reached with regards to the prior legal-architectural aspects.

Inability of EAPR to account for the specificity of property as a set of rights as opposed to pre-legal fact of possession leads to further lack of recognition of the specific type of right that property involves. Hodgson (2015a: 6) only notes in passing what has been the central concern of others that criticized EAPR for its ignorance of the legal character of property rights – the fact that they generally involve in rem rights as opposed to in personam ones that we find in contracts.

As Arruñada (forthcoming) explains, rights in personam are only valid against specific persons, inter partes, [while] rights in rem are valid against all individuals, erga omnes. Merrill and Smith (2001a: 783) recapitulate Hohfeld’s (1919) analysis of specificity of in rem rights in contrast to in personam rights, as they are characterized by both an indefinite class of duty holders that come large numbers of duty holders; as they attach to persons through their relationship to particular things rather than to persons as persons; as they are numerous and indefinite in two directions - not only does each in rem right give rise to a large and indefinite number of duty holders, but also each duty holder holds such duties to a large and indefinite number of right holders; and as they are always claims to abstentions by others as opposed to claims to performances on the part of others.78

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6 Of course, Merrill and Smith show that besides the pure cases there is a wide space in between, and that, for example, common property is legally realized through in rem rights that to certain extent specify the parties that have duties towards the owners.
7 For example, in the Nordic countries jurists have even gone so far as to draw the line between property law and the law of obligations on the basis of the person-relation types.
8 One and the same patrimonial right (private law right) may have both obligational and proprietary aspects to it, depending on which person relations we look at – the obligational ones appear between the parties, the proprietary ones in relation to third parties. For example, in the transfer (assignment) of claims, questions between the transferor and transferee are
Inability of EAPR to account for the *in rem* character of property rights stemming from the treatment of possession as a right leads its proponents into problems with conceptualization of relation and interaction between contract and property. The fact of possession interpreted as (economic) property right is not determined in terms of what relation the possessor has with others. This allows for both treating property as purely a basis for contracting as the possessor can relate to determine other parties with regards to control over the possession (either by exchanging it, offering services, etc.) or assuming that possession necessarily becomes backed by exclusionary rules. The example of the first case can be found in Barzel (1997: 4) who explicitly recognizes the reduction he makes stating that “[a]t the heart of the study of property rights lies the study of contracts.” As Merill and Smith (2001b: 377) show that Barzel starts with contractual exchange and then defines “property” as those attributes left over after all maximizing contracts that are possible within transaction-cost constraints have been exploited. Property is not a baseline but a residuum of value. As Merrill and Smith (ibid) notice: one cannot enter into contracts over the use of resources without some baseline to determine who contracts with whom. Because of this they conclude that Merill and Smith (2001b: 378) Barzel ends up with a theory of property in which the *in rem* dimension is entirely missing:

Barzel develops a powerful framework for analysing issues that arise between buyers and sellers of property or between co-owners of property—relations that are essentially *in personam*. Outside these contexts, however, property recedes into the background as a stand-in for the assignment of use rights that is employed only when the possibilities for contracting run out.

The best example of the second case is Demsetz’s analysis that is concentrated on rights of exclusion (Smith 2002: 454), which are thought to be characteristic of private property. In exclusion, decisions about resource use are delegated to an owner who, as gatekeeper, is responsible for deciding on and monitoring specific activities with respect to the resource. To set up such rights, rough proxies like boundaries and the *ad coelum* rule are used. These exclusion rights are used when the audience (of duty holders) is large, and their simplicity reduces the processing costs that would be high for such a large and anonymous audience.

Smith (2002: 455) argues that at the pole opposite of exclusion there are “governance rules ...that... pick out uses and users in more detail, imposing a more intense informational burden on a smaller audience of duty holders.”

2.2 The answer to criticism

obligational, but questions between the transferee and, say, the transferor’s creditors are proprietary. More generally, modern property law mostly focuses on ‘dynamic’ questions of disposition of rights, and the exchange of rights (especially third-party conflicts), whereas EAPR seems to have a much more static perspective.

Merrill and Smith (2001b), this has its origin in Coase and Hohfeld.

