

LAND ACQUISITION FOR INVESTMENT IN ETHIOPIA: ECONOMIC ANALYSIS OF LEGAL OPTIONS

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Abstract

The idea that public ownership of land restricts the efficient allocation of land mainly because it increases transaction costs and inhibits exchange of land for private investment has been re-examined in land law reforms. Particularly, with the rise of property rights economics as analytical framework, the thesis that land rights can be treated as a bundle of property rights in which the state and the public retains the right to common ownership of the land but legally assign the right to use, transfer, inherit and benefit from land to any person who values it most has been advanced. However, there is no scholarship in the Ethiopian context that provides normative insight on how the different legal rules that enable investors to acquire land for Investment purpose affect transaction costs. This article addresses this issue by examining the modalities of acquiring land for investment purposes under the Ethiopian land law by identifying 'legally desirable' or suitable options available for investors from the vantage point of their capacity to foster the reduction of transaction costs. The article employs law and economic analysis as a method of inquiry to normatively evaluate how legal rules designed to regulate the exchange of property rights to land affect transactions costs during the process of investment land acquisition. The finding of the analysis indicates that the legal rules for acquiring urban land through land auction entail lower transaction costs compared to government land allotment and rural land rental arrangements.

Key-terms: law and economics, investment, land lease, allotment, tender, rental, transaction costs, property rights

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Introduction

Land as a tangible, durable and inextensible good, is a basic factor of production upon which landed investment activities are attached. Scholars of law and economics have long argued that the proclivity to acquire land for investment depends on the existence of secured property rights in land capable of transferability.¹ Acquiring land for investment purposes poses a serious challenge for investors in some developing countries since legal systems restrict property rights to land with land tenure system that hinders easy transferability of land rights beyond the tenure right holders. Above all, the existence of ill-defined property rights to land inevitably affects the effort to facilitate reallocation of production factors to maximize allocative efficiency in resource use.² Therefore, making land rights more secure and transferable is viewed as a prerequisite for facilitating land-related investment activities as productive economic endeavours.³

In Ethiopia, where land is considered as public property and its transferability is limited to acts of donation and inheritance, allocation of land for investment purposes raises serious concern viewed from the vantage points of transaction cost economics.⁴ The 1995 Constitution of Ethiopia limits the right to exercise ownership over both urban and rural land to the state and the people restricting land transfer through sale.⁵ The government is also required to ensure the rights of private investors to the use of land on

¹ M Roth et al., *Land Ownership Security and Farm Investment: Comment*, 71 AMERICAN JOURNAL OF AGRICULTURAL ECONOMICS 211 (1989).

² Claudia R Williamson, *The Two Sides of De Soto: Property Rights, Land Titling, and Development*, in THE ANNUAL PROCEEDINGS OF THE WEALTH AND WELL-BEING OF NATIONS 97 (Emily Chamlee-Wright ed., 2010).

³ Klaus Deininger et al., *Tenure Security and Land-Related Investment: Evidence from Ethiopia*, 50 EUROPEAN ECONOMIC REVIEW 1245-1277 (2006)

⁴ Rural Land Administration and Land Use Proclamation No. 456/2005, art. 5(2): 'Any person who is member of a peasant farmer, Semi pastoralist and pastoralist family having the right to use rural land may get rural land from his family by donation, inheritance or from the competent authority.' See also art. 8 sec 5: 'Any holder shall have the right to transfer his rural land use right through inheritance to members of his family'.

⁵ F.D.R.E Const., Proclamation No. 1/1995, art. 40 sec 3.

the basis of payment arrangements established by law.⁶ Despite this constitutional guarantee of access to land for private investors, the debate on the need for recognition of private ownership of land still lingers in the public discourse which the State characterizes as a ‘neo-liberalist’ outfit to bring back ‘landlordism’ to the Ethiopian mass. The assumption that land is not a commodity par excellence and, hence, should not be subjected to alienation through the channel of land market has long inhibited private investments in urban and rural land.⁷ However, individuals can exercise possessory (holding) or usufruct rights to the land while transfer is limited to family members through inheritance or donation.

As opposed to public ownership of land, it is widely argued that the arrangement of restricted ownership rights to land weakens the incentives for the landholders to allocate such valuable resource for the efficient user thereby hindering long-term capital investments over the land.⁸ It is argued that the current public ownership of land in Ethiopia profoundly hinders the efficient allocation of land to private investors in order to facilitate economic development.⁹ Gradually, the consideration of land markets as pivotal to development policy has gained acceptance in the enactment of urban land lease law in which the imperatives of transferable land use rights either on a temporary or permanent basis are seen as playing a key role in the allocation of land to more efficient users thereby increasing productivity and employment.¹⁰

⁶ *Id.*, art. 40 sec 6.

⁷ FASIL NAHUM, *CONSTITUTION FOR A NATION OF NATIONS: THE ETHIOPIAN PROSPECT* 160 (Red Sea Press, 1997).

⁸ Gershon Feder and David Feeny, *Land Tenure and Property Rights: Theory and Implications for Development Policy*, 5 *THE WORLD BANK ECONOMIC REVIEW* 140 (1991).
Land Acquisition for Investment: Economic Analysis of Legal Options

⁹ Deininger, K and Jin S, *Tenure Security and Land-Related Investment: Evidence from Ethiopia*, 50:5 *EUROPEAN ECONOMIC REVIEW* 1245-77 (2006).

¹⁰ Klaus Deininger & Songqing Jin, *Securing property rights in transition: Lessons from implementation of China’s rural land contracting law*, 70 *JOURNAL OF ECONOMIC BEHAVIOR & ORGANIZATION* 24 (2009).

Despite the constraints of public ownership of land, the idea that investors could opt for acquiring land for investment purposes by evaluating available legal options capable of reducing transaction cost is gaining wide acceptance.¹¹ For instance, the ‘physicalist definition of property as the exclusive right of possessing, enjoying and disposing of a thing’ was revisited paving way to the legal possibility of investing in the different shades of the bundles of rights to land.¹² Therefore, based on such legal possibility of enjoying bundle of property rights to land, private investors in Ethiopia can acquire land through three major alternative legal options.

The first option relates to acquiring a plot of land through tender process as per the urban land lease holding system. This option introduces land lease market in which investors are provided with the opportunity to acquire land from the government through public auction at the ‘prevailing transaction value of land’.¹³ The second legal option available for investors is through government allotment of urban and rural land for industrial and agricultural investment purposes.¹⁴ The third option for investors to acquire land for investment purpose is through private land rental system from the rural land use right holders.¹⁵

¹¹ Bacry Yusuf *et al.*, Land Lease Policy in Addis Ababa 13 (2009).

¹² Denise R. Johnson, *Reflections on the Bundle of Rights*, 32 VERMONT LAW REVIEW 249 (2007). It is argued that “Ownership can be shared in an almost infinite variety of ways. Thus, the concept of the bundle of separate sticks, with different “owners” holding different sticks, meant that property ownership was a very flexible concept, largely unconcerned with the object itself.” (*Id.*, at 254). See also Shitong Qiao & Frank Upham, *The Evolution of Relational Property Rights: A Case of Chinese Rural Land Reform*, 100 IOWA LAW REVIEW 2490 (2015). It is argued that ‘the most important implication of the bundle-of-rights metaphor is that it shifts our attention from asking who owns the property to understanding who has what rights to the property and to examining the social relationships around a piece of property that is “beset by conflicting values and competing interests’.

¹³ Urban Lands Lease Holding Proclamation No 721/2011, art 4 sec 3.

¹⁴ *Id.*, art 12 sec 1.

¹⁵ Rural Land Administration and Land Use Proclamation, *supra note* 4, art 5 sec 4 *para.* (a), art 8 sec 1 & 8 sec 4.

In all of the three legal options of acquiring land for investment activities, investors face a myriad of transaction costs depending on how the legal rules are designed to govern the transfer of land use rights. However, the issue as to which legal options of acquiring land for investment yield efficient outcome, in terms of minimizing transaction costs, during the transfer of landholding rights requires closer analysis. Such analytical approach helps to create insights on the economic implications of Ethiopian land law designed to regulate the acquisition of land. This research endeavour is vital in normatively assessing the rules governing the modes of acquiring landholding rights as it typically informs investors to make rational choices by weighing the available options to acquire land based on understanding of the existing rules that either reduce or increase transaction costs.

In view of the above background, the article examines the modes of acquiring land for investment purposes under the Ethiopian land law by evaluating the available legal options from the vantage points of reducing transaction costs for investors. The article examines how the different legal modalities of acquiring land for investments purposes facilitates the reduction of transaction costs under the Ethiopian land law. In order to answer this question, the article employs economic analysis of law as a method of inquiry to normatively evaluate how legal rules designed to regulate investment related land markets affect transaction costs in the process of acquiring land for investment purposes.

