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Chandran KUKATHAS
Singapore Management University, kukathas@smu.edu.sg

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Does Capitalism Infringe Property Rights? A Reply to Peter Morriss

CHANDRAN KUKATHAS*
Linacre College, Oxford

In a research note on 'How Capitalism Infringes Property Rights' (*Political Studies*, XXXI (1983), pp. 656–61), Peter Morriss attempts to demonstrate that a Nozickian version of rights theory is incompatible with that account of capitalism which emphasizes the importance (and value) of entrepreneurial risk-taking and entrepreneurial failure. Because bankruptcy is an *accepted* consequence of entrepreneurial failure, capitalism, which *condones* bankruptcy, in fact condones the violations of the rights of creditors. Thus those who, like Nozick, defend property rights as sacred and inviolable, 'should be in the vanguard of capitalism's opponents' (p. 657) Since the rights-based argument for capitalism is that rights can *never* be legitimately violated, 'once the rights theorist admits that capitalism necessarily condones some violations of property rights—however little—he must either oppose capitalism or jettison his insistence on the inviolability of property rights. Or, of course, both.' (p. 661) While Morriss's interesting essay illuminates a number of issues involving capitalism and property rights, this reply argues that he is wrong on almost all counts. While rights violations may occur in capitalist societies, *capitalism* does not infringe property rights. The paper attempts to show this by identifying the weaknesses in Morriss's arguments to the contrary.

What is not clear in Morriss's argument is why a Nozickian rights theory is incompatible with capitalism. Morriss summarizes the Nozickian version of rights theory as follows:

> (1) It is impermissible to do anything to another's property except insofar as the owner of the property has explicitly contracted;
> (2) It is impermissible to break one's contract. (p. 657)

This, he argues, is incompatible with the 'idealized account of capitalism' which he provides on p. 656, which states:

> No injustice is involved if some would-be capitalists go bankrupt. They embarked—freely—on the risky business of enterprise, tempted by the great riches that could be made; *if they failed, whether through their own mis-calculations or through bad luck, no wrong has been done to them.* (emphasis added)

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Yet there is an injustice, argues Morriss, because the creditors of the bankrupts have had their rights violated. Of course this is perfectly correct. But why does this entail that *capitalism* infringes property rights or condones rights violations? It is not at all clear that capitalism must condone these rights violations; more particularly, it is not apparent that a rights based theory must condone bankruptcies. Indeed, some rights theorists, drawing on Nozick, have argued that bankruptcy law is an unjustifiable *intervention* in the operation of the market, one which shifts the costs of economic activity from entrepreneurs to creditors, and so introduces distortions in the capital market. Lawrence White, for example, argues that 'Bankruptcy law is a system of interventionary legislation which interferes with the ability of individuals freely to establish the terms of loan contracts. It benefits the less prudent and less scrupulous borrowers—indeed may encourage their conduct—while making their loans costlier for the honest and conscientious.'[1] For a rights theorist this view is not incompatible with the view that bankruptcy plays an important part in a free market.[2] In a free market the inefficient (and the unlucky) go out of business and capital will be shifted until it can be profitably invested. But this in no way implies that the entrepreneur is *entitled* to default on his payments to creditors should he become insolvent. What encourages him to go bankrupt is laws offering him the opportunity to *discharge the debt*. More precisely, it provides an opportunity for the extra-contractual dissolution of debts and, in so doing, reduces the incentives to internalize the arrangements concerning the burden of loss in the case of bankruptcy. In the unhampered market, of course, parties to any contract need not adopt a rule of strict liability. As White points out, loans could be made on the basis of a 'gentleman's agreement' with no repayment obligations should the debtor go bankrupt.[3] Or rules akin to bankruptcy laws could be contracted, with provision to employ arbitration to settle details of such cases. Quite possibly, although perhaps unlikely, the contracting parties could even agree to bind the debtor's future earnings in the event of bankruptcy. Morriss is quite right to say that neither 'history nor logic gives us any reason to hope that bankruptcy can be avoided solely through the good sense or virtue of the potential bankrupt.' (p. 657) But he is misleading when he suggests that '*In the absence of external regulation* he (the unsuccessful entrepreneur) could continue making contracts until he drifted into insolvency.' (p. 657—emphasis added) It is the *presence* rather than the *absence* of external regulation, in the form of laws favouring bankrupts, that has encouraged the unsuccessful and the unscrupulous to drift into insolvency.

