

# Property Rules & Liability Rules

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# Property Rules, Liability Rules and Inalienability: One View of the Cathedral

- Guido Calabresi & Douglas Melamed
- Integrated Approach
- For legal relationship, covered under property law, torts and crime

# Entitlement & Its Protection

## ➔ Issues faced by legal system

### Step 1 Problem of Entitlement – whom to entitle

- In conflicting interests which person or group to favour
- If entitlement is not certain result may be “Might is Right”

### Step 2 Manner in which entitlements are protected

- Property Rule, Liability Rule or Inalienability

# Property Rule

- Entitlement is treated as property
- To buy entitlement – by voluntary transaction
- Value agreed by the seller
- To sell it and decide value is Seller's decision  
i.e. Veto right
- No state intervention

# Liability Rule

- If someone destroy / damage entitlement, he will have to pay objectively decided value
- Value of entitlement is decided by some organ of State – value at which Holder would have sold it
- State intervention is required to determine value
- Applicable when voluntary transaction or ex-ante bargain is not possible

# Inalienability

- Initial entitlement is determined
- Forbid Sale – Transfer is not permitted even if seller and buyer are willing

# Mixed Application of Different Rules

- ▶ Land protected by Property Rule
- ▶ Exercise of Eminent Domain under Liability Rule
- ▶ “Drunken Owner” - Inalienability

# Reasons for Deciding Entitlement

To whom the entitlement should be provided

Reasons

1. Economic efficiency
2. Distributional preference
3. Other justice considerations



# Economic Efficiency

- ▶ Not only administrative efficiency
- ▶ Allocative efficiency also
  - ▶ Further change would not improve the condition of those who gained by it and could compensate who lost from it
  - ▶ Risky activities – likely to lead to lowest sum of accident cost and cost of avoiding accident

# Transaction Cost Aspects

- ➔ Zero Transaction Costs
- ➔ No difference between Property Rule or Liability Rule or Which Side had entitlement

# Transaction Cost Aspects

- High Transaction Cost
  - Cost of Market
  - Cost of Court
    - Property Rule preferred if Market Costs are lower than Costs of Court
    - Liability Rule preferred if Market Costs are higher than Costs of Court

# Four Combinations

- Entitlement
  - Right to polluter to pollute
  - Right to pollutee to clean air
- Means of Protection
  - Property Rule
  - Liability Rule