The same approach can be found in (Cheung 1970)
In answering to these criticisms, proponents of EAPR did get into a content of Hodgson’s arguments on two points – transaction costs and degrees of state enforcement of law. Still the main focus of their answers can be found in their discussion of the semantic implication of Hodgson’s criticism. To begin with, they admit the apparent contrast of their definitions of property rights to those that can be found in dictionaries. Barzel even goes on to regret that as it happens, once the definitions get accepted within a certain academic milieu it is very hard to change them. But all of this only implies that even if the desired change could occur it would not make a difference when it comes to the analysis performed assuming those definitions. To think that it would, implies putting the findings of EAPR analysis into question and as it has already been mentioned there seems to be no one who is really willing to take upon that position. Of course, this in turn makes the implication of the criticism quite ambiguous. In general, there is a very visible confusion related to this issue and the adherents to the two sides of discussion end up spending a lot of effort to determine precisely what is contested and what is not. For example, EAPR authors respond to cases for analysis (e.g. collateralization, blockchain, etc.) brought up by Hodgson as non-analysable utilizing the adopted definitions of property by pointing out that EAPR proponents conducted productive analysis of those cases. Obviously, Hodgson did not imply the opposite. The crucial question is that of the framework used in these EAPR analysis is deficient in the precise way that Hodgson accuses it to be and what limitations to the possible findings this entails. In that way, this question gets to be ignored. The same can be said of multiple other cases brought up as problematic for EAPR type of analysis such as (a) whether numeros clausus or default rules will develop (Merrill and Smith 2001b: 385-388) or (b) what difference the sequential character of the majority of exchanges makes (Arruñada 2017) or (c) that of outcome of interplay between social norms and enforceability of legal rules.

In general, EAPR proponents closely follow the strategy that was already noticed by Merrill and Smith (2001a: 775f): when they are confronted with evidence that “[their] notions [of property] may be incomplete, [they] often retreat by saying that the "economic" definition of property is different from the "legal" definition, with the implication being that they are absolved of any obligation to explain the function of the legal institution.”

They try to delimit this “economic” context of property as something that can be adequately approached even without considering legal definitions related to it. Outside this context, they seem to be willing to admit the relevance of these definitions. However, if this is accepted, the question that is left unanswered is why would they want to consider what is outside these contexts (Merrill and Smith 2001b). Barzel argues that answering this question boils down to distinguishing what is useful and he admits that he considers “economic rights (by whatever name) as useful, whereas [he doesn’t] view as useful Hodgson’s understanding of what either kind of rights is.” The following phrase by Barzel (2015: 722) is particularly illustrative of this nominalist attitude:

Whereas the term ‘economic rights’ may be ill chosen, the substance behind it – its role in affecting behaviour – is basic. Such a role is largely absent from rights as viewed by Hodgson (though he vacillates about this)... Generalizing, a person in possession of an asset will maximize its value to him by choosing the appropriate
form of protection. One form of protection, of course, is establishing legal rights.

Allen further provides a systematic answer to Hodgson’s reasons for thinking that his criticism implies something more than semantics claiming that the use of word “right” for control is just a matter of labels, that it does not necessarily exclude the attention to moral duties and that in any case issues like collateralization get to be included in EAPR analysis. (Allen 2015: 714)

Hodgson (2015b: 737) answered these arguments by pointing out that because an ‘economic property right’ refers to de facto possession and is not necessarily a right (although of course it may become one)... “[the EAPR] depiction of behaviour as ‘economising’, conjoined with the terminology of ‘economic property rights’, wrongly leads to the suggestion that ‘legal property rights’ are instrumental means rather than ends in themselves, and [to the proposition]... that people are never directly motivated to obey the law simply because they believe it is the right thing to do. They fully accept that law affects behaviour, but only instrumentally, as a cost or constraint.”

Hodgson (2015a) contests that ‘economic rights’ are primary and more relevant for understanding behaviour. He argues that legal factors – involving recognition of authority and perceived justice or morality – have also to be brought into the picture to understand human motivation in modern societies, even in the economic sphere. But this articulation of criticism still allows proponents of EAPR to respond that these different aspects of motivation for economic behaviour do not necessarily need to be analysed hand in hand, and that, as far as their findings uncover a part of the existing economic behaviour, this justifies at least conditional adoption of their definitions.

