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Current Issues In Just Compensation

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THE 2005 "BLIND-LEADING-THE BLIND" AWARD

"At the [Department of Transportation's] request, the jury was taken on a bus tour of defendants' property. The parties vigorously dispute what the jurors saw on this tour. [The Department] contends that the jurors saw mainly an undeveloped tract with some commercial buildings under construction . . . . Defendants contend . . . that the jurors saw many completed office buildings . . . and only a small portion that remained undeveloped. There is no record to support either party's contention."

Michigan DOT v. Haggerty Corridor Partners Ltd. Pshp.,
473 Mich. 124, 700 N.W.2d 380, 383 (2005).

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I. INTRODUCTION: IN THE WAKE OF KELO, A NEW FOCUS ON JUST COMPENSATION.

Prior to the U.S. Supreme Court's June 2005 decision in Kelo v. New London, 125 S. Ct. 2655 (2005), just compensation was generally regarded as a mere remedy, i.e., an amount of money to be calculated, either as part of eminent domain proceedings or in the relatively unlikely event that a court held that an inverse or regulatory taking had occurred. While the principles and methods for valuing property interests and calculating just compensation for a taking of property are sometimes difficult to apply and widely acknowledged to not compensate a property owner for all losses that she incurs in direct or inverse condemnation, prior to Kelo the efficacy of the calculation rules themselves was rarely the focus of takings litigation or commentary, or legislation.

For the moment at least (that is, as of the drafting of this paper), the debate has changed; property owners, government officials, judges, and legislators are newly focused on just compensation, for three reasons. First, even though no compensation issue was before the Court in Kelo, at the oral argument Justices Kennedy and Breyer peppered counsel for both sides with questions about two aspects of compensation: whether the traditional "fair market value" just compensation standard makes a condemnee whole; and whether a condemnor who increases the unit value of properties by assembling them should pay some of this increased value to the condemnees, in the form of "premium" compensation. Second, the Kelo decision, of course, by strongly reaffirming federal court deference to legislative and policy judgments about condemnation, reminded us that for condemnees, especially residential owners and tenants, just compensation is not just a calculation of money but a potential way to shape when and how eminent domain is used. See, e.g., Laura Burney, Just Compensation and the Condemnation of Future Interests: Empirical Evidence of the Failure of Fair Market Value, 1989 B.Y.U. L. Rev. 789, 790.

Third, with the Kelo decision expressly inviting state legislatures and courts to fashion their own balances between condemnation authority and property owner rights, legislators and judges are likely now to at least reconsider if not reconfigure the efficacy and adequacy of long-established compensation principles and statutes, and to determine whether just compensation should be adjusted in order to control when and how eminent domain powers are utilized.

In other words, in the wake of Kelo, just compensation has been transformed from a mathematical formula for awarding damages to a part of the policy debate about eminent domain, regulatory takings, and protection of property rights.

This paper attempts to illuminate several aspects of this current debate. It begins with a brief summary of the long-established, basic principles used in determining just compensation, including the primary goals of compensation awards and the most significant limitations on what appraisers and courts may consider when determining values. As a way to illustrate several of these principles and limitations in practice, § III reviews several recent judicial decisions in which valuation methods were vigorously contested.

Section IV discusses the "premium compensation" question raised by Justice Kennedy. It reviews the rationale for higher awards and problems that might result from such increases, and from using changes in compensation formulas to limit or redirect governmental use of eminent domain. This section discusses, as an example, bills currently pending in the New York legislature that would award 150 percent of market value or rent to owners or tenants whose residence is taken by eminent domain to promote economic development.

The last section of this paper discusses yet another emerging complexity in the law of just compensation, by reviewing the growing split among state courts over the issue of whether environmental remediation costs may be deducted from just compensation awards in eminent domain proceedings.

II. BASIC PRINCIPLES OF JUST COMPENSATION.

A. The Stated Goal: "Making The Property Owner Whole."

The Fifth Amendment to the Constitution provides that the "government shall not take private property for public use without just compensation." U.S. Const. Amend. V. The Fourteenth Amendment has been interpreted to impose this requirement on the states as well. Chicago B. and Q. R. Co. v. Chicago, 166 U.S. 226, 17 S. Ct. 581 (1897). State constitutions or state takings jurisprudence implement this federal constitutional requirement, and thus whenever a taking by eminent domain occurs, or a court holds that government is liable for an inverse or regulatory taking, the issue of just compensation will arise.[1]

The right to just compensation is universally described in two companion phrases. The first is that the condemnee "is entitled to be in as good a position pecuniarily as if his property had not been taken." See, e.g., Olson v. United States, 292 U.S. 246, 54 S. Ct. 704, 708 (1934). "The owner is to be put in the same position monetarily as he would have occupied if his property had not been taken." Almota Farmers Elevator & Warehouse Co. v. United States, 409 U.S. 470, 93 S. Ct. 791, 794 (1973); United States v. Miller, 317 U.S. 369, 63 S. Ct. 276, 279 (1943); Amen v. City of Dearborn, 718 F.2d 789, 799 (6th Cir. 1983). "The purpose of just compensation is to put property owners in as good a position as they would have been in had their property not been taken from them." State ex rel. Department of Transportation v. Barsy, 113 Nev. 712, 941 P.2d 971, 975 (1997); Miller Bros. v. Department of Natural Resources, 203 Mich. App. 674, 513 N.W.2d 217, 222 (1994). "[T]o the extent that a court awards less than just compensation for a taking out of concern for the public purse, it has provided a constitutionally

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[1] In several states, of course, constitutional provisions or statutes, or both, require compensation for property that is taken "or damaged." This latter phrase broadens the range of potential compensation, but interpretation of its scope varies from state to state. This paper focuses on compensation for property that is "taken," which is the more prevalent standard.

insufficient remedy." Wisconsin Retired Teachers Association v. Employee Trust Funds Bd., 207 Wisc.2d 1, 558 N.W.2d 83, 96 (1997).

The companion phrase is that the purpose of just compensation is "to make the property owner whole" – thereby implying that, one way or the other, all losses caused by the government's action will be directly compensated or otherwise recognized and indemnified or ameliorated. United States v. 564.54 Acres of Land, 441 U.S. 506, 99 S. Ct. 1854, 1860 (1979); Olson v. United States, 292 U.S. 246, 54 S. Ct. 704, 708 (1934).

A similarly expansive statement of just compensation goals is the inclusion of the full range of interests taken by the condemnor. Just compensation includes "all elements of value that inhere in property" and must be determined by "all factors relevant to its cash or market value," Michigan DOT v. Haggerty Corridor Partners Limited Partnership, 473 Mich. 124, 700 N.W.2d 380, 386 (2005), quoting U.S. v. Twin City Power Co., 350 U.S. 222, 76 S. Ct. 259, 266 (1956) (Burton, J., dissenting). Similarly:

> Every kind of right or interest in property which has a market value must be compensated for . . . . In a determination of what [the appropriate] amount should be, all elements legitimately affecting value of the [property interest taken] should be considered.

Canterbury Realty Co. v. Ives, 153 Conn. 377, 216 A.2d. 426, 430 (1966).

These broadly stated goals are reinforced by the universally-accepted principles that just compensation is an equitable rather than legal determination, and that flexibility in valuation approaches by courts are essential to ensuring that compensation goals are met in particular cases. "The question of just compensation contemplated by the Constitution is more an equitable question rather than a strictly legal or technical one." Winchester v. Cox, 129 Conn. 106, 26 A.2d 592, 597 (1942). See also, e.g., Bedford v. U.S., 23 F.2d 453, 456 (1st Cir. 1927); Hardin v. South Carolina Dep't of Transp., 359 S.C. 244, 597 S.E.2d 814, 816 (Ct. App. 2004).[2] In his influential San Diego Gas dissent, Justice William Brennan emphasized this point: "It should be noted that the Constitution does not embody any specific procedure or form of remedy that the States must adopt. . . . The States should be free to experiment in the implementation of this rule, provided that their chosen procedures and remedies comport with the fundamental constitutional command." San Diego Gas and Electric Co. v. City of San Diego, 450 U.S. 621, 101 S. Ct. 1287, 1308. "It is difficult, if not impossible, to lay down a rule of universal application as to what may be considered as elements of damage, as the equities of the parties must more or less depend upon the particular facts and circumstances of each case." Aladdin, Inc. v. Black Hawk County, 562 N.W.2d 608, 611 (1997).

