The Political Coase Theorem and the Peaceful Domain Abolition of 1871 in Meiji Japan

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Abstract

This paper applies the Political Coase Theorem to explain why Japan's 1871 abolition of the feudal domains (*haihan chiken*) occurred peacefully despite the central government and local elites both being armed with a large hereditary warrior class. We argue that the Meiji government and the *daimyo* reached a Coasean bargain that exchanged local sovereignty for credible compensation. Facing mutual fiscal crises, both sides benefited from an agreement in which the state assumed domain debts and granted new nobility status (*kazoku* titles), stipends, and government offices as institutionalized side payments in exchange for sole ownership over tax collection. These arrangements transformed former rivals into stakeholders and made the new centralized regime self-enforcing. By embedding elite privileges within emerging political institutions, the Japanese case demonstrates how credible commitment can arise through elite status incorporation.

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1. Introduction

One of the most striking episodes of Japan's institutional transformation during the Meiji Restoration was the peaceful abolition of the domains (*haihan chiken*) in 1871. In less than two years, the Meiji state dismantled a centuries-old system of feudal governance by abolishing the fiscal autonomy of local elites and eliminating their claims to tax revenue. The local elites, the *daimyo*, willingly relinquished their fiefs and tax rights in exchange for pensions, nobility titles, and offices within the new imperial order. The peaceful nature of this transition suggests that the institutional change was mutually beneficial. If the *daimyo* had perceived the centralization process as purely extractive, they could have resisted militarily as they did only a few years earlier during the Boshin War (ca. 1868–1869). Instead, they accepted the Meiji state's terms, suggesting that both sides perceived credible gains from cooperation. The Political Coase Theorem provides a useful framework for understanding why the 1871 domain abolition proceeded without conflict. In particular, the Meiji central government's credible commitment to incorporate former domain elites into the new order through *kazoku* (nobility) status and government positions lowered transaction costs and allowed for a political bargain.

The Political Coase Theorem (PCT) extends the Coasean logic of bargaining to political settings. If transaction costs are sufficiently low and property rights are well-defined, then political actors will negotiate efficient institutional arrangements rather than resort to conflict regardless of the initial allocation of property rights. However, Acemoglu (2003) argues that high transaction costs, particularly the absence of credible commitment mechanisms, make PCT applications exceedingly rare.[1] Rulers often face a commitment problem: they must convince powerful local elites to surrender resources or authority in exchange for future benefits that the ruler could later renege on. If rulers provide a credible commitment to share the gains from cooperation, local elites prefer peaceful bargaining over conflict (Weingast, 1997;

[1] Galiani et al. (2014) provide experimental support for Acemoglu's claim that commitment problems undermine PCT applications.

Garfias, 2019; Leeson and Suarez, 2016). However, such cooperation requires institutional mechanisms that enforce credible commitments and constrain future opportunism. Recent work discusses how PCT can practically be applied (Munger, 2017; Robson, 2014; Balestri, 2016; Lai, 2024; Medema, 2020; Holcombe, 2018).

North and Weingast (1989) emphasize that credible commitments emerge from institutional constraints that limit state predation. The literature emphasizes democracy as one institutional framework to secure credible commitments from a ruler (Acemoglu and Robinson, 2006). Bates and Lien (1985) argue that representative institutions arise when rulers depend on elites with resources, incentivizing power-sharing. Meiji Japan's challenge was to consolidate power without provoking resistance from domain lords whose local authority rivaled that of the central government. The Charter Oath was promulgated in 1868, and its first article stated that "deliberative assemblies shall be widely established and all matters decided by public discussion."[2] This articulated goal of the Meiji government was cemented when it reorganized the nobility status in 1869. The creation of the *kazoku* peerage system in 1869 fused the aristocratic court nobility (*kuge*) with the feudal elite (*daimyo*). Crucially, *kazoku* status came with privileges: salaries, honors, access to high office in the central government. These privileges linked social prestige to political inclusion and decision-making, aligning elite interests with regime stability.

