

Private vs. Government Eminent Domain: (Why) Does it Matter?

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Railroad, electric transmission, and petroleum and gas pipeline companies have long enjoyed various degrees of eminent domain powers in the US.¹ Typically, these common carriers, as public utilities, serve the public interest by servicing all users at regulated prices. The process of obtaining the land corridors necessary for long-distance electric transmission systems or petroleum pipelines resembles the land assembly problem confronted by a government acquiring the land needed for a public highway. Reducing the transactions cost of acquiring essential land routes lowers common carriers' prices. Thus, it is argued, eminent domain powers can translate into more efficient provision of these important goods and services.

A handful of states grant specific private sector firms extensive eminent domain powers, a practice that is controversial. Some of the public concern over private eminent domain is doubtlessly motivated by the troubling reminder to individuals that it is not necessary to give consent or default on a mortgage or property taxes to lose title to property. But this source of popular dissatisfaction is not unique to the exercise of eminent domain by private sector firms; it also pertains to government eminent domain. Like jury duty for citizens, eminent domain is a fact of life. And like jury duty, the burden of eminent domain falls narrowly on a select few. Given the necessity of such powers, the US Constitution, as interpreted by the Supreme Court, defines restrictions on the uses for which property can be taken as well as how the owner must be compensated. Concerns about private eminent domain, however, do not touch on either of these two issues. Instead, this debate is really over procedure, that is, defining "who" has the power to initiate condemnation.

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1. See G. K. Turnbull, "Delegating Eminent Domain Powers to Private Firms: Land Use and Efficiency Implications," *Journal of Real Estate Finance and Economics*, 2012, 45: 303-325, for complete analysis of many of the issues raised in this *Note*.

Private eminent domain has always existed in the US but began to generate controversy by the late nineteenth century. The 1877 Michigan Supreme Court decision *Ryerson v. Brown* (35 Mich. S.C. 333) represents a landmark in this regard. This decision struck down legislation giving eminent domain powers to any firm constructing a mill-pond to generate water power. The court based its decision on two factors, the public use doctrine and changing technology. First, the court decided that the law violated the public use doctrine since it gave eminent domain power to firms engaged in manufacturing purposes other than grist mills or similar common carriers of the time. The second reason the Michigan Supreme Court struck down private eminent domain powers in *Ryerson* was that by the late 1800s it was no longer essential to construct dams to create man-made ponds to generate water power because steam power had become an economically viable alternative. The newer technology meant that the public would suffer no loss of essential common carriers by denying them eminent domain powers for constructing mill-ponds.

The *Ryerson* decision provides background for understanding the rationale underlying private eminent domain in the US. Eminent domain allows some private sector firms to more easily obtain an essential resource—land—needed to fulfill their special roles as public utilities. Thus, such firms have long satisfied even the narrowest reading of the public use doctrine for eminent domain.

Currently, natural gas and oil products interstate pipeline operators draw eminent domain powers from the federal government. Eleven states grant intrastate eminent domain powers to industries ranging from electric power transmission to timber transport. These powers vary across states, but Georgia, Oklahoma, and Texas stand out as the least restrictive—and perhaps the most controversial. For example, six counties in Georgia each tried to use their own regulatory powers to wrest control over electricity transmission line routes within their jurisdictions from firms; the Georgia Supreme Court put a stop to these efforts in its 2003 decision *Cobb County v. Georgia Transmission Corp.* (2003 Ga. LEXIS 285). In light of this decision, the relevant question is whether the preeminence of private eminent domain over local governments' zoning and other regulatory powers makes economic sense.

Based on court documents and discussion in the popular press, local government efforts to stem private eminent domain in Georgia appear to be motivated by concern that regulated utilities with eminent domain powers do not carefully consider the costs of their decisions. Does allowing these firms to freely choose their land routes create incentives to choose inefficiently long routes or to use more valuable land when less valuable land is available?

Economists have long recognized that a common carrier or public utility subject to rate-of-return regulation has an incentive to use relatively more plant and equipment than is efficient because increasing these inputs increases both the company's rate base—hence allowed total profit—as well as its ability to generate the higher revenues needed to increase profit. This is relevant to private eminent domain because transmission line or pipeline corridor width and route decisions resemble capital plant and equipment employment decisions in that using more land or more valuable land increases the rate base and the allowed profit of the regulated firm. But it turns out that land route selection fundamentally differs from the choice of other inputs included in the rate base. In part this is because, unlike plant and equipment, increasing the rate base by choosing an unnecessarily indirect route or using more valuable land does not increase the firm's ability to generate revenue, hence does not allow it to actually attain the greater allowed profit. Thus, the firm does not have an incentive to use either more or more costly land than is minimally necessary because doing so needlessly sacrifices profitability. Therefore, empowering regulated privately owned common carriers with eminent domain does not by itself create incentives for inefficient route selection or excessive use of land.

The only alternative to private eminent domain is government eminent domain. While the debate over private eminent domain rests on the premise that government eminent domain will result in better decisions, economic research provides no solid support for this premise. State and local governments are organizations that are not inherently motivated to pursue efficient resource allocation. So the question of relative efficiency revolves around how the political process balances residents' NIMBYism against the interests of the distant consumers and industries outside the jurisdiction who are served by the transmission system capacity. There is no convincing rationale for why government route selection should necessarily lead to land route choices that are lower cost or more productive than those made by a regulated private sector firm, a conclusion backed up by empirical evidence that state and local governments do not use eminent domain efficiently in other aspects.²

2. G. K. Turnbull & R. F. Salvino, "Do Broader Eminent Domain Powers Increase Government Size?" *Review of Law and Economics*, 5 (1), 2009, art. 32. doi: 10.2202/1555-5879.1395

It is true that some local governments allow undesirable economic activities like regional landfills when they bring in local jobs and increase local tax revenues. But the direct benefits of high tension electric power transmission or pipeline corridors to the locale's economic well-being are usually negligible. The reluctance of a community to allow these transmission corridors within its boundaries is exacerbated by the fact that the economic benefits of these systems—like delivered electric power or petroleum products—typically accrue to distant communities. With no direct local economic payoff and distant beneficiaries, it is not surprising that local governments restrict these land uses when their residents object to them even when such restrictions lead to inefficient outcomes for the broader economy. In sum, there is good reason to expect state and local politics to promote less efficient transmission line or pipeline routes than those preferred by private sector firms.

Finally, compensation is another concern raised in almost all discussions of eminent domain. But complaints about inadequate or unfair eminent domain compensation apply equally to governments and private firms, since all are required to compensate owners at market value. Issues about equity or fairness arise in takings cases because most property owners are not willing to sell their property at current market prices. These individuals are enjoying use value above market value (the higher use value perhaps arising from a family's long attachment to a particular property or from a business' long term efforts to build a customer base centered on its location). While courts interpret the "just compensation" required by the Fifth Amendment of the US Constitution as market value, it has been long recognized that such compensation neglects owners' idiosyncratic use values and in that sense does not fully compensate them for their losses. But full compensation is difficult to accomplish because idiosyncratic value cannot be independently observed. In any case, questions about appropriate compensation are endemic to takings in general and therefore do not reflect an inherent weakness of private eminent domain over government eminent domain or vice versa.

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