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[2] On the other hand, it has been held that just compensation differs from remedies in equity because it "is a compensatory remedy." City of Monterey v. Del Monte Dunes, 526 U.S. 687, 119 S. Ct. 1624, 1639 (1999).

> The specific formulas of valuation developed by the courts are all designed to assure that the condemnee receives just and adequate compensation. These formulas are all means to this end; there is no artificial formula by which alone such compensation may be determined. Specific formulas of valuation . . . should be used to effectuate this end, not to defeat it.

State ex rel. Department of Highways v. Terrace Land Co., Inc., 298 So.2d 859, 863 (La. 1974).

B. Limitations On Compensation.

The reality of modern just compensation jurisprudence is that, after intoning the broad goals of restoring the owner to his original position and ensuring that she is made whole, courts routinely apply limitations that result in a variety of actual, financial, personal, and business losses going uncompensated in eminent domain proceedings and cases of liability for regulatory takings. Thus, the principles of making the property owner whole and putting him in the same position as if the taking had not occurred are tempered by these significant limitations: (1) compensation is limited to the market value of the property taken, and does not include consequential or collateral financial or personal losses; (2) compensation may not be awarded based on speculation or insufficient proof of loss; and (3) compensation is based on what the condemnor loses, not what the condemning authority gains.

This first limitation is illustrated by the seminal case of Kimball Laundry Co. v. United States, 338 U.S. 1, 69 S. Ct. 1434 (1949). The underlying case, of course, involved the government's appropriation of a laundry business during World War II. The Court emphasized that even though the scope and consequences of government's interference with private use of property may have been broad, when the issue turned to compensation for that interference, courts were obligated to use objective standards and provable facts that have "external validity" and are not dependent on the condemnee's subjective attachment to it or unique ability to exploit its value:

> The value of property springs from subjective needs and attitudes; its value to the owner may therefore differ widely from its value to the taker. Most things, however, have a general demand which gives them a value transferable from one owner to another. As opposed to such personal and variant standards as value to the particular owner whose property has been taken, this transferable value has an external validity which makes it a fair measure of public obligation to compensate the loss incurred by an owner as a result of the taking of his property for public use.

69 S. Ct. at 1437 (emphasis added).

The second limitation is that just compensation awards may not be based on speculation. See U.S. v. Bodcaw Co., 440 U.S. 202, 99 S. Ct. 1066, 1067 (1979); Mitchell v. U.S., 267 U.S.

341, 45 S. Ct. 293, 294 (1925); Sixth Camden Corp. v. Township of Evesham, 420 F.Supp. 709, 729 (D.N.J. 1976). In addition to reflecting the basic requirement of evidence law that only reliable, probative facts are admissible, this limitation reflects the reality that while the market for property rights is usually readily identifiable (for example, "home builders in the region surrounding the subject, residentially-zoned property"), subjective losses, consequential damages, and the market for a business or its products or services is likely to be more expansive and more difficult to identify. In Eljay Realty Co. v. Argraves, 149 Conn. 203, 177 A.2d 167, 179 (1962), the court stated that, "[I]t is generally recognized that neither the past nor estimated future profits of a business are reliable evidence of the value of the land on which the business is located because business profits depend on so many factors that their effect on the market value of the real estate is too remote." In other words, in determining the value of real estate and factors influencing it, appraisers and courts are able to define the geographic scope of the market and the participants who will be the "willing buyers" in a value determination. On the other hand, the value of a business or an owner's subjective attachment to land are likely to depend on a broader array of factors, including the company's financial condition, domestic and international competition, and available financing. Thus, the valuation of transferable real estate is less speculative than the valuation of a commercial enterprise.

The third general, important limitation is that value of land is not measured by what the government gains, but by what is taken. "The general rule is that the loss to the owner from the taking, and not its value to the condemnor, is the measure of damages to be awarded in eminent domain proceedings."[3] Gray Line Bus Co. v. Greater Bridgeport Transit District, 188 Conn. 417, 449 A.2d 1036, 1042 (1982). See also Brown v. Legal Foundation of Washington, 538 U.S. 216, 123 S. Ct. 1406, 1419 (2003), citing Boston Chamber of Commerce v. Boston, 217 U.S. 189, 30 S. Ct. 459, 460 (1910).

Two exceptions have been recognized to this third principle. The first is the so-called "scope of the project" exception. United States v. Miller, 317 U.S. 369, 63 S. Ct. 276, 281 (1943). This exception states that while just compensation should not be affected positively or negatively by the government's plan to use eminent domain, if one owns property that is outside the scope of the government's original or primary project, she may be compensated for enhanced value if the government later expands the project and condemns her land. The second exception arises when government acts to intentionally drive down property values by announcing condemnation but then engaging in inordinate delay or oppressive tactics, during which the owner's property is devalued by being in limbo. In such a case, the owner may be compensated at the value that preceded commencement of the project. The best known case of this type is Klopping v. City of Whittier, 8 Cal.3d 39, 500 P.2d 1345 (1972).

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[3] A national sampling of decisions stating this principle appears in Professors Callies' and Saxer's forthcoming book chapter, "Is Fair Market Value Just Compensation," n.25 (see Acknowledgment, supra).

These limitations, of course, reveal that just compensation in reality is not an indemnity but a compromise between the owner's loss and the government's obligation to compensate. The owner is not made whole, but is limited to demonstrable and transferable value of property. In other words, when a private property owner's land, residence, or business, or interest therein, is taken by eminent domain or so unjustly burdened as to constitute a regulatory taking, the owner is likely to receive as just compensation the identifiable, non-speculative, transferable value of her real property, but will not receive compensation for (1) any real property interest whose value cannot be determined with reasonable accuracy; (2) any enhancement to value resulting from the government's plans; (3) any increase in value that is offset by some other factor; (4) consequences to a business or commercial enterprise, such as loss of goodwill or interruption; (5) transaction costs, such as attorneys' fees; and (6) losses preceding the date of taking.

C. Most Widely Used Valuation Methods In Takings Cases.

The polestar in determining just compensation is market value, which entitles the condemnee to what a willing buyer would pay him as a willing seller, for the property's highest and best use, in cash at the time of the taking. Kirby Forest Indus. v. United States, 467 U.S. 1, 104 S. Ct. 2187, 2194 (1984). The determination of market value depends in the first instance on the type of taking.

1. Total permanent takings.

There are three accepted methods for valuing real property taken by eminent domain. First is the comparable sales approach, in which value is determined by comparing the subject property to substantially similar properties that have sold in the same market recently, making adjustments to account for differences, and determining what a willing buyer would pay if the property were marketed. The income approach is employed for any property, such as an apartment building, whose value is primarily dependent upon the amount of cash generated by its on-going operations. This method is generally regarded as a check on the accuracy of comparable sales, and is used instead of comparable sales where insufficient sales data exist in the relevant market. This method is also dependent upon the existence of reliable and relatively consistent income and expense data going back several years prior to the taking. See e.g. Correira v. New Bedford Dev. Auth., 375 Mass. 360, 377 N.E.2d 909, 911 (1978).

Replacement cost is disfavored as a method. It is used for properties that are unique or built for a special purpose, and therefore are not income-producing and are not sold enough to generate data for a market. In addition, replacement must be economically feasible. Heidorf v. Town of Northumberland, 985 F.Supp. 250, 261 (1997).

2. Partial, permanent takings.

When only part of a piece of property is taken, the landowner must be compensated for the land taken, plus any decrease in value experienced by the remaining property. Bauman v. Ross, 167 U.S. 548, 17 S. Ct. 966, 976-77 (1896). Generally, the courts will determine the fair market value of the property before and after the taking and award the landowner the difference. See United States v. Virginia Electric & Power Co., 365 U.S. 624, 81 S. Ct. 784 (1961). Awards for damage to the remaining ownership after a partial taking are referred to as "severance damages." City of Manchester v. Airpark Bus. Ctr. Condo. Unit Owner's Ass'n, 148 N.H. 471, 809 A.2d 777, 780 (2002).

3. Temporary takings.

Corrigan v. City of Scottsdale, 149 Ariz. 538, 720 P.2d 513 (1986), cert. den. 479 U.S. 986, 107 S. Ct. 577 (1986) is regarded as one of the most thorough discussions of temporary taking valuation methods. In that case, the Arizona Supreme Court identified five basic methods for compensation for a temporary taking: rental return, option price, interest on lost profit, before-after valuation, and benefit to the government. 720 P.2d at 518. However, recognizing that each of these measures works well in some cases and not well in others, and that no one rule adequately fits each of the many factual situations that may be presented in a particular case, the court declined to adopt any particular damage rule applicable to all cases. Instead, it held that "the proper measure of damages in a particular case is an issue to be decided on the facts of each individual case." Id.