As Hodgson (2015b: 743) rightly notices, the crux of this argument lies in its nominalist foundation according to which validity of concepts stems from their analytical success and not in the fact that they correspond to reality. In fact, this only criterion of fit with reality a nominalist accepts is that of success of his functional explanation of what is observed in phenomena related to interaction of individuals with law. From a nominalist standpoint, the analytic framework used by EAPR is justified by the success and verifiability of its explanations. Thus the criticism is plausible only as demanding a semantic restructuring of the framework so that the (unchanged concepts) are expressed in terms that are more in tune with accepted legal and lay definitions. To put it another way, a nominalist recognizes something as a reality only as much it can be found in a conceptual framework that explains the phenomena related to interaction of individuals with law. For a nominalist, the fact that property and rights in general exist as a legal reality and that ‘property rights’ should be defined in way that is in tune with that reality, can only mean that his definitions should change if this change is necessary for explaining further insights about the phenomena related to interaction of individuals with law that are connected to those that EAPR framework is intended to explain. From the nominalist standpoint it follows that if IAPR offers a different analytical framework that explains a different set of phenomena than its criticism of EAPR is an overextension as these different frameworks should exist side by side and be used for explanatory purposes they suite best.
In this manner EAPR authors make use of the fact that both distinctions (that between pre-legal fact and legal right and that between *in personam* and *in rem* rights) introduced by the critics are not used to contest the findings that they reach with their analytical framework but only to notice that this framework is not in tune with legally recognized concepts. Even if the legally recognized concepts can be of relevance for economic analysis it seems that EAPR authors ascribe importance to the fact that this is a separate analysis that does not contest their own. In other words, the criticism is interpreted as either being purely directed at concepts as labels or contesting the adequacy of the EAPR findings about the phenomena related to interaction of individuals with law.

If this interpretation is accepted, it seems that there is very little to be discussed and even less to be gained from the discussion in terms of research. It should be clear from the previous depiction that the root of the problem really lies in how the *explanandum*, i.e. the object of explanation is defined. Nominalist presupposes that if the EAPR explanation of the regularities that it is used to explain is not contested by IAPR than we end up having two separate objects of explanation – one that EAPR is engaged with and another that IAPR is engaged with. Nominalists are not keen on speaking about reality, but one could understand the previous argument as saying that if a success in explanation of the phenomena related to interaction of individuals with law is the criterion of fit of reality of different concepts than the issue between IAPR and EAPR boils down to having two separate and *unrelated* objects of explanation. Finally, according to the implicit nominalist argument, differences in explanandum justify the differences in the *explanans*, concepts used to construct the explanation. Notice that a nominalist necessarily has to claim that these objects of explanation are *in principal* unrelated, because if they were related than the findings reached with one framework would contested by the findings of the other. One can observe how brusque the claim is, as in the last instance it implies that explanation of something that is defined as property rights can do without any reference to property law and that utilization of concepts that do refer to it would not bring the explanation of the intended object any further! In any case, EAPR proponents do not seem to express their nominalist answer as if it points to an impossibility, but they surely do claim that this furthering of explanation of the same object of explanation by IAPR concepts has not yet occurred.

It should be clear by now that this claim is not explicitly expressed by the EAPR authors, but that it does follow if the nominalist argument is coherently presented. It should also be clear that even if this discussion is related to the most practical concern of doing research on institutions it has at the same time an essential philosophical underpinning. Essentially, a nominalist of Quinean (1948) type that utilizes Occam’s razor justifies different concepts within frameworks as far as they are related to experience. It is fully dependant on the naturalist basing of meaning of concepts in the experience. Clearly, one can do away with all this simply by pointing out to a different position in philosophy of science, but there is much more to be gained if we focus on validating the claim about the objects of explanation of the two frameworks. That is if we take a look at the exemplary explanations of two frameworks, do we find that what they intend to explain is really unrelated?

