

Real World Graduation: Question 21

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Question 21

The Mayor and City Council of a certain city desired to raise the amount of tax revenue received by the city. They made a secret arrangement with a mall developer as follows:

1. The city would designate a certain district of the city, consisting of 150 homes and a few small businesses as suitable for development. This district was selected because most of the homes are more than 30 years old, and it has excellent access to major freeways.
2. With the area so designated, the city would send notices to each homeowner and business owner that they had 90 days to move out of their homes, and the land turned over to the developer.
3. In order to save taxpayers money, the city would offer 85% of the current appraised values of the homes and businesses as compensation. On average, the homes in the affected district are appraised at \$130,000.
4. The total amount paid to the homeowners by the city as compensation would be repaid by the developer. He would be allowed to collect an additional 2% surcharge sales tax on everything sold by stores in the mall. That way, the city would be repaid the amount given to the original homeowners, and also collect all the usual sales taxes.
5. The Mayor, City Council, and their respective staff members were to do all of the foregoing without any public hearings or notices until the formal designation letters were mailed to each affected resident.

The Constitution of the state in which this was to occur contains a "takings" clause, in which people are to be compensated for any seizure of property devoted to public use (i.e., the same as the U. S. Constitution's Fifth Amendment). If this plan were enacted, which of the activities contained in the secret plan would violate both Constitutions?

- a) A government entity entering into a secret financial agreement with a private entity.
- b) Seizing property from a group of private owners and giving it to another private owner for the benefit of the new private owner (as well as the city).
- c) Arbitrary designation of a certain district for unusual treatment simply because of the age of the homes and their location.
- d) Forcing each homeowner to take a \$19,500 loss on their property, since they will be paid only \$110,500 for homes that were appraised on average for \$130,000.
- e) All of the above.

Answer to Question 21

This is a trick question. None of the elements of the secret plan violate the law or either Constitution.

This process as described is now considered legitimate under "Eminent Domain" and "Tax Increment Financing". "Eminent Domain" originally meant that the government can take private property for public use, so long as the original owners were fairly compensated. Traditionally, the local government could take property from private individuals only if the objective was to build improvements for use by the general public: expansion of roads, canals, bridges, etc. However, in recent times, eminent domain has been expanded to allow the government to take from one private owner and give to another private owner simply because the new private owner promises to generate more revenue for the government [1]. Also, the government doing the taking gets to choose how much to pay the original owners for their property.

The process begins when the political entity designates the area to be seized as "blighted". This is actually a legal term, having nothing to do with the actual condition of the area. "Blighted" means that the entire area becomes subject to control by the local government. Once an area is declared "blighted", the current owners cannot sell their homes to another buyer: the homes are technically worthless because the entire area is now legally designated for "development". In other words, once the "blighted" designation is made, only one buyer is permitted (the government), and only one entity sets the price (the government). "Tax Increment Financing" is the method by which the city advances the money to the developer to buy the properties from the current owners. The mall developer pays this loan back to the city because it is allowed to collect a special tax to be paid by the people who shop at the mall. In other words, the taxpayers pay twice (the original money given by the city, which came from the taxpayers), and through higher taxes such that the developer can repay the loan from the city.

Typically it is too expensive for the original owners to contest the amount they are to be paid, so they have no choice but to accept what the city offers as compensation for their homes and businesses. The alternative is to bankrupt themselves in legal fees by trying to sue the city.

Another twist on this scheme is for the commercial entity to set up a dummy corporation, usually with names containing the words "Progress", "Improvement", "Revitalization", "Empowerment", "Civic Action" or similar innocuous titles, whose only purpose is to manage the paperwork required by the tax assessors' office to carry out the confiscations. The political entity (in this case, the city) then passes an ordinance permitting the dummy corporation to act in the political entity's behalf to perform the actual "eminent domain" procedure. This way the political entity can claim that it did not actually perform the deed; it was done by the dummy corporation. Then the same politicians who authorized the confiscation of private property at a net loss to the current owners can blame "greedy corporate interests" for destroying the lives of the affected people. Never mind that the corporation is only carrying out the politicians' conspiracy.

As for the \$19,500 average loss on each home, those (former) homeowners should pony up some gratitude for the high quality local government that is doing what is necessary to increase government revenue in order to obtain more good government. The only remedy for this situation is not to own anything of any value in an area with a convenient location that some developer with good political connections finds attractive for his use.

[1] This was the situation in *Kelo et al vs. City of New Haven, CT.*, in which residents sued the city for taking their property to give to another private entity. Although this should have been resolved within the state of Connecticut, an appeal was made to the U. S. Supreme Court, which ruled in favor of the city

(545 U. S. 469 (23 Jun 2005)), on the grounds that "public purpose" is close enough to "public use", and that "economic development" is a suitable "public purpose".