The recent decision of the U.S. Court of Federal Claims in Cienega Gardens v. U.S., 2005 U.S. Claims LEXIS 254 (Aug. 29, 2005) (also discussed in § III.D, infra), discusses the distinguishing characteristic of temporary taking claims: the plaintiff has possession of the subject property at the start of the case and at the end, and thus the goal is to measure the loss of the particular asset for the duration of the taking. The court noted that in such cases, measuring before and after changes in value may overlook the interference, and may result in no compensation if the value is the same:

> For example, a temporary taking of a bar of gold is different than that of an income-generating beach house – the owner of the gold is returned the same property at the end of the taking, but the revenue stream from the beach house for the duration of the taking is gone forever. [Citing Independence Park Apts. V. U.S., 62 Fed. Cl. 684, 707 n.12 (2004]. Accordingly, the appropriate measure of just compensation for the temporary taking of a bar of gold might well be interest on the value of the bar for the pertinent period, while that for the beach house is its owner's lost rents.

D. Alternative Methods, Consequential Damages.

The principles, goals, and court decisions summarized above reveal an obvious contradiction: The goal of just compensation is to make property owners whole, and yet appraisers and judges apply limitations that often blink at the real-world consequences of government action. This tension results in two other lines of judicial decisions: those in which courts use alternatives to fair market value, and those in which courts engage in result-oriented approaches to the many subsidiary decisions that are made during the valuation process. As to market value:

> [T]his Court has refused to designate market value as the sole measure of just compensation. For there are situations where this standard is inappropriate. As we held in United States v. Commodities Trading Corp., 339 U.S. 121, 123, 70 S. Ct. 547, 549, 94 L. Ed. 707 (1950): "[W]hen market value has been too difficult to find, or when its application would result in manifest injustice to owner or public, courts have fashioned and applied other standards."

United States v. 564.54 Acres of Land, 441 U.S. 506, 99 S. Ct. 1854, 1858 (1979). Departure from the standard methods of valuation occurs "when market value has been too difficult to find, or when its application would result in manifest injustice to the owner or public." United States v. Commodities Trading Corp., 339 U.S. 121, 70 S. Ct. 547, 549 (1950). "Although the market value of the taken property is ordinarily the most appropriate measure of fair compensation, we have long held that other measures may be appropriate when the fair market value measure of damages does not fully compensate the owner." Alemany v. Commissioner of Transportation, 215 Conn. 437, 576 A.2d 503, 507 (1990).

The Wisconsin Supreme Court in Luber v. Milwaukee County, 47 Wisc.2d 271, 177 N.W.2d 380 (1970) provided a thoughtful explanation of the modern realities that justify discarding the historical reliance on fair market value, in favor of awarding "incidental or consequential damages" where appropriate:

> The importance of allowing recovery for incidental losses has increased significantly since condemnation powers were initially exercised in this country. During the early use of such power, land was usually undeveloped and takings seldom created incidental losses. Thus the former interpretation of the "just compensation" provision of our constitution seldom resulted in the infliction of incidental losses. The rule allowing fair market value for only the physical property actually taken created no great hardship. In modern society, however, condemnation proceedings are necessitated by numerous needs of society and are initiated by numerous authorized bodies. Due to the fact people are often congregated in given areas and that we have reached a state wherein *re*-development is necessary, commercial and industrial property is often

> taken in condemnation proceedings. When such property is taken, incidental damages are very apt to occur and in some cases exceed the fair market value of the actual physical property taken.

177 N.W.2d at 384-85.

Damage to a business is more readily accepted as a measure of compensation in temporary takings cases, in which, by definition, the plaintiffs owns or has use of the land before and after the government's interference, and the focus of compensation is valuation of the disruption. The Michigan Court of Appeals in Miller Bros. v. Department of Natural Resources, 203 Mich. App. 674, 513 N.W.2d 217 (Ct. App. 1994) held that the trial court erred in basing compensation on the pretaking fair market value of the property, opting instead for a return on the delay in receipt of income incurred by the plaintiffs. In that case, the defendant had prohibited the plaintiffs from exploring or developing their oil and gas rights. Similarly, in McClimans v. Board of Supervisors, 107 Pa. Commw. 542, 529 A.2d 562 (1987), the court directed that if the zoning ordinance preventing extraction of coal by the plaintiff were to be amended, then the defendant township would be required to pay just compensation for the temporary taking. "This just compensation would include damages appellants could prove as a result of the delay in extracting the coal caused by the Township's ordinance." Id. at 570. See also, Prince George's County v. Blumberg, 44 Md. App. 79, 407 A.2d 1151, 1175 (Ct. App. 1979), aff'd. in part and rev'd. in part on other grounds, 418 A.2d 1155 (Md. 1980), cert. denied, 449 U.S. 1083, 101 S. Ct. 869 (1981) (approving award of damages for delay in receiving profits where county revoked permits for construction of apartment complex, but remanding for a redetermination of the amount); see Poirier v. Grand Blanc Township, 192 Mich. App. 539, 481 N.W.2d 762 (Ct. App. 1992) (lost profits recoverable if "proven with a reasonable degree of certainty as opposed to being based on mere conjecture or speculation"); Austin v. Teague, 570 S.W.2d 389, 395 (Tex. 1978). "Where there has been a temporary taking or damaging, the landowner is entitled to recover such sum as would compensate for loss of profits and necessary expenditures." San Antonio River Authority v. Garrett Bros., 528 S.W.2d 266, 274 (Tex. Ct. Civ. App. 1975). See also, Anbe Realty Co. v. City of New York, 636 N.Y.S.2d 767, 223 A.D.2d 416, 417 (App. Div. 1st Dep't 1996) (affirming trial court's award of lost profits to developer who planned to convert building to condominiums, "since plaintiff's experts provided the fact finder with a sound basis for approximating with reasonable certainty the profits lost as a result of defendant's action").

As to result-oriented decisions, Professor Christopher Serkin has observed that appraisers and judges, in the valuation process, deal with a variety of factors that are laden with value judgments and are subject to adjustment depending on one's view of the proper goals of the Takings Clause. These include: highest and best use definitions; the availability of permits and the likelihood of rezonings; the likelihood of restrictive regulations; development process risks and expenses; transaction costs and fees; and the date of taking. See Christopher Serkin, The Meaning of Value: Assessing Just Compensation for Regulatory Takings, 99 N.Y.U. L. Rev. 677 (2005).

E. Consensus Of Commentators: Just Compensation Does Not Make The Property Owner Whole.

This introduction to basic just compensation law may be summarized, and the balance of this paper prefaced, by reviewing past and recent commentary on just compensation.

Overall, commentators agree that the well-established just compensation rules systematically fail to indemnify property owners for several types of losses that regularly occur when government takes land by eminent domain or so restricts its use as to create an inverse taking. The most frequent uncompensated losses are consequences to an ongoing commercial use, such as lost profits and goodwill; any influence of the condemnor's plans on the property; transaction costs, such as relocation expenses, and attorneys' fees; and a property owner's personal or idiosyncratic attachment to property or unique ability to make it valuable. In addition, as noted earlier, even a loss of real property will not be compensated if the loss cannot be reasonably demonstrated, or if some substantial positive influence on value offsets it.

This conclusion that just compensation rules as presently employed do not "make the owner whole" must be separated from commentary on whether the current rules ought to be changed. On this issue, the authors recommend Professor Serkin's article, 99 N.Y.U. L. Rev. 677 (2005), which discusses the extent to which valuation mechanisms and rules are and are not aligned with the purposes of the Fifth Amendments Takings Clause. The article reviews the wide variety of choices that are made by appraisers and judges in the valuation process, and suggests how these factors may be grouped, aligned, and prioritized in varying ways either to increase compensation and restrain government regulation and use of eminent domain, or decrease compensation and thereby encourage condemnation.

