

Invited Takings: Supermajority, Assembly Surplus, and Local Public Financing

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ABSTRACT: Fear of the abusive exercise of eminent domain power and of potentially high costs resulting from serious holdout could cause slowdown and even suspension of land assembly for urban redevelopment, which is particularly devastating for the developing world, as evidenced by urban slums and vulnerable infrastructure. Invited takings, as recently emerged in China, delivered success in overcoming holdout without a heavy dose of eminent domain. Property owners are empowered to decide whether to sell their property to the government with a supermajority vote at two distinct stages in the project, while subjecting the dissenting minorities to eminent domain. Invited takings differ from private techniques for land assembly by implementing equal treatment and transparency within the group of property owners. It also deviates from conventional wisdom by allocating a substantial portion of assembly surplus to property owners. Such a strategy was made possible and attractive with certain background institutions as a response to limited local government revenue, such as debt financing provided by a wide range of residents, directly linked to specific land assembly projects. Finally, it better aligns costs and benefits of land assembly, shedding light on institutional design for other developing countries. For the first time within and outside of China, this Essay provides a systematic description and analysis of invited takings, based upon information on 23 invited taking projects that occurred in eight provinces and two provincial-level cities in China over the past ten years.

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I. INTRODUCTION

Throughout the world, land assembly is necessary for more efficient use of land, economic development, and the improvement of living conditions and infrastructure. However, holdout by property owners can prevent efficient land assembly, causing devastating and long-lasting problems, especially in the developing world. Consequently, urban slums and vulnerable infrastructure remain widespread, causing misery to the lives of hundreds of millions. Moreover, it reduces the value of and causes nuisance to surrounding areas. Compared to the developed world, private costs to holdout are lower in the developing world, causing more substantial and longer-term harm. Unfortunately, eminent domain and private purchase, which are the two conventional solutions to holdout, are of little help. Secret purchase, the most common technique used in private purchase, is generally too costly (if feasible at all) for large-sized groups, thus deterring private assemblers. The exercise of eminent domain power, meanwhile, has long been abused and has been associated with violence and corruption due to loose institutional supervision and scrutiny, which, in turn, causes resistance among citizens and reluctance among officials. As a result, local government developed systematic inertia in using eminent domain, which inevitably prevented the efficient assembly of land.

During the past decade or so in China, a new model of land assembly has emerged with respect to urban redevelopment projects (“URPs”), which I define as “invited takings.”¹ It developed as a local government practice that spontaneously responded to the deadlock caused by serious holdout and government inertia in using eminent domain. URPs involve building new or replacing old and poor infrastructure to provide decent housing and to improve the overall look of cities. It is a typical scenario of a “thin market” closely resembling the situation of one wanting to buy adjacent land to expand an existing site and thus justifying the use of eminent domain power.² But eminent domain has become too risky for local officials to use because of widespread conflicts and complaints about past practice. Use of secrecy has been suggested as an alternative in such a setting,³ but the government can

1. In official documents and media reports, it is often referred to as “taking simulation” (模拟拆迁) in renewal of old town (旧城改造 or 棚户区改造). But we believe that the current term of “invited taking” would capture the features of such arrangements and practices—especially their voluntary nature—more accurately. In China, land is divided into two systems: rural land owned by collective communes and urban land owned by the state. Invited takings only refer to takings of real property on urban land.

2. Thomas W. Merrill, *The Economics of Public Use*, 72 CORNELL L. REV. 61, 75–77 (1986) (describing a situation where the target adjacent land was in poorer condition with lower value and the buyer’s property was in a better condition with a higher value).

3. Sanford J. Grossman & Oliver D. Hart, *Takeover Bids, the Free-Rider Problem, and the Theory of the Corporation*, 11 BELL J. ECON. 42, 43 n.3 (1980) (“In the case of real estate, this ‘unexcludability’ is avoided by the use of secrecy . . .”).

hardly hide the location of URPs or the buyer's identity in the way that private developers can.

Under invited takings, the government would not make a purchase offer or start the associated preparatory work unless and until it has been "invited" by a supermajority of property owners in a given community. Once this supermajority has been obtained, the government would make a real offer to purchase, which, however, would not become binding unless and until another supermajority of the same group of owners accepted the offer by entering into a standard form compensation agreement with the purchasing government. If the second supermajority is obtained within the set deadline, the government would be entitled to exercise eminent domain power over the silent or dissenting minority. If the government fails in obtaining the second supermajority consent, the offer would lapse and the existing property owners' title would remain intact. In most invited takings about which I have information, a supermajority at the second stage was reached and the possessors vacated the land rather quickly.⁴ The conflicts, complaints, and litigation usually associated with the use of eminent domain are almost absent in the case of invited takings. Even the government in Shanghai, one of the most developed cities in China, mandated the core institutions of invited takings be used for a wide range of URPs.⁵

Supermajority voting unleashed the power of autonomous and collective decision-making of owners whose interests are most affected by the decision. Unlike the individualized treatment that is the paramount feature of secret purchasing, supermajority voting operates like a tender offer, providing everyone with a uniform compensation standard and with transparency. Insiders lost no incentive to rush to approve the invited taking offer to receive the benefits: if insiders wait like everyone else, a serious holdout problem would occur and the benefits of the invited takings would dissipate. It also discouraged people from holding off on voting in order to receive a premium price, because that would upset those who voted earlier and unravel the whole process. Invited takings thus help deter corruption and conspiracy between officials and individual owners, which eventually increases the legitimacy of a potential exercise of eminent domain power. It also successfully switched the focus of judicial review from substantive issues of use and amount of compensation to procedural issues, for which rules are more specific and evidence is more straightforward. This feature radically reduces both decision costs and the error rate of judicial review. In terms of inducement and

4. See *infra* Appendix: Summary of Invited Takings Projects in China (including data that shows it is common for hundreds or thousands of households involving tens of thousands of individuals to move out in just a few months).

5. Shanghai Municipal Government (上海市人民政府), Several Opinions on Development of Urban Redevelopment Projects (关于进一步推进本市旧区改造工作的若干意见) (2009) [hereinafter Shanghai 2009 Rules], available at <http://www.shanghai.gov.cn/shanghai/node2314/node2319/node10800/node11407/node22592/userobject26ai17516.html>.

deterrence, invited takings are also rather unique. The poor living conditions and infrastructure may have caused life of property owners whose properties are to be taken—similar to the community described by Parchomovsky and Siegleman, which was the town of Cheshire and located near a polluter—where the potential costs of staying were prohibitively high due to the pollution⁶ and the danger of “remaining in a town stripped of most of its amenities by the departure of many of its residents.”⁷ However, the owners under invited takings are not facing the same liquidity problem that residents in Cheshire suffered,⁸ because the rental income is likely staying stable, and the market price of housing is likely to keep rising along with the value of the surrounding property. One thing that seems to matter in all cases is the dominance of the state as an employer, given that the state is also the purchaser under invited takings.

To be sure, it is not a new invention to use supermajority consent and a mandatory buyout of the minority group when facing the delay and dissent of minority members of owner groups in an urgent circumstance. Tender offers are a long existing and successful application of such a mechanism. “Yank the bank” provisions in syndication loans are also a close cousin. These provisions allow a borrower to buy out minority lenders at par, if the supermajority of lenders has approved a waiver or amendment to the original loan agreement. In the area of real property law and land regulation, scholars have previously proposed similar mechanisms as a substitute to unanimity consent or government decisions for large groups of property owners. For example, Professor Colwell has proposed using the tender offer mechanism as a substitute to government zoning.⁹ Professors Heller and Hills envisioned Land Assembly Districts (“LAD”) as a replacement of government takings in certain qualified circumstances.¹⁰ Apparently, the same attempt to modify standard private property rights was successful for some, such as shareholders of public companies and syndication loan lenders, but not so for real-property owners except for invited takings. Two reasons may help explain the appeal of invited takings to local government: (1) it exerts less coercion over the

6. Gideon Parchomovsky & Peter Siegelman, *Selling Mayberry: Communities and Individuals in Law and Economics*, 92 CALIF. L. REV. 75, 111 (2004) (“To residents with children, the potential cost of staying was simply prohibitive. But leaving was also difficult or impossible.”).

7. *Id.* at 115–16.

8. *Id.* at 111 (“The residents faced a real-world liquidity constraint . . .”).

9. Peter F. Colwell, *Tender Mercies: Efficient and Equitable Land Use Change*, 25 REAL EST. ECON. 525, 525–27 (1997) (introducing the following advantages of a tender offer system: simplicity in implementation instead of amending the constitution, equity, and efficiency).

10. Michael Heller & Rick Hills, *Land Assembly Districts*, 121 HARV. L. REV. 1465, 1469 (2008) (introducing the concept of Land Assembly District: “persons who hold a legal interest in a neighborhood’s land should *collectively* decide whether the land ought to be assembled into a larger parcel . . . [P]roperty law can retrofit a community with a condominium-like structure tailored to solve the problem of land assembly.”). For more details of the institutional design of LAD, see *id.* at 1483–97.

minority compared with a tender offer; and (2) it is less vulnerable to potential abuse by agents compared with LAD. Even though invited takings are not completely immune to government manipulation, similar to the problem of partisan gerrymandering,¹¹ this Essay demonstrates that the risks are lower in China compared to developed countries.

