

THE ISSUES REGARDING THE “FAIR COMPENSATION” IN THE EXPROPRIATION PROCESS

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Abstract: *The compensation issue it is a very strong one and it is binding in a compulsory purchase process as well, without it the essence and the security of the ownership will vanish. By compensating those whose land was taken will secure the creditors, which means the banking system will remain vital. Moreover, the significance of compensation is crucial for a state, because in this way the people will fill that their right are protected and in case of expropriation they will have the possibly to settle somewhere else, which will give a social stability in the country. Usually, in the Constitution is stipulated that without a fair compensation the expropriation process cannot be fulfilled*

Keywords: *compensation, fair compensation, expropriation, market value, property, ownership.*

Under the term “compensation” is understand the loss that the real estate owner will eventually have after the procedure will take place. In many legal acts it is stipulated that the compensation must be in such a way that the owner’s situation before the procedure and after shall remain the same. The general idea of compensation is to assure the owners who will have to surrender their lands that at least from the financial point of view they will be assured. In the most cases the compensation is monetary; however there are cases when the loss of the land is substitute by other place (a parcel of land, another house etc) which is usually called alternative compensation.

Moreover, it is hard to provide a universal definition for the term “fair” especially when we deal with some economical gains. Anna Conte and Peter G. Moffat in their article discuss the fact that an individual’s decisions regarding the allocation of income between them and others are determined partly by the individual’s “fairness ideal”, and partly by their motivation to maximize income. Furthermore, to establish a bridge between two bargain parties is quite complicated and that is why a definition of a fair or just compensation shall be well-defined and mentioned in the legislation as well.

From property owner’s point of view the situation of the expropriation itself is unfair, yet there are people who have the incentive to make profit from it. In his presentation Leif Norell highlights some issues regarding the reservation price which is defined as the “lowest price at which the owner would agree to sell the property in a voluntary transaction”.

When the object of the expropriation is the whole property than applying the market value of the property as compensation is fair and objective. The only important thing here is that the market value shall be estimated according to the sales comparison approach not to the cost, in case there is no active market the expropriator shall take care that these people will be moved somewhere else to live or there will be given other similar properties. From my point of view it is important because if the is not an active market than:

- It will be difficult to find a seller in that area;
- The value according to the cost approach can be very low because of the physical depreciation;

It would be fair to propose them other similar places because it is not their fault that they have to move from their places or in case they will disagree the compensation shall express the market value of those properties.

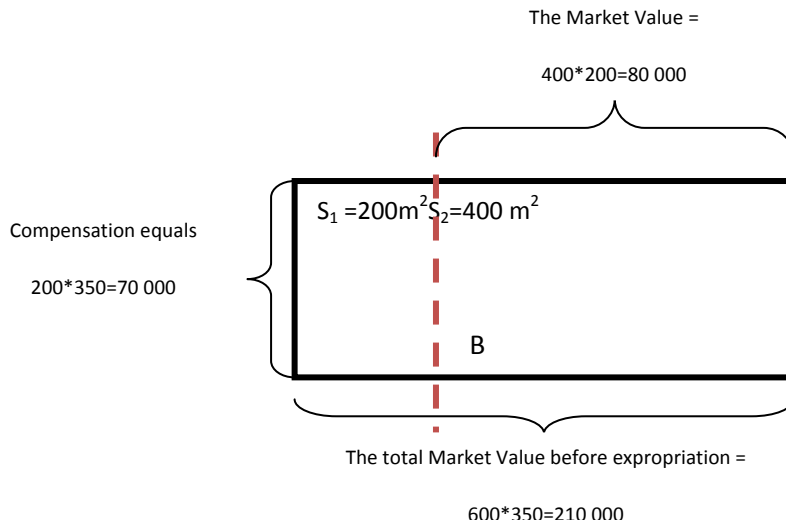
Another situation is when a part of the property is taken and here I consider that it shall be taken into consideration the future possibility of using the property in order to compensate equitable the owners. There can be 2 cases:

- When the part which is taken does not aggravate the further exploitation;
- When the expropriation part is bigger than the remaining one and the property owner will not be able to use the land as before.

In the first case the “encroachment money” shall be paid which represents the impairment of the real estate market value. In the most cases this loss is calculated by finding out the market value per one square meter, km etc. and multiplies with the surface. I consider that in this case such compensation is a reasonable

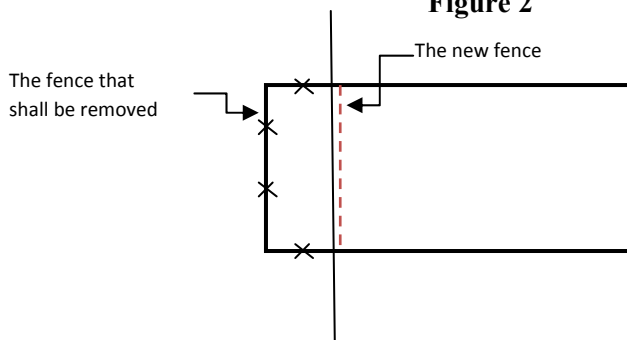
one. However, I believe that it shall be taken in consideration (depending on different types of properties) how the amount of land is related to the final value, for instance after a market study the appraisal reveals that for a property A of 400 m² the price for 1 m² of land is 200 € but for the property B with 600 m² the price is 350 € (the market value before expropriation is 210 000€), so the property B will be the expropriation subject, the expropriator needs 200 m². Then according to the common use practice the encroachment money will be calculated in this way 200*350 =70 000€, the remained value of the property will not be 210 000€-70 000€ = 140 000€ but according to the market it will be 80 000€ which means that the property owner is automatically losing the difference (60 000€).