The article is structured as follows. Following this introduction, Section 1 outlines the research methods by describing how it has employed transaction costs as a normative framework for the economic analysis of the law that regulates the process of acquiring land for investment purposes. Section 2 provides a general overview of property rights to land under the Ethiopian land law by reviewing land rights and the accompanying legal restrictions on their transferability. Section 3 specifically examines legal modalities of acquiring land for investment purposes under Ethiopian land and investment legislation. This section mainly sheds light on how the existing legal frameworks provide alternative legal options to ensure investors access to land for investment activities. Section 4 offers economic

analysis of the three modes of acquiring land for investment purposes to identify whether these alternative legal rules qualitatively foster the reduction of transaction costs. The article closes by providing concluding remarks.

1. Methodological Approaches of the Economic Analysis of Law

The economic analysis of law employs the instruments of microeconomic theory to the analysis of legal rules and institutions.¹⁶ According to David Friedman, there are three distinctive but related features of economic analysis of law that use economic principles and reasoning to analyse legal rules.¹⁷ The first characteristic is economic analysis of law engages ‘economics to predict the effects of alternative legal rules.’ The second feature relates to ‘the use of economics to determine what legal rules are economically efficient in order to recommend what the legal rules ought to be.’ The third feature involves ‘the use of economics to predict what legal rules will be.’ Based on Friedman’s characterization, the economic analysis of law may be defined as ‘the use of economic principles and reasoning to understand legal materials.’¹⁸

The economic principle used to analyse existing legal rules is ‘rational choice theory’ that rests on the assumption that humans are rational beings who behave according to the rules designed to regulate individual behaviours.¹⁹ This economic theory could be used to analyse whether the existing legal rules provide incentives for individual actors in the market to behave in

¹⁶ ROBERT COOTER & THOMAS ULEN, *LAW & ECONOMICS* 11 (6th ed., Pearson Education, 2012).

¹⁷ David Friedman, *Law and Economics*, in *THE NEW PALGRAVE: THE WORLD OF ECONOMICS* 371-380, 371 (J Eatwell, M Milgate & P Newman (eds), 1991).

¹⁸ Geoffrey P. Miller, *Law and Economics versus Economic Analysis of Law*, 19 *AMERICAN BANKRUPTCY INSTITUTE LAW REVIEW* 459 (2011).

¹⁹ *Id.* at 12-13. See also Alessio M. Paces & Louis Vissche, *Law and Economics: Methodology*, in *Interdisciplinary Research into Law* 85-107, 86 (B. van Klink, & S. Taekema (eds.), 2011). See also Hanna Almlöf & Per-Olof Bjuggren, *A regulation and transaction cost perspective on the design of corporate law*, 47 *EUROPEAN JOURNAL OF LAW AND ECONOMICS* 403, 411 (2019).

economically rational way.²⁰ However, the way the existing legal rules are formulated may have effects on the behaviour of relevant actors to act in a socially desirable way.²¹ It is widely argued that legal rules that facilitate individuals' actions in economically efficient way is socially desirable.²² According to Stephen Margolis, an efficient legal system is 'one in which property rights are assigned and liability rules are formulated so that the value of things present in society, as measured by willingness to pay, is maximized over all alternative legal environments, given the costs of contracting.'²³ It is argued that a legal rule that facilitates reduction of transactions costs in every phase of property rights exchange is economically efficient since it maximizes the ability of individuals to efficiently allocate property rights among themselves.²⁴

The concept of transaction costs for the purpose of analysing the economic efficiency of legal rules was profoundly illuminated by Ronald Coase.²⁵ The Coasean notion of transaction cost refers to costs linked to a given transfer of property rights that are necessary for a legal exchange to take place.²⁶ As

²⁰ Thomas S. Ulen, *Rational Choice and the Economic Analysis of Law*, 19 LAW & SOCIAL INQUIRY 487, 488 (1994).

²¹ L Kaplow & S Shavell, *Economic Analysis of Law*, in 3 HANDBOOK OF PUBLIC ECONOMICS 1661-1784, 1661 (Alan Auerbach and Martin Feldstein (eds), 2002); see also GUIDO CALABRESI, *THE FUTURE OF LAW AND ECONOMICS: ESSAYS IN REFORM AND RECOLLECTION* 2 (2016).

²² Albert Sanchez-Graells, *Economic analysis of law, or economically informed legal research*, in RESEARCH METHODS IN LAW 170-193, 171 (Dawn Watkins and Mandy Burton 2nd (eds), 2018).

²³ Stephen E. Margolis, *Two Definitions of Efficiency in Law and Economics*, 16 THE JOURNAL OF LEGAL STUDIES 471, 473-4 (1987).

²⁴ Jonathan R. Macey, *Transaction Costs and the Normative Elements of the Public Choice Model: An Application to Constitutional Theory*, 74 VIRGINIA LAW REVIEW 471, 472 (1988).

²⁵ It should be noted that Coase in his 1937 Article use the phrase 'transaction cost' to refer 'the costs of the price mechanism'. see Douglas W Allen, *Transaction Costs*, in ENCYCLOPEDIA OF LAW AND ECONOMICS: THE HISTORY AND METHODOLOGY OF LAW AND ECONOMICS 894 (Bouckaert & De Geest (eds), 2000).

²⁶ It should be noted that the narrow version of the notion of 'transaction costs' have been presented in the economic literature in terms of 'monetary interpretation' that assumed 'transaction costs as the direct costs that an economic agent incurs when engaging in a

will be discussed in Sub-section 4.2 in detail, these costs include search costs, bargaining costs and enforcement costs incurred by parties during the process of property rights exchange. The economic analysis of law, based on such understanding of transaction costs, emphasizes the normative imperatives that ‘law can either provoke transaction costs to rise or it can help to reduce them.’²⁷

Having described the approach of economic analysis of law, it is imperative to also explain the justification and limitation of utilizing it as a method of analysing legal rules taking transactions costs as a unit of normative analysis in the process of acquiring land for investment purposes. To begin with the justification, unlike the traditional legal research methods of analysing legal rules on a given issue, carrying out legal research by incorporating the insights from the economic analysis of law provides additional yardsticks against which the social or economic desirability of legal rules are evaluated.²⁸ It is contended that carrying out legal research without incorporating the insights of economic theory is ultimately unsatisfactory.²⁹ Hence, it is highly recommended to carry out an ‘economically informed’ legal research at least by consulting the insights resulting from previous economic analysis of law relevant to the research area.³⁰

Like the vast majority of studies that employ economic analysis of law, this article is limited to the normative frameworks of economic analysis of law as

market transaction’. See Tomasz Famulski, *Selected Legal Aspects of Transaction Costs*, 4 JOURNAL OF FINANCE & FINANCIAL LAW 23-27 (2017).

²⁷ *Id.*, at 27.

²⁸ Warren J. Samuels & Steven G. Medema, *Ronald Coase on Economic Policy Analysis: Framework and Implications*, in COASEAN ECONOMICS: LAW AND ECONOMICS AND THE NEW INSTITUTIONAL ECONOMICS 162 (Steven G. Medema (eds), 1998). See also Alession M. Paces, *A law and economics perspective on normative analysis*, in FACTS AND NORMS IN LAW: INTERDISCIPLINARY REFLECTIONS ON LEGAL METHOD 171 (Sanne Taekema, Bart van Klink & Wouter de Been (eds), 2016).

²⁹ Sanchez-Graells, *supra note 22* at 173. See also Tom R. Tyler, *Methodology in Legal Research* 13 UTRECHT LAW REVIEW 131, 132 (2017); see also ROBIN PAUL MALLOY, *LAW IN A MARKET CONTEXT: AN INTRODUCTION TO MARKET CONCEPTS IN LEGAL REASONING* 70 (Cambridge University Press, 2004).

³⁰ Sanchez-Graells, *supra note 22* at 192.

a methodological approach.³¹ Accordingly, it is not the intention of the article to be an empirical work of transaction costs economics involving Ethiopian investment land transactions for two major reasons. The first reason relates to the expertise of the author who is accustomed to the doctrinal methods of legal research which is commonly used in the legal profession. Thus, it is not the intention of the article to directly engage with task of empirically testing the economic methods and theories of transaction costs. The second related reason is attributable to limitations of expertise and resources. It goes without saying that a research work of empirical transaction cost economics requires the mathematical application of econometric techniques with the ‘task of linking concepts with observations’ that ‘demands a great deal of detailed knowledge of the realities of economic life’.³² In addition, on top of demanding an expertise on mathematical economics, conducting the empirical aspects of transaction costs on the legal regulations of land exchange process requires resources to gather first hand micro analytical data relevant to assess the practices of land transaction contracts.³³

With these considerations in mind, the article aims to offer a modest explanation as to why economic analysis of legal formulations should not be overlooked given the involvement of transaction costs in each step of process of acquiring investment land. The article aims to examine the existing Ethiopian land law regulating various modes of acquiring land for investment purposes to show the extent to which such legal options facilitate the reduction of transaction costs.