The ultimate attractiveness of invited takings to property owners lies in the fact that a substantial portion of the assembly surplus is allocated to property owners, contrary to conventional belief and institutional arrangement. Heller and Hills raised doubts about the three reasons used to object to allocating assembly surplus to property owners, namely administrative costs, distributive justice, and corrective justice.¹² This Essay demonstrates that these concerns are substantially mitigated in the circumstances of invited takings. The administrative costs in calculating assembly surplus were decreased by a fast developing real estate market, in which hypothetical post-assembly housing on the same land is easily available. Corrective justice is also accounted for because the improvement over existing in-kind housing benefits is less like a windfall. Distributive justice concerns are also substantially eased by the fact that such allocation is not a pure wealth transfer from taxpayers to property owners. Instead, a broader range of entities benefiting from the invited takings are brought to share the burden of costs, including bond investors and real estate consumers related to the post-assembly projects,¹³ better aligning costs and benefits of specific invited taking projects.

A seemingly viable solution to holdout problems that is affordable, effective, and attractive to the local government, invited takings may provide an example for other developing countries and even some developed regions to follow to combat the delay of urban development due to serious holdout. The institutional arrangements for overcoming strategic holdout problems in land assembly are documented, and the implications of those arrangements are explored in this Essay. As of October 12, 2014, I have collected public information on 23 invited takings projects, by reviewing media reports,¹⁴

11. To speed up the process in obtaining supermajority consent and paying less, there is a possibility that the government may manipulate the boundaries between low-market-price communities and high-market-price communities to make sure that the low-market-price-community members would become the supermajority in a given project. For a general introduction to problems associated with partisan gerrymandering, see generally Adam B. Cox & Richard T. Holden, *Reconsidering Racial and Partisan Gerrymandering*, 78 U. CHI. L. REV. 553 (2011).

12. See generally Heller & Hills, *supra* note 10.

13. Under Chinese law and practice, the state exercises the function of owner and zoning within one system. When it grants a long-term tenancy over a given lot of land, it charges a lump-sum fee in return, which is calculated according to the specific use purpose and term of the tenancy.

14. These reports were identified through searches in a leading Chinese social science and news database (<http://www.cnki.net>), dated as of October 12, 2014. By using the Chinese key words corresponding to “taking simulation” (模拟拆迁) and combined a search of “takings” (拆

government guidelines, and project documents. For three out of the 23 projects in the cities of Jiaxin, Wenzhou, and Chengdu, I conducted field studies and interviewed relevant parties.¹⁵ For two of these projects in Shanghai, I relied upon information reported by a legal scholar who verbally reported at a conference on his site visits and interviews of local officials and property owners.¹⁶ These 23 projects took place from 2004 to 2014¹⁷ in eight provinces and two provincial-level cities in China. A summary of these projects is included in the Appendix at the end of this Essay. In interpreting the information that I collected about these 23 projects, I took into account verbal reports and analysis made at a closed-door conference by a practicing lawyer and a couple of judges in Shanghai who claimed to have worked on similar projects in Shanghai.¹⁸ The practice in Shanghai and the underlying rationale, as described by the lawyer and judges, is consistent with what has been reported about invited takings as practiced in other places in China.

Part II of this Essay sets out the challenge posed by using eminent domain or private techniques to assemble land for URPs, especially in the developing world. Part III lays out the institutional features of invited takings based on the practice in China. Part IV draws comparisons between tender offers and LAD, emphasizing coercion of the minority and potential abuses by government agents. Part V addresses the allocation of assembly surplus under invited takings, its justification, and the grounds for its feasibility. In a brief conclusion, the spontaneous nature of invited takings is emphasized, and I call for confidence and trust in rational individuals in creating welfare-enhancing institutions.

II. HOLDOUT IN LAND ASSEMBLY AND SPECIAL CHALLENGES FOR DEVELOPING COUNTRIES

Land assembly for URPs is particularly vulnerable to the holdout problem. Daniel Kelly rightly pointed out that “[t]he existence of strategic

迁) and “supermajority” (多数), I identified these projects after deleting duplicates and apparently irrelevant reports. I believe this is a rather exhaustive search of such projects on media reports and potentially academic discussions of such projects, even though I did not identify any academic piece on this topic. I noticed a media report of 12 more invited takings projects in the Sichuan Province, but I could not obtain further information about them. I, therefore, did not include these 12 projects in this Essay.

15. Due to time constraints, such trips and interviews were very brief and in many aspects generated more questions instead of finding answers to existing questions.

16. Mang Zhu, *Measure of “Public Interest” in Takings by Government of Housing on State-Owned Land* (国有土地上房屋征收过程中的“公共利益”的确认方式), Address at the Conference on Comparative Study of Taking of Land in China and the United States (中美土地征收制度比较会议) (Oct. 11–12, 2014) (on file with author).

17. For 3 out of the 23 projects, I tried, but failed, to obtain reliable information about when they took place.

18. The Conference was titled “Comparative Study of Taking of Land in China and the United States,” (中美土地征收制度比较会议) and was hosted at NYU Shanghai on October 11–12, 2014. Upon the requests of the lawyer and the two judges, I kept them anonymous in this Essay.

sellers, coupled with the lack of a mechanism for distinguishing between strategic and nonstrategic sellers, is the crux of the holdout problem.”¹⁹ To make it worse, even if we could try to separate non-strategic holdouts from strategic ones by using certain tools such as self-assessment,²⁰ the financial and administrative burden can become appalling when the number of property owners increase. Compared to the developed world, URPs in developing countries suffer more from the problem of holdout largely because more incidents are likely to occur and the resulting damage will be more severe.

Because they are in the process of developing, more URPs have been carried out and are in the pipeline in developing countries, usually in areas with high population density. For most property owners in the developing world, especially in East Asia, real property has quickly become one of the most valuable assets for residents.²¹ The financial benefit of resisting eminent domain thus can be extremely high. In places where private property ownership is a relatively recent phenomenon, such as in China, ownership and possession of private property is associated with social status and has political implications beyond the value gained from neighbors and the community. Meanwhile, it is reasonable to believe that the opportunity costs to hold out tend to be lower than in developed countries due to generally lower levels of individual income, thus inducing more individuals to hold out.

The overall damage of the failure of a project due to holdout can be roughly viewed as a function of the loss of marginal improvement for each household in terms of infrastructure and better neighborhoods in both financial terms and quality of life, multiplied by the size of the population involved. In developing countries, both factors are substantially larger, causing the overall damage of holdout to be much more substantial in the developing world. In developing countries, however, suspension and abandonment of URPs by government can be a matter of life and death for urban residents who are suffering from the effects of bad neighborhoods as well as rural residents who are moving to cities for jobs and a modern lifestyle.

19. Daniel B. Kelly, *The “Public Use” Requirement in Eminent Domain Law: A Rationale Based on Secret Purchases and Private Influence*, 92 CORNELL L. REV. 1, 19 (2006).

20. See, e.g., Lee Anne Fennell, *Taking Eminent Domain Apart*, 2004 MICH. ST. L. REV. 957, 995–96 (proposing a new system to ask people to give consent to sell the property at a given price in filing the tax form); Saul Levmore, *Self-Assessed Valuation Systems for Tort and Other Law*, 68 VA. L. REV. 771, 778 (1982) (“A self-assessed property tax system can be thought of as one that seeks to improve the accuracy and lessen the expense of subjective, institutional assessments by avoiding the futile quest for an elusive market value and relying, instead, on the owner’s internal value or reservation price,” which also illustrates that the usual problem of getting a lie from self-assessment can be overcome by penalty on over-statement and under-statement. (footnote omitted)).

21. See Haibin Zhu, *The Structure of Housing Finance Markets and House Prices in Asia*, BIS Q. REV., Dec. 2006, at 55, 60 tbl.1 (noting that the ratio of mortgage debt to GDP in 2005 was 10% for China, 44% for Hong Kong, and 61% for Singapore). Given that many housing purchases in China were settled in cash instead of loans, the actual ratio of real property to GDP might be even bigger.

The two conventional tools for resolving holdout are private techniques and eminent domain. In the developing world, unfortunately, these two tools prove more difficult and costly to implement.

A. *PRIVATE TECHNIQUES: CHALLENGE FROM LARGE-SIZED GROUPS*

In both the United States and in the developing world, real-estate developers have been reported to have successfully assembled land with various techniques. Secret purchases, combined with signing bonuses and other private techniques, have proven effective even in certain metropolitan areas involving a substantial number of owners.²² However, this technique is likely an ineffective tool for the government, especially for URPs in China and other developing countries.

The difficulty in keeping a land purchase secret necessarily increases as the number of people involved goes up. Projects involving 300 to 500 owners are apparently regarded as unusually large and rare in the United States.²³ However, a few hundred owners are the norm for URPs in the developing world, and the number can easily reach into the thousands. It thus takes much longer to bargain and to reach a compensation and settlement agreement with owners, resulting in more legal fees and opportunity costs for the government. When a larger group of owners is involved, the government also must pay much more to obtain confidentiality covenants.

