

Private Compulsory Acquisition and the Public Interest Requirement

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1. INTRODUCTION

A strong connection exists between, on the one hand, land use in an area and, on the other hand, the structure of ownership and properties. Because land use is constantly changing in a dynamic society, the structure of ownership and properties also has to be adapted to new conditions.

Adjustments of ownership, rights and property division can often be achieved on a voluntary basis. In other words, properties and rights can be transferred through market transactions. But property owners can also be made, subject to certain conditions, to relinquish land and property rights against their own wishes. One basic precondition of this kind for compelling a property owner to surrender his property or accept restrictions on his use of the land is that the compulsory acquisition must be for a purpose which is in the *public interest*.

Some decades the question of *public interests* presented less of a problem in many countries. Expropriation, for the most part, was carried out by "the public", meaning national or local government, and the involvement of public interests did not, normally, need to be challenged. It went more or less without saying that when public authorities had to acquire land, this was a matter of public interest.

A more complicated scene has evolved, however, during the past twenty years or so, due to the privatisation of traditionally public undertakings. For example, former State Bodies for telecommunications, with a monopoly of telecommunication services, has now become limited companies operating for profit. Private consortia are developing new generations of mobile telephony.

Given this transfer of formerly public tasks to the private sector – and the need of land for different purposes – the question of private compulsory acquisition demands consideration. This being so, how is the "public interest" requirement to be met in order for compulsory acquisition to be possible? That is the question which this essay attempts to shed light on.¹

2. A LEGAL FOUNDATION OF COMPULSORY ACQUISITION

Forcing someone to surrender land against their will is of course a powerful incursion on the individual right of ownership. Accordingly, there have to be very good reasons for building up legislation sanctioning this kind of coercion. In the European Convention one fundamental legal prerequisite is that compulsory acquisition may only be prompted by purposes which are in the *public interest*.²

¹ The paper is based on an article published in *Social Strategies*, Vol. 38. 2004.

² Or more correctly, the European Convention for the Protection Human Rights and Fundamental Freedoms, Protocol March 20th 1952, Article 1.

Every natural or legal person is entitled to the peaceful enjoyment of his possessions. No one shall be deprived of his possessions except in the public interest and subject to the conditions provided for by law and by general principles of international law.

However, the European Convention does not specify more exactly *who* is entitled to acquire property by compulsory purchase. The same goes for the amount of *compensation* payable.

3. THE PUBLIC INTEREST – JUSTIFICATIONS FOR COMPULSORY ACQUISITION?

Changes of land use, property subdivision, ownership and rights can often be achieved by voluntary agreement, based on negotiations between buyer and seller. But, as we have now seen, property owners can be forced to surrender property and rights against their wishes. Thus it is legally possible for a buyer to acquire properties/rights at a *lower price* than would probably have resulted from free negotiations with the seller. Fundamentally, then, the coercive rules are related to the amount of *compensation* to be paid.

This price regulation, then, presupposes the existence of a public interest, the more detailed implications of which have been defined through legislation and case law in different countries. The question has also been discussed, however, in the academic discipline commonly termed “law and economics”.³ We shall now turn to consider the main outlines of that discussion.

The siting of many facilities – roads, railways and utilities, for example – is often more or less confined to certain places. In other words, *certain specified areas of land* are needed for the purpose, and so the buyer cannot approach any property owner whatsoever with a view to acquiring the necessary land on the open market. The seller, accordingly, has a *monopoly status* in relation to the buyer.

If, then, compulsory purchase were not possible, these measures could be prevented by the owner refusing to part with his land. The owner of strategically situated land could frustrate measures which are desirable from a community viewpoint. In other words, the owner could *veto* the implementation of a planned use of the land. One argument in favour of compulsory purchase legislation, then, is that it prevents the individual property owner from acquiring such power.

In the situation described above, it is also conceivable that the property owner is not prepared to go to the extent of refusing to sell on any account. But in order to agree to a sale, the owner, conscious of occupying a monopolistic situation, demands a very high, “unreasonable”, price. A second argument in favour of legislation, then, is that it prevents a property owner from obtaining monopolistic profits by owning land which happens to occupy a strategic position.⁴

³ Se e.g. Werin (1978) och Miceli & Segerson (1999).

⁴ In the terminology of law and economics, this is commonly referred to as the *hold-out* problem, in the sense of the seller being able to “hold out” for a higher price in his negotiations with the buyer.

