A. The concept of adverse possession

The doctrine of adverse possession allows an occupier of a parcel of land who is not the true owner to acquire title to the land without consent from or compensation to the ‘true’ owner. This legal rule, firmly established in both civil and common law legal systems, specifies that after a certain period of time, termed the limitation or statutory period, not even the true owner of the property can bring action to eject an unauthorized possessor.

Adverse possession was formalized in English common law in 1632 in the Statute of Limitations. It fits within the framework of the general doctrine of limitations, which fixes the time within which parties must follow suit to bring an action. After a certain period of time a person, whether he had acquired the possession of property rightfully or wrongfully is to be protected from actions to recover possession of the property (Callahan, 1961). Under the Statutes of Limitation which were in force in England prior to 1833 the effect of remaining in possession for the prescribed period was to bar only the remedy of the person dispossessed, not his rights. His title remained intact. If he were to obtain possession of the land in a lawful manner his title would prevail against the possessor. Under the statutes that have been in force since 1833 the right as well as the remedy of the dispossessed owner is extinguished. The usucapio of Roman law, as adopted in civil law systems, represents what is often called acquisitive prescription in the sense that adverse possession conferred a positive title upon the occupier, who had remained in possession for a certain time.

Although the doctrine of adverse possession was adopted as a rule in all states of the United States, statutory rules and judicial interpretations vary across states (see Netter, Hersch and Manson, 1986). Similarly, differences in the implementation of adverse possession exist across countries around the world.

The remainder of this chapter will focus on the various economic explanations of adverse possession, the various conditions of adverse possession, the optimal length of the prescription period, and the distinction between good and bad faith possessors.
B. The economic foundations of adverse possession

Various economic explanations of the doctrine of adverse possession have been forwarded in the literature.

First, adverse possession is presumed to reduce evidence costs. With the passage of time, it is increasingly difficult to keep track of facts that occurred a long time ago. As a result, adverse possession serves the dual purpose of litigation and uncertainty costs. By limiting the amount of (more complex) cases that can be tried after a substantial amount of time has passed, adverse possession may reduce litigation costs in the long run. Also, by quieting old title claims, the doctrine of adverse possession reduces uncertainty to adverse possessors and third party purchasers. To the latter, adverse possession reduces the risks associated with title transfer (Baird and Jackson, 1984; Netter, Hersch and Manson, 1986). Search costs and verification costs are reduced as the potential purchaser is assured of the validity of the title presented. A potential purchaser who knows that the current possessor has occupied the property for the requisite statutory period is assured that the title he acquires is good. In this sense, adverse possession reduces transaction costs and uncertainty with regard to the title of the property concerned. On the other hand, adverse possession increases the costs of landowners who, with the possibility of losing title through adverse, will likely incur more monitoring costs over their land (Ellickson, 1986).

A second justification of adverse possession holds that the doctrine seeks to reward adverse possessors for making productive use of land. A related explanation focuses on the true owner, suggesting that adverse possession serves the purpose imposing a penalty on punishing dormant owners for sitting on their rights. In this sense, adverse possession promotes the productive use of property. Both the reward and penalty explanations of adverse possession presume that the original owner has failed to maximize the value of the property by not using it. A potential objection to this conception of adverse possession relates to the difficulty with assessing the most valuable use of the property. Often, the value maximizing use of certain property at a certain time might be to wait until one develops or uses the land.

Third, adverse possession can be regarded as an incentive mechanism to reduce both the occurrence and costs of boundary mistakes. Prior to the running of the prescription period, the possibility of ejection encourages adverse possessors to avoid boundary errors (the first-best solution). At the same time, the possibility of adverse possession maintains the incentives for true owners to mitigate errors in a timely fashion (the second best solution). Additionally, adverse possession reduces the ability of a true owner to extract rents from a possessor who has started
to rely on an error, for instance by improving the property or development (Miceli, 1997). Without a limitation period, a true owner would indefinitely be in a position to exercise his or her property rule protection in order to extract payments while the reliance costs of the adverse possessor increase over time with his or her investments in the property. Accordingly, by imposing a time-limited property rule, the doctrine of adverse possession provides owners incentives to correct errors in a timely manner and limits the ability to appropriate quasi-rent from adverse possessors that have relied in good faith on a boundary mistake (Miceli, 1997).