The Japanese case aligns with a successful application of the PCT but offers a distinctive mechanism through status incorporation. Rather than limiting rulers through representative assemblies or constitutional checks, the Meiji oligarchs limited themselves by granting former regional rulers a stake in the central government. Essentially, domain abolition reorganized the political property rights held by elites in Meiji Japan. Political property rights (Salter, 2015a,b; Piano and Salter, 2021; Salter and Young, 2023) describe the elites' rights to the revenues from governance. Political property rights determine an elite's *de facto* control over tax revenue, political decision-making, control over the military, etc. Domain abolition

[2] See What Was the Charter Oath and Why Does It Matter? — LegalClarity.

changed a *daimyo*'s political property rights by removing their fiscal autonomy and claim to tax revenue. These changes decrease the wealth of a *daimyo*, so resistance would seem to be a *daimyo*'s reaction to such a policy, yet that is not what happened in Meiji Japan. We contend that the Meiji government compensated the *daimyo*'s lost revenue through institutional side payments, particularly the *kazoku* system.

The *kazoku* system allowed the central government to internalize potential opposition by transforming rivals into collaborators. This system effectively lowered the expected cost of expropriation and raised the cost of rebellion. The Meiji oligarchs could credibly signal restraint because the continuation of *kazoku* privileges depended on regime stability and imperial favor, not coercion. Moreover, important *daimyo* were awarded high-level positions in the Meiji government, which allowed them to oversee other members of the central government and ensure that they honored their obligations made during the domain abolition.

Meiji Japan's case presents a situation of bargaining between two armed elite groups: the central government and the various domain rulers across the country. The Meiji oligarchs, though victorious in the civil war, faced the problem of consolidating power without reigniting rebellion. The *daimyo*, in turn, faced declining revenues, rising debt burdens, and eroding military strength. The declining fortunes of both the Meiji government and *daimyo* opened the possibility of mutually advantageous exchange. Under PCT reasoning, the Meiji state credibly committed to compensate local elites through privileges, ranks, and government inclusion. The new arrangement effectively transformed the *daimyo* from autonomous rulers into stakeholders in a unified polity. In this sense, the domain abolition was not a confiscation but a negotiated exchange: the *daimyo* traded fiscal sovereignty for status, security, and participation in the new government.

2. Historical Setting

The 1868 Meiji Restoration established a new central government, but the fundamental control over Japan's land, taxation, and military forces remained dispersed. This power was held *de facto* by approximately 260 autonomous *daimyo*, or feudal lords, in their respective *han*, or domains (Gordon, 2002; Ravina, 1999). The new Meiji state faced a critical state-building dilemma. It could not function without securing a monopoly on taxation and violence, but a forced expropriation of the *daimyo*'s authority would have ignited a second, catastrophic civil war. The nascent government, financially depleted by the recent Boshin War (the concluding war of the Meiji Restoration), viewed this as a prohibitively high-cost option (Beasley, 1989).

This situation was not, however, a simple stalemate. The *daimyo* themselves, as rulers of these *han*, were facing a parallel fiscal crisis, as their domains were economically unsustainable. The core liability was the requirement to pay hereditary stipends to a large samurai class. This was not a minor expense. At the domain level, this cost was so high that the domain of Chōshū, for example, had been forced to implement radical reforms in the 1840s, including cutting samurai stipends by as much as 50 percent, just to stave off "imminent financial collapse" (Craig, 1961). When the Meiji state inherited this system, the problem became national. In 1875, the total annual cost of these stipends was 18.78 million yen, consuming 32.8 percent of the entire national government's expenditure (Banno, 2010; Gordon, 2002). The total capitalized value of this liability was later calculated at 174 million yen, a sum equal to 37 percent of Japan's 1877 GDP (Morck and Nakamura, 2007, p. 560). This dual insolvency—the state's need for centralization and the *daimyo*'s need for a fiscal bailout—created the necessary conditions for a political bargain, as a negotiated "buyout" presented the lowest-cost solution for both actors.