Of course, one way to answer this question would be to point out to some additional variables that IAPR utilizes in its explanations and see what would be their impact if they were taken into account in the explanations of EAPR. Another way to answer it, which might
not be as forceful in its conclusion but still has persuasive power, would be to try to compare a set of exemplary explanations given by the two frameworks and see if and how they interrelate. It is important to check whether one can observe that they do interrelate quite strongly, that is the explanations given are concerned with explaining similarly defined objects. If this comes out to be true, then it could serve as an argument against the EAPR claim that these objects are fully separate and that a nominalist is not obliged to develop concepts defined in a way that combines EAPR and IAPR elements. We prepare the material necessary to fulfill this task in the following section.

3. Explaining property

3.1 Traditional economic approach

In fact, we do not have to go far to find exemplary explanations of EAPR. Possibly the most interesting part of the answer to Hodgson’s criticisms consists of the examples of EAPR explanations that their proponents presented and commented upon.

In one of the examples, Allen (2015: 712) considers “someone walking down a city street late at night.” According to Allen (ibid) the person might choose to “take a short-cut down a dark alley [but] if, after three steps into the darkness the pedestrian sees the shadow of a shady character lurking up ahead, the fact that he has the legal property right to walk through the alley is quite irrelevant for what he does next.” In this case what EAPR proponents define as economic property rights and Hodgson defines possession is relevant for the explanation of behaviour of the agents. As Allen (ibid) argues, “the explanation for why the walker turns around and spurns the alley for a longer route rests on the set of realistic choices held at that moment [and it is] the economic rights count for behaviour.”

Barzel (2015: 720) considers a similar example in which even though a company is the legal owner of that brand name. In practice, “the public expropriated the term, using it generically as a term in common use, essentially depriving the company of the brand name’s value.” Barzel (ibid) notes that EAPR framework has a lot of pertinence as it explains that “although the state recognizes the brand name, it did not protect it from the public using it generically and company’s legal ownership over the name is of little value as it essentially, it has no economic rights over it.”

The point for Barzel of making the distinction in the precise manner that EAPR makes it, has to do with the way that economic rights can be backed by law (to some degree) and become legal property rights, but in many cases they are not, for reasons that are either illegal or do not have to do with law at all:

When legal rights are granted and enforced, it enhances the corresponding economic rights. Whoever actually drives the car over which I have legal rights has economic rights over it, be it myself, a person I authorized to use it, or a thief, though if it is a thief, the state will help me recover it. A Jewish Hassid diamond trader has the economic rights over the value of expensive diamonds he just passes to another

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11 For a comment on this example from IAPR standpoint see footnote 15.
Hassid with a promise to pay guaranteed by a handshake. Indeed, in case of dispute they are likely to resolve it not by the state court, but via their rabbi. (Barzel 2015: 720)

There is a particular goal that EAPR authors try to achieve in defining the concepts in the way that they do. As Merrill and Smith (2001b: 376) point out their world “consists of a multitude of assets, each of which has multiple attributes. Some of these attributes are the subject of specific contracts. But because of positive transaction costs, the attributes of assets will never be fully reflected in contracts. For example, in a wage contract, incomplete specification of duties and imperfect monitoring of performance—both results of positive transaction costs—will leave some of the value of the employee’s labour up for grabs; the employee can capture this value by shirking. Barzel describes attributes not captured by contracts as being in the “public domain.”

Thus (Merrill and Smith 2001b: 376) Barzel treats someone who has the ability to capture attributes of assets in the public domain as a type of residual claimant. Focusing on residual claimants implies having close attention how, when and to what effect legal titles follow possession and control in economising with resources. As Barzel (2015: 719) claims, “Legal rights are neither necessary nor sufficient for economic rights. For the sufficiency, suppose Congress grants me ownership over an accurately delineated chunk of the Pacific Ocean. This secures my legal rights, but what good are these rights without (costly) naval protection? As for necessity, suppose two neighbours fully recognize and respect the border separating their properties even though its legal delineation is fuzzy. Nevertheless, these neighbours will use their border resources efficiently.”

Once the clarity on what legal and what economic rights mean is reached, EAPR utilizes the traditional economic framing of the problem relying upon a utility maximising actor with a set of preferences. Coupled with a carefully designed set of transaction costs this can lead to interesting insights about negotiation and contracting. Also, it can be useful in approaching the cases of emergence of legal titles as it has been famously done by Demsetz and others. Finally, the EAPR framework fits especially well in an analysis that focuses on enforcement of law as obedience can be expressed in relation to a determined probability of enforcement within a function that utility maximisers maximise.

