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An economic analysis of takings in Korea: endogenous probability and announcement effects

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Abstract

This paper analyzes a taking project which has recently come to the fore of public attention in Korea. Hypotheses as to why some ostensibly unreasonable incidents have occurred during this project will be presented. Also, starting with a general government incentive to maximize the discretionary budget, a theoretical reasoning will be developed to formally establish the hypotheses. The major features of taking focused on are the endogeneity of the takings probability and the government's opportunistic use of announcement effects. The paper seeks to explain various phenomena that tend to emerge when the compensation rule and taking procedure are superficially established, thereby fostering a political game whereby the resident's resistance deviates the taking probability from the efficient one.

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Although vaguely confident from the outset that fieldwork in Shasta County would turn out to be enlightening in one way or another, I began with no particular hypothesis in mind. Nevertheless, after only a few interviews I could see . . . (Ellickson, 1991, p. viii)

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1. Introduction

The Fifth Amendment to the U.S. Constitution declares: “[N]or shall private property be taken for public use, without just compensation.” An identical clause is found in Article 23 (3) of the Korean Constitution. Believing that this clause should be the foundation for delineating the property rights between the government and the private sector, this paper concerns the likelihood of a government taking being endogenous; the government can affect the extent of resistance to a taking by the promised amount of compensation.

Recent research on eminent domain has striven to efficiently determine what constitutes just compensation. This research assumes that society already has in place legal mechanisms that guarantee the due process of takings. It adheres to the academic convention that the takings probability is determined exogenously and passed to both parties of expropriation. This paper presumes that the taking probability is affected by political support or resistance, rendered to be an endogenous variable.

We further emphasize the detrimental effects of the government’s taking announcement on the residents. The residents may have to bear some costs imposed by a possible taking once the official government announcement is made. Wide-ranging announcement effects exist. For instance, a variety of regulations restricting the local development are imposed after the announcement, and they are expected to remain in force for a considerable period of time, sometimes inflicting losses on residents, even in cases where proposed taking would be canceled. Furthermore, the repeal of such regulations in Korea frequently requires a tough bureaucratic approval process which takes a long period of time. Under these circumstances, the government may strategically exploit the announcement effect as it continuously guarantees a high taking probability. If the losses resulting from the announcement become large enough, the reservation price for compensating the residents decreases, therefore allowing for lower compensation. In short, announcement effects reduce, as Kanner’s “condemnation blight” (Kanner, 1973, p. 765) does, residents’ resistance while lowering the reservation prices of compensation.

All in all, a possible contribution of this paper would be a substantive nature of inquiry on taking; what motives are involved with the government’s signaling its compensation rule on which the resident’s investment decisions rely. By illustrating a specific taking case of the Tong River in northeastern Korea, we search for an answer to intriguing puzzles as to why the Korean government intentionally over-appraised the affected land and thereby inducing residents’ over-investments. We explain various phenomena that tend to emerge when the compensation rule and taking procedure are superficially established, thereby fostering a political game whereby the resident’s resistance deviates the taking probability from the efficient one.

Section 2, based on a simple analytical framework, discusses the major points in the literature regarding compensation warranting economic efficiency. Section 3 analyzes a proposal which has come to the fore of public attention; the construction of a dam on the Tong River.¹ Hypotheses as to why some apparently unreasonable incidents occurred will be presented based

¹ In late 1997 the authors obtained a media report stating that the residents of the Tong River area, in stark contrast to other takings cases, strenuously urged the construction of the proposed dam. This immediately caught our attention, inspiring the current research.

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