To understand this dual insolvency, one must first understand the Tokugawa fiscal system. A domain's official wealth was its *kokudaka*, a formal assessment of its total economic productive

capacity, nominally measured in *koku*.[3] This *kokudaka* assessment served as the official tax base for the domain. From the revenue generated by this tax base, the *daimyo* had to pay all administrative costs, perform public works, and fund his military. The single largest and most rigid of these costs was the payment of samurai stipends (*chitsuroku*). Samurai were not independent actors but a salaried bureaucratic and military class, and their income was a hereditary right (Gordon, 2002; Drea, 2009). This meant a *daimyo* was legally obligated to pay a fixed, inherited stipend to thousands of retainers, regardless of their individual utility or the domain's actual fiscal health (Craig, 1961). This system created a massive, structural, and unserviceable liability.

The *Hansei Ichiran*[4] , an 1870 government survey, provides quantitative data to demonstrate this widespread crisis. To compare the relative fiscal burden across domains of different sizes, we use the metric of retainers per 1,000 *koku*. This ratio provides a standardized measure of a domain's fiscal distress by showing the density of its fixed, hereditary payroll against its economic base. A higher ratio indicates a more severe structural insolvency, as a larger portion of the domain's resources is obligated to stipends, leaving less for all other state functions. The data show this distress was severe and widespread. For instance, Kumamoto domain supported a very high density of 111.8 retainers per 1,000 *koku*. Even one of the wealthiest domains in terms of *koku* amount (just over 1.2 million), Kaga, carried a significant density of 55.9. The domains of Satsuma and Chōshū, who were at the head of the Meiji Restoration, had many more retainers to support. Satsuma supported an unsustainable density of 220.9 "samurai only" retainers[5] per 1,000 *koku*. The data also show Satsuma had almost no rice-based revenue (only 8,669 *koku* in inflows from what is now modern-day Okinawa) to pay this massive, fixed payroll, which helps explain its reliance on unorthodox cash-based monopolies (Gordon, 2002).

[3]A *koku* was a unit of volume, primarily for rice, that functioned as the basic unit of account for the entire feudal economy; it was used to assess the value of land and to pay for services.

[4]For more information on the *Hansei Ichirian*, see Beasley (1960)

[5]There also existed *ashigaru*, or foot soldiers, that we are excluding here due to not having a count of them for other domains and the difference in payment between them and samurai.

This largely national insolvency, as indicated by the retainer burdens domains faced, explains why elites of the nascent imperial government, like Okubo Toshimichi of Satsuma, were so motivated to orchestrate a national solution. The only apparent outlier, Chōshū, appears "leaner" (22.2 retainers per 1,000 *koku*), but this is only because, as historical texts show, it had already undergone financial reforms (Craig, 1961). This universal fiscal distress meant that for most *daimyo*, their political authority was no longer a valuable asset but a massive financial liability. This economic reality made them receptive to a bargain that would secure their personal wealth and status, aligning their private interests with the state's centralizing goals.

The primary agents of this centralization were not the *daimyo* themselves, but a small group of lower-ranking samurai who had become the *de facto* administrators of the most powerful domains. Men like Okubo Toshimichi of Satsuma and Kido Takayoshi of Chōshū had risen through their administrative and strategic skill, managing their domains' finances and military modernization for years before the Meiji Restoration (Craig, 1961; Ravina, 2003). Having successfully led the military coalition that won the Boshin War, they used this victory to form the new provisional government and appoint themselves and their allies to its key ministerial posts. Okubo became a dominant Imperial Councilor (*Sangi*), while Kido, also a Councilor, helped draft the new policies (Beasley, 1989).