Commentary on just compensation dating back to the early 1900's is well summarized in Michael DeBow's article, Unjust Compensation: The Continuing Need for Reform, 46 S.C. L. Rev. 579 (1995). Articles discussing the failure of just compensation to compensate landowners for the subjective value they place on their property include: Lee Anne Fennell, Taking Eminent Domain Apart, 2004 Mich. St. L. Rev. 957; James E. Krier and Christopher Serkin, Public Ruses, 2004 Mich. St. L. Rev. 859; and Thomas W. Merrill, Incomplete Compensation for Takings, 11 N.Y.U. Envtl. L.J. 110 (2002).

III. RECENT CASES ILLUSTRATING JUST COMPENSATION PRINCIPLES AND PROBLEMS.

A. *City of San Diego v. Barratt American, Inc.*, 128 Cal. App. 4th 917 (2005).

In Barratt, the property owner's agriculturally-zoned land was located in an area where the City planned to construct a freeway, but the road's exact placement was debated and revised over several years. Most plans had the freeway running beyond Barratt's property, but the final approved plan placed part of the freeway on Barratt's parcel. While considering alternative

highway routes, the City identified the area of Barratt land as suitable for rezoning to high density residential use. The City condemned five of Barratt's 38 acres.

This case illustrates the difficulty of applying the principle that valuation should not be influenced by the condemnor's plans. Here, the problem was how to properly instruct the jury to determine the fair market value of the Barratt's property without considering the proposed final, highway construction, but taking into account appreciation that the property had experienced as a result of earlier, publicized plans that had the freeway running near, but not through, the Barratt property.

The City proposed that the jury should determine the value the land as if the entire highway project had been abandoned on the day of the taking. If the project had been abandoned, it would have taken years of planning before another project had replaced it, and therefore it would have been years before Barratt's land could realistically have been developed. Because no development would have been possible, the land would have been zoned for agriculture and valued on that basis rather than proximity to a freeway and suitability for high density residential.

Barratt argued that the "abandoned project scenario" failed to account for the appreciation of the land that resulted from years of contemplation of proposed plans that did not include taking the Barratt property. Barratt sought to have this appreciation considered under a common law exception to ignoring the impact of the condemnation; the exception stated that "increases in value, attributable to a project but reflecting a reasonable expectation that property will not be taken for the improvement, should properly be considered in determining 'just compensation.'" Merced Irrigation District v. Woolstenhulme, 4 Cal. 3d 478, 483 P.2d 1, 12 (1971). Barratt suggested that the fair market value should be determined on the basis of likely rezoning to high density residential, due to the inevitability of some form of nearby highway construction. In fact, Barratt's planning expert testified that "the property enjoyed a reasonable probability of a zoning change" even without the City's project.

The court rejected the City's "abandoned project" construct because it would have required jury members to consider the "value-depressing effect" an abandonment would have had on the property. For this reason, the court affirmed jury instructions based on Barratt's theory of valuation, and awarded Barratt $3.5 million for just compensation, as against the City's claim of $1.5 million.

B. *Cienega Gardens v. United States*, 62 Fed. Cl. 28 (2005).

The Plaintiffs were owners of rental properties purchased under the National Housing Act ("NHA") of 1968. As part of the NHA, the Plaintiffs had a contractual option to prepurchase their mortgage after 20 years without HUD approval and then to charge market rates for apartments. This right was temporarily taken by the ELIHPA (Emergency Low Income Housing Preservation Act of 1987) and the LIHPHRA (Low Income Housing Preservation and Resident Homeownership Act of 1990). The ELIHPA required private owners to obtain permission from

HUD to prepay their mortgage and simultaneously established what the court termed "draconian criteria" for obtaining such approval. According to the court, LIHPHRA "made permanent ELIHPA's temporary ban on prepayment without HUD approval." The Housing Opportunity Program Extension Act of 1996 ("HOPE") later superseded the prepayment restrictions set by ELIHPA and LIHPHRA; the issue before the court was how to compensate the plaintiffs for their temporary inability to prepay.

The court first determined that the deprivation of the right to prepay had constituted a temporary taking. As to just compensation, plaintiffs urged that just compensation should be measured by the difference in value between the rent they would have been able to receive had they been permitted to prepay, and the actual rent received. The United States countered this model by arguing that the Plaintiffs were only entitled to nominal damages; it calculated the value of the prepayment option and concluded that plaintiffs were only entitled to lost interest on the option's value.

The court chose the landlord's model, concluding that the properties at issue were income-producing, and a comparative discounted cash flow analysis most accurately valued the impact of the abrogation of the prepayment right. Moreover, the court concluded that the value of the prepayment option was difficult to determine due to lack of a market for such an interest.

C. *Dept. of Trans. V. M. M. Fowler, Inc.*, 611 S.E.2d 448 (N.C. 2005).

Defendant was the owner of a gas station. Plaintiff, the DOT of North Carolina, condemned a portion of defendant's property in order to expand a highway, thus leaving him with one entrance to his business rather than two. Defendant produced evidence that his business revenue had decreased as a result of the partial taking.

The court acknowledged that one typically determines just compensation in a partial takings case by subtracting the fair market value of the property immediately after the taking from the fair market value immediately before the taking, and lost profits are generally not considered. However, the court recognized an exception that allows compensation for lost business "when the taking renders the remaining land unfit or less valuable for any use to which it is adapted." Kirkman v. Highway Comm'n, 257 N.C. 428, 126 S.E.2d 107, 110 (1962). Because the taking of the second entrance rendered defendant's land less valuable as a gas station, the court upheld the jury's award of lost profits.

D. *Michigan DOT v. Haggerty Corridor Partners Limited Partnership*, 473 Mich. 124, 700 N.W.2d 380 (2005).

Defendant's land was zoned agricultural on the date of taking, but two years later it was rezoned for business use. Defendant wanted to present evidence of the rezoning in order to prove fair market value on the date of taking, i.e. the likelihood at that time of rezoning to commercial. It stated that the proof of actual rezoning indicated that the land had a higher value

in anticipation of rezoning. Plaintiff objected to this evidence because the rezoning occurred as a partial result of the condemnation, and fair market value may not be determined based on the government's proposed use for the property. The DOT argued that the property owner show that there had been a reasonable probability that the land would have been rezoned, without the taking, on the date of the taking. The evidence of actual rezoning two years later was irrelevant.

The court agreed with the DOT, although the judges were sharply divided. The majority determined that proof of a zoning change two years after a taking was irrelevant to proving the value of the land at the time of the taking. However, other members of the court believed that such evidence could be used to show a reasonable probability of a zoning change on the day of the taking.

These recent cases illustrate the tug-of-war that often results from the limitations that just compensation rules placed on condemnees, and their struggle to find a way to evade or ameliorate their impact.

IV. JUSTICE KENNEDY'S "PREMIUM COMPENSATION" QUESTION.

A. The *Kelo* Oral Argument: Justice Kennedy's Question.

When individual parcels of land are assembled by a condemnor, the property as a whole is usually worth more than the sum of its parts. Thomas W. Merrill, The Economics of Public Use, 72 Cornell L. Rev. 61, 85 (1986). However, as discussed above, when determining fair market value, courts are directed to find what a willing buyer and a willing seller would have paid at the moment of the taking, without considering any increase or decrease in value based on the taker's intended use. See, e.g., United States v. Virginia Electric & Power Co., 365 U.S. 624, 81 S. Ct. 784, 792 (1961); United States v. Miller, 317 U.S. 369, 63 S. Ct. 276, 280 (1943). Also, as discussed above, limiting just compensation to the value of real estate taken by the government excludes consequential or future losses.

It was this combination of circumstances that led Justice Kennedy, during oral argument in Kelo, to ask whether the calculation of just compensation should be different in economic development cases, where "A is losing property for the economic benefit of B." Oral argument transcript at 23. Specifically, Justice Kennedy asked:

> Are there any writings or scholarship that indicates that when you have property being taken from one private person ultimately to go to another private person, that what we ought to do is to adjust the measure of compensation, so that the owner – the condemnee – can receive some sort of premium for the development?

Id. at 22.

Set forth below is a compilation of valuation theories by which premium compensation might be determined by experts and awarded by courts, followed by a review of the problems that would arise from these theories.

B. Rationale For Premium Compensation.

Kelo, of course, involved the condemnation of occupied single-family residences for the purposes of implementing a validly-adopted, comprehensive municipal economic development plan. Thus, with respect to "premium compensation," the case presented a narrower and more specific case than Justice Kennedy's inquiry regarding "A losing property for the economic benefit of B." In other words, and although we don't know for sure, it appears that Justice Kennedy was asking about the availability of compensation greater than fair market value in the specific instance of condemnation of residences occupied by several "A's," so as to permit the condemnor to assemble a group of parcels that, when put together, have a greater value than the unit values paid to the A's, which land value is then transferred to private developer B, who executes the municipal development plan.

