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Using Eminent Domain for Private Economic Development: A Wider Channel for Public Command over Economic Resources?

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The fallout from the recession continues to burden households, businesses, and local and state governments nationwide. Unemployment is high, home prices are depressed and thirty states and many local governments continue to face budget shortfalls. Local governments across the country have enacted new taxes, raised existing taxes, and cut spending in an effort to address these shortfalls. And given their ability to do so, some local governments may turn to eminent domain in their struggles to deal with their fiscal challenges.

The U.S. Supreme Court decision *Kelo v. New London* (2005) upholds government use of eminent domain to transfer private property from one party to another when it serves a broadly defined public purpose such as economic development. The decision represents the culmination of the steady expansion of the "public use" restriction, as stated in the Fifth Amendment of the U.S. Constitution, to a broader operational concept of "public purpose." The changing definition of public use to public purpose began in *Berman v. Parker* (1954) to justify large scale "public-private partnership" urban renewal programs. According to *Kelo* it is appropriate to use eminent domain to increase the local tax base. Local governments often point to the anticipated increase in tax revenues when justifying controversial eminent domain plans to the public. But this type of activity raises questions about whether the practice actually serves the interest of the public in a broader sense. What do state and local governments do with the proceeds from the larger tax base? Do they reduce taxes on the remaining residents or do the new tax proceeds stay in the public sector to support higher government spending?

The relevant question is: Do states that allow their local governments to use eminent domain for private economic development tend to have larger public sectors than those that do not allow this use of eminent domain? If so, then the current expansive public purpose doctrine adopted in *Kelo* eliminates an effective constitutional constraint on governments' command over economic resources and states that give local governments expansive eminent domain powers will generally have significantly larger public sectors than those that do not.

A recent study by Geoffrey K. Turnbull (UCF) and Robert F. Salvino (Coastal Carolina University), published in the *Review of Law and Economics,* addresses this question, carefully evaluating the relationship between an expansive public purpose doctrine for eminent domain and the size of state and local governments.[1] The study focuses on the empirical relationship between the explicit use of eminent domain for private economic development and the size of the public sector using various measures of government revenue as a share of total state personal income, while controlling for the structure of government and other factors expected to influence government size.

The empirical study tests the " leviathan government" hypothesis: state and local governments that are free to use eminent domain for economic development and related tax revenue purposes will do so to increase their relative size. Looking at the pre-*Kelo* era, local, state, and combined local and state revenue data for each of the continental U.S. states over the 1990 and 2000 Census periods reveals that allowing eminent domain for economic development has significant positive effects on the relative size of the public sector. States that have explicitly embraced the broad public purpose doctrine tend to have larger state and local public sectors than those that have not clearly embraced the doctrine regardless of how public sector size is measured. Other results also support previous studies investigating the leviathan behavior of governments. In particular, the analysis offers more evidence that the structure of the state-local public sector matters as well. Decentralizing tax and spending responsibilities to lower level governments tends to restrain the total size of the local and state public sector as competition

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[1] G.K. Turnbull and R. Salvino, "Do Broader Eminent Domain Powers Increase Government Size?" *Review of Law and Economics.* 5(1), 785-806, 2009.

among numerous local governments constrains their expansionary tendency more so than at the state level, where inter-jurisdictional competition is limited.

It is important to note how the effect of eminent domain on the size of local governments varies across policy specifications, as some reveal a significant positive effect on the size of the local public sector and others find no significant effect. Local economic development practices that shift land use from residential or agricultural use to industrial or other commercial use tend to transfer a balance of the taxable activities to the state. These economic development practices also often include incentives to developers or industrial recruits that reduce their local tax burden. These types of practices have an offsetting effect on local revenue. However, regardless of their usefulness in economic development programs, it appears that broad eminent domain powers open additional channels through which state and local governments increase their command over resources in the economy.

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