This direct control of the central state apparatus gave them overwhelming bargaining power. Against other domains, they held two levers: first, they controlled the new Imperial Army, a modernized force that had already proven its superiority by *confiscating* the lands of a resisting northern coalition, and second, the credible economic *offer* of the 1871 buyout. Against their *own* domains, their power was more complex but just as strong. When a conservative *daimyo* like Shimazu Hisamitsu of the Satsuma domain opposed the abolition of the feudal domains, Okubo (his retainer) was no longer in a weak position (Ravina, 2003). Okubo held the superior bargaining hand. As an Imperial Minister, he could leverage the Emperor as the sole source of political authority, framing Hisamitsu's opposition as "treason"

and thereby isolating him from other potential allies. This move raised the price of resistance. Okubo's goal was not simply to save a failing domain, but to unite all domains under the new imperial state. Satsuma staved off a domain debt crisis in 1827 by establishing a highly profitable sugar monopoly and also repudiating their debts to merchants (Craig, 1957; Jansen, 2009). This success created a "financial base" that funded Satsuma's modern military and left it with cash reserves. This very solvency explains *why* Hisamitsu resisted; he had no *economic* incentive to accept a buyout from the nascent imperial state.

Okubo, deeply and centrally involved in the abolition, had to force the issue. To do this, he first lobbied another Satsuma elite and figurehead, Saigō Takamori, to create a ten-thousand-man Imperial Guard, securing a military force loyal to the state. Second, Okubo was appointed Minister of Finance, giving him control over the national fiscal reorganization. The *Hansei Ichiran* shows a massive 192,049-man feudal-era retainer class of Satsuma that, while currently funded by a precarious monopoly, was a political and military threat to centralization. The 1871 *haihan chiken*, where the state offered to assume all domainal debts and stipend liabilities, was thus an Imperial Edict. It was backed by Okubo's new military (the Imperial Guard) and political (the Emperor) power, which presented the buyout as the only rational, cost-effective alternative to certain political and military ruin for all *daimyo*, including the solvent and reluctant Hisamitsu.

This raises the critical question of how the new imperial state, which was also in a weak financial position after the Boshin War, could credibly afford this massive buyout. The government did not, in fact, pay these obligations with a large, immediate cash sum, which it did not possess. Instead, the buyout was a two-part financial reorganization. First, the state assumed the *han*'s existing debts, consolidating these liabilities under the new central government (Gordon, 2002). Second, it converted the hereditary stipends of both the *daimyo* and the samurai into new, interest-bearing government bonds, which were finalized with the 1876 *chitsuroku shobun* (Morck and Nakamura, 2007; Gordon, 2002). This meant the state's immediate problem was not paying the entire principal of the buyout (which totaled

174 million yen), but rather securing a stable annual revenue stream sufficient to service the *interest* on these new bonds and the assumed debts (Banno, 2010; Morck and Nakamura, 2007).

The Meiji leaders solved this problem by radically reforming the entire national tax system. The Land Tax Reform of 1873 (*chisō kaisei*) was the mechanism that created this revenue stream. This reform abolished the old, inconsistent, domain-level tax system based on rice *koku* and replaced it with a modern, uniform, national tax. It assessed the value of all land in Japan, and then imposed a fixed 3 percent tax in cash on that land value, payable directly to the central government by the private landowner (Gordon, 2002; Yamamura, 1986). This single reform, while politically difficult, was a massive success. It gave the Meiji state, for the first time in Japanese history, a predictable, stable, and enormous cash revenue stream, which is precisely what it used to honor the domain buyout and finance its modernization.

The 1871 *haihan chiken* thus completed the transfer of *de facto* power, but it simultaneously created the central puzzle of the Meiji settlement: the commitment problem. The *daimyo*, by surrendering their domains and armies and relocating to Tokyo, had relinquished all credible means of resistance (Gordon, 2002). Their financial futures, and indeed their entire social and political existence, now rested entirely on the new state's willingness to honor its expensive stipend and debt-assumption promises. The Meiji government, having successfully centralized power, now faced a significant incentive to default on these obligations. The annual stipend payments, as established, consumed nearly a third of the entire state budget (Banno, 2010; Gordon, 2002). Defaulting on these payments would free up enormous capital, which the oligarchs desperately needed for their primary goals of industrialization and military modernization to "stand with the nations of the world" (Ravina, 2017). The *daimyo* were now a disarmed, politically vulnerable class of creditors, concentrated in Tokyo where the state could monitor them. The core question, therefore, is *why* did the state not renege? What mechanism made the government's buyout offer a credible commitment, assuring the *daimyo* that the state would continue to pay once they were powerless to enforce the bargain?