Within this more specific context, potential rationales for paying premium compensation to the "A's" would include the following:

1. Traditional just compensation rules do not cover consequential damages; personal attachment or unique ability to exploit a parcel's value; speculative losses; enhancement resulting from the condemnor's plans; most transaction costs; or losses that precede the date of taking.

2. Condemnation is a forced sale, and one of the most drastic and draconian powers of government.

3. Residence, whether ownership or rental, includes a right of non-disturbance (or as the late Paul Davidoff once called it, "the right to stay put"), and this right should be given independent recognition in compensation determination.

4. When government, as in the case of New London, Connecticut, takes residences that are not blighted or unsafe, and does so for economic development, it is engaging in a quasi-proprietary action, as opposed to a governmental function.

5. The increase in value obtained by a condemnor through assemblage is a form of unjust enrichment, see T. Merrill, Incomplete Compensation, 11 N.Y.U. Envtl. L.J. at 117-18 (2002).

6. An entity authorized to use eminent domain powers has been granted a form of monopoly, and should be required to provide an economic return to those whose property contributes to this monopolistic enterprise, see T. Merrill, Incomplete Compensation, Id. at 124-25.

7. In many American metropolitan areas where low income, low property value areas are surrounded by substantially more affluent neighborhoods and expensive housing, payment to a condemnee of market value for a residence may provide few, or perhaps no, opportunities to find another comparable residence in the vicinity or the region.

8. Relocation expenses provided by statute are generally so small as to not count as "premium" compensation.

9. Attorneys' fees are ineffective as a deterrent to eminent domain.

10. One of the long-recognized purposes of the Takings Clause of the Fifth Amendment is to ensure that burden that should be borne by the general public are not imposed on individual property owners, see Armstrong v. U.S., 364 U.S. 40, 80 S. Ct. 1563 (1960).

If a court were to accept one or more of these rationales, it would have to assign values in one or more of the following ways:

1. Measure the value created by the condemnor's assemblage of land above the cost of the individual, condemned parcels.

2. Consider the location of the condemned homes in the assemblage as their highest and best use, and base market value on being part of the assemblage.

3. Assign a value to the forced sale characteristic of condemnation.

4. Assign a value to the right of non-disturbance of a residence.

5. Assign value to the occupant's unique or personal attachment to her residence.

6. Discount (or ignore) any diminution in value caused by degradation of the surrounding neighborhood, especially if exacerbated by the government's redevelopment plans.

7. Determine the amount by which the condemnor is enriched by the condemnations.

8. Determine the value added or savings received by the condemnor through assembling land through eminent domain, as opposed to acquisition in a competitive market.

9. Consider replacement cost, by inquiring into the cost and availability of comparable housing (median prices, affordability indexes) in the surrounding region, and setting compensation at a level that will ensure the condemnee's ability to purchase and move to a similar residence within the same municipality or region.

The problems inherent in these theories are numerous and obvious. They include:

1. Overruling decades of established precedent that bases just compensation on market value.

2. Overruling established precedent regarding exclusion of the impact of the condemnor's plans.

3. The inapposite nature of an unjust enrichment theory (stemming in part from the fact that, as we learned in Lingle v. Chevron, takings law does not judge the efficacy of government action, but only whether compensation should be paid, and if so, how much).

4. The difficulty of line-drawing: If a residence will be compensated above fair market value, what about a business? What about a residence in an indisputably blighted area, or one whose continued existence poses a health or safety concern? What about a condemnation that serves both economic development and blight removal on public safety? What about a minimum length of occupancy before eligibility for premium compensation?

5. The theories listed above contain numerous invitations to speculation, and compensation for items that are not susceptible to expert appraisal testimony, and thus will necessitate subjective judgments by judges.

6. The economic reality that, while a condemnor may create a greater unit value by assemblage, the condemnee does not own or have any rights to the other assembled parcels, and thus any premium compensation is a pure windfall.

7. The fact that premium compensation, paid in order to satisfy the perceived problems first listed above, will make condemnations more expensive for governments and taxpayers.

C. Specific Proposal: Pending New York Legislation.

Listing the potential theories of premium compensation awards and the problems inherent in each one leads to the conclusion that such compensation, if provided through the judicial system, is an effort to fit a square peg in a round hole. Whether the market value standard for just compensation is fair or not, it is based on longstanding precedent that is rooted in accepted valuation and appraisal methods, favors admissible evidence over speculation, and prevents judges from making truly subjective calls.

If we accept this conclusion, then the only remaining alternative is legislation, that is, an approach that papers over the problems noted above in favor of a policy approach to provide additional financial protection to condemnees who lose their place of residence.

Although many states have proposed legislation in response to Kelo, it appears that this legislation is limited to the state's use of eminent domain rather than calculation of just compensation. See National Conference of State Legislatures, available at http://www.ncsl.org/programs/natres/Emindomain Memo.htm. According to the National Conference, there are five types of pending legislative responses to Kelo: (1) authorization of eminent domain only for a recognized public use; (2) restriction of eminent domain for economic development to blighted properties; (3) enhanced public notice requirements; (4) local government approval requirements; and (5) prohibitions of eminent domain for specified economic development purposes. Id. As of the date of this writing, New York stands alone as having proposed a new method by which to determine just compensation for residential owners and occupants.

Assembly Bill 9043 (copy attached) would require the government to offer a homeowner 150 percent of the fair market value of condemned property when that land will be taken for economic development. Assembly Bill 9043 applies to condemnation of a "home" or "dwelling" in connection with an "economic development project." "Home" is defined as owner-occupied residential premises consisting of not more than six units, while "dwelling" is a residential premises with not more than 30 units, none of which is owner-occupied. The bill also defines cooperative apartments. Condemnees falling into one of the covered categories are entitled, in addition to any other compensation requirements under this article, to a minimum of 150 percent of fair market value, while renters are entitled to 150 percent of their annual rent. Senate Bill 5946 is similar to this proposal (copy attached).

Assembly Bill 9050 (copy attached) defines "home" as owner-occupied premises with not more than five separate units, and includes common interest ownership and cooperative units. A "dwelling" is a single unit that is not owner-occupied. The condemnee of a "home" is entitled to an offer from the condemnor of 125 percent of the "highest approved appraisal." The

tenant of a dwelling who has resided there for six months is entitled to two months' rent. In addition, owners and tenants are entitled to:

> transportation and storage of household goods; real estate brokerage fees, costs, charges, or commissions; title searches and title insurance; attorney's fees; any costs, fees, charges, or taxes required by the state or a political subdivision of the state to be paid in connection with recording, filing, or approval of any instruments pertaining to real property; expenses for transitional housing for up to three months, taking into consideration the market conditions of the locality and the value of the housing from which the condemnee is displaced; and housing financing costs.

The bills are intended to "strike a balance between the rights of individual property owners and the desire of municipalities to support economic development initiatives in their jurisdiction." John Tokasz, Memo on Assembly Bill 9050, New York State Assembly, available at http://assembly.state.ny.us/leg?bn=A09050&sh=t.

E. Conclusion.

For the reasons stated above, judicial refashioning of just compensation to provide premium compensation would require overturning decades of legal precedent and involve judges in subjective evaluations. Legislative responses, like those being contemplated in New York, would avoid these problems, but of course, would constitute rough justice, a sledgehammer approach to situations that often require a more surgical or precise remedy. Ultimately, the efficacy and political viability of awarding premium compensation by legislation may depend on whether the backlash against the Kelo decision is a temporary phenomenon, or whether the case has engendered a more permanent conclusion that residential owners and tenants should be protected from the use of eminent domain for economic development purposes.

V. COLLISION OF EMINENT DOMAIN AND ENVIRONMENTAL LAW: THE GROWING STATE COURT SPLIT ON DEDUCTION OF REMEDIATION COSTS FROM JUST COMPENSATION.

A. The Basic Issue.

States are increasingly divided on the issue of whether the government, when it takes title to real property by eminent domain, may deduct from just compensation the costs of environmental remediation. One approach taken is to exclude all evidence of environmental contamination and remediation, thus prohibiting the government from deducting such costs when determining and depositing eminent domain. The contrasting view is to allow evidence pertaining to contamination and remediation and allowing deductions. A few states embrace a third view. Florida, for instance, excludes evidence of the cost of remediation, but allows evidence of contamination. New York and New Jersey exclude evidence of remediation cost,

but value the property "as if remediated," as opposed to "as if clean." Florida courts also favor putting money into escrow until such time as remediation costs are determined.