³¹ See generally Edward Rubin, *The New Legal Process, The Synthesis of Discourse, and the Microanalysis of Institutions*, 109 HARV. L. REV. 1393 (1996); see also Keith N. Hylton, *Law and economics versus economic analysis of law*, 48 EUROPEAN JOURNAL OF LAW AND ECONOMICS 77, 78 (2019).

³² Oliver E. Williamson, *Transaction Cost Economics Meets Posnerian Law and Economics*, 149 JOURNAL OF INSTITUTIONAL AND THEORETICAL ECONOMICS 99, 113-14 (1993).

³³ *Id.*, at 114.

2. Property Rights to Land in Ethiopia

2.1. Limitations of Property Rights in Land

The existing legal framework on land maintains the common ownership of rural and urban land as well as natural resources by the state and the people of Ethiopia.³⁴ In actual terms, while state controls land ownership, urban dwellers, rural peasants, semi-pastoralists and pastoralists are guaranteed only 'landholding' rights. The term 'holding rights' is defined under federal rural land law as,

the right of any peasant farmer or semi-pastoralist and pastoralist (...) to use rural land for purpose of agriculture and natural resource development, lease and bequeath to members of his family or other lawful heirs, and includes the right to acquire property produced on this land thereon by his labour or capital and to sale, exchange and bequeath same.³⁵

In the parlance of property rights, landholders are assigned with the usufruct rights—without alienation right through sale (*abusus*).³⁶ Implicitly, usufruct rights basically involve the right to use, rent and lease land lawfully acquired by any person. In terms of usufruct land rights transferability, it is important to closely look at the provisions of the Constitution that distinguish between landholding rights *per se* and the rights to immovable property built on the land. The issues of land transferability through alienation, bequeath (donation or inheritance) or transfer of title are explicitly mentioned to refer to the full right to the immovable property built on the land and to the permanent improvements made on the land by the labour and capital of the

³⁴ F.D.R.E Const. *supra* note 5, art. 40, sec 3. However, it is important to note that federal rural land administration and land use law expressly refers 'government as being the owner of rural land'. See Rural Land Administration and Land Use Proclamation, *supra* note 4, art.5 sec 3.

³⁵ Rural Land Administration and Land Use Proclamation, *supra* note 4, art.2 sec 4.

³⁶ The phrase 'shall not be subject to sale or to other means of exchange' in art. 40 sec 3 of the F.D.R.E Const. generally indicates that the *abusus* concept of ownership rights on land is absent, precluding private ownership of land.

landholders. Hence, no mention is made in the Constitution as to whether landholding rights *per se*, could be transferable through donation or inheritance.³⁷ It is the Rural Land Administration and Land Use Proclamation that mentions the possibility of acquiring rural land through donation or inheritance of family members.³⁸ It is understandable that the public land ownership regime in Ethiopia imposes significant restrictions on the transferability of landholding rights *per se* affecting the magnitude of allocable property rights. Therefore, this makes it difficult if not impossible for investors to acquire land as a sellable economic good because of such constitutional prescription that eventually hampers alternative economic possibilities of land reallocation.

In the Ethiopian land law literature, scholars widely argue that limitation on property right to land through alienation has some socio-economic reasons which land policymakers forward as justification to maintain state ownership of land.³⁹ It is argued that the issue of land in Ethiopia touches upon the sensitive cords of the society that transcends from one generation to the next unless it is taken seriously as a constitutional matter in which state takes the responsibilities to protect such right and allocate for the common benefit of the Ethiopian people.⁴⁰ There are two important reasons put forward in defence of the constitutional stance of state land ownership in current Ethiopia — social equity and tenure security.⁴¹

³⁷ The cumulative reading of F.D.R.E Const. art. 40 secs. 1 & 7. The Constitution also distinguishes between Ethiopian peasants and pastoralists on the one hand and private investors on the other to obtain land. The former two have ‘the right to obtain land without payment’ or free land for grazing and cultivation purposes. But the later have the ‘right to the use of land on the basis of payment arrangements established by law’. See F.D.R.E Const. art. 40 secs. 4, 5 & 6.

³⁸ Rural Land Administration and Land Use Proclamation, *supra note 4*, art.5 sec 2.

³⁹ For detailed nuances on this issue, see Muradu Abdo Srur, *State Policy and Law in Relation to Land Alienation in Ethiopia* 15-20 (PhD Thesis University of Warwick, December 2014).

⁴⁰ Nahum, *supra note 7* at 54.

⁴¹ Daniel W Ambaye, *Land Rights in Ethiopia: Ownership, equity, and liberty in land use rights*, TS02D-CUSTOMARY AND GROUP LAND RIGHTS 26-27 (2012).

The social equity argument relates to the obligation of the government to ensure free access to rural land for peasants and pastoralists as provided under the FDRE Constitution and federal and regional rural land legislation.⁴² The tenure security argument was advanced in terms of the constitutional prohibition of forced eviction of peasants and pastoralists from their rural land and restrictions on land sale.⁴³ Hence, public ownership of land in Ethiopia is viewed as the preeminent device to protect the peasants against market forces. The assumption is that creating a property rights regime where the right to alienate land would create incentive for 'poor farmers' to sell their landholding ultimately resulting in 'migration of the farming population' through massive eviction.⁴⁴ Nonetheless, scholars widely argued that this assumption was not supported by empirical evidence.⁴⁵ For instance, Muradu Abdo opined that what is more important is realizing security of land use rights to the rural community that would facilitates 'agricultural productivity and stimulates local industries'.⁴⁶ According to Muradu, such approach requires thinking outside both land ownership debates that 'rest on an underlying narrow conception of land rights which regards land rights simply as a tradable asset.'⁴⁷ The emerging trend that land should not necessarily be fully owned to be a tradable asset found its express normative traction ushering a shift in private-public ownership debates. Specifically, the move towards the conception of bundle of property rights to land capable of assignable legal or

⁴² As it stands now in rural Ethiopia land redistribution by the state with the view to ensure free access to land would prove difficult if not impossible as it is difficult to find unoccupied farm land. The government considers pastoralists grazing land as untapped arable land.

⁴³ See Daniel, *supra* note 41. Various studies conducted by the World Bank which is in favour of private property in land (often attacked by the ruling part as neo-liberalist economic thinkers) argue otherwise. These donors contend that State ownership of land creates lack of tenure security. They argue that absence of tenure security for land users provides little or no incentive to improve land productivity through long term investment; increase transaction cost because of land dispute; and it hinders the emergence of property market such as credit availability/land mortgage.

⁴⁴ *Id.*, at 27.

⁴⁵ Muradu, *supra* note 39 at 20.

⁴⁶ *Id.*, at 18-19.

⁴⁷ *Id.*, at 20-21.

contractual rights received wide policy acceptance opening an enabling environment to acquire land from landholders.

2.2. Types of Property Rights to Land

One can identify three basic types of property rights regime in land in the context of public ownership of land that confer varying degrees of holding rights. The first type of landholding is termed as private landholding that resembles individual property rights to land except the right to sell one's own landholding.⁴⁸ The categories of persons entitled to 'minimum private holding' rights to land includes 'farmers, pastoralists and semi-pastoralists and other bodies who are entitled by the law to use rural land.'⁴⁹ The framework of property rights in land within this regime relates to the assignment of individual minimum holding rights to use and enjoy the fruits of the land. The second category relates to 'communal holding' which refers to the holding of 'the local residents for common grazing, forestry and other social services.'⁵⁰ This category of holding rights allows individuals to use land for the legally assigned purposes on the basis of open access to the local residents. This property regime is susceptible to the 'tragedy of the commons' in the absence of clearly defined communal holding title capable of excluding non-local residents. The third category is 'state holding' which refers to 'demarcated rural land and those lands to be demarcated in the future by the federal and regional governments which includes forest lands, wildlife protected areas, state farms, mining lands, lakes, rivers and other rural lands'.⁵¹ This category should not be conflated with the conception of state or public land ownership as construed under the Constitution. As indicated in the definition of state holding, it rather refers to landholding schemes which are closely controlled and administered by government

⁴⁸ See F.D.R.E Const., *supra* note 5, art. 40, sec 3 & sec 4. See also Rural Land Administration and Land Use Proclamation, *supra* note 4, art 5 & art. 2 sec 4.

⁴⁹ Rural Land Administration and Land Use Proclamation, *supra* note 4, art. 2 sec 11.

⁵⁰ *Id*, art. 2 sec 12.

⁵¹ *Id*, art. 2, sec 13.

agencies in view of their significance to the socio-economic development of the country.

In a nutshell, drawing the proper limits to the legal assignment of property rights on land and distinguishing subjects of these rights would help to closely understand the context of acquiring land for investment purposes in Ethiopia. Moreover, it could be difficult to indulge into the economic analysis of options of acquiring land for investment without clearly identifying potential landholders with which any private investor has to deal with to lawfully acquire land for investment purposes. It is also vital to further discuss the modes of acquiring land rights for investment activities within the indicated frameworks of land property rights regimes.