The cost of enforcing contracts in general (and confidentiality covenants in particular) is also normally much higher in the developing world, largely due to the lack of supporting legal institutions and best practices in the market. When enforcement is weak and ineffective, it is simply useless to use high liquidated damages to deter breaches. The widespread custom for employees to share with each other the details of compensation packages is a vivid example of the difficulty in preventing breaches of confidentiality obligations in developing countries. In addition, it can be politically unpopular for a government to pursue its own citizens in a lawsuit for money damages, especially when almost all of the property owners involved in URPs are individuals. Moreover, URPs are, by definition, projects involving a less-developed area, where disadvantaged individuals are likely to reside. These individuals are unattractive targets for enforcement actions. Finally, property owners often have a special tie with the state, and these relationships are likely to make the government reluctant to take enforcement action against them. For example, some property owners in the invited takings projects recorded

22. Kelly, *supra* note 19, at 24 (citing land assembly in West Palm Beach that “needed only nine months to purchase over 300 separate parcels from 240 different landowners” (internal quotation marks omitted)).

23. Brief for John Norquist, President, Congress for New Urbanism as Amicus Curiae Supporting Petitions, at 16, *Kelo v. City of New London*, 545 U.S. 469 (2005) (No. 04-108), 2004 WL 2811055; see also *id.* at 5 (discussing Las Vegas’s private sector acquisition of 2400 acres of land).

for this Essay received title to housing as in-kind housing benefits due to their current or ex-employment by the state or state-owned enterprises.

B. EMINENT DOMAIN POWER: EITHER WILD OR DEAD

Eminent domain is both costly and time-consuming with respect to large groups. Moreover, political processes can play a critical role in the use of eminent domain power in China as well as in the United States. The condemnation of land for building Chicago's expressways illustrated how complex the political economy aspect of an exercise of eminent domain can be in the United States.²⁴ Even though the United States has a longer and much stronger tradition of protecting private property, disadvantaged property owners can be exploited during a physical taking.²⁵ In developing countries, unchecked political processes have caused even worse abuse and more associated corruption. In China, for example, the caps on compensation legally mandated for government takings of arable land owned by collectives of farmers have long been regarded as ridiculously antiquated and undoubtedly too low.²⁶ The abuse of eminent domain power has long been the most hotly disputed subject in administrative litigation and the petitioning system, the two formal channels in China for addressing disputes regarding government decisions. In certain circumstances, the conflicts between property owners and the government became so fierce that owners set themselves on fire in public to protest alleged predatory takings of land and housing.²⁷

The conventional check on eminent domain power is judicial review. In China, however, it seems to play a limited role in curbing or deterring abuse by the government on the one hand, or in resolving the deadlock caused by holdout on the other. Judges tend to skip independent assessments of the "public interest" test and defer heavily to zoning decisions made by the government.²⁸ The finality of a judicial decision is threatened by weak enforcement and various statutory channels through which the losing party can reopen the case. While the gains from using judicial procedures to resolve holdout are limited, the potential costs of the same procedure are extremely

24. See Nicole Stelle Garnett, *The Neglected Political Economy of Eminent Domain*, 105 MICH. L. REV. 101, 110–21 (2006).

25. Saul Levmore, *Just Compensation and Just Politics*, 22 CONN. L. REV. 285, 305–08 (1990).

26. See Ruoying Chen, *Informal Sales of Rural Housing in China: Property, Privatization and Local Public Finance* 37 (June 2010) (unpublished J.S.D. dissertation, University of Chicago), available at <http://gradworks.umi.com/34/08/3408511.html>.

27. See, e.g., Geoff Dyer, *After Protests, China Restricts Seizure of Land for Redevelopment*, WASH. POST (Jan. 30, 2010), <http://www.washingtonpost.com/wp-dyn/content/article/2010/01/29/AR2010012902990.html>.

28. This has been an anecdotal report and was confirmed in interviews conducted by the author on October 11 and 12, 2014. Interview with two judges, Shanghai High People's Court, and two lawyers, Shenzhen & Shanghai, in Shanghai (Oct. 11–12, 2014) [hereinafter Shanghai Interview].

high for officials. For courts, litigation and enforcement action against property owners can be costly, especially because the performance of individual judges and courts are measured by incidents of resistance to enforcement, appeals, petitions, and complaints by property owners who lost their case. Courts have rather strong incentives to reduce these incidents by proactively helping the government persuade property owners to accept offers and to refine documents and procedures to be used by the government.²⁹

In response to the brutal exercise of power by local officials and costly judicial review, farmers in China took a smart preemptive action to reduce and even eliminate the possibility of the government using eminent domain power. Often in collaboration with private developers, farmers built and informally sold a large amount of housing units to urban residents, which are otherwise not allowed by law, because the underlying land must first be converted to state-owned land through a government taking.³⁰ The practice became extremely popular in all major cities and was reported to have accounted for more than one-third of the overall housing market for urban residents at one point, largely because the price was only a fraction of the prevailing market price for housing with proper title.³¹ So far, these urban “owners” cannot obtain formal title issued by the government and cannot receive loans to finance the purchase or capitalize on it. Such restrictions, however, did not deter urban residents from buying the informal housing as their residence or from collecting rental income. The coalition forged between the weaker rural residents and the more powerful urban residents substantially delayed and even stopped takings by the government.

III. INVITED TAKING BY THE GOVERNMENT IN CHINA

Invited takings seemed to have provided a solution to resolve serious holdout without a heavy dosage of eminent domain. Hundreds and even thousands of property owners often happily vacated their property within months, without any substantial conflicts with officials. For example, the government in Shanghai, the financial center and market engine of China, even passed rules to formally recognize and recommend the practice of

29. See for example, a news report on the official website of a local court, Lin He District Court in Inner Mongolia (内蒙古自治区巴林卓尔市临河区法院). Network Mgmt. Publicity Bureau, *Kanawha Court Escort for Demolition Work*, CHINACOURT.ORG (Mar. 25, 2011), <http://lhqfy.chinacourt.org/public/detail.php?id=307>.

30. Chen, *supra* note 26, at 60–68 (introducing the development of market of sale of informal property on rural land in all major cities in China); see also Shitong Qiao, *Small Property, Big Market: A Focal Point Explanation*, 63 AM. J. COMP. L. (forthcoming 2015), available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2399675.

31. Chen, *supra* note 26, at 2–3 (citing *A Comprehensive Underground Market Has Developed into Good Shape and the Petit-Title Housing in Shenzhen Has Formed One Chain of Development*, YANGCHENG NIGHTLY (June 14, 2009), http://www.ycwb.com/ePaper/ycwb/html/2009-06/14/content_520891.htm).

invited takings.³² Urban redevelopment was quickly put into place, creating better facilities for modern life, such as subways, shopping centers, public institutions, and better residential buildings. For more than a decade, more and more cities in China applied this new technique of land assembly. It is thus worthwhile to investigate the institutional details that seemingly produced successful land assembly.

A. *SUPERMAJORITY CONSENT IN TWO STAGES*

Under invited takings, the government is entitled to exercise eminent domain power when certain supermajority consent is obtained at two consecutive stages. In the first stage, the government must receive consent from a supermajority of property owners to initiate the purchase. This first supermajority is a pre-condition the government must satisfy to start preparatory work for the potential purchase, such as measuring, evaluation, and preparation of offer documents. Failure to get this first supermajority means the government gives up the initiative and the property owner's title remains intact. In other words, if the government fails to receive an "invitation" from a large enough group of property owners, it will not have a chance to proceed further. The invitation often takes the form of signatures of property owners. Without any information on price or any other critical term for a potential purchase, the invitation is not binding on either side. The whole process is, thus, best viewed as a mechanism to uncover information on owners' willingness to sell, which helps the government better allocate public funds and other resources.

Once the government obtains the first supermajority, it then proceeds to prepare and make an offer of purchase. The coordinating mechanism is a contingent form contract, which does not become effective unless and until a supermajority of owners enter into the agreement by a specific deadline. If the supermajority requirement is not met by this deadline, the offer lapses, leaving both the government and property owners free from any obligations. In practice, it is not uncommon for the government to give up a proposal plan due to a failure to meet this requirement. For example, among the ten invited projects carried out in Sichuan Province as of April 2011, four projects failed due to exactly this reason.³³

It is noteworthy that the supermajority threshold is close to unanimity in both stages. Among the 23 projects addressed in this Essay, most required a threshold of higher than 90%. Some even required unanimity. Given that these projects involved rather large communities and the speed of completion was rather impressive, it begs the questions of what unique mechanisms have

32. See Shanghai 2009 Rules, *supra* note 5.

33. Liang Xiaoqin, *House Demolition is Not Removed, the Owners Have the Final Say*, PEOPLE'S DAILY (Apr. 29, 2011, 12:00 AM), <http://politics.people.com.cn/GB/1026/14511620.html>.

been used to persuade and induce consent, and what deterrence strategies were deployed to discourage against holding out.