B. Rationale for Admitting Evidence of Remediation Costs Allowing Deduction.

Seven of the twelve states that have weighed in on the issue have admitted the evidence of contamination. J. Sackman, Nichols on Eminent Domain § 13B.03 (3d ed. 2005). These states reason that environmental contamination is a factor that affects fair market value of real property and therefore is relevant to eminent domain valuation proceedings. See N.E. Econ. Alliance Inc. v. ATC P'ship, 256 Conn. 813, 776 A.2d 1068 (2001).

In N.E. Econ. Alliance, the Town of Windham, Connecticut, through the Northeast Connecticut Economic Alliance, Inc. (Northeast) used its eminent domain power to take 40 acres. 776 A.2d at 1072. Northeast filed a "statement of compensation in the amount of $1 in connection with the taking . . ." Id. The compensation was nominal because the town felt that property had no value when taking into account the cost to cure its environmental contamination. Id. at 1074. The property had been used by previous owners as a textile mill. Id. at 1072. The buildings on the property contained over 35,000 linear feet of asbestos-laden material and tens of thousands of square feet of wall and ceiling that were covered in lead-containing materials. Id. at 1074. Before the town could demolish these buildings, the asbestos and lead "had to be abated, contained, removed, or disposed according to applicable health and other codes . . ." Id. The town further alleged that the property contained soil contamination by petroleum substances as well as potential ground water contamination. Id.

The landowner applied to have this statement of compensation reviewed. Id. at 1073. At trial, the landowner's motion in limine to exclude the evidence relating to environmental contamination and remediation costs was granted. Id. As a result, the landowner was awarded $1,675,000 in just compensation. Id. at 1076. The town appealed from this award, arguing that evidence of contamination should have been allowed. Id.

The Connecticut Supreme Court held that contamination evidence must be admitted because a willing buyer would consider the economic consequences of contamination upon the land, including specifically the cost of remediation. Id. at 1080-81. The court reasoned that excluding evidence of contamination

> is likely to result in a fictional property value – a result that is inconsistent with the principles by which just compensation is calculated. It blinks at reality to say that a willing buyer would simply ignore the fact of contamination, and its attendant economic consequences, including specifically the cost of remediation in deciding how much to pay for property.

Id. at 1080. The court added that a willing buyer would consider the other costs associated with contamination, including: "(1) potential liability under various environmental statutory schemes;

(2) potential litigation brought by members of the public for damages relating to the contaminants; (3) stigma to the property even after full remediation; (4) higher financing costs charged by lending institutions by virtue of the contamination; and (5) increased regulation."

On remand, the trial court held that the market value of the property was $1,721,165 after subtracting $6,534,875 in remediation costs. N.E. Econ. Alliance Inc. v. ATC P'ship, No. X04 CV 94 0124630, 2003 Conn. Super. Lexis 368 at *26-29 (Conn. Super. Ct. Feb. 14, 2003). The town appealed this award, arguing that the trial court improperly calculated the market value of the property by considering a $3 million state grant available to assist with clean up, and remediation compensation potentially from previous owners. N.E. Econ. Alliance Inc. v. ATC P'ship, 272 Conn. 14, 861 A.2d 473 (2004). The Connecticut Supreme Court affirmed the trial court's decision, holding that a prospective investor would consider the state grant and the possible recovery of money from prior landowners when valuing property. 861 A.2d at 491. As to the state grant, the Supreme Court stated that "the crucial question for the trial court was whether funds were *available* to potential buyers at the time of taking in September, 1994, not the funds that actually were awarded." Id. at 483-84. Accordingly, the court held that "the trial court properly considered the availability of state economic development grant in funds in calculating the fair market value" because the case law in Connecticut directs courts "to be broadly inclusive when considering the admissibility of factors that reasonably might influence a property's fair market value." Id. at 484.

The Kansas Supreme Court preceded Connecticut in holding that evidence of contamination and remediation is relevant to an eminent domain proceeding. Olathe v. Scott, 253 Kan. 687, 861 P.2d 1287, 1290 (1993). In Olathe, the city appealed from condemnation awards paid to the defendants because it was dissatisfied with the appraisal of the defendants' property. 861 P.2d at 1289. The appraiser's award was $1,512,000 for two tracts taken from the defendants. Id. The city argued that the tracts, which had been both operated as service stations, were contaminated by leakage from underground gasoline and diesel fuel storage tanks. Id. The city claimed that the appraiser failed to consider evidence of petroleum contamination on the two tracks. Id. At trial, the jury was allowed to hear evidence on contamination as well as the total cost of remediation. Id. at 1290. Consequently, the jury returned a decision that reduced the appraiser's award by ten percent. Id.

On appeal, the defendants argued that it was not appropriate to consider the impact of contamination on property value in an eminent domain proceeding because the Kansas Storage Tank Act "is a specific statute that preempts all other common law or statutes that might address funding the cleanup cost incurred because of releases from USTs [underground storage tanks]." Id. at 1292. The defendant's contention was that the "funding of the cost on environmental remediation should be pursued in an action brought pursuant to the statute specifically enacted to address such contamination." Id. at 1292-1293. The Kansas Supreme Court affirmed the judgment of the district court, reasoning that evidence of an underground petroleum contamination must be admitted because such "contamination necessarily affect the market value of real property." Id.

A Tennessee Court similarly held that evidence of contamination and remediation costs should be admitted. Tennessee v. Brandon, 898 S.W.2d 224, 226 (Tenn. Ct. App. 1994). In Brandon, the State condemned the landowners' property as part of its improvement to the intersection of two State highways. 898 S.W.2d at 225. The property had been used for 40 years as a bulk oil distributorship and retail service station. Id. After the State took possession of the property it removed three above ground and one underground storage. Id. Additionally, the State discovered that the soil and water on the property were contaminated with petroleum in excess of the safe drinking water levels set by the Tennessee Department of Environmental and Conservation Department. Id. In total, the State spent $65,000 remediating the property. Id. At trial the landowners were awarded $85,000 as compensation for the taking of their property. Id. The State appealed this award because evidence of contamination and the costs of remediation had been excluded at the trial. Id. at 226.

The Appellate Court reversed the trial court's decision to exclude evidence of contamination and remediation and remanded the case for a new trial. Id. at 228. The court's rationale was that the Tennessee Rules of Evidence deem evidence relevant so long as "its probative value is substantially outweighed by the danger of unfair prejudice, confusion of the issues, or misleading the jury, or by considerations of undue delay of waste of time, or needless presentation of cumulative evidence." Id. at 226. The court concluded that "there can be no doubt that the contaminated nature of the property would be evidence relevant to the issue of valuation." Id.

The Oregon Court of Appeals used the identical reasoning as Brandon to reach the conclusion that evidence of contamination must be admitted. Oregon v. Hughes, 162 Ore. App. 414, 986 P.2d 700 (Ore. Ct. App. 1999). The landowner in Hughes operated a motorcycle dealership and service center along the Columbia River Highway. 986 P.2d at 701. The State condemned part of the landowner's property as part of its project to widen the highway. Id. When the State began work on the highway project, it discovered that the property was contaminated with hazardous materials. Id. The court explained that Oregon law defines relevant evidence as "evidence having any tendency to make the existence of any fact that is of consequence to the determination of the action more or less probable than it would be without the evidence." Id. at 703. The court then held that evidence of contamination on the property would directly impact the fair market value, and therefore meet the "very low threshold for evidence to be considered relevant." Id.

Michigan has also held evidence of the cost of remediation to be relevant when calculating just compensation. Silver Creek Drain Dist. v. Extrusions Div., Inc., 468 Mich. 367, 663 N.W.2d 436 (2003). In Silver Creek, the Silver Creek Drain District (drain district) chose the defendant's property as the site for a new retention pond, and in May 1994 filed a Declaration of Taking, "declaring that [the defendant's property] Old South Field was being taken to effect a necessary public improvement." 667 N.W.2d at 439. In the 1997 valuation hearings, the value of the property without contamination was found to be $278,000. Id. However, the trial judge held that the property was contaminated and that the reasonable cost of a formal Type C Closure must be subtracted from the fair market value because at a minimum a reasonable purchaser

would require it before closing on the property. Id. As a result, the trial judge declared the net fair market value of the property was $41,032. Id.