The solution to this commitment problem was not financial but institutional. The primary mechanism, established in 1869, was the creation of the *kazoku*, or national peerage (Gordon, 2002). This new system merged the two highest-ranking pre-Restoration elites: the *kuge* (the ancient, non-martial court nobility based in Kyoto) and the *daimyo* (the feudal military lords) (Beasley, 1989). This was a critical act of political re-engineering. It dissolved the *daimyo*'s identity as semi-autonomous regional sovereigns and replaced it with a new, unified identity as a *national* aristocracy. Crucially, this new status was derived directly from the Emperor, the single source of legitimacy for the new government (Beasley, 1989). The state further "bundled" these interests by requiring the *daimyo* to relocate to Tokyo, a move that physically severed their local power bases and transformed them into a centralized, metropolitan elite (Gordon, 2002). Their wealth and status were now entirely dependent on the survival and stability of the Meiji state itself. This was a self-enforcing bargain: the oligarchs needed the *kazoku*'s collective prestige to legitimize their new state, and the *kazoku* needed the state to guarantee their new stipends and status. This institutional "status swap" was the first and most immediate signal that made the state's promise credible.

The Meiji government did not let this new "bundled" arrangement remain an informal understanding; it moved to give the *kazoku* a distinct and formal political function. In 1875, the state established the *Genrōin*, or "Senate of Elders," as a national deliberative assembly. Its membership was drawn almost exclusively from the new *kazoku* and high-level bureaucrats (Beasley, 1989). While the *Genrōin* was not a true legislature and lacked final decision-making power, its creation served as a crucial, tangible signal to the former *daimyo*. It demonstrated the government's intention to integrate them into the new central state apparatus, giving them a formal role and a national platform rather than just a pension. This was followed by the 1884 Peerage Ordinance, which was a far more significant step in making the 1871 bargain permanent. This ordinance, heavily influenced by European (particularly German) models, reorganized the *kazoku* into five hierarchical ranks: Prince, Marquess, Count, Viscount, and Baron (Beasley, 1989). This was not a cosmetic change. It was the

necessary legal and structural prerequisite for the *kazoku*'s planned role in the forthcoming constitution, transforming them from a class of state pensioners into a formal pillar of the new state's permanent institutional architecture. These later political developments in Meiji Japan further cemented the role the *kazoku* class played in governance. We focus on the initial *kazoku* allocations to understand how the *daimyo* were compensated for their forgone political property rights.

The 1889 Meiji Constitution, promulgated after years of deliberation, was the institution that made the 1871 bargain a permanent and credible commitment. The constitution established a bicameral legislature, the Imperial Diet, which was designed to share power between the executive and a new, limited representative body (Beckmann, 1957). Its upper chamber, the House of Peers, was the key institution that finalized and secured the *daimyo* bargain. This house was not fully elected but was composed primarily of the *kazoku*, thereby institutionalizing their new role as a pillar of the state. The provisions were explicit. The higher ranks of the *kazoku* (Prince and Marquess)—ranks reserved for the most powerful former *daimyo* and court nobles—were granted automatic, hereditary seats in the legislature. The lower three ranks (Count, Viscount, and Baron) elected representatives from among their own orders to sit in the house (Beckmann, 1957). This arrangement made it constitutionally impossible for the Meiji state to default on the *daimyo*'s status or stipends without simultaneously destroying its own legislature. The *daimyo*'s political power and economic security were no longer secured by their private armies, but by constitutional law and *ex officio* membership in the government. Their interests and the state's interests were now inextricably and credibly bundled, making the 1871 bargain self-enforcing.