The monopoly situation in which the seller thus finds himself is liable, furthermore, to entail protracted negotiations etc., i.e. completion of the purchase may entail high *transaction costs*. To appreciate this point, we need only imagine a negotiating procedure connected with the construction of a motorway or railway

So the main reason for sanctioning compulsory purchase is the buyer's need of certain specified areas of land, and the concomitant risk of his having to pay a higher price than he would if there were more potential sellers, and also of the cost of negotiations being unnecessarily high.

The buyer's need of a certain particular area of land is commonly regarded as a necessary precondition for the justifiability of compulsory purchase, but it is not the sole precondition. The purpose of the acquisition has to be rated, generally speaking, "important". If, for example, I wish to add a few square metres of my neighbour's property to my front lawn, this definitely requires a particular area of land, but the requirement will not justify compulsory purchase, because my front lawn can hardly be termed an important purpose. In order for a purpose to be important from a public point of view, the benefits of the purpose/acquisition have to be significant to a larger group of people, as is normally the case, for example, with common facilities like roads, utilities and green spaces.⁵

Finally, in order to legitimate compulsory acquisition, the purpose with the purchase have to be "profitable" in the view of society, i.e. the value of the new land-uses must exceed the value of the existing use.

However, these three criteria say nothing about the *form* of activity (public authority, private limited company etc.) conducted by the purchasing party. It is the *activity* itself and the *purpose* of the acquisition that matter.

This problem can be instanced with a topical activity in Sweden, namely the development of the 3G (Third Generation) mobile telephony network, which poses the issue of compulsory purchase.

In December 2000 the National Post and Telecom Agency, PTS, decided to award UMTS licences to four private enterprises: Europolitan, HI3G, Orange and Tele2. All four applicants made commitments for coverage of at least 99.98 per cent of the population of Sweden as early as the end of year 2003. This would mean the erection of large numbers of masts throughout the country, an undertaking for which, one way or another, the four companies would have to obtain the necessary rights.

Opinions may differ among the general public concerning the usefulness of being able to communicate speech and data by mobile telephone, but most people would probably agree on the whole that this is an "important" activity and "profitable" from a societal point of view. Thus two preconditions for compulsory purchase for the purpose of erecting mobile telephony masts are satisfied.

On the other hand it is a debatable point whether the masts really have to be sited in certain

traversing a large number of properties. In cases of this kind, the negotiating costs could well be prohibitive.

In certain respects, a property owner's compensation demands also may be deemed "excessive", even if the asking price is not based on the owner being in a monopolistic position. To rectify this situation, the law may prescribe a rate of compensation below the price which the buyer would have had to pay in an entirely voluntary transaction. In other words, the law seeks to favour the buyer, e.g. for equity reasons. Thus another purpose of compulsory purchase legislation is that of *reallocating* wealth from seller to the buyer.

⁵ See e.g. Epstein (1985).

particular areas of land. If the number of masts involved is limited, the answer will clearly be negative, because then there would be many alternative locations for these few masts. Such a situation of choice cannot justify the right to acquire land (or acquire the right to erect a mast) by compulsory purchase from one landowner.

In actual fact, however, we are talking about a continuous system of many masts, not just a few, and the argument goes that, once the siting of one mast has been determined, this will affect the siting of other masts as well (see figure 1). And so, for the construction of whole system, each individual mast will in practice have to be sited within a limited area (offering suitable access, topography etc.). In this case all public interest requirements would be fulfilled.

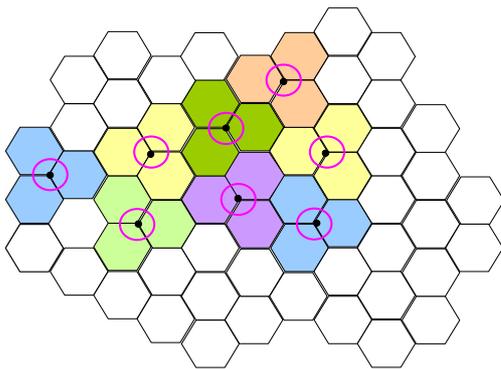


Figure 1 Radio planning and placement of radio base stations. (Source: NCC Sverige AB, 2002).