Figure 1



In the second situation to apply the same technique will be unfair because the actual remaining property can worth nothing on the market which means no willing persons to buy it. So frankly speaking the actual loss of the property owner is not only the market value of the needed part but the market value of the whole property. The same logic has to be followed in the cases when on the expropriated land there is a fence (or it can be other edifice), for instance after the expropriation 2 km of the fence was appraised as its market value let's say 150€, in order to restrict the rest of the property the owner has to pay 250 € for the same functional characteristics of the new fence, but because those 2 km had an advanced physical depreciation appeared the difference and the property owner are forced to pay more for a new fence even if the first one could serve him for 20 years. I consider that in such cases it will be honestly to take into consideration the actual losses which will deal the property owner with. However, it is important to start the calculation from the same functional and technical characteristics of the edifice (if the previous fence was a simple one than the cost calculation for the new one shall be based on the same characteristics).

Figure 2



When on the expropriated land were different improvements like sheds, wells, ponds etc. In this case it will be reasonable to use the cost approach since these real estate assets are rarely sold apart from a dwelling and they are not taken into consideration from the potential buyer because the house is the center of the attention and other elements in the most cases are rebuild by the new owner according to his/her desire and

this is a typical situation for Moldova's countryside. After studying a valuation report which was made by the local Cadastral Office and coordinated by the Cadastral Agency I have noticed that the methodology which was chosen by the appraisers is not a modern one and from my point of view does not fulfill the aim of the valuation as compensation because they are relying on the cadaster value calculated according to the reproduction cost which means that they do not take into consideration the construction cost of the new real estate object that will have to construct the property owner.

The error of the mentioned method can be quite high especially for the objects which are not standardized because it is based on the prices from 1969 which are actualized with the inflation in the construction sector.

According to the Moldavian Law only the state can take the role of expropriator for the both purposes the national and local one. So, it will be studied the economic effect of "fairness" from the state point of view which means from the tax payers point of view as well. Everyone want to save as much money and time as they can, and the expropriation process is not an exception.

The state or the delegated authorities has one goal to spend as less money as it is possible, however the foreign practice shows that the lack of good regulations can lead to corrupt officials to provide higher amounts of compensations to those who are willing to offer bribes. In such cases it will be justly that in the law regarding the expropriation process it will be followed the principle of the "fairness and equity" which express the fairness and the transparency of the process and based on an open exchange of the information. Furthermore, such changes within the legislation can prevent:

- The further debates in the Courts because people will feel that they were treated honestly.
- The corruption in the state authorities.

Another issue is that the expropriator takes into consideration the compensation only for the property not for the owner's losses within the process of the expropriation and continuing this idea - all the additional losses related to the expropriation are born by the owner. Moreover, from the state's point of view it is important to let the property owner in the same economic situation not in the same psychological one, it is not important if the owner has some special feeling regarding the property and I consider that there are some good reasons for that:

- It will be difficult or even impossible to compensate equally all the participated owners because in their nature people are different and no one will know where the actual limit is between a real feeling and a faked one.
- The corruption factor may grow rapidly and in fact the state will be in a worse situation from the economical point of view;
- The debates between parties will be too long, because there are now standards or basic rules of the compensation determination though the psychological factor point of view.

Well, it can be said that from the expropriator point of view it is highly important and "fair" to compensate only the objects which can be identified and assessed. In the most cases the expropriator is not interested in paying the reservation price especially when it considerably exceeds the market value.

Conclusions:

The main negative aspects from the economical point of view (which are related to the compensation) of the mentioned process are: the term of the "real value", there are no explanatory regulations and methodology regarding the determination of the compensation and of "other damages".

The determination of the reservation price can be quite complicated because one component of it is the individual value that includes a moral attitude of the property owner which is obviously impossible to asses, so the appraisals together with the surveyors have to list all the possible damages which have a value in money.

In case of expropriation the market value shall be estimated according to the sales comparison approach not to the cost, in case there is no active market the expropriator shall take care that to the expropriated people will be given other similar properties. In case when a part of the property is taken it shall be taken into consideration the future possibility of using the property in order to compensate equitable the owners.

There are good chances that the acquiring authority will not be willing to pay to the property owners the expenses incurred and losses sustained and according to the property owners from Moldova the state is not interested to seek all the actual damages and in some cases it is difficult to convince them even if the necessary proofs are collected. Of course the expropriator will not take into consideration that certain surrender chose the most expensive service companies (removals, lawyers, appraisers etc). It is important to

prevent the owners that they shall choose a middle cost services. Furthermore, I believe that a certain type of services must be excluded from the list of the damages, for example payments for the lawyers.

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