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## An economic analysis of horizontal property

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### Abstract

Horizontal property is a common legal institution in many codified law countries that establishes property rights on apartment or office buildings among different owners. Applying a version of the Coase theorem, in this paper we analyze it as a solution to establish rights on assets that jointly yield services subject to individual and joint consumption (private and public goods). Under certain conditions, this institution seems to economize transaction and governance costs, especially in cases where the governance costs of a centralized condominium are relatively high and the number of economic agents involved (that is, the number of apartments of the building) is also high. © 2001 Elsevier Science Inc. All rights reserved.

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The term “horizontal property” (*propiedad horizontal*) refers to a set of property rights assigned on a certain apartment or office building in which there are portions that are individually owned and other portions that are collectively owned by the proprietors of the building. In this paper we apply economic analysis to explain the rationale of this institution and find a number of points that relate it to the theory of transaction cost economics and to the theory of public goods. Although horizontal property is common in many codified law countries, our examples will mostly rely on the Argentine Horizontal Property Act (Law No 13,512, from 1948).

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## 1. Origins and characteristics of horizontal property

Although some of its characteristics come from the ancient Roman law, the first written legal reference to horizontal property appears on the French Civil Code of 1804, known as the “Napoleon Code.” On its article 664, this code ruled about the case in which “.. different floors of a building belong to different owners” and established a number of imperfect rules concerning the duties of those owners regarding the improvements and maintenance of the building. Based on this article, commentators and jurisprudence began to elaborate legal theories about the nature of this sort of common property, and from then on many civil codes passed in different countries incorporated the concept in one way or another.<sup>1</sup>

The basic characteristic of horizontal property as it is commonly understood today is the mix between individual ownership and common ownership. Portions that are privately used (the apartments or offices themselves) are individually owned, but all common parts (ground, external walls, entrance halls, central heating systems, stairs, elevators, etc.) are subject to collective ownership by all the proprietors of the building. What owners possess in a horizontal property regime is a bundle of property rights that implies exclusive use of their apartments or offices and nonexclusive use of the common parts of the building, and these rights are perpetual and transferable. Exclusive and nonexclusive rights are nevertheless indivisible, in the sense that it is not possible to sell the rights on the individually owned portions without adjoining the rights on the collectively owned portions, or viceversa.

The particular nature of horizontal property has given rise to the interpretation that the object on which ownership rights are exercised is a combination of individual and common parts known as “functional unit” (*unidad funcional*). From a legal point of view, therefore, horizontal property is fundamentally different from the kind of ownership exercised by a cooperative partnership, that assigns apartments to its different members but retain all property rights on the head of a single owner (which is the partnership itself). It is also different from the concept of “communal ownership” or “condominium,” where all the owners own everything and exclusive use of certain parts of the building comes from a contractual arrangement.

In the institution of horizontal property, all the decisions concerning the common parts are taken by an entity known as “owners’ consortium” (*consorcio de propietarios*), which is the set of all the owners of the building. The way in which this consortium operates is established by a “regulation of co-ownership and administration” (*reglamento de copropiedad y administración*) and by general legal rules. Conversely, decisions concerning individually owned parts are taken by individual owners, although they are subject to a number of restrictions based on general property law rules and specific entitlements given to the owners’ consortium.

## 2. The Coase theorem and the provision of public goods

Based on an idea that originally appeared in Coase (1960), the Coase theorem is no doubt the most important principle used by the economic analysis of law to deal with issues of property right assignments. The Coase theorem is basically a statement of the efficiency of

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