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# Property Matters

**One of the most basic, but often overlooked aspects of modern democracies is the significance of individual property rights. From a child in a schoolyard with a ball, through to the largest corporation with billions of dollars of assets, the concept of property that belongs to somebody is at the core of the functioning of an economy.**

**For farmers, the property rights that are held to land are the basis of the operation of a farm business. Whether held as freehold, leasehold, rented, sharefarmed, or simply grazed under a temporary licence, these rights a farmer holds as a result of his or her legal relationship with the land dictate how the business operates. And contrary to most people's general understanding, these rights are not well defined, nor are they as secure as may have been believed in the past.**

An Australian farmer, in the course of preparing a paddock for cultivation prior to sowing a crop, discovers a small population of ground-dwelling native birds living in part of the paddock. The farmer knows that the birds are thought to be extinct, and they are certainly listed as endangered species under various pieces of environmental legislation.

The dilemma that now confronts this farmer is an extreme one. To proceed to cultivate and grow a crop on the area will almost certainly damage the bird population, if not destroy it completely.

To alert relevant authorities to the existence of the bird population will almost certainly trigger a protection order under either State or Commonwealth legislation, that will severely restrict the farmer's ability to use that area of land for cultivation, and perhaps even to graze livestock. Furthermore, under either State or Commonwealth legislation, the farmer has no right to compensation for the loss of utility of the land in question.

The dilemma that faces a farmer in this situation arises because the property rights held for the piece of land in question are not well defined. Nor are they secure from being summarily removed by Government, irrespective of what many may believe is said in the Constitution.

## Some Property Right Basics

While the notion of legally protected individual property or possessions seems to be as fundamental to modern living as breathing, it hasn't always been the case. Some early civilisations such as the Greeks and Romans are thought to have developed reasonably sophisticated rules regarding property, but for much of human history ownership of possessions has been secured by might, rather than right. The change from securing property by force to securing it in law highlights an important aspect of property rights. It was the development of the concept of human rights that secured the rights of individuals to property. Property in fact has no intrinsic rights, rather it is the people who own it who are granted legal rights to that property.

Many ascribe the origin of the concept of legal protection of an individual's property under English law to the Magna Carta, signed by King John in 1215. There were in fact several Magna Cartas, with each having a provision that the Crown would no longer remove an individual's property without the legal judgement of their peers.

While the Magna Carta may be the basis of the protection that property rights now enjoy, its signing was certainly not the point at which the importance of individual property rights was suddenly recognised as a foundation stone for advancing economic and community wellbeing. Common ownership of land and other property, rather than individual property rights, has been a feature of many societies over the last thousand years. The most notable recent 'experiments' in this regard have been some of the early European settlements of the USA, and economies such as the former USSR and its satellites.

Even the early history of European settlement in Australia included a trial of a 'common property' economy. It was quickly abandoned however, when it was found that giving ex-convicts rights to farm areas of land was a much better way to attain food self-sufficiency than was forcing people to work on Government farms.

The laws surrounding property have progressively developed over the centuries. Historically, property has been thought to describe a legal or customary relationship between a person and a thing.[1]

[1] Bethell (1998) The Noblest Triumph. Property and Prosperity through the aAges, St. Martin's Griffin Publishers.

Sir William Blackstone, the first ever Professor of English law, defined property as "that despotic dominion that one man claims and exercises over the external things of the world, in total exclusion of the right of any other individual in the universe."[2] The thing may be physical (land) or abstract (copyright of a novel). People with property rights enjoy legally enforceable claims over that thing.

Title to property confers rights to the titleholder, but the rights may differ enormously, depending on the nature of the property. In more recent times, it has become commonplace to describe title to property as a "bundle of sticks" with each "stick" being a right held by the titleholder. The sticks in the bundle may include the right to use the thing; the right to exclude others from using it; the right to alter its physical configuration; the rights to the income it produces; and most importantly the right to transfer the title of ownership of any or all of these 'sticks' to another person. The rights traded by the owner of a financial derivitive, or the holder of rights to computer software are examples of how complex the bundle of 'sticks' (ie title) can be.