3. Legal Modalities of Acquiring Land for Investment in Ethiopia

It is argued that economic development policy and strategies of Ethiopia encourages ‘commercialization’ of land for large-scale agriculture and urban industrial expansion through a massive transfer of land to private investors.⁵² In order to realize the transfer of land to private investors, legislative instruments are put in place to facilitate investment land acquisition. As highlighted in the Introduction to this article and as discussed in the following sub-sections in detail, there are three major legal options in which investors acquire land for investment purposes — land lease through tender, government land allotment and private land rental.

3.1. Acquiring Land through Public Auction: Lease Tender

The leasehold tenure system is considered as typical device to ‘leasing public land to lessen the tension between the government’s desire to uphold public land ownership and the reformists’ demand for increasing private property

⁵² Dessalegn Rahmato, *Land to Investors: Large-Scale Land Transfers in Ethiopia*, FORUM FOR SOCIAL STUDIES 4 (2011).

rights.⁵³ It is contended that the existence of credible institution that is committed to lease contracts, guarantees of security for the users and transferability options, and long-term lease rights will promote investment benefits.⁵⁴ Likewise, for the first time, the 2002 Urban Land Lease Proclamation in Ethiopia envisioned ‘that transferring urban land by lease for a fair price, consistent with the principles of free market’ in order to assist the country to ‘achieve overall economic and social development’.⁵⁵ More specifically, this proclamation emphasizes the necessity ‘to develop optimal conditions in which lease will become exclusive urban landholding system and to remove obstacles of and to expedite the process of permitting and holding urban land by lease based upon investment plan.’⁵⁶ The Urban Lands Lease Proclamation 721 of 2011 also recapitulates the need to put in place ‘appropriate administration that is efficient and responsive to land resource demand’ that ‘ensures the rights and obligations of the lessor and lessee’.

Given that land is the property of the state and the people of Ethiopia, its use is subject to specific legal rules. According to the Urban Lands Lease Holding Proclamation, ‘no person may acquire urban land other than the lease holding system.’⁵⁷ Under this proclamation, the term ‘lease’ is defined as ‘a system of land tenure by which the right of use of urban land located within an administrative boundary of an urban center is acquired under a contract of a definite period.’⁵⁸ Furthermore, the term ‘tender’ is also defined as ‘a modality of transferring lease of urban land to a bid winner fulfilling the competition requirements issued based on the rule of market competition of urban land tenure’.⁵⁹ Hence, any investor who wants to acquire land for investment undertaking is legally expected to pass through the tender

⁵³ Y Hong & S Bourassa, *Why Public leasehold? Issues and Concepts*, in LEASING PUBLIC LAND: POLICY DEBATES AND INTERNATIONAL EXPERIENCES (Steven C. Bourassa and Yu-Hung Hong (eds, Lincoln Institute of Land Policy 2003) 3-38.

⁵⁴ *Id.*

⁵⁵ Re-Enactment of Urban Lands Lease Holding Proclamation No 272/2002 at preamble.

⁵⁶ *Id.*

⁵⁷ Urban Lands Lease Holding Proclamation No. 721/2011, art.5 sec 1.

⁵⁸ *Id.*, art. 2 secs. 1 & 2.

⁵⁹ *Id.*, art 2 sec 9.

process administered by the relevant public bodies authorized to allocate urban land.

The effectiveness of acquiring land through tender or public auction depends on fulfilment of four legal preconditions. The first precondition involves the obligation of appropriate government body to prepare land that is free from legal claims of any third party with a clearly delineated and assigned parcel.⁶⁰ In the absence of land free from third party claims under state possession within the urban plan, the land prepared for lease tender should be acquired by authorized government bodies through the process of expropriation of urban land upon payment of commensurate compensation in the public interest from lawful possessor.⁶¹ Once the decision of expropriation is made, the lawful possessor of the land is served with a written clearing order stating the time the land has to be vacated, the amount of compensation to be paid and the size and locality of the substitute plot of land to be availed. The other source of land for lease tender could be prepared by clearing order of an illegally occupied urban land by the appropriate body without the payment of compensation by merely serving a written notice of seven working days to the occupant in person or by affixing it to the property situated on the land.⁶²

The second precondition to obtain land through the tender system relates to the process of availing information about land prepared for tender that should contain the land grade, the lease benchmark price and other pertinent data.⁶³ The law requires that such information should further comprise development program and action plan where the urban land prepared requires special development program and implementation action plan.⁶⁴

⁶⁰ *Id.*, art. 8 sec 1 para, a & d.

⁶¹ *Id.*, art. 26 sec 1.

⁶² Urban Lands Lease Holding Proclamation, supra note 69, art. 26 sec 4.

⁶³ *Id.*, art. 9 sec 1.

⁶⁴ *Id.*, art 9 sec 2.

The third precondition relates to publicity of tender plans that requires the relevant authorities to make publicly accessible the demand for urban land and development priorities and their annual plans indicating the quantity of urban land that will be offered for tender.⁶⁵ The fourth precondition refers to the timely supply of urban land for the lease tender in accordance with the publicized tender plans.⁶⁶

After the fulfilment of these four preconditions, ‘the investor with the highest bidder shall be declared a winner on the basis of his bid price and the amount of advance payment he offers’.⁶⁷ Therefore, the leasehold system of acquiring land assists for implementation of the constitutional right of private investors to ‘the use of land on the basis of payment arrangements established by law’.⁶⁸ The urban land lease hold system ensures the accessibility of land for private investors based on the payment of lease price set by the government.

3.2. Acquiring Land through Government Allotment

The term ‘allotment’ refers to the ‘modality applied for providing urban lands by lease to institutions that could not be accommodated by way of tender’.⁶⁹ In this modality, investors are provided with urban land through government allotment for undertaking investment projects which are exceptionally provided under the law. Accordingly, investors who plan to invest in manufacturing industries and investment projects with special national significance may acquire land through allotment upon the ‘decisions of the cabinet of the concerned region or the city administration’.⁷⁰ The Investment Proclamation 1180 of 2020 further prescribes that pertinent regional bodies are required to allocate land for

⁶⁵ *Id.*, art. 10 sec 1, *para.*, a & b.

⁶⁶ *Id.*, art. 10 sec 2.

⁶⁷ *Id.*, art. 11 sec 5.

⁶⁸ F.D.R.E Const. *supra note 37*.

⁶⁹ Urban Lands Lease Holding Proclamation, *supra note 69*, art. 2 sec 10) & art.7 sec 2.

⁷⁰ *Id.*, art.12(1)(e).

investors holding investment permit in ‘the manufacturing’ and ‘other sectors’ within sixty days and ninety days, respectively.⁷¹

The application of an investor for land allotment should be accompanied by the following three procedural requirements.⁷² Firstly, the investor is required to present support letter from the supervising authority of the requesting institution or from pertinent sectoral bodies. Secondly, the investor should provide evidence of a detailed study of the project to be implemented at the requested land site. Thirdly, the investor should present evidence that shows the budget allocated for implementing the project.

In the context of rural land, the 2005 Federal Rural Land Use and Land Administration Proclamation states that ‘private investors that engage in agricultural development activities shall have the right to use rural land in accordance with the investment policies and laws at federal and regional levels’.⁷³ At the federal level, the demand for land to undertake large scale commercial agriculture investment was handled by the Ethiopian Horticulture and Agricultural Investment Authority in collaboration with regional states.⁷⁴ The authority is mandated to register, administer and transfer those lands under its land banks on the basis of delegation obtained from regional states.⁷⁵ Furthermore, the authority is responsible to collaborate with the regional states in the identification of suitable agricultural investment lands, facilitate supply of investment land, and provide suitable documents that are accessible to the investors.⁷⁶ More recently, the Investment Proclamation 1180 of 2020 requires regional states

⁷¹ Investment Proclamation No 1180/2020, art. 51.

⁷² Urban Lands Lease Holding Proclamation, *supra note* 69 art. 13.

⁷³ Rural Land Administration and Land Use Proclamation, *supra note* 4, art. 5 sec 4 *para.* a.

⁷⁴ Ethiopian Horticulture and Agricultural Investment Authority Establishment Council of Ministers Regulation No. 396/2017, art 5.

⁷⁵ *Id.*, art 2 sec 6; art 6 sec 4 (see *Amharic* version); For discussion on the constitutionality issues of federal land administration, see Temesgen Solomon Wabelo, *Legal and Institutional Frameworks Regulating Rural Land Governance in Ethiopia: Towards a Comparative Analysis on the Best Practices of Other African Countries*, 11 BEIJING LAW REVIEW 64, 72-73 (2020).