B. TRANSPARENCY AND UNIFORMITY

The use of form contracts distinguishes an invited taking from conventional private techniques for land assembly in one major way. For secret purchases, providing discriminatory prices and obtaining and enforcing confidentiality covenants are the keys to success. To resolve the last holdout without being able to use coercion, the private assembler needs to offer a price potentially much higher than the prices already accepted by other owners. For it to work, confidentiality obligations are imposed and enforced to prohibit owners who already agreed to sell from sharing information about their own deal with potential sellers. With respect to owners who already agreed to sell, the confidentiality obligation and associated penalty lowers the likelihood of a breach of contract and requests to renegotiate for a higher price. With respect to potential sellers, keeping price and other major terms secret makes it more difficult to calculate the potential gains and losses of holding out, reducing the chances of a successful holdout.

Under invited takings, however, discriminatory pricing and confidentiality are replaced with their opposites: equal treatment and complete transparency. The government takers oblige themselves to calculate compensation according to the size of each housing unit and apply the same level of compensation, relocation assistance, and bonuses to all owners in a given project. Such information is announced upfront, updated in real time, and eventually becomes part of the compensation contract between the government takers and each individual owner. To ensure compliance, the government takers even promise to reward whistle-blowers who identify a breach of the obligation of equal treatment and transparency.

This institutional arrangement serves at least three functions, which help speed up the acceptance of the takers' offer and reduces conflicts: (1) revealing information to keep unreasonable holdout in check; (2) triggering persuasion within the owner group; and (3) resolving potential abuse or corruption by government officials in charge of takings.

This mechanism provided a clear benchmark for owners in deciding whether or not to hold out, forcing them to be more realistic about the probability of success in holding out. This reduces the incidents of unreasonable holdout. Similarly, as the percentage of owners accepting the offer increases, transparency shows the equal treatment of owners, thus increasing the legitimacy of the offer. This puts pressure on holding-out parties to take the offer because the benefits that others expected may suddenly vanish if the last few owners refuse to take the offer. Meanwhile, the earlier the supermajority threshold is reached, the sooner the early-bird property owners receive real cash. Once the information regarding who is

holding out reaches the neighborhood, property owners may carry out an easy cost-benefit analysis in deciding whether or not to use private information and resources to persuade their neighbors to enter into the same contract.

Such an institutional arrangement can also be understood as a strategy to resolve the government's problem in controlling the behavior of officials of the same government and officials of lower government: showing the government agency's credibility by self-binding.³⁴ In a traditional setting, when one or a few holdouts remain, agents of either private or government takers may have strong incentives to "bribe" the last holdout. This, however, destroys the credibility of the offer and invites people who accepted earlier to breach, leading the almost-completed process to unravel. Even if the bribe is a success, the overall cost of the purchase increases as a result, and sometimes the project even becomes unaffordable. Bribing holdouts also encourages conspiracies between officials and certain property owners to delay solely for the purpose of obtaining and sharing the "bribe," which causes serious moral hazard and wastes public funds. By enforcing transparency, similar to the equal treatment requirement in a tender offer, the government could successfully prevent officials from overpaying property owners and taking kickbacks, thus reducing the likelihood of successful holdout.

C. BONUSES FOR SIGNING AND MOVING OUT

The second technique widely used in invited takings to encourage offer acceptance is the use of bonuses to induce owners to accept and move out quickly. The idea to use fixed-percentage bonuses when property is taken by eminent domain was long ago proposed by scholars like Richard Epstein,³⁵ but the practice of it has not been seen in the United States. Under invited takings, the amount of bonuses offered by the government took the form of a lump sum available to all owners, payable upon signing the sales and compensation contract and vacating the land. The bonus can be as high as 30% of the housing value. The earlier that one enters into the agreement and moves out, the larger bonus one can get. Those who refused to take the offer would lose the chance of receiving any bonuses. In one project in Shanghai, 11 out of approximately 200 owners did so and litigated in court the government's decision to use eminent domain power on dissenting minority owners in a successful invited taking in court.³⁶ The court affirmed the condemnation decision based on the government's compliance with the

34. Eric A. Posner & Adrian Vermeule, *The Credible Executive*, 74 U. CHI. L. REV. 865, 868 (2007) (introducing the various "mechanisms . . . that [executives may use to] send a signal of credibility by committing presidents to [certain] actions or policies that only a well-motivated president would adopt").

35. RICHARD A. EPSTEIN, *TAKINGS: PRIVATE PROPERTY AND THE POWER OF EMINENT DOMAIN* 184 (1985) (discussing fixed-percentage bonuses such as the 10% bonus used in England).

36. One of the two projects of invited takings in Shanghai (东园坊项目) was reported by Professor Mang Zhu. See Zhu, *supra* note 16.

supermajority consent rules and the fact that the compensation offered by the government was above the statutory requirement. However, the compensation awarded by the court did not include any bonuses.³⁷ This forces an owner to recognize that she has little leverage against the government, making her more willing to sell.³⁸

D. GOVERNMENT AS INFORMATION EXCHANGE AND NEGATIVE COMMUNITY EXTERNALITY

Negotiation of compensation packages is an indispensable part of both private and public land assembly. In the United States, “[s]tate and federal laws require Takers, in most instances, to seek to purchase property on the market before resorting to eminent domain.”³⁹ Under invited takings, the parties carrying out negotiation, and the reasons used to persuade and coerce owners to accept offers are different from those in land assembly by a private entity or by the government through the exercise of eminent domain power.

In a secret purchase by a private land assembler and takings by the government with eminent domain, the land assembler is the party on one side, negotiating with each owner on the other side. Under invited takings, however, once the government announced the terms of the offer, it retreated from negotiation. This leaves property owners to decide whether or not to take the agreement, and more importantly, it leaves owners to persuade each other among themselves.⁴⁰ As such, it is no longer one party to the negotiation, standing opposite to the property owners. Instead, it becomes more or less a neutral information exchange, keeping all owners updated on details of the offer and to what extent the offer has been accepted by others. In such a process, instead of a potential buyer persuading sellers, persuasion and coercion are carried out by different entities, including other owners in the neighborhood, street-level officials,⁴¹ state employers of some property owners, sellers’ relatives, and members of the community of a much broader scope.

For group members to negotiate with each other, the existence of some degree of interdependence and shared values would generate more success

37. See *id.* This decision and the underlying rationale were confirmed as a standard practice in Shanghai by a judge from the Shanghai High Court, as interviewed by the author. Interview in Shanghai, *supra* note 28.

38. See Henry E. Smith, *Property and Property Rules*, 79 N.Y.U. L. REV. 1719, 1770–72 (2004).

39. Garnett, *supra* note 24, at 126.

40. Zhu, *supra* note 16.

41. This term refers to staff of *Jie Dao Ban Shi Chu* (街道办事处) and *Ju Wei Hui* (居委会). Their offices are located in the community, and many of the latter are retired owners of property in the community. Due to the long-term physical proximity and the dual identities as owners as well as officials, they often possess detailed information about the history and current status of owners in the community and may possess private resources that can be leveraged upon property owners in the community.

in negotiation. The unanimity and supermajority requirement under invited takings does create some degree of interdependence among owners in a given project: the expected benefits from the sale will not be realized unless and until all or most other owners agree to sell. The owners also shared the same goal of either living in a better neighborhood or increasing the value and liquidity of their housing property. Because they are of a purely economic nature, such interdependence and shared values are likely a rather weak force, which can be easily offset by economic interests in holding out.

A potential alternative to unity and persuasion is the so called “community externalities,” which was the proposed explanation of the successful buyout of the whole town of Cheshire by the American Electric Power Company. Strong interdependence among the costs and benefits of village residents in the decision of staying or leaving the place was proposed as the explanation as to “why essentially everyone in the village decided to sell,” even though bargaining with groups usually “leads to holdouts and other high transaction costs.”⁴² Under invited takings for URPs, however, the potential community value can be extremely low. Non-monetary interdependence, such as friendship and a unique memory of family history, were largely absent in invited takings. Constant frictions and even-conflicts often dominated the history of the community. These neighborhoods tended to be extremely crowded and became more uninhabitable due to poor conditions of shelters and facilities. High density created two types of constant frictions and even-conflicts. The first type is nuisance on a daily basis, including the building of shelters and facilities in private areas.⁴³ The second type results from fights for temporary or permanent possession of limited common and public areas. Uncoordinated building of various temporary constructions and shelters in the public and common space became a common occurrence. Legal and governing rules dealing with such issues were lacking and property management was near absent;⁴⁴ life in such a community could hardly generate warm feelings within the community, leaving actually negative community externality.

In other circumstances, the residents in a given invited takings project were almost all tenants, who had no legal title justifying compensation under law or common practice. URP housing is usually located in prime locations in the heart of cities, naturally attractive to tenants for residential and commercial purposes. When the individual housing and neighborhoods

42. Parchomovsky & Siegelman, *supra* note 6, at 82.

43. Information was collected through interviews, which is also verified by numerous novels, soap operas, and movies about such neighborhoods. See, e.g., *Garrulous Zhang Damin's Happy Life* (Pinzui Zhang Damin de xingfu shenghuo) (2000).