3. Theoretical Framework

3.1 Political Property Rights and the Structure of Elite Bargaining

This paper applies the Political Coase Theorem to explain peaceful domain abolition by modeling the 1871 domain abolition as a bargain over political property rights between two elite groups: the central government and the regional domain rulers (the *daimyo*). We follow the constitutional political economy literature (cf. Salter, 2015a,b; Piano and Salter, 2021; Salter and Young, 2023) in defining a political property right as a legal or customary entitlement that grants its holder a share of decision-making power in governance and specifies the costs and benefits that those decisions accrue.

In the previous political order, each *daimyo* held political property rights over territorial governance, including the authority to tax domain lands, command retainer forces, and make decisions on local policy. These rights had observable, measurable value in the tax flows from the domain, the control services provided by samurai, and the prestige and autonomy that came with regional authority. We conceptualize a *daimyo*'s bargaining power as the net present value of the political property rights he possessed. A *daimyo* with a large and productive fief, a large retainer army, and strong political legitimacy (from supporting the Meiji Restoration) held higher-valued political property rights and thus greater bargaining power. Conversely, a *daimyo* with a small fief, heavy pre-existing debt obligations, or compromised political standing held lower-valued rights and thus a weaker bargaining position.

The core problem Meiji Japan faced was achieving efficient allocation of these property rights. The central government desired monopoly control over taxation and the military, which required removing some of the *daimyo*'s political property rights, but could not afford to acquire them through open confiscation without triggering costly resistance. The *daimyo* held assets that had become economically unsustainable but remained politically valuable, for "the government's efforts to streamline the taxation systems has always been hindered by the

domains' retention of, as part of their fiefs, villages in geographically remote areas" (Umegaki, 1988, p. 101). Both sides thus faced incentives to bargain, where the central government would absorb the *daimyo*'s territorial governance rights in exchange for offering new political property rights through status, stipends, and access to national office, whose value depended upon continued participation in the new centralized order.

Silberman (1964) documents that *han* finances had been in secular decline since at least 1750, with domain debts "rising consistently" and reform attempts repeatedly failing to reverse the trajectory (p. 26). Umegaki (1988) shows that domains absorbed costs as the price of demonstrating loyalty to the new Imperial order during the Boshin War, directly accelerating the depletion of treasuries that were already structurally insolvent (p. 79). When the central government offered to absorb domain debts and capitalize future *daimyo* incomes into government bonds, it was offering an exit from a position that had already become a net liability (Tsurutani, 1973, p. 208). The result was that the political rights enshrined in the domain system had become economically costly to hold even as they retained considerable political value. The central government valued these political property rights and encouraged political bargains that rearranged them, and the diminishing economic value made the domain lords receptive to such bargains.

This is a Coasean bargain in the sense of the Political Coase Theorem because both parties benefit from a reallocation of political property rights, and the critical obstacle is not the absence of gains from trade but in ensuring credible commitment. How could the *daimyo* trust that the central government would honor promises of stipends and status once they had surrendered their armies and moved to Tokyo? How could the central government credibly promise not to expropriate these former elites later when fiscal pressure mounted? Without institutional mechanisms to solve these mutual commitment problems, rational actors would defect, making peaceful bargaining implausible.

3.2 Institutional Solution: Bargaining Power through *Kazoku*

Historians have more recently (Ravina, 1999; Beasley, 1972; Jansen, 2000) described the Meiji Restoration as the result of an elite coalition rather than a revolution from below. The domain abolition, in particular, was a bargain among elites. Our approach builds on this by formalizing the logic of that bargain through the PCT. The *daimyo*'s willingness to cooperate depended on their bargaining power, which derived from measurable fief characteristics and political alignments. Thus, *daimyo* with more bargaining power held more valuable political property rights, requiring more compensation from the Meiji government to ensure a peaceful transition.