3.2 Legal institutional approach

Turning to applications of IAPR framework we face the same problem with picking the explanations that can be exemplary. Again, as in the case of EAPR framework it might be best to consider those explanations that they consider while criticising the EAPR.

Hodgson gives away the predominant theme of these explanations. It focuses on evolution of rules instead of focusing on interaction between utility maximisers. Hodgson’s powerful argument about the change in the understanding of motivation in contemporary economics basically and the importance of normative structures. These normative structures

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12 For a comment on this example from IAPR standpoint see footnote 16.
simply exist in society. They can be discovered both in terms of laws followed because they are considered legitimate but also of any type of social rules that are established. The importance of the focus on behaviour from the standpoint of evolution of rules lies in the fact that long surviving sets of rules can lead to more resilient and growth generating institutions and institutional environments (Ostrom 2010).

Merrill and Smith (2001a) and Arruñada (2012 and 2017) provide two good examples IAPR explanations that also relate to phenomena of interaction of individuals with law. They consider resilience of different type of legal rules dealing with different types of resources and activities over resources based in distinguishing between in rem and in personam rights.

Among other things, Merrill and Smith analyse the fencing practices among farmers. According to traditional EAPR approach, as it was originated by Coase (1960??), the issue between fencing in and fencing out will be solve differently in individual cases depending on values of resources and transaction costs. In fact, legal rule does allow for both solutions. At this point, Merrill and Smith (2001b: 388) notice that, “not only do informal norms of fencing in versus fencing out fail to correlate with the legal rule, the norm is always fencing in, regardless of differences in the legal rule or in local conditions.” They (ibid) add that from the EAPR standpoint, “the uniformity of the fencing-in norm is puzzling. It is doubtful that fencing in is always efficient, especially in locations where ranchers far outnumber farmers.” To solve this puzzle and explain the uniformity Merrill and Smith introduce the well-know numeros clausus principle.

As Merrill and Smith (2001b: 387) explain, “the numeros clausus is a device to standardize property rights, and thereby reduce the widespread information-gathering and processing costs imposed on third parties by any system of in rem rights.” This principle is directly related to “the in rem nature of property rights, and the information-cost burden on third parties that is created by any system of in rem rights.” In the case of fencing following this principle and subsequent uniformity in fencing reduces information costs for parties involved as in rem rights oblige the owner to take care of the property with regard to any possible party that would interact with it (Merrill and Smith 2001b: 386). The problem that EAPR has with this kind of examples lies in “that parties can achieve virtually any idiosyncratic use of resources they want by contract, and thus he finds that standardizing property makes little sense.” Merrill and Smith (2001a: 776) show that far from being an exception this differentiation in types of rules and rights adopted on the basis of specificity of different types of resources and their uses is a pervasive feature that determines the difference between the filing of a contract and that of property:

[There is] one pervasive difference in the legal doctrine associated with contract rights and property rights. Contract law typically permits free customization of the rights and duties of the respective parties to any contractual agreement; in other words, contract rules are generally default rules. Property law, in contrast, requires that the parties adopt one of a limited number of standard forms that define the legal

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13 See Hodgson 2014

14 Hodgson (2014) provides evolutionary models that consider altruism and morality.
dimensions of their relationship; generally speaking, these are mandatory rules that may not be modified by mutual agreement... On the one hand, contract rights are in personam; that is, they bind only the parties to the contact. The contracting parties are in the best position to evaluate the costs and benefits of adopting novel legal terms to govern their relationship, and in the typical bilateral contract there are no significant third-party effects associated with the adoption of idiosyncratic terms. Property rights, on the other hand, are in rem — they bind "the rest of the world."