C. The requirements of adverse possession

For the rules of adverse possession to apply, a few interrelated conditions have to be met. The possessor must hold the property actually, exclusively, continuously, in open and notorious manner, and adversely to the owner, with a claim of right. The interpretation of these conditions has been the subject of debate and the interpretation differs between states (see Netter, Hersch and Manson, 1986). Generally, it is required that the possessor holds the possession exclusive from others for a period at least as long as the statutory period, without being dispossessed (continuously), in an open and visual manner that is inconsistent with the title of the owner (adverse) and without the owner’s permission (hostile). With the exception of variations in time periods and some minor differences the doctrine of adverse possession under common law does not differ much from that found in most civil law systems.

The above conditions comport quite naturally with the purposes of adverse possessions set out in the previous section. Especially the reward/punishment explanation of adverse possession seems to justify the legal requirements of adverse possession. For instance, if adverse possession is to punish land owners that fail to act and alert good faith possessors before the latter rely on the use of land that they do not own, it is within reasonable expectations that such duty is imposed only if the acts of adverse possession are reasonably visible (open and notorious) and provide sufficient signal to the outside world that the adverse use is premised on an ownership claim (exclusive possession, claim of right). Similarly, the protection of any reliance interest on behalf of the adverse possessor is warranted only if the possessor has made sufficient use of the property (continuous) in a manner that would traditionally be associated with ownership (exclusive, with claim of right). Similarly, the legal conditions of adverse possession fit well the purpose of reducing the occurrence and costs of boundary mistakes. The requirements that possession during the statutory period must be actual, open, notorious and exclusive ensure to the true owner
an opportunity to discover boundary errors prior to investment by the encroacher (Miceli and Sirmans, 1995b).

One notable difference between the rule of adverse possession within civil law and common law systems is the significance of the state of mind of the adverse possessor (‘does the adverse possessor realize that the property is not his/hers?’). In the United States there is a debate whether the intention of the possessor matters for the applicability of the adverse possession doctrine. The so-called Maine rule (mistaken possession is not found to be sufficiently hostile to the owner’s right) has generally been abandoned in favor of the newer Connecticut rule which emphasizes that the possessor’s state of mind is irrelevant. While this represents a formal legal shift from the favorable treatment of bad faith possessors – which is more in line with the punishment theory of adverse possession – to include also good faith possessors as potential benefactors of adverse possession – corresponding with the reward and incentive theories – judicial practice has traditionally favored good faith possessors, often by manipulating the application of the conditions to the facts so that good faith possessors may acquire ownership through adverse possession (Helmholz, 1983). By contrast, most civil law systems more explicitly distinguish between good and bad faith adverse possessors. Generally, prescription periods are longer for bad faith possessors than for good faith possessors.

Distinctions between good and bad faith possessors are difficult to justify from the perspective of the evidence costs-reducing justification of adverse possession. Good faith errors are difficult, often impossible, to distinguish from intentional errors, for instance with regard to real property issues such as boundary encroachments (Bouckaert and De Geest, 1998). Any attempt to prove bad faith might significantly increase high litigation costs, notably if the plaintiff must reverse the presumption of good faith against the defendant possessor. Also, the current, differing treatment of good and bad faith possession does not sit comfortably with the reward and punishment explanations of adverse possession. If the focus of adverse possession is on preventing good faith mistakes and preventing strategic behavior on behalf of the true owner, adverse possession can simply be limited to good faith possession. By contrast, the adverse possession suggest to reward productive use of property that is held by dormant land owners, especially bad faith possessors should be awarded for making productive use of resources, provided that sufficient notice is provided to landowners (see for example Fennell, 2006, suggesting bad faith oriented system of adverse possession).