⁷⁶ Ethiopian Horticulture and Agricultural Investment Authority Establishment Regulation, *supra note* 74, art., 5 sec 1.

to handle land requests for investments in the manufacturing, agriculture, and other sectors in an efficient, transparent and predictable manner.⁷⁷ However, it is not clear as to whether large scale agricultural investment lands are allotted by the Ethiopian Horticulture and Agricultural Investment Authority since the new investment law don't specifically distinguish based on the scale of agriculture investment land.

In brief, the modalities of government allotment and public auction are similar since benchmark lease prices are commonly applicable despite the absence of competition process for acquiring the land in the former case. The modes of acquiring land through government allotment provide opportunity for the investor to bypass the hustle of competitive public auction which may take long duration to complete acquisition of the land.

3.3. Acquiring Investment Land through Rental System

Unlike the previous two modes of acquiring land for investment that are considered as a primary channel for land use transactions through the state land lease system, land rental option depends on secondary contractual arrangements between private landholder and an investor. Accordingly, investors may acquire land through rental system based on at least two contractual arrangements. The first arrangement for an investor to acquire land for investment purposes relates to rental land use rights concluded between the investor and the rural or urban landholder. Any person who lawfully holds urban land may lease or rent his usufruct rights to any investor who wants such land for investment purposes through contractual arrangements. Similarly, investors may also acquire rural land use rights for agricultural investment purpose from farmers or pastoralists on the basis of contractual arrangements.⁷⁸ The Rural Land Administration and Land Use Proclamation states,

⁷⁷ Investment Proclamation, *supra note* 71, art 51 sec 1.

⁷⁸ Rural Land Administration and Land Use Proclamation, *supra note* 4, art. 8 sec 3: In addition to use rights a landholder may also undertake development activity jointly with the investor in accordance with the contract he concludes.

Peasant farmers, semi-pastoralist and pastoralist who are given holding certificates can lease to other farmers or investors land from their holding of a size sufficient for, the intended development in a manner that shall not displace them, for a period of time to be determined by rural land administration laws of regions based on particular local conditions.⁷⁹

However, valid transfer of rural land use right to private investors in this situation should fulfil two conditions as an acceptable land lease or rental arrangement in the eyes of the law. First, the rural land rental agreement to be concluded should secure the consent of all the members who have the right to use the land and be approved and registered by the competent authority.⁸⁰ Second, any rural land held through lease or rental should be registered by the competent authority.⁸¹

The second arrangement for an investor to acquire land for investment purpose relates rental or lease of land from another investor who already acquired land through allotment or tender process and holding lease hold title deed but wants to sub-lease together with on-built facilities or landed property.⁸² This is clearly provided under the urban land lease law as the lease hold right of an investor who may transfer his leasehold right or use it as collateral or capital contribution.⁸³ It should be noted that unlike urban land lease holding system that permits investors to sub-let or transfer all the contractual rights over the leased land, an investor who has leased rural land may only present his use right as collateral.⁸⁴ This feature of acquiring rural land use rights for investment makes the option of land rental unique from the concept of lease hold system because the former lease arrangement does

⁷⁹ *Id.*, art 8 sec 1.

⁸⁰ *Id.*, art 8 sec 2.

⁸¹ *Id.*, art. 6 sec 6 & art 8 sec 3.

⁸² Urban Lands Lease Holding Proclamation, *supra* note 69, art. 24 sec 1 & 2.

⁸³ *Id.*

⁸⁴ Rural Land Administration and Land Use Proclamation, *supra* note 4, art. 8 sec 4.

not involve transfer of lease hold title deed which in the rural land context is land 'holding certificate'.⁸⁵

In general land rental system as a mode of acquiring land use rights for investors differs from the avenue of land provision provided through tender process and government allotment since parties to the land rental arrangement are both private parties. The role of government in this case is limited to registration of rental agreements while rental price including terms and conditions are determined based on the mutual agreements of private parties.

4. Economic Analysis of Legal Options for Investment Land Acquisition

In the preceding section, the legal frameworks that set out rules to regulate the three modes of acquiring land for investment operations were examined. This section examines whether these legal options for acquiring land for investment purposes foster the reduction of transactions costs within the law and economics frameworks articulated in Section 1.

4.1. Property Rights Economics and Transaction Costs

In the law and economics scholarship, the recognition of the relationships between property rights and transaction costs lays the normative foundations for analyzing different structures of property ownership. Hence, it is important to evaluate the legal rules that regulate property ownership of land under the agency of state monopoly to unfold the extent to which law helps to realize efficient allocation of resources by reducing transaction costs during the exchange of property rights to land.⁸⁶ In the early economic thoughts, efficiency of property rights under public ownership of land was

⁸⁵ For more discussions see Tesfaye Teklu, *Rural Land, Emerging Rental Land Markets and Public Policy in Ethiopia*, 16 AFRICAN DEVELOPMENT REVIEW 176 (2004).

⁸⁶ Peter J Boettke and Rosolino A Candela, *Development and Property Rights* in, ENCYCLOPEDIA OF LAW AND ECONOMICS (Jürgen Backhaus (ed.), Springer 2015).

contended because of the thinking that such property rights regimes are insufficiently protected and not well-defined as is the case in private property rights regime.⁸⁷ For scholars of economics, property right regimes ‘that do not contain the right of alienation are considered to be ill-defined’.⁸⁸ It is a widely held economic view that absence of right of alienation in property right system presumably leads to inefficiency as it impedes the transfer of such property to the highest valued use.⁸⁹ Thus, private land ownership is viewed as a typical assignment of property rights that gives the owner of an asset the right to the use and enjoys the fruits of the asset to the exclusion of others and the freedom to transfer these rights to others.⁹⁰ It is on the basis of such assumptions that private property rights in land is argued to encourage efficiency of land allocation by facilitating market exchanges through land transferability that ‘allows such resources to end up in the hands of producers and consumers with higher valuation’.⁹¹

With the introduction of new property rights economics, the idea that common or public property regimes are inefficient when compared to private property regimes was revisited. In recently advanced property rights theory, it is contended that most of the property system that are considered common or public property regimes also involve individuals or groups who hold ‘sufficient rights to make decisions that promote long-term investment and harvesting from a resource’.⁹² Hence, the fact that individuals in public land ownership system do not possess the right to alienate their property

⁸⁷ E Ostrom & C Hess, *Private and Common Property Rights*, in ENCYCLOPAEDIA OF LAW AND ECONOMICS 338 (Boudewijn Bouckaert (eds), Edward Elgar 2000).

⁸⁸ *Id.*, 339.

⁸⁹ *Id.*

⁹⁰ Ilya Segal & Michael D Whinston, *Property Rights*, in HANDBOOK OF ORGANIZATIONAL ECONOMICS 100-158 (R. Gibbons & J Roberts (eds), Princeton University Press 2013); Demsetz (1964) and Alchian (1965) also define ‘property rights as individuals’ rights to the use, income, and transferability of assets, a definition corresponding to the partition in Roman law between *usus*, *fructus*, and *abusus*, respectively’. See Armen A Alchian, *Some Economics of Property Rights*, 30 IL POLITICO 816–829 (1965); H Demsetz, *The Exchange and Enforcement of Property Rights* 7 JOURNAL OF LAW AND ECONOMICS 11 (1964).

⁹¹ Demsetz, *supra note* 90, at. 11-26.

⁹² Ostrom & Hess, *supra note* 87 at 341.

rights does not necessarily mean that they do not have the right to earn income from the resource and the right to determine who may access and harvest from a resource.⁹³

The recognition of the idea that public property regime such as public ownership of land could be malleable to multiple use rights leads to bundle of rights capable of contractible rights.⁹⁴ According to Ronald Coase, what matters more is not who owns certain thing in the context of full ownership but whether rights on such things could be set up with ‘zero transaction cost’ making resource allocation system efficient and independent of the pattern of ownership.⁹⁵ The Coasean analysis assumes that in a condition of ‘costless market transactions’, monopolies of full ownership rights may not influence its allocability⁹⁶ that makes all property regimes alternatives efficient.⁹⁷

However, in real world, transaction cost may not be zero since property as a bundle of rights is authoritatively prescribed or assigned by the state for each resource. In such situation, it would matter whether property rights assigned by the state are ‘broad or narrow, clear or ambiguous, or *in rem* or *in personam*’, since it may impose positive transaction costs on participants in the economy.⁹⁸ In other words, how legal rules are designed to facilitate transactions of property rights determines the feasibility of exchange of rights. Hence, it could be argued that the ability of a legal institution as a means to facilitate the efficient allocation of resources is evaluated in terms of measures it takes to reduce transaction costs necessary to setup the exchange of property rights. Such is the version of transaction costs notion mainly espoused in the law and economic analysis of property rights thought

⁹³ *Id.*

⁹⁴ Arruñada Benito, *Coase and the Departure from Property*, in THE ELGAR COMPANION TO RONALD H. COASE 305-319, 308 (Claude Ménard & Elodie Bertrand (eds), 2016).