Arruñada provides an example of explanation that builds upon the in rem versus in personam distinction to show how law deals with the specificity of different economic activities. A central difference between economic activities is that whether the exchange occurring is sequential or not. As Arruñada (2012: 3) states, in the simplest sequential exchange, “with only two transactions, one or several “principals”—such as owners, employers, shareholders, creditors, and the like—voluntarily contract first with one or several economic “agents”—possessors, employees, company directors, and managers—in an “originative” transaction. Second, the agent then contracts “subsequent” transactions with third parties.” The point is that in sequential exchange, not only use externalities but also exchange externalities are prevalent (Arruñada 2017: 3), and two additional elements of public ordering are needed to contain them: mandatory rules must establish the conditions for in rem enforcement, and enforcers must enjoy a wider scope of impartiality.

Arruñada (2012: 16) shows that EAPR completely misses the specificity of sequential exchange because in following Coase who analyses only transactions over direct (non-sequential) externalities it “is dealing only with in personam rights (...) and thus it disregards the more mundane but no less important problem of routine transactions on ordinary private property.” In this way ends up ignoring the foundation of impersonal exchange which (reconciling) “requires rights on assets, not merely on persons.” The point is that (Arruñada 2012: 11) “rights in rem, on things, enjoy an enforcement advantage and are therefore more valuable than rights in personam” and that is why individuals and legal systems rely heavily on rights in rem:

These sequential exchanges offer the benefits of specialization in the tasks of principals and agents—between landowners and farmers, employers and employees, shareholders and managers, and so on. But they also give rise to substantial transaction costs, because, when third parties contract with the agent, they suffer information asymmetry regarding not only the material quality of the goods or services being transacted but also the legal effects of the previous originative contract. In particular, third parties are often unaware whether they are dealing with a principal or an agent, or whether the agent has sufficient title or legal power to commit the principal. This constitutes a grave impediment, especially for the impersonal transactions that are necessary to fully exploit the advantages of specialization.... Moreover, principals also face a serious commitment problem when trying to avoid this asymmetry because their incentives change after the third party has entered the subsequent contract. Before contracting, principals have an interest in third parties
being convinced that agents have proper authority, but, if the business turns out badly, principals will be inclined to deny such authority. This is why the typical dispute triggered by sequential transactions is one in which the principal tries to elude obligations assumed by the agent in the principal’s name, whether the agent had legal authority or not (Arruñada 2012: 4).

Arruñada (forthcoming) shows that to overcome the conflict, expanding the set of viable contractual opportunities with minimal damage to property rights, different solutions will be appropriate, depending on the circumstances of each type of right and transaction. The legal system may directly choose to enforce some rights in a certain way or, more generally, give freedom to right holders about which rule to apply. This is the way in which law... overcomes the trade-off of property enforcement and transaction costs by protecting acquirers while preserving the crucial element of the consent of the owners (in general, right holders). Arruñada warns that “granting of consent needs to be verifiable by judges, to prevent right holders from opportunistically denying their previous choices.”15

These two cases show how IAPR can be used to explain how in cases of specific activities over specific resources legal and informal rules, public and private ordering can interact towards resilient outcomes. On the other hand, it should be clear that discovering the connection between rules, resilience and growth can be a difficult task (Ostrom ???).16 In fact, IAPR has been able to analyse not only the cases of success of sets of rules, but also their failure. The fact that it analyses failure as much as it analyses success is maybe the most

15 Having this in mind one could go back to the example made by Barzel and ask why would EAPR proponents limit themselves here to something as superficial and restricted as a brand name and its protection. Why not instead focus on the main function of a brand name – that is, the independence of one’s goods from goods produced or sold by others? This would help to notice the various other ways in which the law protects the function – including the regulation of marketing and unfair commercial practices, and the possibility of registering a new trademark. Even though, all of these have been an important topic of other analysis, some of them made by EAPR proponents, the point here is that the broader legal framework, the system of law, matters in such a way that one has to take care under what conditions some of its parts can be isolated at all.