On the other hand, there are economic arguments in favor of extending the prescription period of bad faith possessors. Prolonging the prescription period likely reduces the incidence of preying by squatters and the
Adverse possession consequences demoralization costs on behalf of surprised landowners that are faced with a completed adverse possession period (Ellickson, 1986). In this vein, Thomas Merrill has argued in favor of adjusting the rule of adverse possession to provide liability rule protection against bad faith possession (Merill, 1985). Such remedial shift, from property rule to liability rule protection, on behalf of a true owner at the end of the prescription period of a bad faith possession, reduces the incentives of a true owner to be vigilant, but likely reduces the lure of preying on behalf of bad faith adverse possessors (in this manner it has a similar effect as a lengthening of the prescription period, see below).

D. The Optimal Prescription Period
Adverse possession essentially involves the following efficiency trade-off between the adverse possessor and the true owner: a shorter statutory period reduces uncertainty as to the title in subsequent transfers, while a longer statutory period reduces the costs to property owners to protect their land from potential adverse possessors.

On the other hand, there are costs to the application of the adverse possession doctrine. With the risk of losing title, owners must monitor their land. When they are not using the property they need to be careful not to lose ownership to a possessor. By reducing the costs of mistakes of encroachments, adverse possession introduces a moral hazard problem, in the sense that there is less incentive to make sure mistakes are not made in the first place (Netter, 1998).

Figure 8.1 illustrates this trade-off. At point $e$, where the time of occupation (on the vertical X-axis) required to obtain title is set optimally, a balance is found between prevention and uncertainty costs. As the

\[ T_{\text{occupation}} \]

\[ t_{\text{opt}} \]

\[ \text{PC/MC} \]

\[ \text{UC} \]

\[ \text{Limitation period} \]
limitation period is set beyond point $e$, the uncertainty costs, represented by the UC curve, increase further. The longer the statutory period is set, the lower the monitoring costs of owners. If the limitation period is set below $e$, the prevention and monitoring costs, as represented by the PC/MC curve, increase while uncertainty costs reduce.

Economic theory holds that the greater the benefit from reducing uncertainty with regard to the ownership of a good, the shorter should be the time period required of adverse possession.

A fairly recent study of prescription statutes in the different North American states (Netter, Hersch and Manson, 1986) provides empirical evidence on the various differences and examines the determinants of the length of the occupation period in the statutes of limitations of states’ adverse possession at the time of statehood.

First, a negative relationship between property value in a state and statute length was observed. When the property has great value, there is simply a higher return to be obtained from ending potential disputes about ownership that arise from mistakes. Also, the costs of mistakes are higher when property value is high. In such circumstances it is recommendable that adverse possession requirements (length, type of possession) are less demanding. However, it should be acknowledged that if property values are high, owners have more to lose from adverse possession.

Secondly, a positive relationship between population density and statute length was found. As population density increases more property transfers take place, which raises the probability that errors (in determination of boundaries, identification of the title holder, registration, and so on) will occur. The length of the prescription period will affect incentives in various ways.

Protection costs will be lower when protection periods are relatively long. The shorter the prescription time period, the more theft or deceit is encouraged. Stolen, lost and fraudulently acquired goods will have a higher market price when potential buyers know that the possibility of claims and other repossession actions are restricted to only a limited period of time. Thus, the introduction of a prescription period will affect criminality and tortuous acquisition rates. The possibility of becoming a true owner through mere adverse possession increases the value of an adversely possessed good. A thief who wants to resell the stolen good will be able to charge a higher price to the buyer under a system where the latter can become the legally unchallenged owner after the elapse of a short period of time. As theft, fraudulent and deceptive acquisition will become more profitable, property owners will need to invest more into protection of the property.

Also, short prescription periods force owners of lost, stolen or
fraudulently divested goods to concentrate their search and repossession acts within a short period of time, which leads to higher opportunity costs of search (Bouckaert and De Geest, 1998). On the other hand, short prescription periods provide the possessor with efficient incentives with regard to investment decisions.

**Bibliography**