⁹⁵ Ronald H Coase, *The problem of social cost*, 3 J. LAW & ECON. 1, 19 (1960).

⁹⁶ Eirik G. Furubotn & Svetozar Pejovich, *Property Rights and Economic Theory: A Survey of Recent Literature*, 10 JOURNAL OF ECONOMIC LITERATURE 1139 (1972).

⁹⁷ Steven NS Cheung, *Transaction costs, risk aversion, and the choice of contractual arrangements*, 12 J. LAW & ECON. 23–42 (1969).

⁹⁸ Thomas W. Merrill & Henry E. Smith, *Making Coasean Property More Coasean*, 54 J. LAW & ECON. S77-S104, S78 (2011).

by Ronald Coase and further elaborated by other scholars. The Coasean transaction costs involve setup costs to carry out exchange of property rights leading to a natural classification of transaction costs that can be obtained from the different phases of the exchange process itself.⁹⁹ Coase explains that,

In order to carry out a market transaction it is necessary to discover who it is that one wishes to deal with, to inform people that one wishes to deal and on what terms, to conduct negotiations leading up to a bargain, to draw up the contract, to undertake the inspection needed to make sure that the terms of the contract are being observed, and so on.¹⁰⁰

The term 'transaction costs', as emphasized by Coase in the above quote mainly involves search costs, communication costs, bargaining costs, contract drafting costs, and contract monitoring cost as 'the costs involved in the process of exchange of property rights. However, Carl Dahlman further crystallized the concept of transaction costs by classifying them into 'search and information costs, bargaining and decision costs, policing and enforcement costs.'¹⁰¹

The concept of transaction costs in the form of search and information cost involves the time and resources incurred to successfully identify appropriate parties in order for an exchange between such parties to be set up as a necessary precondition.¹⁰² Given the existence of imperfect information in the exchange market, costs for conveyance of information may be incurred to reduce uncertainty about property rights subject to transactions.¹⁰³ When parties agree to exchange property rights voluntarily, they do so because they believe that what they will obtain from the exchange is worth more than what they offer in return. According to Yoram Barzel, the transaction cost involved is 'the measurement costs of inspecting attributes of goods' in

⁹⁹ *Id.*,

¹⁰⁰ Coase, *supra note 95*, at 15.

¹⁰¹ Carl J. Dahlman, *The Problem of Externality*, 22 J. LAW & ECON. 141, 148 (1979).

¹⁰² *Id.*, at 147.

¹⁰³ *Id.*, at 148.

which a party interested in their acquisition should incur to access information detailing the properties of the goods in question.¹⁰⁴

Transaction cost incurred in the form of ‘bargaining and decision cost’ involves costs of decision making during the process of negotiation to determine the positions of the parties leading to the conclusion of the property exchange contract.¹⁰⁵ However, the involvement of several parties in the negotiation process can likely increase the cost of decision making since agreeable contract terms can only be determined after costly bargaining between the interested parties involved.¹⁰⁶

The last but not least form of transaction cost involves ‘policing and enforcement costs’ incurred after the conclusion of the agreement for the purpose of policing and monitoring the other party to ensure compliance with the terms and conditions set out in the contract. The behaviors of opportunism that result from non-compliance of one of the parties to the transactions can be prevented by incurring costs for the enforcement of the agreement concluded.¹⁰⁷

In general, the above discussions show the instrumental role of the laws and institutions that structures property rights in shaping transaction costs that encourages the efficient allocation of resources. In the economic system where exchange of property rights to land underscores the importance of transaction costs, the way legal rules are designed to delineate and enforce property rights influences the ability of rights holder to facilitate transfer.¹⁰⁸ Hence, the law and economic analysis of property rights provides compelling insights on how economically efficient way of acquiring land in public property regimes may be achieved as it associates transaction costs

¹⁰⁴ Yoram Barzel, *Measurement Costs and the Organization of Markets*, 25 JOURNAL OF LAW AND ECONOMICS 27, 28 (1982).

¹⁰⁵ Dahlman, *supra* note 101 at 148.

¹⁰⁶ *Id.*

¹⁰⁷ *Id.*

¹⁰⁸ Luz M Velencoso, *Economic Questions Concerning the Rules for the Transfer and Publicity of Immovable Property*, in *TRANSFER OF IMMOVABLE PROPERTY IN EUROPE FROM CONTRACT TO REGISTRATION 4* (Andrea Pradi (ed.), 2012).

with the resources spent on delineating, protecting, and capturing control over resources in use and in exchange'.¹⁰⁹ From such a point of view, vague definitions and unsecure allocation of property rights militate against wealth production mainly because they increase transaction cost and inhibit exchange.¹¹⁰ Well defined property rights that clearly establish the scope of one's legal rights in any given parcel of land would reduce the transaction costs involved during the process of property rights exchange.¹¹¹ Therefore, when the law defines land rights in simple and clear terms, it is easier to exchange property rights since transaction costs would be lower than when they are complicated and uncertain.

The following section normatively evaluates the different options of acquiring land for investment purposes in Ethiopia. Therefore, the three options for acquiring land for investment previously identified under the land and investment laws of Ethiopian laws are analyzed from the perspectives of the three forms of transaction costs involved in the transfer of property rights.

4.2. Normative Assessment of Legal Options for Acquiring Land Use Rights

As discussed in section 2, land market in Ethiopia is characterized by the monopoly of the state where land is allocated through the limited channel provided by the law. In addition, transfer of land through sale is restricted and the lawful means of acquiring land is limited to the three major options—land lease tender, government allotment and land rental by lawful possessor or private landholder. Based on the outline of the three modes of acquiring land for investment purpose made above, the involvement of transaction costs in the process of property rights exchange can be

¹⁰⁹ N.J Foss, *Property Rights Economics*. in ELGAR COMPANION TO TRANSACTION COST ECONOMICS 97 (Peter G. Klein, Michael E. Sykuta (eds), Edward Elgar Publishing, 2010).

¹¹⁰ CB Kerekes & CR Williamson, *Unveiling de Soto's mystery: property rights, capital formation, and development*, 4 JOURNAL OF INSTITUTIONAL ECONOMICS 300 (2008).

¹¹¹ Harold Demsetz, *Towards a Theory of Property Rights*, 57 THE AMERICAN ECONOMIC REVIEW 356 (1967).

categorized into two major segments. The first segment of transactions costs involves the process of land lease transfer rights through lease tender, allotment and rental options between government and the lessee investors. The second segment of transaction costs involve land use right transfer through rental system through the contractual arrangements as between farmers or pastoralists on the one hand and tenant investors on the other. The major difference between the two segments of transaction costs emanates from differences of parties involved in the process of acquiring land use rights. The process of acquiring land use rights for a specified duration in the former segment involves government agency and private investor while the later involves private parties with relatively equal, if not identical, bargaining powers. Thus, the law and economic analysis of transaction costs that involves the exchange process whereby investors acquire land use right in all three options are examined as follows.

4.2.1. Search and Information Costs

The search and information cost with regard to the process of acquiring urban land through the structure of lease tender system relates to the cost of searching for information of potential land auction or bid advertisement including the buying of bid document from the appropriate government office. In addition to the public advertisement of urban lands presented for lease tender, the law sets the rules on how information that relates to the parcel of land including the quantity, and quality of land grade, lease benchmark price and other detailed relevant data are freely accessible to the investors by obligating the appropriate government authority to publicize such information.¹¹²

Furthermore, the law also tries to minimize the information costs that relate to the attributes of land use property rights by setting rules requiring the government to prepare urban lands that (a) are free from legal claims of any party; (b) are prepared in conformity with the urban plan; (c) have access to basic infrastructure; (d) are parceled, delineated, assigned with unique parcel

¹¹² Urban Lands Lease Holding Proclamation, *supra note* 69, art. 10 sec 1 para. (a).

identification numbers; and (e) have site plans and fulfil other necessary preconditions prior to advertising urban lands.¹¹³ Thus, since there are specific norms that mandate the government bodies to implement urban land lease tender process following the rules of transparency and accountability, information costs incurred by the investor could be minimized if not totally avoided. This is because investors are still required to deal with the costs of incompleteness and imperfections of information acquired from the public bodies.

The information cost incurred to acquire land through government allotment is different from the information search costs of acquiring land through lease tender because there is no legal requirement on the part of the government to publish important information relating to the properties of land for investment. It requires investors to approach appropriate government bodies to seek similar information on urban land prepared for allotment by presenting feasible investment projects. Hence, one can easily realise that in the absence of accountability and transparent bureaucracy, the effort of acquiring information on allocable urban land without going through the established tender process could be as difficult as acquiring the land itself.¹¹⁴ Thus, an investor is required to expend much of his time and resource to search for insider information to know more about government's urban land development plan for investments. Furthermore, information search costs incurred in acquiring rural land for agricultural investment through government allotment could be minimal when it comes to the cost of collecting data on the quality of the land since responsible government agency is required to provide appropriate information that document on matters of agro-ecology, soil topography, agricultural products and crop suitability of the agricultural investment lands.¹¹⁵

¹¹³ *Id.*, art. 8.