Title to a specific bundle of property rights does not exist in isolation from titles to other property. Title rights cannot be exercised if, for example, to do so would infringe on the property rights of others. Pollution control laws that protect air quality and restrictions on the use of land susceptible to erosion are examples of regulations that have been enacted to implement this restriction on property rights. Nor is it possible to isolate one title completely from the network in which it was established. For example, the value of land adjacent to a publicly-owned beach is vastly different to the value of land adjacent to an oil refinery, even if the land in question is identical in size.

A bundle of property rights can also be 'unbundled'. A person may own land, but temporarily transfer the rights to farm it to another person for a defined period of time. Similarly, someone may own a house but have it permanently rented out to another person, while at the same time having the title to that property mortgaged to a bank.

If anything, defining the rights that a person can expect to enjoy as a result of owning a title have become more complex, as technology has made different rights easy to define and economical to record and transact.

## The Economics of Property Rights

One intriguing aspect of individual property rights is the critical role they play in the functioning of modern democratic economies, despite the fact that emperical proof of the relative importance of secure property rights is almost impossible to obtain.

There is ample evidence that the rate of economic growth and the extent of community wellbeing is higher in economies where individual property rights are relatively secure.

For example, many consider the economic dominance of England over the centuries largely resulted from the extent to which property law was relatively well-defined under English law for a long period. On the other hand, the fall of the former USSR, and the poverty and starvation reported to exist in North Korea are considered to be a product of insecure or non-existing property rights, despite an abundance of natural resources. Even the recent economic growth that has occurred in China is attributed to policies that have created much more private property ownership.

While economists can examine relationships between economic growth and say, interest rates or fiscal policy, with property rights the relationship is much less clear. Short of having two identically resourced nations with different standards of property rights, it is not possible to quantify the role such rights have in contributing to rates of economic growth.

What is known from centuries of experience is that people work harder, and are more committed to working more efficiently when they work for themselves. Despite all the experiments in communal living that have been attempted over time, and despite all the idealists who wish for a better society in which all would contribute equally for the common good, the simple fact is that self-advancement is the key motivator of humankind.

A second key aspect of property rights that makes them better generators of economic wellbeing is the role that long-term investment has in improving the productivity of resources. Many resources, such as farmland, will generate more wealth in the long-term if adequate levels of investment is made in improvements. Farmland, for example, will be more productive if improved pastures are established, if appropriate fencing is constructed, if fertilizer is applied and if shelter belts of trees are established in various locations. Each of these is a long-term investment where initial costs are recouped over an extended period of time. An owner will only make these investments if they hold secure, perpetual title to the land in question and the bundle of rights associated with that title remain certain. A landowner is unlikely to incur the costs associated with establishing plantations of trees, for example, if there is uncertainty about what rights may be held to harvest or thin those plantation areas in the future, or to change the area sown to trees in the light of changed markets or technological developments.

A direct example of the significance of property rights in investment decisions can be seen in the development of biotechnology over recent decades. For most of the last century, Governments of developed economies invested large amounts of public money on programs to breed better varieties of agricultural plants. This public investment was made on the basis that the cost of these programs was something that no individual farmer could afford. This was especially so because the benefits of investment in breeding an improved variety of wheat, for example, would spillover to everyone in the farming sector. Around the mid 1980s, a number of countries introduced legislation that

[2] Blackstone, cited by Bethell. op. cit.

provided secure ownership rights to plant varieties, and technology advanced to a stage where specific varieties could be identified and protected via licencing. The result of the creation of these property rights has been an absolute explosion in the investment now being made in plant breeding by private organisations. In the USA alone, private investment in plant breeding now far outstrips Government spending in this area.