On appeal, the defendant argued that since it did not cause the contamination it was not liable in condemnation for the remediation. Id. The appellate court overturned the trial court's decision, but the supreme court granted review and reversed. Id. The supreme court held that evidence of contamination can be considered in the determination of just compensation because it is "a factor affecting fair market value." Id. The court further reasoned that the phrase "just compensation" in the Michigan Constitution of 1963 is a term of art that when given its proper meaning "takes into account all factors relevant to market value." Id. at 442.

California is also among the seven states whose courts allow evidence of contamination and remediation at condemnation hearings. Redev. Agency v. Thrifty Oil Co., 5 Cal. Rptr. 2d 687, 689 (Cal. Ct. App. 1992). In Thrifty Oil, the City of Pomona employed its eminent domain power to take the defendant's property. 5 Cal. Rptr. at 688. On the property was a 23 year old gasoline station. Id. Gasoline spillage on the property had resulted in soil contamination. Id. When the City took possession of the property, it spent $182,000 to remediate the property. Id. At trial, the jury heard evidence of contamination on property as well as the cost of remediation. Id. The jury's award to the defendant of $136,000 reflected about a $100,000 reduction in "just compensation" for the reasonable cost of remediation. Id. The Appellate Court held that evidence of remediation was correctly allowed at trial. Id. at 689. The Court reasoned that "as a characteristic of the property which would affect its value, the remediation issue was properly before the trier of fact." Id. at 689.

Finally, Georgia includes evidence of contamination when determining just compensation. Shealy v. Athens-Clarke County, 24 Ga. App. 853, 537 S.E.2d 105, 107 (Ct. App. 2000). In Shealy, the landowners alleged that their property became contaminated when hazardous substances escaped from a landfill owned by the county. At the time the county initiated the condemnation proceedings, the landowner brought an inverse condemnation suit against the town. 537 S.E.2d at 106. The county sought to condemn the property for the public use of facilitating environmental remediation efforts. Id. The court held that the landowner's just compensation must reflect the reduction in value of the property due to the contamination from the landfill. Id. at 108. The court reasoned that "in determining the market value of the property as of the date of taking, the general environmental condition of the condemned property, including need for remediation is a relevant factor." Id. at 107. The condemnation award reflected the reduced the price of the property due to the contamination, even though the contamination was allegedly the fault of the party condemning the land. The landowners was required to bring an inverse condemnation suit, separate from the eminent domain proceedings, to recover for any damages caused by the hazardous substances that allegedly escaped form the county's landfill. Id. at 108.

Florida has taken a different approach. Florida is the only state that treats evidence of remediation costs separately from evidence that the property is contaminated. Finkelstein v. Dept. of Transp., 656 So.2d 921 (Fla. 1995). In Finkelstein, the Florida Department of Transportation (DOT) condemned landowner's property in 1990. 656 So.2d at 923. Prior to the

DOT's taking the landowner had discovered petroleum groundwater contamination on the property. Id. The landowner reported the contamination to the Department of Environmental Regulation to obtain reimbursement for remediation costs pursuant to Florida's Early Detection Program. Id. At the valuation trial the DOT sought to include evidence that property was contaminated and that the cost of remediation was about $800,000. Id. The trial court denied the motion and did not allow evidence of contamination or the cost of remediation. Id. The appellate court reversed, after which the Florida Supreme Court granted review. Id.

The supreme court held that evidence of remediation costs were not relevant to the eminent domain proceeding when an Early Detection Incentive program exists that provides reimbursement of remediation costs. Fla. Stat. Ann. § 376.3071 (2005) provides for a reimbursement of remediation costs, but does not discuss the impact of eminent domain in connection with this reimbursement program. Id. at 924. The court emphasized that the holding was limited to the facts of the case, which included this program for reimbursement of remediation costs. The court did not decide whether remediation costs would be relevant in an eminent domain proceeding when such a program did not exist. Id.

Despite excluding evidence of remediation costs, the court held that due to the "stigma" attached to contaminated properties, evidence that property has been contaminated was relevant to valuation. Id. The court defined "stigma" as the "reduction in value caused by contamination resulting from the increased risk associated with contaminated property." Id. (internal quotations omitted). The sources of "stigma" identified by the court, included potential liability under state and federal environmental statutes, potential liability to the public, and financing problems. Id.

Importantly, the court required that "there must be a factual basis . . . upon which to base a determination that the contamination has decreased the value of property." Id. Consequentially, in Florida a real property expert's opinion of a reduction in market value is only admissible if it has a sufficient factual predicate. Simply opining that because the property is contaminated and imposing a corresponding reduction in value will not meet this standard. Id. at 925.

C. Cases Excluding Remediation Costs.

The other major approach, taken by several jurisdictions, is to exclude remediation costs. Two lines of reasoning run through the opinions that do not admit evidence of environmental contamination. First, condemnations proceedings lack the procedural safeguards that protect a landowner in environmental cost recovery proceedings and thus resulting in condemnation violating the landowner's right to procedural due process with regard to environmental laws. Second, a landowner who receives reduced compensation in an eminent domain proceeding due to contamination may face double liability subsequently in an environmental cost recovery proceeding.

In Aladdin, Inc. v. Black Hawk County, 562 N.W.2d 608, 616 (Iowa 1997), the landowner operated a laundry business, which the county condemned in 1992 for construction of

a county jail. 562 N.W.2d at 610. During the valuation proceedings, the county offered evidence indicating groundwater contamination on part of the block in which the landowner's property is located. Id. at 614. The county's expert witnesses assessed the cost of clean-up of the block at $561,000, "and that, based on the percentage of land owned by [the landowner] in the block, [the landowner's] portion of the estimated clean-up cost would be $406,560." Id. Consequently, the county Compensation Commission reduced the landowner's award of $425,000 by $135,000 to reflect the landowner's share of the remediation costs. Id. at 615. On review, the Iowa Supreme Court held allowing evidence of remediation at a condemnation proceeding would violate due process because "a property owner has a right to have its liability established in a legal proceeding in which the owner has the opportunity to show that the owner did not cause the pollution or hazardous condition." Id. at 616. In support of this holding, the court pointed to Iowa statutes providing that before a property owner is held responsible for clean-up costs, an action must be brought by the Department of Natural Resources ("DNR"), in which the DNR or a citizen "must prove the owner generated the contamination." Iowa Code § 455B.392 (2004) states that "[a] person having control over a hazardous substance is strictly liable to the state for . . . the reasonable cleanup costs incurred by the state or its political subdivisions, by governmental subdivisions, or by any other persons participating in the prevention or mitigation of damages with the approval of the director, as a result of the failure of the person to clean up a hazardous substance involved in a hazardous condition *caused by that person*." See Blue Chip Enters. v. State Dep't of Natural Res., 528 N.W.2d 619, 623 (Iowa 1995) (interpreting § 455B.392 to limit "the liability for cleanup costs by a polluter to the extent of the hazardous condition caused by that person." (In Blue Chip, a defendant company that purchased land was made aware of environmental problems before closing, but after executing the contract did not make an effort to rescind the sale. 528 N.W.2d at 623. The Iowa Supreme Court held that the defendant was not liable for the costs of remediation because the pollution was caused by previous owners. Id. However, the court held the defendant must "share in the cost of investigation, evaluation, and developing a remedial plan for abatement of the contamination" because it stands to benefit from the remediation.) Id. In the condemnation proceeding in Aladdin, there was no evidence to suggest that the landowner was responsible for the contamination on the property. 562 N.W.2d at 615.

The Fourteenth Amendment protects individuals from deprivation of property by a state without due process of law. If an individual is being deprived of a property interest, a court must determine the level of process due using a three-part balancing test. Mathews v. Eldridge, 424 U.S. 319, 96 S. Ct. 893 (1976). Under the balancing test, a court weighs,

> [f]irst, the private interest that will be affected by the official action; second, the risk of an erroneous deprivation of such interest through the procedures used, and the probable value, if any, of additional or substitute procedural safeguards; and finally, the Government's interest, including the function involved and the fiscal and administrative burdens that the additional or substitute procedural requirement would entail.

Mathews, 96 S. Ct. at 903.