Morriss's observations that 'an account of the legitimate transfer of rights cannot rely solely on the notion of sanctity of contract' (pp. 659–60) and that the legal background of rules for adjudicating disputes on the meanings of terms in the contract cannot be settled by contracting (p. 660) do *not* damage my argument. Any system, as he notes, must have a noncontractual basis (p. 660) and this background is 'crucial' and 'contentious' It is precisely this

[1] Lawrence H. White, 'Bankruptcy as an Economic Intervention', *Journal of Libertarian Studies*, I (1977), 281. See also Murray N. Rothbard, *The Ethics of Liberty* (Atlantic Highlands, NJ, Humanities Press, 1982), pp. 142–4.

[2] For an illuminating account of the importance of loss-making and enterprise failure see John Burton, *Picking Losers ? The political economy of industrial policy* (London, Institute of Economic Affairs, 1983).

[3] White, 'Bankruptcy as an Economic Intervention', pp. 283–4.

background that is in contention here. My contention is that bankruptcy law constitutes an unjustifiable intervention in the contract market—an intervention which favours debtors over creditors and encourages rights violations. This is not a characteristic of capitalism but is, rather, a paradigmatic example of interference with individual freedom under capitalism.

Morris is quite right, then, to observe that 'a concern for property rights and enforcement of contracts requires a very different set of laws' (p. 661) Unfortunately, this, for him, means a system different from capitalism, because capitalism 'requires a legal system which protects and encourages such enterprising and risk-taking entrepreneurs' (p. 661) But surely it does not. What it requires is laws which uphold private property rights; and among those rights will be the right to negotiate and contract for the distribution of risk, and the distribution of loss in the event of unsuccessful risk-taking. The importance of this right is reflected in the fact that risk-taking is an unavoidable enterprise. This is a point which Morriss fails to grasp when he writes: 'Under *laissez-faire* we are *forced* to gamble when we contract, whether we choose to or not. And it is safe to assume that we sometimes choose not to gamble. (p. 659) Indeed, he suggests that people often act to minimize risk—for example by insuring property against fire. Those who wanted to gamble, he suggests, would leave their houses uninsured, or put their money on the horses. But this is plainly false. Those who insure their property *are* taking a risk in attempting to minimize risk. They risk wasting their insurance money. For example, if I spend £10 insuring my house against fire I take the risk that, if there is no fire, that £10 will have been wasted (except insofar as it bought some peace of mind). Of course if I decide not to insure I risk losing more than £10. Here *laissez-faire* capitalism simply allows us the choice of which risk to take (and with whom). Under such a system, in which private property rights are upheld, we are forced to gamble when we contract only to the extent that contracting in any social system is a gamble because we cannot be *sure* that others will honour their contracts, no matter how strong the disincentives to violate them. Many legal systems seek to 'protect' us against risk by narrowing the range of options available to us when we gamble, but this simply forces us to gamble on the foresight (and the benevolence) of the person(s) limiting our options (risks). In some social systems, individuals are allowed almost no options and they do not so much gamble as become the passive subjects of chance.

While the rights theorists Morriss criticizes are strongly against the violation of rights, this does not at all mean that they fail to recognize that, in any social system, there will be some rights violations. For Morriss to suggest that rights theorists must be against any system in which there is a risk of rights violations (p. 658) is to go too far. Rights theorists do *not* want to *condone* rights violations but neither do they suggest that it is possible to have a social system in which no rights violations occur. (This would, among other things, commit rights theorists to the view that punishment is never permissible, since punishment risks violating the rights of the innocents who *might* be wrongly convicted. No rights theorist, to my knowledge, holds such a position.) While Morriss may have identified some problems in Nozick's particular account of property rights, he is not entitled to claim that these difficulties are inherent in rights-theory approaches generally. He is completely unjustified in taking the further step of claiming that *laissez-faire* capitalism infringes property rights.