16 Coming back to Barzel’s example, Ostrom’s and Hodgson’s arguments can be interpreted to imply that fuzzy legal delineation does not mean that law can be left out of discussion. In real world situations related to the example, law could play a role in understanding what it means to ‘recognise and respect’ other’s property in the first place. For example, in the Nordic countries the system of ‘everyman’s right’, meaning that certain uses of land owned by someone else are permitted; while in some other jurisdiction, similar uses might count as trespassing or theft. This parallels Hodgson’s claim how in many complex ways, law affects morality, which has a direct link to what is perceived as recognising and respecting other’s entitlements. Another point in this connection is that what enables the harmonious life between the neighbours despite the fuzzy legal border is the knowledge that should problems arise, or should they seem possible (for example if one of the neighbours sells his or her land to an investor whose planned activities are likely to cause negative externalities), then the law and authorities can be invoked to define the border more accurately. In this manner law can serve as a ‘backup plan’.
important single advantage that IAPR seems to offer. Fitzpatrick explains how an interplay between existing social norms, legal institutions and state apparatus lead to devolution, reestablishment of open access or in particular cases, resilience and growth.

Fitzpatrick (2006) focuses on Third World property systems that in many cases remain plagued by widespread legal uncertainty, resource conflicts and environmental degradation. This fact contradicts the EAPR analysis of emergence of property rights according to which rising resource values will induce property rights, either through private ordering or with the assistance of the state. As Fitzpatrick (2006: 1003) notices for EAPR “property rights are primarily a mechanism for internalizing externalities, a perfect-world solution to problems of conflict, pollution, and resource-dissipation.” He blames the cost-focused approach of EAPR for the fact that [while it] “may explain rational decisions to abandon exclusionary efforts or engage solely in acts of incomplete exclusion, [it does] not explain rational decisions to assert exclusionary rights when that assertion fails due to weaknesses or multiplicity in the enforcement environment” (Fitzpatrick 2006: 1021).

Generally, these problems make EAPR incapable of accounting for crucial divergence between state law and local norms (Fitzpatrick 2006: 1002) as well for specificity of in rem rights in the case of land (Fitzpatrick 2006: 1010). In case land is sold it “does not move and thus secondary rights-holders retain their rights unless they consent to sale, and may assert them against other claimants through occupation or use.” Thus, in turn, the attempts to enforce exclusionary claims will lead to open access rather than an authoritative property rights regime.

Because of a lack of capacity of EAPR Fitzpatrick introduces the formation of informal norm-based orders or coalitions of interests that shape conflict between different sources of enforcement capacity (Fitzpatrick 2006: 1000). This process is essentially determined by legitimacy of law and their compatibility with accepted social norms:

...those holding state property rights rely on the coercive authority of state agencies, but the weakness or illegitimacy of these agencies makes them unable to exclude local claimants.... For their part, local claimants often disregard the rules and institutions of formal law, relying instead on their own normative order or coalition of interests, particularly when the state is weak or oppressive. (ibid)

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17 Coase (1960) seems to be the first to make explicitly the analytic connection of failure, law and different types of ordering.

18 Fitzpatrick criticizes the conclusion of Merrill and Smith that “the tried-and-true method of handling potential conflicts over resources among large numbers of claimants is to create in rem property rights—rights that give one person (the owner) the ability to exclude all other claimants to the resource.” He argues that while this may be the case when authoritative allocation of property rights is possible, further analysis of property rights and resource conflicts also needs to account for the possibility that the process of establishing in rem rights can at times be both a cause of and an aggravating factor in certain types of chronic conflict.

19 Previously mentioned counter-criticisms by EAPR proponents concerning the ability of IAPR to treat state in non-idealized manner seem to be fully answered by Fitzpatrick’s analysis of a fragmentation of the state into competing agencies and levels of government.
To analyse this process and its outcomes, Fitzpatrick (2006: 1002) develops a taxonomic category of open access, based on the availability and effectiveness of enforcement mechanisms and shows how different types of open access regimes will evolve in response to the failure, partial failure, or fragmentation of these exclusionary mechanisms. The typical EAPR analysis of demand for property institutions is supplemented with a supply-side analysis of laws, agreements, and norms and the way in which their interaction may create conditions of open access. This allows Fitzpatrick to focus on institutional resilience in contexts far more complex than those analysed by EAPR and show that while a purely contractual coalition for resource governance and exclusion may tend towards instability as the gains from defection increase, “a norm-based system supported by kinship structures is more likely to respond to rising resource values by tightening its governance mechanisms or enhancing exclusionary rights through a process of collective consensus” (Fitzpatrick (2006: 1029)).

