The fight over India's land laws: The Economist explains

ABSTRACT

[...]the opposition Congress party claims that removing the consent clause rewards business interests at the expense of poor farmers.

FULL TEXT

Why is it so hard to settle on rules for the compulsory sale of land?

INDIA'S parliament reopened today after a short break. The government led by Narendra Modi is trying to pass amendments to a 2013 land-acquisition bill through parliament's upper house, where it lacks a majority. Under the existing bill, any forced sale of land requires the consent of at least 70% of affected owners and must also pass a social-impact test. Compensation is set at double the market value for urban plots and quadruple for rural land. The demands of the bill are a leading reason why investment projects are at a standstill. In December Mr Modi's government issued a temporary executive order that did away with the consent clause for certain projects. The amended bill would make that change permanent. But the opposition Congress party claims that removing the consent clause rewards business interests at the expense of poor farmers. Yesterday it mustered a huge rally in Delhi in protest. Why is land acquisition such a contentious issue in India?

Anywhere in the world the forcible sale of land is an infringement on landowners' property rights. Why not simply let buyers and sellers agree to a transaction between themselves, free of any compulsion? Economists call it the "hold-out problem". It crops up whenever a single buyer has to negotiate in sequence with many sellers for the contiguous plots of land it needs for, say, a flyover or a factory. A deal that makes everyone better off might exist in principle, if the social value of the project exceeds the sum required to persuade all land-holders to sell. But in practice once the buyer has acquired a few plots, it makes sense for other would-be sellers to hold out for a higher sum. These hold-outs can render almost any project unviable. Even where sellers are less shrewd, the costs of bargaining with them in series can kill a project. In India especially, even the smallest risk of a facing a challenge in court tends to result in a ruinously costly delay.

That is why even market-friendly economies, such as America's, have laws that provide for compulsory land sales. But the Indian bill causes special bother, even with its apparently generous terms. Politics is one reason. Congress (and many other parties with seats in the upper house) lost badly in India's elections last year; they see a way back to relevance by painting Mr Modi's party as anti-poor and anti-farmer. Their posturing is built on a deep and widespread worry about the unfairness in the restitution for forgone land. The benchmark for compensation is set by recent sales of local land. But such transactions, which are rare at best, tend to have taken place at depressed prices. The direct sale of farmland to industry is anyway banned (ostensibly to protect farmers), which rules out a whole category of potential buyers and drives down prices. High stamp duties have a similar effect. Farmers with fertile land often end up feeling swindled when appraisers fail to take full account of variations in the quality of their land.

How best to ensure that farmers not be ripped off? A suggestion by Maitreesh Ghatak of the London School of Economics and Parikshit Ghosh of the Delhi School of Economics is to invite offers to sell from both the landholders in the specific area required for development--and from landholders close by. Any farmer within the bounds of the proposed development who did not accept the price set by the auction could instead be assigned a nearby plot in compensation. Offers for these extra plots should sidestep the hold-out problem as no one is essential to the project. Not a perfect solution, but as things stand India's land market is a long way from perfection.

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