44. Under the invited takings projects, owners often obtained title as an in-kind housing benefit as employees of the same employer. When the control and management through employment was weakened and even completely vanished, property rules or property management was not put into place instead, creating a status without order.

became extremely uncomfortable for habitants, rational property owners⁴⁵ chose to rent out their property to low-income residents, especially rural migrant workers. These property owners, thus, had no direct contact with residents in the neighborhood and derived no value from the community, other than the economic value of the rental income. Worse still, the lasting and increasing possession of properties by low-income migrant workers on a more or less temporary basis accelerated the deterioration of the quality of living in such neighborhood, making it even less attractive for landlords to move back or for other owners to stay. We, thus, need a more nuanced interpretation as to why invited takings proved attractive to both property owners, especially minorities who are prone to holdout, and the local government, who generally pays a price well above the statutory standard.

IV. TREATMENT OF MINORITIES: COMPARISON WITH TENDER OFFER AND LAD

The combined use of supermajorities and the principles of equal treatment and transparency sounds very similar to one well-established institution and one academic proposal for a new institution, namely tender offer and LAD. In comparing invited takings with tender offers, we need to address concerns regarding coercion of the minority, to which tender offer is vulnerable. Meanwhile, the difference between invited takings and LAD is straightforward: invited takings are not a creation of scholars but a spontaneous arrangement put into place by various parties whose interests are dramatically affected by delayed land assembly. External constraints that local officials face differ dramatically in China as compared to the United States, but there are shared goals and concerns, which seem to have been addressed by invited takings, especially the treatment of the dissenting minority.

A. LESS COERCION: COMPARISON WITH TENDER OFFER

In the finance market, supermajority consent has long been used as a substitute to unanimous consent among large-sized groups. The “Yank-a-Bank” provision⁴⁶ in syndication loan documents and tender offers for shareholders of public companies are two typical examples. One critical concern regarding tender offers is the coercion imposed upon the minority,

45. The term “owners” also refers to registered tenants of housing owned by certain state employers, because there is no difference between registered owners and registered tenants in terms of their right of possession for the purpose of the discussions in this Essay.

46. Under this provision, if a lender refuses to approve an amendment or waiver (among other things) when a supermajority of the lenders has approved it, such as 66% or 75%, the dissenting or silent lenders can be bought out at par and be forcibly removed from the lending group. After the credit crunch of 2008, the supermajority threshold in such provisions has increased. See, e.g., *Syndicated Lending Update: Defaulting Lender Issues*, BRACEWELL & GIULIANI (Oct. 28, 2008), <http://www.bracewellgiuliani.com/news-publications/updates/syndicated-lending-update-defaulting-lender-issues> (discussing the yank-bank clause and its drawbacks).

as pointed out by Professors Brudney and Chirelstein.⁴⁷ The supermajority requirement coupled with the possibility of condemnation of the minority contains a threat not to buy at all, or to buy at a lower price in the future.⁴⁸ Under invited takings, property owners face exactly the same future prospect: if they insist on holding out and, therefore, fail the supermajority or the unanimity requirement, the government would walk away and the property owners would lose the opportunity to sell the property. Such a possibility has occurred, leaving many property owners outraged at their neighbors who refused to sell.⁴⁹ Even if they could hope that the government will come back due to negative externalities imposed upon a nearby area, there is no guarantee that the price would be the same or higher, because real estate prices could go up or down and the government is subject to budget constraints. Such a prospect may, therefore, pressure property owners to sell at a price lower than their true evaluation of the value of their property. Invited takings are not immune from such a concern. But the coercion is mitigated by a few factors which are not present in a tender offer.

A public company and the potential purchasers of its shares hardly know information about the identity of the company's shareholders, except for a few large shareholders. Therefore, it is prohibitively expensive to try to bargain with individual shareholders and adjust the offer so that it could extract consent from the largest number of shareholders. Such bargains and adjustment, however, are feasible under invited takings because the identity of and the process of contracting with each owner are completely transparent to the potential buyer and all other owners. The second factor is the lesser degree of price fluctuation. In the tender offer context, share price can go down dramatically in a second. However, this is unlikely to happen with real property. Moreover, the statutory price floor for coerced sales of real property at "fair market value" or its equivalent has limited the extent to which the future price could decrease, substantially mitigating the coercion effect. Finally, the prospect of a new offer is gloomier after a failed tender offer. Shares left unsold in the hands of shareholders in a failed tender offer normally impose no negative externality upon other entities, creating no incentive for anyone to make another offer at a comparable price soon. Under invited takings, however, the land left untouched in a failed invited taking would impose serious negative externalities on the government, surrounding

47. See Victor Brudney & Marvin A. Chirelstein, *A Restatement of Corporate Freezeouts*, 87 YALE L.J. 1354, 1357-58 (1978) (emphasizing the danger of coercion when the minority of the same class received different forms of compensation that the majority shareholders, such as cash instead of equity or debt in the surviving corporation).

48. See Lucian Arye Bebchuk, *Toward Undistorted Choice and Equal Treatment in Corporate Takeovers*, 98 HARV. L. REV. 1693, 1696 (1985) (discussing the concept of "distorted choice," in different terms).

49. See *supra* note 33 and accompanying text (stating that four out of ten projects in one region failed because the supermajority threshold was not met for the second stage).

property owners, and residents because such land is by definition underdeveloped and often full of urban slums. Over time, as more and more adjacent land was redeveloped with updated urban facilities, the value of the land left by a failed invited taking is more likely to rise relative to surrounding owners and the city. The more costs the land and associated community imposed upon surrounding neighbors and the city in general, the more likely it will eventually induce the government to come back to make another offer, presumably with a higher price to reflect the increased negative externality.

To be sure, both tender offers and invited takings are modifications of standard private-property rights, which need to be carefully justified even if they may look appealing in one or two aspects. In particular, we cannot turn a blind eye to the substantial difference between shareholders rights and real property rights. We, thus, need to make a more careful assessment of invited takings by comparing it with similar proposals specifically in the area of real property and land regulation.

*B. SHARED PHILOSOPHY AND DIFFERENT REACTION FROM GOVERNMENT:
COMPARISON WITH LAD*

Supermajority has been used as a substitute to a government decision, which is subject to judicial review. In the area of property law and land regulation, two other proposals are useful comparisons. One proposal is to use a tender-offer mechanism as a more efficient and equitable alternative to governing zoning.⁵⁰ The closer analogy is of course LAD, which is proposed as a solution to holdout in land assembly under certain circumstances.

Sharing with LAD a similar philosophy and certain features, the practice of invited takings provided a valuable chance and empirical evidence to test the effectiveness of the institutional design of LAD. Both LAD and invited takings respond to the hostility towards potential and actual abuse of eminent domain and aim to reduce the inefficiency caused by holdout. Moreover, Heller and Hills made it clear that LAD should not be applied in cases where the site is uniquely suited for certain purposes, such as building a highway or an airport.⁵¹ However, such a carve-out may not be necessary, as demonstrated by the successful implementation of invited takings in UPRs, often involving building subways and inter-city highways.

Another feature that the two regimes share is the collective autonomy of owners in deciding whether or not to sell, which increases the homogeneity

50. Colwell, *supra* note 9, at 526–27 (introducing a few measures to function as a tender offer system, which would improve equity and efficiency of zoning).

51. Heller & Hills, *supra* note 10, at 1470 (“By contrast, eminent domain still has a role to play where the problem is acquiring *unique* sites for traditionally public infrastructure—say, the only feasible site for a highway or airport or a uniquely noisome parcel of land.”).

of the group and prevents majority tyranny.⁵² The fact that owners in a successful invited taking received compensation above the statutory level provided strong evidence that LAD can bring about substantially more benefits to owners when they get to decide their own matters. Similarly, almost no owner involved in invited takings was known to have brought a lawsuit to challenge the decision to sell, providing strong evidence that the collective decision is a more autonomous and better choice for the minority. The strategy proposed in LAD and adopted in invited takings successfully diffused hostility toward eminent domain and avoided drastic limits on the local government's ability to assemble land, thus achieving land assembly without political fallout.⁵³

Such shared features apparently did not guarantee similar treatment to dissenting minority owners by the local government, in China or in the United States. The differences between LAD and invited takings are as numerous as their commonalities and may help explain the different reactions from local governments.

Examining the entire process of invited takings, it is clear that the government is not a pure invitee in the literal sense. Local planning authorities, investment authorities, and street-level officials must have been working on the proposed area for a long time, and the government's offers are often based upon suggestions and work product provided by private real-estate developers.⁵⁴ I have not seen any reports of successful invited takings purely initiated by property owners. In fact, there has been a report of rising complaints and conflicts resulting from a "rejection" by the government of an "invitation" of property owners for land assembly in China. Meanwhile, even though litigation over the refusal of the planning commission to create a LAD could potentially function as a check over the problem of underutilization,⁵⁵ no report of such litigation has yet been identified. Before assessing the potential value and feasibility of invited takings outside China, it is important to address the question of why LAD and invited takings received different reactions from the local government.

Three factors might shed light on this question: (1) the entity exercising the eminent domain power (the government itself versus the newly formed LAD); (2) distributive concern for the minority; and (3) the financial viability of granting assembly surplus to property owners. Invited takings seem to have fared better with respect to the first two factors. The last concern is largely

52. See *id.* at 1500–02 (explaining why the single purpose of LAD in helping property owners to sell, and at what price, or not to sell helps keep the homogeneity of the group, and why other institutions with multiple purposes would be at a "risk of majoritarian exploitation").