Despite these examples, the relationship between security of property rights and economic growth is not something that can be added to an equation and used to predict an economic outcome. This was pointed out by Douglass North, winner of the Nobel prize for Economics in 1993. In his acceptance speech, he noted that if economists want to know why some economies develop rapidly and some do not, they need to go beyond the normal economic factors. Economists have given mathematical precision to their theories, he said, but they have completely ignored the "incentive structure embodied in institutions", and among these one of the most important is a system of efficient property rights.[3]

As a result, while the impact of a change in interest rates on economic growth can be predicted, there is only anecdotal evidence available about the impact of the removal of one of the sticks in a bundle of property rights on investment and wealth creation.

## The Law and Property Rights

The law surrounding property rights in Australia is based on a number of principles that are common to property law in other countries with an English legal heritage. These principles include legal protection to ensure a person's property cannot be arbitrarily removed by Governments without due process, and also that property holders have a responsibility to ensure their property is not used in a way that results in harm to another person or their property.

Section 51(xxxi) of the Constitution states that the Commonwealth has powers to acquire property on just-terms from any State or person, for any purpose in respect of which the Parliament has powers to make laws. This provision of the Constitution is reinforced by both Commonwealth (the Lands Acquisition Act 1989) and similar legislation in States and Territories.

What is less well understood is that this principle only applies in situations where the actual title to property is acquired by the Government for a public purpose. For example, Governments have purchased houses and land to construct freeways or railways. While invariably there will be arguments about the amount of compensation due in these situations, there is no question that the removal of someone's title to property generates a requirement for just-terms compensation. Where the issue is considerably less clear is when the title to a property is not taken away, but one of the 'sticks' in the bundle of rights normally associated with that title is either impaired or removed. In these situations, the actual title to property is not acquired by the Government. There has, not surprisingly, been quite a number of legal cases where the question of the meaning of Section 51(xxxi) of the Constitution has been tested.

Perhaps the most noteworthy in recent times was the Tasmanian Dams Case.[4] In that case, the Commonwealth enacted legislation to prevent the Tasmanian Government from damming the Franklin River. One of the grounds on which the State of Tasmania challenged the Commonwealth was that the Commonwealth's restrictions on the State's use of the Franklin River and nearby land, amounted to an acquisition of title thus triggering s.51(xxxi) compensation provisions.

On this question, Justice Mason (with the concurrence of two other Judges) ruled that "to bring the constitutional provision (s.51 (xxxi)) into play it is not enough that legislation adversely affects or terminates a pre-existing right that an owner enjoys in relation to his property; there must be an acquisition whereby the Commonwealth or another acquires an interest in property, however slight or insubstantial it may be."

The only dissenting Judge was Justice Deane, who considered that the restrictions imposed by the Commonwealth could be substantial enough to amount to the acquisition of property, and should therefore be compensatable. In a more recent case, Justice Kirby in a minority judgement stated that in his opinion the terms of s.51(xxxi) were "intended to recognise the principle of the immunity of private and provincial property from interference by the Federal authority, except on fair and equitable terms."[5]

Despite Justice Kirby's reasoning, the High Court has so far held that unless the Commonwealth actually becomes a titleholder by acquiring a title from an individual, the just-terms provision of the constitution do not apply. In other words, if Governments remove some of the sticks from the bundle of property rights associated with a particular title, then this action is constitutionally valid and no compensation is payable.

The property rights issue has been subject to close legal scrutiny for a long time in the USA. The legal system operating in the USA is different to that in Australia, as a result of different constitutions. Thus far it seems the outcome of US Court cases has been to provide more protection for property rights than exists in Australia.

In one notable case in 1987, the US Supreme Court ruled by a narrow majority that the Californian Coastal Commission had "taken" property by requiring that a property-owner grant a right of way through his land in return for a permit to rebuild his house.

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3 North (1993) cited by Bethell. op. cit.

4 High Court of Australia. The Tasmanian Dams Case. (1983) 158 CLR 1.

5 Newcrest Mining vs The Commonwealth (1997) 190 CLR 513

This decision was reinforced by a 1994 decision where the Supreme Court decided that a Local Government requirement for a public easement as a condition of granting a building permit was in breach of the constitution.