Jurisdictions that exclude evidence of contamination hold that "reducing just compensation in an eminent domain proceeding due to environmental contamination deprives a landowner of an important property interest." Paul W. Moomaw, Fire Sale: The Admissibility of Evidence of Environmental Contamination to Determine Just Compensation in Washington Eminent Domain Proceedings, 76 Wash L. Rev. 1221, 1249 (2001). Furthermore, the risk of erroneous deprivation of this property interest is high in an eminent domain proceeding because the procedural framework that exists in an environmental cost recovery proceeding is not available to a condemnee. Dep't of Transp. v. Parr, 259 Ill. App.3d 602, 633 N.E.2d 19 (Ct. App. 1994).[4]

In a condemnation proceeding, a land owner cannot implead responsible third parties or raise defenses. In a cost recovery proceeding, however, "allows for third party claims against insurers, title companies, and prior owners, none of whom have a place at the condemnation table." Hous. Auth. of New Brunswick v. Suydam Investors L.L.C., 177 N.J. 2, 826 A.2d 673,687 (2003).

The Michigan Supreme Court explained that a cost recovery action is

> an *in personam* proceeding specifically designed to assign liability for remediation costs. Those costs are typically sought under CERCLA or NREPA [Michigan's Natural Resources and Environmental Protection Act] and the fair market value of the property is not relevant in such proceedings. Further, in a cost recovery action, in addition to the agency and the owner, any other person or entity, such as prior owners, lessees, adjacent property owners, or other third parties who may have contributed to the contamination may be parties.

Silver Creek, 663 N.W.2d at 443. By contrast, a condemnation action is an i*n rem* proceeding designed to determine fair market value without consideration of liability or the inclusion of any third parties that may have contributed to the contamination. Id. at 443.

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[4] Parr may not be good law in Illinois any longer. In 1997, Illinois passed a law that stated, "evidence is admissible as to . . . (2) any unsafe, unsanitary, substandard or other illegal condition, use or occupancy of the property, *including any violation of any environmental law or regulation*; (3) the effect of such condition on income from or the fair market value of the popery; and (4) the reasonable cost of causing the property to be placed in a legal condition, use or occupancy, including compliance with environmental laws and regulations." Ill. Comp. Stat. 735/7-119 (2005). However, the annotated statute lists Parr for the proposition that evidence of environmental remediation is not admissible at trial. Moreover, Illinois case law does not suggest that the statute overrules Parr. But see Hous. Auth. of New Brunswick v. Suydam Investors L.L.C., 355 N.J. Super. 530, 810 A.2d 1137, 1149 (2002) (stating that [a]s a result of amendments to the statutes governing eminent domain actions, Parr apparently is no longer controlling law in Illinois.").

Without the basic procedures available to a landowner at a cost recovery action, but not available at a condemnation action, the risk that a landowner will be held liable for contamination he did not create is high. Finally, the government interest is low because the opportunity exists to bring an action under the applicable environmental statute to recover remediation expenses. Therefore, the level of process due to protect a landowner exceeds the process available in an eminent domain proceeding. Aladdin Inc., 562 N.W.2d at 616.

A second major argument in support of excluding contamination evidence at valuation proceedings is the risk of double liability to the property owner. Double liability occurs when the property owner's just compensation award is reduced for contamination in the condemnation proceeding, and then the owner is subject to cleanup costs in an environmental cost recovery action. Hous. Auth. of New Brunswick, 826 A.2d at 686. In Hous. Auth., the City of New Brunswick, through the Housing Authority (Authority) sought to acquire the defendant's downtown property as part of a redevelopment project. Id. at 677. Prior to taking the property, the Authority offered the landowner $972,000 for the property, to which the landowner responded with a counteroffer of $2,500,000. Id. After failed negotiations, the Authority filed a Declaration of Taking with just compensation of $972,000. Id. at 678. However, the Authority's award was "based upon the assumption that the [p]roperty is not subject to any matters not of record, including any assessment, clean-up, requirement . . . that may be imposed pursuant to any environmental statute . . ." Id. The landowner did not oppose the taking and accepted the $972,000. Id. Subsequently, the Authority discovered the property contained asbestos, leaking underground storage tanks, and lead-based paint. Id. The trial court granted the Authority's motion to amend complaint to adjust the just compensation award for the costs of remediation. Id. at 679. The landowner appealed.

The New Jersey Supreme Court reversed the trial court's decision to allow the cost of remediation to be deducted from just compensation. Id. at 680. The court explained that due to the contamination on the property, the landowner would face strict liability under New Jersey's Spill Act. Id. at 683. Additionally, the Act afforded "government entities that acquire property by eminent domain with qualified immunity from costs associated with the cleanup and removal of hazardous substances that began or occurred prior to the transfer of the title." Id. at 684. Therefore, the statute assured that the landowner would bear the cost of the remediation. Accordingly, the court held that if just compensation was reduced at the valuation proceeding, the condemnor would receive a windfall "by ultimately obtaining the property in a remediated state at the condemnee's cost, yet paying a discounted price due to the contamination." Id. at 686.

D. Possible Solutions.

The most recent cases have evidenced an attempt to find a middle ground between the two opposing views on whether to include evidence of contamination at trial. The most widely acknowledged variation is the trust/escrow approach. This approach has been described in Nichols on Eminent Domain as "an appealing practical compromise for those courts that are disinclined to or are barred from excluding evidence of contamination in the valuation trial."

J. Sackman, Nichols on Eminent Domain, § 13B.03 (3d ed. 2005). Under the trust/escrow approach, evidence of contamination is excluded from the condemnation proceeding, but a portion of the condemnation award is escrowed or held in trust until the exact cost of remediation has been determined at the appropriate environmental cost recovery proceeding. Hous. Auth. of New Brunswick v. Suydam Investors, 177 NJ. 2, 826 A.2d 673, 687 (2003); see also Silver Creek v. Extrusions Div., 468 Mich. 367, 663 N.W.2d 436,443 (2003) ("the primary connection between a condemnation proceeding and a cost-recovery action is the escrow that may be created during the condemnation proceeding to provide security for payment of the potential cost-recovery award"), New York v. Mobil Oil Corp., 12 A.D.3d 77, 783 N.Y.S.2d 75 (N.Y. 2004) ("hold into escrow any condemnation award pending the outcome of the Navigation Law proceeding").

A further middle ground approach is to value the property "as if remediated." This approach differs from valuation of "clean" property in that "the term 'as if remediated' takes into account any residual stigma which may attach to real property as a result of the fact it was previously contaminated." Mobil Oil Corp., 783 N.Y.S.2d at 80. In addition to employing the trust/escrow approach, both New Jersey and New York value the property "as if remediated." See id.; Hous. Auth. of New Brunswick, 826 A.2d at 685.

The question of whether to include evidence of environmental contamination in the valuation of "just compensation" has no easy answer. The principle from Olson that a landowner be placed in as good a position pecuniarily as if the land was never taken underscores the complexity of the question. Olson v. United States, 292 U.S. 246, 54 S. Ct. 704, 708 (1934). If evidence of contamination is included, the owner will be forced to pay the costs of remediation regardless of liability. This puts him in a worse position than if the property was never taken. On the other hand, if evidence of contamination is excluded, the owner may receive an inflated value for the property. Even the trust/escrow approach fails to live up to the Olson principle. When the economic burden of the present duty to pay remediation costs exceeds the mere prospective liability of clean-up costs, the owner's position is worse than if the property was never taken at all. J. Sackman, Nichols on Eminent Domain, § 13B.03 (3d ed. 2005).

Given the shortcomings of each approach, there is no clear cut answer to this question of valuation. However, treating the land "as if remediated" may provide the most practical solution. Under this approach the existence of contamination is accounted for through the "'stigma" that attaches to remediated property. Furthermore, the cost of remediation can be recovered through the appropriate cost recovery action. This approach ameliorates the due process and double liability problems, while also ensuring the government does not pay an inflated price for the property.

VI. CONCLUSION: THE NEED FOR RE-EXAMINATION OF JUST COMPENSATION.

If, as presently appears, condemnations of residential property, going forward, will be a *cause celebre* in local communities, judges and legislators may feel ongoing pressure to reconsider the traditional just compensation rules that fail to make condemnees whole. Because

the courts will have a more difficult time providing greater compensation without making distinctions or drawing lines that will appear to be unfair or arbitrary, it is likely that if change is to occur, it will be legislative – and thus dictated primarily by whether Kelo promotes lasting political change.

ATTACHMENT

New York General Assembly Materials, 2005, Assembly Bills 9043 and 9050, and Senate Bill 5946, Proposed New York "Premium Compensation" Bills

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