53. *Id.* at 1490 ("LADs redirect hostility about eminent domain away from politicians, allowing land assembly without political fallout.").

54. This seems the case, according to anecdotal evidence and interviews with managers of a number of domestic real-estate developers.

55. See Heller & Hills, *supra* note 10, at 1490.

eased because of the more diversified financing methods available to the Chinese local government, which will be addressed in detail in Part V below.

C. *ENTITY TO CONDEMN: AUTONOMOUS ORGANIZATION V. THE GOVERNMENT*

For LAD, the entity that would exercise condemnation power is the LAD. The LAD is a newly-formed autonomous organization, representing the choices of the majority owners. It has no track record and is subject to no institutional checks other than those to be set out in the charter creating the LAD. Until a LAD has actually been created, it is hard to predict what those details will be. Even though proposals have been made in this aspect, no existing institutions or individuals have had real experience in enforcing them, leaving more uncertainty as to how the LAD would carry out the substantive and procedural requirements of the land-assembly process. For courts, the natural candidate to carry out *ex post* review and to handle challenges from the minority, the LAD is a completely new type of entity. Even though invited takings are not immune from abuse or corruption by officials, LAD adds another layer of agents—individuals organizing and managing the LAD.

Under invited takings, however, the condemnation entity is the local government, if unanimity fails but supermajority is obtained. The local government has a long and solid track record in exercising eminent domain power. In modern society, the local government has long been subject to well-established external and internal checks on decisions and the enforcement of condemnation. Mature and experienced institutions and professionals have been put in place to safeguard the implementation of these checks, such as the court and judges in charge of reviewing the exercise of eminent domain power. It is natural for the local government to be sensitive to distributional concerns and to the complexity and problems associated with using coercion by a non-government entity, and it may not be as enthusiastic about LAD as it is for invited takings.

D. *TREATMENT OF MINORITIES*

Due to the heterogeneity in property owners' valuation, LAD may suffer the potential of underassembly and overassembly because it is only concerned about the medium owners' valuation.⁵⁶ Invited takings, meanwhile, may fair better in its ability to reflect the valuation of a larger percentage of property owners in a given group. Moreover, invited takings treat the dissenting minority better than LAD. Once a majority vote is obtained, the dissenting minority in the LAD context faces three scenarios: (1) participate and get their proportionate percentage of the bargained-for price; (2) opt-out and have their property condemned by LAD in exchange for fair market value; or

56. Daniel B. Kelly, *The Limitations of Majoritarian Land Assembly*, 122 HARV. L. REV. F. 7, 9–10 (2009).

(3) opt-out and be left outside of the sale. Under invited takings, meanwhile, scenario (1) is exactly the same and scenario (3) would not occur. Under scenario (2), minorities would receive a price between (1) and the statutory floor. In practice, the minority would still be able to get a share of the bargained-for price, and would only lose out on bonuses for signing and vacating the property. In addition, more owners could belong to the minority camp in LAD given that LAD requires only a simple majority instead of a supermajority, lowering the efficiency of the final decision to sell and the bargained-for price. It also raises more concerns of distributive justice among owners, because a simple majority, compared with a supermajority, leaves a smaller group of owners to share the surplus, creating a bigger gap between the minority and the majority in terms of the share of compensation. Similarly, under invited takings, the veto power of each owner is stronger than that in the case of LAD, giving the minority a much better chance to block the sale or to bargain for higher compensation.

E. RISKS OF MANIPULATION BY GOVERNMENT

Invited takings emerged as a spontaneous response by local government in front of serious holdout and the potential abuse of eminent domain. The rules and procedures of invited takings are more like voluntary contractual terms instead of binding legal requirements. With respect to judicial review launched by the dissenting minority owner in an invited taking, the court showed a high degree of deference to the local government. Once the court was satisfied that the supermajority voting procedures were in compliance with the terms announced by the government and included in the contingent form contract, it validated the takings by the government, without touching on the substantive issue as to whether the taking satisfies the requirement of “public interest” in China⁵⁷ or the United States’ equivalent criteria of “public use.” The lacking of review and supervision of local governments’ practice of invited taking may potentially invite two types of manipulation.

The thresholds for the two rounds of supermajority voting were unilaterally set by the local government, in the form of a requirement and general guidelines issued by the local government on invited takings and an announcement made upfront with respect to each specific invited taking project. Currently, the requirement ranges from 80% to 100%. We could imagine the danger that local government may start lowering the threshold when they see more and more successful invited takings with a relatively lower threshold. Such a move by the government would coerce more minorities and generally lower the total price offered to property owners. This risk cannot be completely ruled out unless some form of legislative or judicial mandate is imposed upon local government, which is currently absent in China.

57. As reported by Zhu Mang, *see* Zhu, *supra* note 16, and confirmed by a judge, *see* Interview in Shanghai, *supra* note 28.

Meanwhile, the magnitude of this risk might be lower than it first appears. We first need to understand why local governments in China voluntarily imposed supermajority (and even unanimity) requirement upon themselves in the first place, instead of using a simple majority (such as in LAD). One factor that may have restrained local officials from lowering the thresholds is the competition among local officials for promotion by higher authorities by reducing social conflicts and maintaining social stability. To lower the voting threshold in invited takings would generate more minority owners, potentially increasing the probability of complaints by property owners. This concern has apparently driven them to choose supermajority or unanimity in the first place. There seems no reason to believe that this competition would disappear in the near future. In essence, in requiring a higher threshold instead of a lower one, local officials are making a trade-off between two types of costs: costs on officials' promotion prospect and financial costs in paying property owners. The former is clearly born by individual officials. The financial burden, however, is on the government instead of individual officials. So long as officials could figure out a way to finance the invited taking, they would, for sure, prefer a higher voting threshold. Having said so, one possible way to mitigate such a risk is of course to require local government to announce the threshold for the second stage up front and make it binding on them.

The second potential manipulation by local government is similar to the concern for partisan gerrymandering, i.e., manipulate the boundary between neighborhoods to generate an artificial mix of high-value owners and low-value owners, which would lower the offer price and the overall costs. This is particularly of a concern, because the boundary of a given neighborhood subject to invited taking is often drawn by the government rather than being proposed by property owners.

This risk can be explained with the following example. Let's imagine that we have two adjacent neighborhoods. One is a high-price neighborhood where there are 50 property owners and 90% of them would accept an offer price at or above \$300. The other neighborhood is a low-price one where there are 450 property owners and 90% of the owners would accept an offer price at or above \$60 and the other 10% would accept an offer price at or above \$80. Let us also assume that the voting threshold for the two neighborhoods is the same: 90%. If we divide them into two separate invited taking projects, the government would need to spend an amount of \$15,000 for the first one (\$300 multiplied by 50 property owners), and \$27,000 for the second one (\$60 multiplied by 450 property owners). Hence, the total cost for the two projects would be \$42,000. However, if the local government combines the two neighborhoods into one single invited taking project, the offer price would be \$80 and the total cost would be reduced to \$40,000 (\$80 multiplied by 500 property owners). By manipulating the boundary of different neighborhoods, the government could save \$2000 in total.

We have no reason to completely rule out the above risk. However, such a risk might be rather low for the following reason. Such manipulation can be easily detected by property owners if the government could not offer convincing reason for combining two neighborhoods together shortly before an invited taking is to take place. Once the manipulation is detected, the low-price property owners may strategically raise their expectation of the offer price, and then the amount of cost-saving might be reduced and even completely dissipate. Even if the invited taking gets through with such a manipulation, it would for sure generate serious complaints from the high-price property owners, which may impose serious costs on individual officials by negatively affecting their prospect of promotion. Facing such a potential trade-off, local officials might resist such a strategy by letting the government pay more and maintaining the original boundary between neighborhoods, hence keeping their career and promotion intact. To control such a risk, we could imagine a rule that if there is sufficient evidence proving that the government is manipulating the boundary to lower offer price and to save costs, the court shall invalidate the whole invited taking and require the government to carry out separate invited taking.

V. ASSEMBLY SURPLUS: MARKET, BENEFITS, AND LOCAL PUBLIC FINANCE

A long-lasting concern regarding coerced sales of property to the government has been the potential of under-compensation when implementing the statutory standards of fair market value.⁵⁸ Such a concern is apparently not relevant to invited takings, because the offered price is substantially greater than the statutory minimum. Bonuses and relocation assistance with no caps further raise the price to be received by property owners. More to the point, compensation packages in invited takings include a large portion of the assembly surplus, because the baseline for “fair market value” is referred to as the value of hypothetical housing on the *post-assembled* land. Traditionally, there are three reasons against the government’s sharing assembly surplus with condemnees: administrative costs,⁵⁹ corrective justice, and distributive justice.⁶⁰

A. ADMINISTRATIVE COSTS

One important reason that a supermajority can be induced to sell under invited takings is that property owners would receive some portion of the

58. For a summary of this concern, see Fennell, *supra* note 20, at 962–67 (referring to three types of losses: surplus generated by the transfer, subjective value of the landowner, and autonomy in deciding whether and when to sell).