Partly as a result of the earlier decision, a Presidential Executive order was issued in 1988 requiring federal agencies to evaluate and report on the effect of their actions on property rights. As well, the US Supreme Court has developed a series of rules used to decide whether a regulation amounts to the taking of property rights. These are referred to as the Agins Rules.[6] In that judgement, the Court stated that for a property regulation to be constitutional, it must:

- have as its purpose a 'legitimate state interest'
- it must substantially advance this interest
- it must not deny the owner "economically viable use of his land."

The third rule has subsequently been explained to contain two tests, which can apply to part or all of a property. First, the regulation must not make it commercially impractical to develop the property, and second, there must be no undue interference with the owner's investment-backed expectations.[7]

This area of law is still a source of controversy in the USA, however it appears that the 'rules' are much better developed than they are in Australia, and the rights of US property owners are more carefully protected.

## Property Rights and Farming in Australia

For an Australian farmer faced with the potential that normal farm operations may damage or destroy an endangered species, the situation is quite dangerous. Nothing in the Constitution, or in High Court decisions on this issue provides any comfort that if the farmer takes appropriate action and notifies authorities, his or her rights will be protected and adequate compensation will be forthcoming.

The High Court has held that Government removal of some or most of the sticks in the bundle referred to as a property title does not contravene the Constitution. This is despite a number of Judges pointing out that this could logically lead to a situation where all the rights an individual owns as part of a title could be removed, and the person would be left with a meaningless title. A farmer could still hold title deeds to the land, but be unable to grow crops, graze livestock, or even drive across the area where the endangered birds were located. Until the High Court makes decisions about which of the sticks in the bundle should be protected, the concept of secure title to land in Australia is somewhat precarious.

It is possible that the High Court may develop this area of law further and establish rules similar to those existing in the USA, however there is an added complication. In Australia, most of the legislation governing landuse is generated by State Governments, who are not bound in the same way that the Commonwealth is by the Constitution. As a result, even if the High Court did develop such rules, they would not automatically operate in relation to actions taken under State legislation.

But perhaps even more significant is the fact that these issues are unlikely to ever be tested in the High Court, unless the Commonwealth itself begins to take action to restrict property rights using legislation such as the recently enacted Commonwealth Environmental Protection and Biodiversity Conservation Act.

Even this may not be a likely course of events. A Commonwealth Environment Minister concerned about the risk the Commonwealth might face if it did take action could, for example, simply provide an inducement or penalise the relevant State Government to encourage it to take the desired action. The end result would be that these issues will never be tested through the High Court, and the degree of protection property rights are starting to get in the USA will never evolve in Australia.

Both the Australian economy and the Australian environment will pay a penalty as a result of this. Economically, the nation will be worse off because land owners' decisions about the use of their land will increasingly be driven by the need to circumvent laws which remove property rights, rather than by straightforward economic considerations. This is already happening in NSW under the State's Native Vegetation Conservation Act. That legislation prevents farmers from damaging native vegetation, with native vegetation being defined as a population of predominantly native species that has existed for more than ten years. To avoid having an area of land restricted by this legislation, farmers are simply ploughing up native vegetation after nine years, irrespective of whether it makes sense to do so on productivity grounds.

Environmentally, the nation will be worse off because in the absence of better definition and protection of the property rights of landowners, there exists a substantial incentive for desirable environmental aspects of land to be either hidden or destroyed. In addition, landowners are discouraged from making long-term investments in the environmental health of their property if there is a danger that these investments, such as the planting of trees, may result in them facing further restrictions on their property rights in the future.

**COMMENTS CONTAINED IN THIS DOCUMENT ARE BASED ON INFORMATION AVAILABLE AT TIME OF PUBLICATION.**

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6 Agins vs City of Tiburon (1980) US Supreme Court.

7 Siegan (1997) Property and Freedom. Transaction Publishers.