¹¹⁴ *Id.*, art. 4 sec 2: Clearly hints these assertion as it states; 'the offer of lease tender and land delivery system shall adhere to the principles of transparency and accountability and thereby preventing corrupt practices and abuses to ensure impartiality in the processes'.

¹¹⁵ Ethiopian Horticulture and Agricultural Investment Authority Establishment Regulation, *supra note* 74, art. 6 sec 3.

The transaction costs incurred to acquire land through rental system from lease holding investor (who may decide to sub-let his holdings), farmers, semi-pastoralists and pastoralists could involve the search costs about the potential partner with lawful land holding right. It also involves incurring additional cost of information on specific situations of acquiring knowledge that relates to the rental market and quality of land. The FDRE Rural Land Administration and Land Use Proclamation contemplates the need to put in place land information system with the view to gather, analyse and distribute to the users.¹¹⁶ It also authorizes rural land administration authorities to maintain registration database that describes the holder of the rural land, the holders of the bordering lands, the types of use, and the rights and obligations of the holder.¹¹⁷ However, in rural land use system where land titling and registration is absent or ambiguous, an investor would inevitably cost time and resources to ensure that he is dealing with lawful possessor of the given parcel of land. In particular, if the investor is a new face to the area, discovering the lawful landholder of a given parcel of land under rental system may result in the high search and information cost. In this situation, 'the return to searching for the true' landholder with valid landholding certificate 'is the value of the increased certainty resulting from the augmented information concerning property rights in the land'.¹¹⁸ Thus, the investor may find it unproductive or unprofitable to undertake enough searches to acquire enough information to attain absolute certainty, due to diminishing marginal returns to search.¹¹⁹

It could be argued that the search costs involved in the identification of legally entitled landholder in the process of acquiring land in the cases of land lease tender and allotment would be relatively low when compared to the case of search costs involved to identify lawful possessor in the process of acquiring rural and urban land rights through lease or other contractual arrangements. In the former cases, investors are dealing with government

¹¹⁶ Rural Land Administration and Land Use Proclamation, *supra note* 4, art 2 sec 16.

¹¹⁷ *Id.*, art. 6 sec 5. See also Investment Proclamation, *supra note* 71, art. 52.

¹¹⁸ Omotunde E. G. Johnson, *Economic Analysis, the Legal Framework and Land Tenure Systems*, 15 J. LAW & ECON. 261 (1972).

¹¹⁹ *Id.*

bodies legally authorized to transact land use rights unless of course the property title of land prepared for allotment or tender is disputable. In the latter case absence of land registration system and landholding certificate puts investors in the limbo of legal uncertainty as it may be costly to deal with the wrong person who pretends to be the lawful holder of land use rights.

4.2.2. Bargaining and Decision Costs

In both processes of acquiring land through tender process and allotment, the investor bargains with the government on terms and conditions of land lease contract with varying degrees. In the former case, negotiation on further terms and conditions of the lease contract is conditioned upon participating in the bid and winning of the public tender. But in the latter case, the investor is required to persuade the relevant government body by justifying the importance of government land allotment without going through the tender process.¹²⁰ In both cases, investors who acquire land are subject to the rules of urban land lease hold system as they are required to sign lease contract with the relevant government body.¹²¹

The lease contract signed by the government and the lessee investor is adhesive by nature and should 'include the construction start-up time, completion time, payment schedule, grace period, rights and obligations of the parties as well as other appropriate details.'¹²² Decision making on the terms and conditions of the lease contracts are difficult for the investor since those terms and conditions listed under the contract are further regulated by the mandatory rules of land lease law as the obligations of the lessee investor. However, an investor may incur lawyering or agency cost to facilitate the conclusion of the agreement and appreciate 'the contents of the lease contract' through an informed decision.¹²³ In addition, there could also be

¹²⁰ Urban Lands Lease Holding Proclamation, *supra note* 69, art.2 sec 10 & art. 12.

¹²¹ *Id.*, art. 16(1).

¹²² *Id.*, art. 16 sec 2.

¹²³ *Id.*

re-bargaining costs that inexorably result from the incomplete nature of the contract.¹²⁴

The cost of bargaining and decision to acquire rural and urban land through rental system somewhat presents a unique transaction cost analysis compared to the monopolistic land market dealings with the government revealed in the previous options. First, an investor who wants to acquire land through rental arrangement from rural landholders for ‘development activities’ deals with multiple potential land renters with the tendency to increase negotiation costs. The cost of negotiation is further exacerbated by the mandatory provisions of the rural land law that require the investor to secure the consent of all the members who have the right to use the rural land and seek the approval and registration of the competent authority.¹²⁵ As such, an investor may be required to seek the consent of all family members of the rural landholder who want to rent the land to investors. Furthermore, the contracting cost also relates the costs of drafting the contract and registering the land rental before the competent authority.¹²⁶ Though land rental system provides a wide array of opportunities to negotiate land with rural land renters on competitive basis, the diversity of negotiation could be very costly.

¹²⁴ It is argued that in the transaction cost economics approach, the complete-contract benchmark is unattainable. The vital question is not incompleteness in itself, but rather ‘the reasons for which some contracts are more incomplete than others.’ Contracting parties are supposed to be unable to take into account all contingencies that might affect a transaction. Moreover, they do not always know the optimal response to foreseeable contingencies that should be stated in the contract. The completeness level is, therefore, difficult to evaluate. Every provision in a contract is assumed to be imperfect, and specifying a particular provision may be worse than specifying nothing.’ See Stéphane Saussier, *Transaction costs and contractual incompleteness: the case of Électricité de France*, 42 JOURNAL OF ECONOMIC BEHAVIOR & ORGANIZATION 189, 192, (2000).

¹²⁵ Rural Land Administration and Land Use Proclamation, *supra note* 4, art. 8 sec 2.

¹²⁶ *Id.*, art. 6 sec 6 & art.8 sec 3.

4.2.3. Monitoring and Enforcement Cost

The costs of monitoring and enforcement, in the context of acquiring land through land lease tender and allotment, involves the costs incurred to ensure compliance with the terms and conditions of the lease contract and protection of lease-hold land use rights from third party interference. For instance, prior to advertising urban lands prepared for tender an appropriate government body is required to ascertain that the plot of land prepared for public auction is free from legal claims of any party.¹²⁷ The government body who signs land leasehold contract with the investor should comply with this legal obligation in order to reduce the monitoring costs of the investor who acquire land through lease tender and allotment.

Furthermore, to secure the enforcement of the land lease holding rights acquired through tender and allotment, the investor is required to expend resources to renew the land lease contract in addition to the costs incurred to maintain the protection of landholding rights from third party claimants. The interference of third-party claimant could hamper the peaceful enjoyment of land use rights. In particular, the failure of the government to transfer land use right free from third party claims could further exacerbate the enforcement costs of the investor as disputes over a plot of land usually end up with litigation.¹²⁸ For instance, the proclamation that regulates, expropriation of landholdings for public purposes, payment of compensation and resettlement of displaced people provides that any person

¹²⁷ Urban Lands Lease Holding Proclamation, *supra note* 69, art. 8 sec. 1.

¹²⁸ The urban land lease law describes potential land disputes that could arise due to failure of the government to pay commensurate compensation for expropriated land and unlawful land clearance orders. See Urban Lands Lease Holding Proclamation No. 721/2011 Articles 28—30. It should be noted further that a permit holder's urban land right is subjected to expropriation for public interest and upon payment of compensation. In such case cost may be incurred from litigation to defend holding rights by challenging the existence of public interest justifying expropriation. The law stipulates 'the use of land defined as such by the decision of the appropriate body in conformity with urban plan in order to ensure the interest of the people to acquire direct or indirect benefits from the use of the land and to consolidate sustainable socio-economic development'. See Urban Lands Lease Proclamation, *supra note* 69, art 2 sec 7.

who received an order of expropriation of his landholding or who has an interest or claim on the property to be expropriated may file an application to the appeal hearing body and to the appeal hearing council.¹²⁹ Hence, in the absence of payment of compensation and resettlement of displaced lawful landholders for public purposes, the likelihood of complaint and court litigation may require investors to involve in the process of defending leasehold rights. This is because a landholder who is dissatisfied with the decisions of appellate courts has ‘the right to continue his claim’ while it is a requirement to ‘surrender his landholdings for the continuance of the development’.¹³⁰ This indicates that there is a probability for an investor to acquire expropriated land under dispute as the relevant government body may transfer landholdings of displaced persons with the right to continue their claims over such land even after surrendering their landholding.