4. THE LEVEL OF COMPENSATION?

If compulsory purchase is to be allowed, then from a strictly legal point of view it has of course to be determined whether or not the purpose of the acquisition is in the public interest. There are no two ways about this: the answer has to be either Yes or No. On closer inspection, though, the problem is less straightforward. There are degrees of strength, even where public interest is concerned, which leads Epstein (1985), for example, to argue that the degree of public interest can have a bearing on the amount of *compensation* which should be paid. That is to say, the lower the degree of public interest, the higher the compensation. This question will be dealt with in the section which now follows.

As a starting point we can ask ourselves; what will the price be if a property is sold voluntarily?

4.1 The Price in Voluntary Transactions?

In voluntary transactions the following observations can be made:

In order for the sale of a property to materialise in the first place, buyer and seller must value the property differently. In order for the seller to be prepared to part with the property, the buyer must pay a price at least equalling the value put on it by the seller. At the same time, of course, the buyer is not prepared to pay more than the value which he himself puts on the property. In other words, there must be an agreement on price between the values put on the property by seller and buyer.

- The *profit* resulting from a voluntary sale can be seen as the difference between the values put on the property by the buyer and seller. If the price comes close to the seller's valuation, the buyer will have a bigger share of the profit. Conversely, the closer the price comes to the buyer's valuation, i.e. the higher the price, the greater the seller's share of the profit will be (see Figure 2).

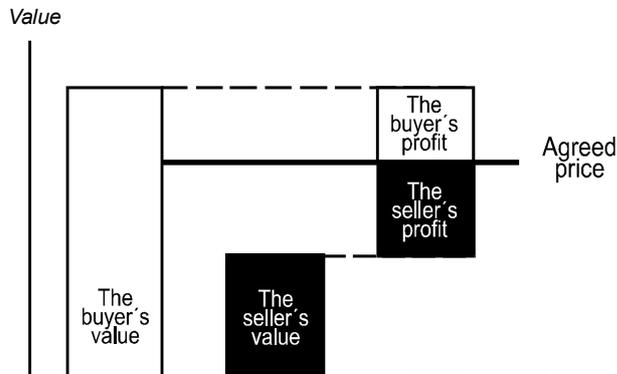


Figure 2 Profit-sharing and voluntary transactions (Source: Kalbro and Sjödin, 1993).

The same argument can also be applied to parts of a property which are transferred to another property (or to an easement created in one property in favour of another). In order for a voluntary transfer to take place, the land must be differently valued by the parties respectively acquiring and parting with the land. And the price must come somewhere in between those two values.

This is a theoretical argument. The question is how the price is determined and how the profit is apportioned in actual practice. Here it has to be admitted that our knowledge of price formation in different situations is limited, i.e. there is great uncertainty regarding the appropriate level of payment. Some light has been shed on this problem by Kalbro and Lind (2007) in bargaining experiments. The experiments indicate an interesting combination of ethical principles and self-interest. The participants tended to argue in terms of principles of fairness, but they chose the principles that furthered their own interest.

4.2 Compensation for Compulsory Acquisition

The basic idea behind the rules of compensation is, in many countries, for the property owner forced to surrender land, to be in the same economic position as if the compulsory purchase had never happened. The property owner shall be compensated for the damage he suffers, and in this sense compensation can be said to be based on a principle of indemnification.

The main rule for the compensation, is normally, to correspond to the *market value* of the property, i.e. the price which it would fetch in the open market.⁶ When only part of the

⁶ Definition of the „market value” is not without its problems, but space will not allow us to consider this any further. Nor will space permit us to describe valuation methods which can be used for estimating market value in different situations. See instead Norell (2007)

If compensation with the loss of market value does not fully cover the economic injury to the property owner, compensation can also be paid for “other damages”. Compensation for such damages may come into question, for example, when a property owner has to move house or close down a business conducted on the property.

property is affected by compulsory purchase, the compensation must equal the *loss* of market value which the compulsory purchase entails.

Besides the principle of compensation based on the damage of the seller's property, some countries⁷, apply more generous compensation principles in some cases when private compulsory acquisition is at hand.

In these cases seller/conveyor is to be compensated for, at least, the reduction of market value. But in addition, when fixing the compensation, "reasonable allowance" shall also be made for the value of the land to the buyer. In other words, the compensation paid to the seller must correspond to compensation for the injury and to *a share of the profit* which the measure implies. This rule of compensation, then, is more favourable to the seller, the reason being that in private compulsory purchase it has not been considered fair to favour the buyer in the same way as happens under "normal" expropriation by public bodies.