Institutions create credible commitment devices when they lower elite coordination costs and raise the cost of ruler default (Garfias, 2019). The Meiji state's solution was to institutionalize the side payments offered to the *daimyo* by transforming informal promises into durable, rule-based entitlements that were costly to revoke. The creation of the *kazoku* peerage in 1869 performed two critical functions. First, it priced out the *daimyo*'s loss of political property rights by converting them into a new, hierarchically differentiated status system embedded in the emerging political order. Rather than offering ad hoc financial compensation, the central government offered access to national decision-making power through *kazoku* rank, stipends benchmarked to former domain wealth, and guaranteed or preferential access to governance positions. Crucially, the rank allocated to each *daimyo* reflects the present value of the political property rights he surrendered. A *daimyo* holding territory with large *kokudaka*, commanding many samurai, and enjoying strong political legitimacy transferred more valuable rights and thus should have received compensation reflecting that higher value: higher *kazoku* rank, larger stipends, and more prominent office. Conversely, a *daimyo* whose domain was indebted, militarily weak, or politically tainted transferred less valuable property rights and thus received lower-ranked titles and smaller compensatory packages.

Second, embedding these transfers in a formal, legally recognized institution increased the

cost of reneging. Dismantling the *kazoku* system or reneging on stipend payments would require dismantling visible, hereditary status structures and undermine the very legitimacy institutions that the Meiji oligarchs had invested heavily in constructing. Institutionalizing side payments raised the costs of reneging above the costs of continued compliance. A promise to maintain the *kazoku* system became self-enforcing not because rulers were inherently honest but because violating it would be institutionally and politically costly.

The framework predicts that *kazoku* rank allocation correlates with observable measures of bargaining power. We identify four primary dimensions along which a *daimyo*'s bargaining power varied: (1) fief size and productivity, (2) military capacity proxied by samurai retainers, (3) debt burden of the domain, and (4) political alignment during the Boshin War. Combining these dimensions into a single measure of bargaining power, we expect the distribution of *kazoku* ranks to reflect a separating equilibrium in which the central government's rank allocation reveals its beliefs about each *daimyo*'s bargaining power. In such an equilibrium, the highest-power *daimyo* receive the highest ranks and most prestigious offices, not out of deference but because offering them inferior compensation would have made their resistance rational, making the entire settlement unstable.

The sequencing of the *kazoku*'s creation was itself a credible signal of the government's intent. Establishing the peerage in 1869—two years before the formal abolition of domains in 1871—served as a costly signal (Spence, 1973) that separated the Meiji government's type: a government genuinely committed to power-sharing would incur the costs of institutionalizing side payments in advance, while a predatory government would not. The *daimyo*, observing this costly move, could rationally update their beliefs about the government's true intent, lowering their reservation value for accepting the bargain. A government intent purely on predatory conquest would have had little reason to establish a hereditary peerage before consolidating coercive power; the institutional machinery of the *kazoku*, once in place, constrained the ruler's future options and made reneging politically visible and costly.

The credibility of this signal depended critically on the institutional language through which the *kazoku* promise was communicated. Silberman (1964, 1966) and Takane (1981) establish that in the Tokugawa period, status and political power were not merely correlated but structurally fused. Silberman demonstrates that elite status was "determined primarily by birth" and that "positions in the Bakufu and *han* governments were limited almost entirely to those born in the elite strata" (Silberman, 1964, p. 49), while Takane's quantitative index confirms that "feudal status was the only statistically identifiable factor influencing promotion to high political status" before the Restoration (Takane, 1981, p. 156). In the Tokugawa order, a high-status ranking was not merely honorific; it was the principal mechanism through which access to political power was allocated. By constituting the new peerage on terms that mapped directly onto the familiar *koku*-based revenue hierarchy, the Meiji government communicated its commitments in an institutional form the domain lords already understood and trusted (Lebra, 1993, p. 53). This institutional legibility was validated in practice: Takane finds that 78 percent of those with high pre-Meiji status retained high political positions in the new government (Takane, 1981, p. 30), and Silberman finds that the traditional upper elite continued to "consider themselves the allocators of power after 1868" (Silberman, 1964, pp. 110–111). The *kazoku* system was credible precisely because, in the short run, it accurately described political reality.

