THE ECONOMIC THEORY OF EMINENT DOMAIN

This book surveys the contributions that economic theory has made to the often contentious debate over the government's use of its power of eminent domain, as prescribed by the Fifth Amendment. It addresses such questions as: When should the government be allowed to take private property without the owner's consent? Does it depend on how the land will be used? And what amount of compensation, if any, is the landowner entitled to receive? The recent case of *Kelo v. New London* (2005) revitalized the debate, but it was only the latest skirmish in the ongoing struggle between advocates of strong governmental powers to acquire private property in the public interest and private property rights advocates. Written for a general audience, the book advances a coherent theory that views eminent domain within the context of the government's proper role in an economic system whose primary objective is to achieve efficient land use.

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The Economic Theory of Eminent Domain

Private Property, Public Use

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To Ana Maria,

whom I can never fully compensate

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Preface

The Fifth Amendment of the U.S. Constitution gives the government the power to take private property for public use as long as it pays the owner just compensation. Though never popular, the government's exercise of this power for the purpose of constructing highways, hospitals, or other truly public projects is generally unquestioned. The recent case of *Kelo v. New London* (2005), however, pushed the limits of what constitutes an acceptable public use. In that case, the city sought to use eminent domain to acquire several private residences and small businesses in order to clear the way for a redevelopment project whose primary beneficiary was a large pharmaceutical company. In a 5–4 decision, the U.S. Supreme Court nevertheless upheld the city's right to take the property based on the enhanced tax revenues and new jobs that the project promised. The public outcry against this decision, and its apparent expansion of the government's power over private property, was loud and immediate, and was soon followed by political efforts in many states to curb the perceived abuse of eminent domain.

The *Kelo* case and its aftermath, however, was only the latest skirmish in the ongoing debate about the limits of eminent domain, pitting proponents of strong governmental powers to acquire or regulate property in the public interest on one side against private property rights advocates on the other. The legal terrain is well trod, yet there continues to be a lack of consensus on certain key issues, owing in part to their unavoidable political dimension. The goal of this book is to ask whether economic theory can help provide workable answers that transcend political affiliations. That eminent domain has an economic dimension is undeniable, considering that at its basis it is concerned with the transfer of land or other property interests from one user to another. An economic approach to takings focuses on whether, or under what conditions, a forced transfer (for that is what eminent domain allows) is preferred to voluntary (or market) exchange as a means of achieving the maximum value of the property in question.

In adopting this perspective, I do not wish to suggest that economic efficiency is the only criterion by which eminent domain should be evaluated, nor do I wish to minimize the political or philosophical dimensions of the debate over this contentious subject. Rather, I hope to illustrate the power of economic theory to provide both a positive (descriptive) and normative (prescriptive) approach to this issue, thereby clarifying the nature of the legal and political debate, if not entirely resolving it.

Economic analysis of eminent domain has a long history, but research in this area has accelerated in the past quarter century as economists have brought increasingly sophisticated tools to bear on the subject. This book attempts to synthesize that research, but it is more than just a literature review. Rather, it seeks to advance a coherent perspective that embeds eminent domain within a larger economic theory of exchange that draws on insights gained from the wider field of law and economics, which in recent decades has had an increasing influence on the study of nearly all areas of law.

The book is aimed at a broad audience that includes legal scholars, economists, and general readers with an interest in how economics can inform legal debates. To accommodate readers with such diverse backgrounds, I have written the main text in an entirely non-technical way, with limited use of numerical examples to illustrate some of the more formal aspects of the various economic models. For economists interested in technical details, an appendix contains formal proofs of the key results that reflect the state-of-the-art of research in this area. (The appendix reproduces some material that previously appeared in a substantially shorter and more technical survey of the economics of eminent domain; see Miceli and Segerson 2007a.)

From a personal perspective, this book is the culmination of nearly twenty years of my own research on the economics of eminent domain. I was first exposed to the topic as an undergraduate in a law and economics course taught by Richard Adelstein, and my interest was revived by the publication of the seminal article by Blume, Rubinfeld, and Shapiro in 1984 while I was a graduate student. I therefore naturally turned to the subject as a new assistant professor in search of a research agenda, and I have worked on it more or less steadily ever since. Much of my work in this area has been done in collaboration with Kathy Segerson, whose insights are reflected throughout this book, as are the comments of Perry Shapiro and several anonymous reviewers who read and provided valuable feedback on the entire manuscript. I also want to thank Scott Parris, who expressed enthusiasm for the project at its early stages and shepherded it through the review and publication process. As usual, my greatest thanks are to Ana, Tommy, and Nick, whose continual support is of incalculable value.

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