59. See generally *United States v. 320.0 Acres of Land*, 605 F.2d 762 (5th Cir. 1979).

60. *Heller & Hills*, *supra* note 10, at 1477–78 (stating that condemnees should not be deprived of the ordinary perquisites of ownership, hence an injustice; it is wrong to assume that landowners made no contribution to the success of land assembly beyond giving up their land, because the speed with which land is condemned depends on landowners’ decision).

assembly surplus no matter whether they fall within the majority or the dissenting minority. In all invited takings, the baseline price for compensation for lost property is set equal to the fair market value of housing as determined by licensed real-property appraisals. The term “housing” here refers to post-assembly housing, or nearby housing that is equivalent to a housing hypothetically existing in the same location in a post-assembled status. This is a position dramatically different from the rule under law in the United States, which only grants fair market value of the pre-assembly housing. High population density made it much easier to find comparable projects that may resemble hypothetical post-assembly housing. The high frequency of land assembly, by the government as well as by private developers in most developing countries, also substantially reduces the administrative costs of calculating assembly surplus.

B. CORRECTIVE JUSTICE

A close look at the calculation of compensation for property loss under invited takings projects can be particularly disturbing in regard to corrective justice if the condemnees made no contribution to the post-assembly status. The portion of compensation representing the assembly surplus would be a windfall to them.

For modern apartments and condos, the baseline housing for determining compensation is not the current housing under its poor conditions, but new and modern housing located nearby in a much better situation. The baseline price is then multiplied by a coefficient, which ranged from 1.2 to as high as 1.6 under some of the invited takings projects.⁶¹ Given that the old apartments tended to be rather small and new ones in the current location were extremely expensive, many chose to buy new apartments with a larger area in other locations where the per-square-meter-price is lower. In calculating the total size of housing for compensation, the buildings constructed without proper approval and in apparent breach of housing code were also included, but often with a discount. As such, owners received a reward instead of punishment for breaching the building code, which provided strong incentives for them to build more of such low-quality housing before a taking occurs. In two sites the author visited,⁶² the opportunity attracted contractors to offer design and construction with a contingent fee arrangement: owners did not need to pay the costs unless and until they received compensation from the government for the newly added part. Unsurprisingly, the quality of such temporary housing was so low in general

61. Such information is collected by the author through review of documents and interviews with property owners with respect to the first 3 out of the 23 projects summarized in the Appendix.

62. The two sites were located in the Guiyang, Guizhou Province and were visited in February 2014.

that it was used as warehouse space only or was not expected to be used at all.⁶³

Many property owners indicated in interviews that the compensation would be more than enough to give them a much better and bigger home with a beautiful interior and high quality furniture. In addition, many property owners indicated their next step would be to purchase automobiles and start living a real “modern” life. In one interview, a woman proudly claimed that she would definitely holdout if the government refused to provide additional apartment units to each of her two sons: both were jobless and had been living with her since they were born. There are also reports of a prosperous gambling business located right by the site of takings.⁶⁴

The potential corrective justice problem is by no means unimportant. In addition to the reasons proposed by Heller and Hills,⁶⁵ we need to look at other possibilities. It might become less controversial if we view housing title as a social benefit instead of a stand-alone statutory right. In China, since the early 1980s until the first decade of the 21st century, the right of ownership and possession of housing involved in invited takings had been provided as in-kind housing benefits by the government to their ex-employees or ex-employees of state-owned enterprises (“SOEs”).⁶⁶ In a new era, with more developed urban infrastructure and better commercial projects, the overall living condition and the standards associated with the housing benefits should also be raised. Therefore, it seems reasonable for the government to provide such improvements to make sure that individuals who live on government benefits live a life with a certain degree of dignity. Many local governments issued rules and guidelines to move low-income residents from run-down neighborhoods to better and newer neighborhoods by providing housing of exactly the same size and charging only a small fraction of the market price

63. Many of these houses are extremely narrow and have no windows.

64. There are also media reports of illegal gambling right next to the site of takings, where property owners used compensation to gamble. See *Fifty Policemen Searched a Gambling Site, Caught 29 Gamblers, Among Them Many Were Property Owners* (50 民警夜袭赌场 抓获 29 名赌徒，其中不少是拆迁户), GUIZHOU PROVINCE NEWS WEBSITE (May 23, 2013, 3:48 PM), <http://finance.gog.com.cn/system/2013/05/23/012310759.shtml>.

65. Heller & Hills, *supra* note 10, at 1477–78 (stating that (1) “failure to pay over some share of the assembly value to condemnees deprives them of value that landowners normally retain”; and (2) “it is an error to suppose that landowners make no contribution to the success of land assembly beyond giving up their land”).

66. This policy was formally abolished in 1998. See, e.g., HONG KONG EXCHANGES & CLEARING LIMITED, REGULATORY OVERVIEW 220 (n.d.), available at http://www.hkexnews.hk/listedco/listconews/sehk/2009/1112/01777_672965/E120.pdf. However, the practice persisted much longer through more implicit forms, such as taking investment from state or SOE employees for “joint development” of residential apartments and then allocating such apartments to these investors at below-market price. See Lin Sun, *New Trend of State-owned Enterprises in Anhui: Sharing Costs of Building Housing or Enjoying Low-Cost Luxury Apartment?* (安徽国企新潮流：集资建房，还是低价造豪宅), 21ST CENTURY BUS. HERALD (May 5, 2011), http://epaper.21cbh.com/html/2011-05/05/content_146687.htm.

with respect to the portion exceeding the original size.⁶⁷ One possible analogy is the government subsidizing the upgrade of public transportation with earmarked revenue from luxury taxes charged for sales of expensive cars. There seem to be no complaints about using newer buses with air-conditioning, heating, and less carbon emissions, when the overall standards for hygiene and comfort increase in the society.

C. DISTRIBUTIVE JUSTICE, SPECIAL ASSESSMENTS, AND LOCAL GOVERNMENT FINANCING

If the vast improvement in housing conditions and infrastructure, including assembly surplus alleged to have been allocated to property owners improperly, are all to be undertaken by the general body of tax payers, serious concerns regarding distributive justice would arise. This concern is particularly relevant to the scenario of a condemnation of blighted land, because “[t]he owner of the blighted site effectively has monopoly power on the resource that must be acquired in order for the government’s goal to be accomplished.”⁶⁸ Invited takings allow the owner to extort revenue from the local government as the price for ceasing the nuisance effect of their properties and lifestyle on the rest of the city. Furthermore, Chinese law automatically qualifies condemnation of blighted land for URPs as satisfying the “public interests” test,⁶⁹ leaving few external checks over payments by the government to condemnees in invited takings.

However, only a small fraction of the costs for invited takings are born by the general body of taxpayers. Instead, at least three specific groups of individuals have been paying for the costs of invited takings to a large degree, and these groups directly derive benefits out of successful invited takings. Similar to the function of the special assessment districts,⁷⁰ invited takings provided an effective mechanism to make the beneficiaries bear the costs and may, therefore, be justified.

The first group directly benefiting from invited takings is of course local residents, especially those whose property and activities are in close proximity

67. Liao Ning province (辽宁省) was one of China’s most important heavy industry hubs. When these heavy industries eventually declined and factories were closed, most employees became essentially unemployed, generating a substantial number of low-income local residents in this province. See Wei Wang, *Between 2006 and the End of 2011, More than 10 Million Apartments Had Been Built or Renovated in China* (2006 年至 2011 年底, 全国累计开工改造各类棚户房超 1000 万户), PEOPLE’S DAILY (Sept. 25, 2012), <http://nb.people.com.cn/GB/n/2012/0925/c200890-17519663.html>.

68. Fennell, *supra* note 20, at 975.

69. Guoyou Tudishang Fangwu Zhengshouhe Buchang Tiaoli (国有土地上房屋征收和补偿条例) [Administrative Rules on Takings of Housing on State Owned Land in China] (effective Jan. 21, 2011), art. 8.

70. See generally ROBERT ELLICKSON & VICKY BEEN, *LAND USE CONTROLS: CASES AND MATERIALS* 619–33 (3rd ed. 2005) (introducing urban infrastructure institutional arrangements and rationale, as well as how courts approach special assessment).

to the sites where invited takings take place. With better roads, facilities, neighborhoods, and higher-income individuals moving into the post-assembly sites, the value of property owned by individuals of this group will rise. Such improvement can also generate more wealth-creating activities, bringing about more jobs and revenue to the local government, which can then be spent locally. Such improvement can also bring about non-monetary value to local residents, such as tidier and more modern architecture, better hygienic conditions, and a more comfortable life in general. Therefore, to make tax payers give up some of the assembly surplus seems a reasonable method of allocation of the assembly surplus.

The second group consists of real-estate consumers, including those who bought the post-assembly development products and those who bought property in a broader local market. They share a substantial portion of the costs by paying a market price for real estate sold by private developers or owners, a substantial part of which is the cost of a land-grant premium.⁷¹ A land-grant premium is a fee charged by the local government as consideration for granting the land-use right and associated development right to real-estate developers and other commercial users. Given that land grant premiums are a substantial portion of local government revenue,⁷² such a link of cost-benefit sharing is straightforward. By paying a market price, again leaving a big chunk of the assembly surplus to property owners subject to invited takings, these new property owners get to enjoy a more modern and comfortable neighborhood in a prime location, access to good public schools, and less waste of time spent commuting to school, work, and public amenities, such as hospitals and museums.