Once the *kazoku* system was created and the domains formally abolished, the interaction between the central government and *daimyo* entered an infinite-horizon repeated setting. Each year, the state collected taxes, paid stipends, and appointed offices; each year, the *kazoku* continued to support the regime through legislative participation, political legitimacy, and acquiescence to centralized authority. The 1884 Peerage Ordinance and 1889 Meiji Constitution institutionalized this repeated interaction by embedding *kazoku* privileges directly in the structure of national government: higher ranks received automatic hereditary seats in the House of Peers; lower ranks elected representatives. This constitutional entrenchment extended the effective horizon of the game to infinity, making punishment threats credible

and salient. The requirement that *kazoku* reside in Tokyo further reduced monitoring costs: concentrated in the capital, former lords could observe government compliance with stipend payments, coordinate political responses, and maintain the dense social interaction that sustained reputational mechanisms. In repeated-games terms, Tokyo residence enabled the private observation and communication sufficient for cooperation via tit-for-tat strategies, so long as the state honored its obligations, the *kazoku* remained loyal; if the state attempted default, the *kazoku* could coordinate collective defection by allying with rival factions within the central government.

What sustained the credibility of these commitments within the central government itself was the structure of factional rivalry among the Restoration oligarchs. Historians of early Meiji have tended to read the Finance Department disputes, the constant reshuffling of personnel, and the "backstage negotiations" over appointments as evidence of institutional deficiency (Umegaki, 1988). From a political economy standpoint, however, the same evidence is better interpreted as a system of competing veto players that structurally prevented any single faction from reneging on the *kazoku* bargain. Umegaki's account of how officials "could derive support from their domains, from other powerful figures within the government, and even from powerful figures within the foreign diplomatic corps" (Umegaki, 1988, p. 118) describes not dysfunction but the operation of factions each capable of punishing defection by rivals. The "constant process of conflict and forced accommodation" Breen (1996, p. 419) documents functioned as a structural guarantee against unilateral expropriation: any faction that reneged on stipend promises or stripped *kazoku* of their offices would hand a coalition-building weapon to its rivals, who could mobilize the aggrieved lords against them. The shifting coalitions that frustrated contemporaries were the mechanism by which the *kazoku* bargain remained self-enforcing in the absence of formal constitutional constraints—a function that the 1889 Constitution would eventually institutionalize permanently. Incorporation into the factional system gave former domain lords a stake in the bargaining game itself, making defection from the new order less attractive than continued participation (Silberman, 1964, p. 91).

4. Conclusion

The peaceful abolition of Japan's domains was not merely an episode of elite compliance but a Coasean bargain between the Meiji state and the *daimyo*. Although this paper has framed domain abolition as arising as a rational bargain between two elite groups. Reality is obviously messier than that. However, by analyzing this period through a PCT framework, we begin to understand how gains from trade arise in the first place between two armed elite groups and how this mutually beneficial trade was expected to happen. Both the Meiji government and the domain lords faced fiscal crises, which lowered the economic value of their political property rights. This helped avoid a transitional gains trap as both sides stood to gain from a reallocation of these political property rights. However, a credible commitment is still necessary to ensure that a beneficial trade actually occurs.

Through the credible promise of political incorporation and status preservation, the central government overcame the commitment problem that typically undermines applications of the Political Coase Theorem. The *kazoku* peerage system was the institutional mechanism that made this credible. By lowering transaction costs and aligning the interests of former regional rulers with the new central state, Meiji Japan achieved what most polities in transition fail to do: a rapid, peaceful, and mutually beneficial consolidation of political power. This paper provides an historical example of a successful application of the Political Coase theorem, proving that credible commitment problems can be resolved so long as the gains from trade are large. Hopefully, by analzying Meiji Japan, one of the most striking episodes of political and economic development, further research can understand the institutional mechanisms that help foster political and economic development.

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