The difference between the compensation principles can be illustrated in the figure below.

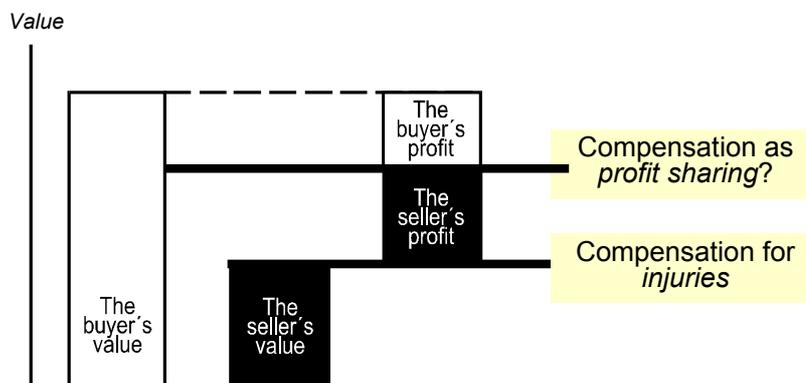


Figure 3 Two different compensation principles.

In connection with the issue of private compulsory acquisition Epstein (1985) argues roughly as follows. If the profit from a compulsory acquisition accrues to many parties, i.e. if the purpose of the acquisition is to cater to a need on the part of many people, it can be reasonable for the profit to accrue to the acquirer. This means that the person surrendering land shall only be compensated for the damage occurring. This could be instanced with the land acquisitions which have to be made for the construction of state-funded public highways. If on the other hand the profit concerns a very limited group, it ought reasonably to be shared between them. This could be instanced with a boundary adjustment between two properties in order to achieve better property subdivision.

Thus, different levels of compensation may be needed, depending on the situation. In practice, though, the crunch issue is when compensation must indemnify the property owner for the damage occurring and in what situations profit-sharing is called for. One argument propounded, in the light of Swedish example presented above, is that profit-sharing must

⁷ E.g. Sweden and Finland.

accompany expropriation for a purpose involving commercial profitability requirements. This applies, for example, to the acquisitions made by private, commercial undertakings responsible for developing mobile telephone networks.

5. CONCLUDING COMMENTS

The changes occurring in many countries during the past decade or so have entailed the transfer of traditionally public responsibility for public utilities to private, sometimes profit-based undertakings. This highlights a number of important questions. Are these undertakings to have the same powers of compulsory land purchase as public authorities? If so, there is cause to consider whether the compensation paid to the party surrendering land should be more generous if the expropriating body is a private business undertaking operating for profit.

Where the first of these questions is concerned, I have in this paper discussed the fundamental precondition of compulsory acquisition, namely the existence of a “public interest”. The definition of public interest in connection with compulsory purchase can be summed up in two criteria, both of which have to be satisfied:

- The purpose of the acquisition must be “important” and “profitable”.
- The acquirer must need a certain specific area of land (and accordingly not be in a position to approach any property owner whatsoever in the free market).

With this way of looking at things, the prime concern is not *who* acquires the land. The criteria can be satisfied regardless of whether it is the public or the private sector that needs land for a certain purpose. And conversely, the criteria are not necessarily met simply because land is needed by a public authority. Thus in the case of privately operated mobile telephony masts, compulsory acquisition can be justifiable by the importance of the purpose and by the areas where the masts can be erected being, in principle, very limited (even if, within certain limits, there may be various siting options).

Once it has been established that private compulsory purchase is permissible, it remains to be decided what compensation should be paid. As stated earlier, two main alternatives are conceivable. One of them is for the property owner affected to be compensated for the damage incurred. The other is for the property owner concerned also to have a share in the profit which the measure entails.

When coercive rules are used by public authorities, compensation is based on the person surrendering land being compensated exclusively for the damage which occurs. Is this also a reasonable principle of compensation in cases of private compulsory purchase? This has been questioned, especially when the acquirer is a private undertaking operating for profit, as for example in the case of the companies now constructing the mobile telephony network. Should there not instead be a sharing of profit between buyer and seller? ⁸ As mentioned earlier, a Government Commission is currently studying this issue. It will be interesting so see the conclusions arrived at.

⁸ In Sweden this question is highly relevant, since a Government Commission, is reviewing the compensation rules in order to see if the present legislation meet the demands of a “fair compensation”.

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