In the context of rural land allotment, the presumption that certain lands are free from farmers and pastoralists could be misleading and may result in third party claims.¹³¹ Because, what is thought to be a land freed from farmers or pastoralists may not be free actually. According to the study conducted by Dessalegn, land that has been transferred to investors includes arable land, land used for grazing, woodland, forest land, savannah grassland, and wetlands inside a formally designated national park, protected area or wildlife sanctuary.¹³² It is noted that the compensation paid to farmers is low when compared to the long term effect of loss of farm land, pasturage and grazing rights, water utilization and the loss of access to firewood and useful plants.¹³³ Hence, agricultural investment lands allotted

¹²⁹ Expropriation of Land holdings for Public Purposes, Payments of Compensation and Resettlement of Displaced People Proclamation No.1161/2019, arts. 18 & 19.

¹³⁰ *Id.*, art. 20 sec. 2.

¹³¹ *See*, for instance, the repealed Ethiopian Agricultural Investment Land Administration Agency Establishment Council of Ministers Regulation No. 283/ 2013, art. 6 sec 1. However, the repealing Regulation, clearly follows more pragmatic approach as it requires the authority to ‘make sure land is free from third party possession’ before transferring to investors. *See* Ethiopian Horticulture and Agricultural Investment Authority Establishment Regulation, *supra* note 74, art 6 sec 3.

¹³² Dessalegn, *supra* note 52 at 17.

¹³³ *Id.*

to investors could be insecure since there could be a high probability of peasant encroachments by grazing livestock on the land, disputing boundary limits, taking one's grievances to court, or appealing to higher authorities for redress of grievances.¹³⁴

For instance, the law stipulates that agriculture investment lands to be transferred to investors through allotment are presumed to be 'free from farmers and pastoralists possession and not required by the regional state for any other specific purpose.'

Similarly, the costs of monitoring compliance in the context of both rural and urban land rental system could be manifested in terms of expending time and resources to prevent the opportunistic desire of the private landholder to change land rental price. Particularly, in the absence of appropriate institutions in rural area to enforce non-compliance of terms and conditions indicated in the rental contract, the likelihood of enforcement costs to restore the rights damaged in the course of execution of the contract could be high through the private ordering. The social and cultural values attached to land in the rural community in Ethiopia may also raise the investor's cost of enforcing land use rights acquired through rural land rental arrangement. Besides, it is a well-established proposition in law and economics literature that the high costs of executing written contracts due to illiteracy (which is prevalent in rural Ethiopia)¹³⁵ tends to increase the enforcement costs.¹³⁶

¹³⁴ *Id.*

¹³⁵ According to the Ethiopian Welfare Monitoring Survey 2011 report, of the total population in the country 46.8 percent are found to be literate. This survey shows that the literacy rate in urban areas is about two times higher than that of rural areas (78.0 percent against 39.5 percent). See Central Statistics Agency Ethiopian Welfare Monitoring Survey 2011 Summary Report (April 27, 2012) available at: <https://catalog.ihsn.org/index.php/catalog/3124/download/46161>

¹³⁶ It is argued that when the legal enforcement of contracts is weak such contracts are discouraged because of too high enforcement costs. Hence, in such situation it opens the door for the costs to be covered by the contracting parties. See Johnson, *supra* note 118 273.

Concluding Remarks

The idea that the restriction of land sale in state or public land ownership system inhibits allocation of land rights for investment has dominated the law and politics of land governance in Ethiopia. But the solution proposed for the supposed ill of the current land ownership regime is private ownership of land in its classical understanding of bundle of ownership rights. Private property regime was vociferously advocated as optimal property rights regime that facilitates efficient land allocation. However, new insights in the field of law and economics have demystified the idea that 'property rights can be and often are disaggregated' in the sense that property rights are 'web of mutually dependent relationships between people rather than relations between persons and things'. The bundle of land rights with defendable and enforceable property rights has profoundly reshaped our approach towards the institution of public land ownership. Normative insights from transaction cost economics have crystallized a new perspective of how property rights in land could be treated as a bundle of rights that accommodates multiple property rights holders. Accordingly, a government as a custodian of public land can retain ownership right and assign usufruct land rights to private investors. What matters in any property regime to land (public or private) is whether legal rules are efficiently designed in such a way to facilitate the transfer of property rights. Scholars in the law and economics field widely argued that the efficiency of legal rules is measured based on its capability to reduce transaction costs during the exchange of property rights.

The thought that law plays an instrumental role for reducing transaction costs during the exchange of land use rights has greatly influenced the legal contours of public land allocation system in many countries. In the Ethiopian context, the introduction of urban land lease hold system since 1993 indicates the imperatives of designing assignable usufruct rights within the frameworks of public ownership of land in order to attract investment activities. Based on this understanding, this piece analyzed how Ethiopian land law regime that regulates different modes of land rights transfer facilitates the reduction of transaction costs. The tools of transaction cost economics are utilized as normative yardsticks to evaluate the extent to which the rules governing three

modes of land rights transfer affect transaction costs. The three modes of acquiring land for investment purpose — leasehold (lease tender), government allotment and rental system — were identified and analyzed in light of the three elements of transaction costs. Hence, the legal rules regulating these three legal options were analyzed in light of the normative frameworks of search and information costs, bargaining and decisions costs and monitoring and enforcement costs. Accordingly, the findings of the economic analysis of the three legal options are provided as follows.

Firstly, it is found out that the legal rules regulating transfer of land use rights to the investors through lease tender system is more efficient as it adequately prescribes rules that assist investors to minimize the overall transaction costs. Investors who opt for acquiring land through lease tender process are legally entitled to access with appropriate information about the land prepared for lease tender including its quality and price beforehand. The rules that regulate land lease tender process relatively address problems of information asymmetry as the law requires the appropriate government body to advertise bid and publish essential information in relations to the quality, quantity and minimum bid price to the public in relation to the land proffered for tender. This modality provides investors with the opportunity to compare and contrast the price and quality of land before participating in the bidding process thereby reducing bargaining and decision costs on price and quality of the tendered land. As regards minimizing monitoring and enforcement costs, the terms and conditions of land lease transactions are regulated by lease contract with a clear back up of default rules under the land lease law. The property right that emanates from land lease system is well defined through two vital mechanisms. The urban land lease requires the government to transfer parcel of land free from third party claimants ensuring security of tenure and minimizing possible future enforcement cost to assert property rights. And once agreement is reached on the terms and conditions of the lease contract, the investor is provided with a leasehold permit certificate.

Secondly, it is also found out that the legal rules regulating transfer of land use rights to the investors through government allotment is less optimal in light of assisting investors to minimize the overall transaction costs when compared to tender-based land lease system. Unlike the modality of acquiring land through

tender-based land lease process, an investor who opts for allotment of land by government is required to search relevant information about the land he requested for investment purposes.

Only those investors who want to compete through tender process are presented with the ease of access to information on the land presented for the public auction. In view of lack of transparency, widespread corruption and political favouritism in Ethiopian land administration system,¹³⁷ the cost of dealing with bureaucratic hurdles and bargaining for land allotment could be unbearable exercise for any investor. The costs of monitoring and enforcement of government allotted land rights are higher when compared with the case of acquiring land through public tender. Because, it is less likely that the government would easily allot parcel of urban land free from third party claims. The cost of monitoring compliance with rural agricultural land allotted for investors could be similarly high given the unique constitutional guarantee that prohibits the eviction of farmers and pastoralists from their rural landholding.

Thirdly, the legal rules that regulate the process of transferring land use rights to investors from rural landholders through rental system represents the least optimal alternative compared to the other two land leasehold systems. The legal regime providing for the right of rural landholders to rent or lease their landholding right to the investors is limited by set of mandatory rules such as the requirements of consent of rural land holder's family member, approval and registration of land rent contract by appropriate government authorities and the cap on rental period. Hence, the legal regime that regulates rental land use rights is more gravitated towards the protection of the rights of land renters than to an investor-lessee. More importantly, the costs to search potential rural land renter and negotiating with all of the family members could discourage investors from renting rural land. In the absence of well-developed rural land information system, the rights of the renter could be poorly secured. The absence of well-defined landholding rights provides opportunities for third party encroachment

¹³⁷ Misganaw Gashaw Beza, *Corruption in the post-1991 urban land governance of Ethiopia: Tracing major drivers in the law*, 4 AFRICAN JOURNAL ON LAND POLICY AND GEOSPATIAL SCIENCES 42-48 2021.

which will increase the time and resources of the investor to monitor compliance with land rights acquired through rental system.

Based on the above findings, the author strongly argues that the legal frameworks governing land allocation for investment purposes mainly facilitate the transfer of land rights from the public body to private investors. The pivotal role of the law as a means for reducing transactions costs is profoundly limited to the process of transferring land rights between the public bodies and private investors. This in turn limits the possibilities of transferring usufruct rights as between individual land holders to enhance the productive use of land resources of the country. The economic implications of state dominated land allocation system with the objectives of facilitating investment projects cannot be underestimated given the scale of land possession in the hands of individuals who may not value it the most. It is hoped that this modest contribution could provoke further research in the legal and economics academia.

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