Property Is Only Another Name For Monopoly

by Eric A. Posner and E. Glen Weyl

ABSTRACT

The existing system of private property interferes with allocative efficiency by giving owners the power to hold out for excessive prices. We propose a remedy in the form of a tax on property, based on the value self-assessed by its owner at intervals, along with a requirement that the owner sell the property to any third party willing to pay a price equal to the self-assessed value. The tax rate would reflect a tradeoff between gains from allocative efficiency and losses to investment efficiency, likely in the range of 5 to 10 percent annually for most assets. We discuss the detailed design of this system from an economic and legal perspective.

INTRODUCTION

Property rights of all sorts—in real estate, in shares of corporations, and in radio spectrum, to take three diverse examples—give the owner a monopoly over a resource. It is conventional to think that this monopoly is benign. It gives the owner an incentive to invest in improving the property because she receives the entire payoff from its use or sale. This aligns social and private incentives for investment in property. This thinking plays a role in libertarian defenses of private property and in the influential work of legal economists deriving from the Coase Theorem (see, e.g., Epstein 1997).

However, the monopoly also creates a serious cost that is often overlooked. Because the owner has a monopoly, she will attempt to sell the property at a "monopoly price", one above the minimum she would be willing to accept for her asset and thus the price she would charge in a market where many individuals with similar valuations of substantially identical property to the owner compete to make a sale. Just like a normal monopolist, a property

owner sets a price that approximates what the seller thinks that the likely buyer's valuation or reservation price for the property is. Because some buyers will have a valuation that is lower than the announced price but higher than the seller's valuation, some efficient sales will be blocked or delayed.

This inhibits the allocation of property to its most valuable uses, a crucial component of a successful market economy. Macroeconomists have found that failure of assets to be reallocated to their most efficient uses is a major drag on aggregate productivity around the world.

When this problem is discussed, authors usually refer to it as the "holdout problem", most familiar in the context of development of real property and purchases of mineral rights and other natural resources, where projects can fail because sellers hold out for excessive prices. The problem also arises prominently in transactions over corporate assets, including corporate takeovers, where negotiations often get bogged down in discussions over the transaction price.

The Federal Communications Commission has spent the last seven years preparing an auction and property-redefinition procedure to deal with holdout problems that have inhibited the reallocation of spectrum to more efficient uses. In intellectual property, scholars have long understood that monopoly power granted to inventors through patent law interferes with allocative efficiency—exemplified by the "patent troll" controversy (Lemley & Shapiro 2007).

But the problem is much more general. In every transaction—home sales, sales of ordinary goods, and so on—private property creates bargaining problems that interfere with allocative efficiency. To put this problem starkly: allocative efficiency and thus an efficient market economy is impossible in the presence of private ownership.

This problem was first clearly articulated by the "marginal revolutionaries", Jevons (1871) and Walras (1896), who laid the foundation for modern formal economic analysis. They, together with George (1879), another prominent economist of the late 19th century, believed that the only solution to the monopoly problem was nationalization (through taxation) of many forms of property. Building on their arguments, the socialist economist Lerner (1944) advocated state ownership of property, together with a public "mechanism" that distributed possessory rights of property to users who valued them the most. In his Nobel prize-winning work, Vickrey (1961) (a follower of George) described how an auction could serve that function. Property is owned in common; the government would allocate temporary possessory and control interests in the property (effectively, leases) to the winners of an auction.

Because users would eventually be required to return property to the government, they could not hold out for a monopoly price, or indeed sell their property at all. The modern literature on mechanism design and related work in law and economics, which was initiated by Vickrey's contributions, have further refined our understanding of the monopoly problem with private property, and explored ways in which markets can be designed to mitigate it.

However, this literature has ignored the traditional concern with common ownership. As we noted at the outset, the benefit of the monopoly granted by private property rights is that it gives the owner an incentive to invest in the property to enhance its value. If the owner can charge whatever price she wants when she sells the property, she will be compensated for an investment that increases its value, because she can increase the price to reflect the increase in value added by her investment. If she cannot—if she must instead return the property to "society" (meaning, to government officials)—then she has weak incentives to invest in it. Probably for this reason, Vickrey's proposal has never been seriously considered by a government.

Instead, the governments of countries where modern market economies exist have addressed the tension between allocative efficiency and investment efficiency by adopting something like a "mixed regime" that consists of strong private property rights for most ordinary types of property and significant deviations in special cases. These deviations include liability rules in tort law for relatively indirect forms of property-rights violation; adverse possession of unused property; time-limited property rights (generally used for intellectual property, but also for a range of government-leased resources like grazing land); redefinition of property rights in the light of technological change (such as with the radio spectrum discussed above); public ownership in limited cases (e.g., roads); and various jury-rigged forms of government intervention like eminent domain for private uses (see discussion in Subsection 4.3 above). In all of these cases, the deviation from private property reduces the holdout problem and thus enhances allocative efficiency, while paying the price in the form of reduced incentives for private investment.

And yet there are serious problems with this mixed regime. First, it does not address the monopoly problem for a huge range of transactions—reallocating mineral rights .... months-long negotiations over house sales, corporate acquisitions that can drag on for years. In these cases, investment efficiency is maintained, but allocative efficiency is sacrificed.

Second, where the regime addresses allocative efficiency by deviating from private property, it relies heavily on bureaucratic or judicial valuations to ensure some level of compensation for the forced sale or transfer, or it denies compensation altogether. But the denial of compensation eliminates investment incentives, and imperfect government-supplied valuations and other forms of intervention interfere both with allocative efficiency and investment efficiency. While the deviations from private property may produce better outcomes for society than a system without such deviations, they fall far short of the social optimum. Our present system mixes elements of an extreme form of capitalism with the more naive forms of central planning.

Read the full article:
https://academic.oup.com/jla/article-abstract/9/1/51/3572441/Property-Is-Only-Another-Name-for-Monopoly