4. Concluding remark: taking care of complexity

As we have seen above the debate between EAPR proponents and their IAPR critics seemed to have been focused on the explanans, i.e., the definitions of the concepts that are applied in the course of explanation. Their nominalist argument gains strength from their implicit separation between their object of explanation (explanandum) from the IAPR one. Because of the apparent difference between these objects, the criticisms of the EAPR explanans made by IAPR proponents seem to miss the target. But this argument seems to beg the question of whether these object of explanation both being related to the institution of property are and can be separated in the sharp manner that EAPR argument presupposes.

From a meta-theoretic standpoint, we can say that in approaching object of explanation, and thereby determine the explanandum, EAPR tries to explain (1) the emergence and evolution of institutions, (2) the behaviour of economic actors in institutional environments and (3) the interaction between the two. With regards to (1), EAPR analyses how private property arrangements get established when value of the resources rises above the level of transaction costs. As to (2), EAPR considers how individual actors with utilitarian rationality in an environment of either not yet established or not fully enforced property rights behave and interact. Finally, EAPR explains how in this environment individual actors form private ordering arrangements and in this manner how the two levels interact.

Now the question that follows is whether IAPR explanations can be interpreted to tackle the same object. Taking into account the depiction of exemplary IAPR arguments, it seems obvious that they offer explanations on all three level. They tackle the issue (1) how

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20 De Soto’s (2000) explanations of reasons for failure of privatization is another common reference of IAPR’s authors. De Soto is particularly precise in showing that legal dimension of rule design is crucial and its effects are much greater than economists tend to realise. At the same time, it should be said that De Soto analyses one type of change in the way that social norms can be integrated into analysis of property and resilience.
different arrangements within a classification of property institutions (based on exclusion and transfer or on different entitlements) evolve towards more resilience, stability and growth, how they transform from one to another but also when and for what reasons these arrangements, fail and lead to instability, growth of externalities, and thus stagnation or even shrinking. Further they consider (2) how individual actors and groups interact confronted with issues legitimacy, morality and enforcement, related to the state authority in legal foundation institutions and adopted social norms in a not-only-utilitarian behavioural setting. Finally, they deal with the problem (3) how individual/group level and state level interact (in both ways) depending on mentioned conditions (legitimacy, morality and enforcement) towards arrangements that along the continuum between property (in rem) and contract (in personam) and finally how the conditions themselves change.

IAPR proponents build upon the distinctions (between possession and property and between in rem and in personam rights) explicitly present in property law. IAPR further introduces three important features absent from EAPR. First instead of looking at property as a monolith, a classification of property institutions is introduced. Second, issues of legitimacy, morality and enforcement (related to the state authority in legal foundation institutions and adopted social norms) in a non-utilitarian behavioural setting with groups (not only individual actors). Finally, IAPR depends on a precise distinction between different types of economic activities and resources involved that are an important determinant of the evolution of institutions in each case.

In many ways, tackling this same object of explanation allows IAPR to provide sophistication to explanations made by EAPR. It explains how actors interact in the shadow of law, but also in convergence and divergence between social norms and legal rules and how depending on legitimacy and morality, utility rationalisation is constrained. It explains how private property emerges but also when it does not, or when it evolves in to something else, and in general what type of property institution emerges. Finally, as law is not taken as external and fixed but subject to influence of groups that appreciate its’ legitimacy, IAPR explains how private ordering evolves but also how public ordering evolves and how the two interact.

This should suffice to conclude that IAPR justly criticises EAPR in a way that cannot be reduced semantic arguments. Hodgson’s arguments sometimes appear as if implying that IAPR criticism only focuses on explanans without getting into the explanandum of EAPR. The nominalist responses try to push the interpretation in that direction. I wanted to show in this paper that the opposite is the case: IAPR has the ability to sophisticate the type of explanations given by EAPR and integrate them with its own set of explanations precisely by widening the explanandum. As a consequence, its criticism of EAPR explanans necessitates redefinitions of key concepts used for explanation. In this manner, the findings of EAPR get to be connected to a set of different related phenomena resulting in an analytic framework that treats private and public ordering and individual, group and state level as parts of the same interface instead of separated issues. As we have seen, part of the work on redefinition has already been done by the IAPR proponents, but it should be clear that the bulk of it is yet to follow.
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