The story of the third group, i.e., bond investors in real estate, however, is more complicated. The municipal government and lower government, the bodies that implement invited takings, have never been allowed to issue bonds or to provide security under Chinese law. They, however, use wholly-owned

71. For example, one of the major Chinese real-estate developers, which recently listed its shares in Hong Kong Stock Exchange, reported that the ratio of land-acquisition cost (primarily including land-grant premiums) to the total cost of property sales for 2011 to 2013 ranges from about 26% to 30%. DALIAN WANDA COMMERCIAL PROPERTIES CO., LTD., GLOBAL OFFERING, <http://image.wanda.cn/uploadfile/2014/1210/20141210092713995.pdf> (last visited Apr. 21, 2015).

72. For the three years of 2011, 2012 and 2013, the percentage of land-grant premiums out of the total amount of local government revenue was 63.27%, 46.69%, and 59.81%, respectively. See *Public Financial Revenue and Expenditure in 2013*, MINISTRY FIN. PEOPLE'S REPUBLIC CHINA (Jan. 23, 2014), http://gks.mof.gov.cn/zhengfuxinxi/tongjishuju/201401/t20140123_1038541.html; *Public Financial Revenue and Expenditure in 2012*, MINISTRY FIN. PEOPLE'S REPUBLIC CHINA, http://gks.mof.gov.cn/zhengfuxinxi/tongjishuju/201301/t20130122_729462.html (last visited Apr. 21, 2015); *Public Financial Revenue and Expenditure in 2011*, MINISTRY FIN. PEOPLE'S REPUBLIC CHINA, http://gks.mof.gov.cn/zhengfuxinxi/tongjishuju/201201/t20120120_624316.html (last visited Apr. 21, 2015).

corporate financing vehicles⁷³ to issue enterprise bonds and borrow from commercial and policy banks, by creating “quasi-collateral” over potential income streams of the land-grant premium. In addition, these banks, especially the policy banks, issue so called financial-institution bonds to raise funds. For example, the single most important lender for URPs is China’s largest policy bank: the China Development Bank (CDB). As of the end of 2013, CDB has advanced more than \$100 billion (623 billion in local currency) in loans for URBs, supporting the construction of housing of more than 640 million square meters, involving more than 25 million individuals.⁷⁴ CDB itself is not taking any deposit from the public. Instead, it heavily relies upon the bond market for capital—more than half of its capital is from proceeds of the issue of various bonds.⁷⁵

To be sure, in a standard bond market, institutions instead of individuals are the major investors. In China, however, both the enterprise bonds and loans with collateral over potential land-grant-premium income streams are ultimately invested by individuals. Since individuals derive benefits from improvement of urban infrastructure and living facilities, they can be viewed as beneficiaries of invited takings.

Yet, this Essay is not making the general claim that debt financing is an ideal method for the government to raise funds for land assembly or for “bribing” potential holdouts. In both the United States and China, the core concern regarding government debt is the possibility that “both politicians and their constituents have an incentive to shift the economic burden of financing current government expenditures to future generation of ratepayers,”⁷⁶ which would in turn induce excessive borrowing and excessive spending. When this danger turned into reality in the middle of the 19th century in the United States, many states enacted constitutional restrictions on state debt, requiring voters’ approval before state debt could be incurred.⁷⁷ China went even further by completely prohibiting municipal government

73. The vehicle is called *Di Fang Rong Zi Ping Tai* (地方融资平台). Local government used to be completely prohibited from incurring debt under Chinese law. Such platform enterprises were then created as a method to allow local government to obtain capital without breaching law. The most recent revision to the Budget Law of China (预算法) has relaxed the prohibition, but central government approval is required, and it will take some time for the provincial government bond market to emerge and develop.

74. *Strategic Focus*, CHINA DEV. BANK, <http://www.cdb.com.cn/web/Column.asp?ColumnId=12> (last visited Apr. 21, 2015).

75. *Composition of Capital Source*, CHINA DEV. BANK, <http://www.cdb.com.cn/web/Column.asp?ColumnId=41> (last visited Apr. 21, 2015).

76. For a summary of arguments for and against government debt, see Julie A. Roin, *Privatization and Sale of Tax Revenue*, 95 MINN. L. REV. 1965, 1974 (2001).

77. *Id.* at 1975–76 (introducing the development of local controls over government debt in the United States since 1840).

and the governments below them from borrowing under the newly passed Budget Law.⁷⁸

What I want to emphasize here is that directly linking bond investors with specific land assembly projects implemented by the government may better align the costs and benefits of these projects. The market discipline imposed upon bond issuers by competition and regulation in the bond market may become cost-effective discipline over government officials' decisions in carrying out a given land assembly project. This is particularly the case with respect to mandatory information disclosure requirements, which could very well force officials to carefully assess and openly explain whether a certain land assembly is financially viable, what the potential costs and benefits are, and how the funds raised have been spent. Improved transparency may then bring about a higher degree of accountability. For many developing countries, where local governments are often running with huge deficits and mired in secret dealings with interest groups, subjecting government decisions to a more mature and transparent market is a potentially valuable path.

VI. CONCLUSION

Invited takings present an example of spontaneous arrangements in response to deadlock created by problems of abused eminent domain power and serious holdout. With almost no coordination, a handful of local governments in difference places carried out these experiments with invited takings during roughly the same period of time. Various entities, including officials, real estate developers, lawyers, property owners, scholars, and journalists, proactively participated and contributed to streamline sporadic institutional details and wisdom that proved effective in practice. The poor and the powerless property owners, who are often worried about being taken advantage of in land assembly, turned out to be the winners of invited takings. They enjoyed a new life, substantially improved from the pre-taking one. Meanwhile, better infrastructure, more commercial-friendly projects, and more modern neighborhoods are made possible by successful invited takings, which make the cities more attractive to businesses and educated residents. Dignity, respect to collective good, and democratic decision making are preserved and respected, replacing the brutal violence and conflicts often seen in eminent domain. The long-term sustainability and consequences of this experiment are yet to be tested, but the result in the short run is encouraging. It should affirm our confidence that rational individuals with different and even conflicting interests, such as property owners and government officials in charge of land assembly, are able to coordinate and create spontaneous order to improve their overall welfare, even in countries

78. See *Zhonghua Renmin Gongheguo Yusuanfa* (中华人民共和国预算法) [PRC Budget Law] (effective Jan. 1, 2015), art. 35.

where individuals are highly unsophisticated, and where property protections and institutional oversight over officials is inadequate.

APPENDIX: SUMMARY OF INVITED TAKINGS PROJECTS IN CHINA
(between 2004 and October 2014)

	City (Province)	Number of Households	Stage-1 Minimal %	Stage-2 Minimal %	Time
1.	Jiaxing B (Zhejiang) ⁷⁹	over 400	95%	95%	05/2012– 09/2014
2.	Wenzhou (Zhejiang)	208	85%	85%	04/2005– 01/2007
3.	Chengdu A (Sichuan)	373	Over 90%	Over 90%	05/2008– 07/2008
4.	Pujiang County (Zhejiang)	N/A	100% in principle, 90% in practice		03/2004
5.	Ningbo A (Zhejiang)	N/A	N/A	90%%	completed in 03/2005
6.	Ningbo B (Zhejiang)	N/A	95%	95%	Started in 2006
7.	Leshan A, B, C, D, E, F, G (Sichuan)	1633	N/A	85%– 100%	06/2010– 07/2011
8.	Chengdu B (Sichuan)	354 ²	100%	100%	Started in 12/2012
9.	Chengdu C (Sichuan)	N/A	90%	90%	N/A
10.	Ma'anshan (Anhui)	107	90.6% signed and project went through		N/A
11.	Chaohu (Anhui)	45	85%	100%	08/2011– 09/2011
12.	Wuhu (Anhui)	917	90%	95%	09/2013
13.	Gaotang County (Shandong)	over 122	N/A	100%	09/2011– 11/2012
14.	Qingdao (Shandong)	108	98%	98%	06/2012
15.	Fuzhou (Fujian)	437	100%	100%	11/2012– 03/2013
16.	Handan (Hebei)	N/A	N/A	85%	04/2014
17.	Chongqing	72	100%	100%	Completed in 08/2014
18.	Shanghai	5056	98%	97.9%	07/2012– 11/2012
19.	Jiaxing A (Zhejiang)	34	N/A		01/2010– 08/2010
20.	Harbin (Heilongjiang) ⁸⁰	N/A	N/A		2008–2010
21.	Baicheng County (Xinjiang)	N/A			
22.	Shanghai A ⁸¹	over 500	N/A		11/2010
23.	Shanghai B	N/A	90%		Completed in 08/2012

79. I went to the site and conducted interviews for the first three projects.

80. For Project Nos. 20 and 21, no information on the exact percentage of the supermajority requirements was available in the reports, but they were otherwise described as invited takings in these reports. I have not been able to obtain further details on these projects.

81. For Project Nos. 22 and 23, I relied upon information reported by Zhu, *supra* note 16.