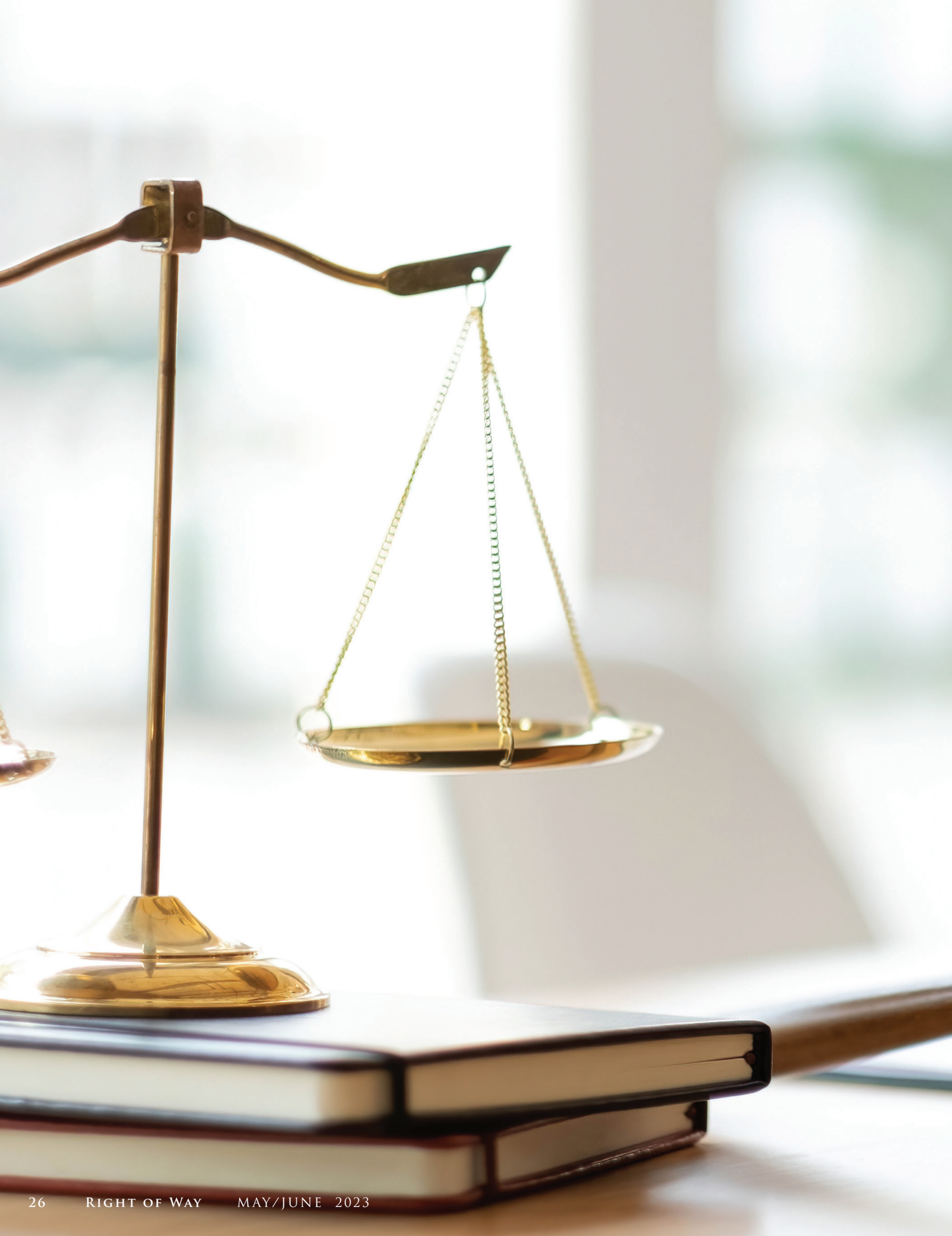


Fundamental Valuation Rules

All ROW Practitioners Should Know **Part 2**

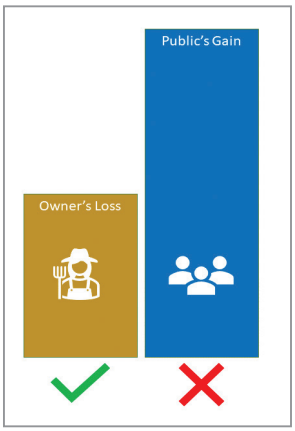
BY DALTON VANN, MAI, SR/WA, R/W-AC AND MATT BROWNE, MAI, R/W-AC

This article is the second and final installment in a series on the fundamental valuation concepts every right of way practitioner everyone should know. In Part 1 (published in Right of Way Magazine, March/April 2023), we addressed the just compensation standard and the Unit Rule, along with its implications for the valuation of the Fee Simple Estate.

4. Value to the Market, not the "Taker"

Compensation is always based on *what the owner* has lost and not what a condemnor has gained[1]. The U.S. Constitution protects citizens, so the interest of a citizen's property is what is valued, not the value generated by the project to the public or the condemnor's use of the property. Therefore, compensation should be paid for the market value of the owner's lost interest, not the public use value or benefit that the public gains from the project. [2]

An example of the application of this concept is that the value of a new easement for a pipeline is based on the owner's highest and best use of the land before the imposition of the easement, not the profits which accrue to the pipeline company. Incidentally, the price a pipeline company pays for an easement across agricultural (ag) land is often driven by business decisions, which does not constitute a typically motivated buyer of ag land (goes to the definition of market value).



Consider also the situation where a sewer easement is planned through floodplain around a streambed in a commercial area. The easement in the unusable area likely will not significantly change the value of the property because the owner lost little value in that area. However, an agency may wish to value the site on the overall unit value of the land in order to increase compensation, leading to a more enticing offer. Again, this concept can vary by jurisdiction.

The so-called "Value-to-the-Taker Rule" is why a landowner's loss is calculated based on the highest and best use of the landowner's property before the acquisition and not the condemning authority's use of the land acquired.

> **Justice and fairness demand that citizens should be compensated in proportion with their loss.**

5.Make the Landowner "Whole"

Compensation for real property in condemnation cannot be more than the total value of the real property before the acquisition. This is an underlying principle that stems from case law. Although the property owner may not be made "whole" in every sense after a partial acquisition, the courts require the principle to be followed when compensating for real estate. In other words, the condemnor must "make the owner whole" from a financial standpoint. That means the landowner should be *no worse off and no better off monetarily* than if the acquisition had not happened. This principle not only provides the foundation for restorative compensation (cost to cure) but also prohibits "double compensation" for improvements valued in the acquisition and then paid for again in cost to cure damages.

In practice, the degree to which an owner can be made "whole" has limits. For example, many states do not allow for compensation from a loss in business value. Additionally, temporary damages during construction (such as noise) may not be a compensable loss to a specific property.

Have a Fence, Get a Fence. But no more.

Being Made Whole	More than whole:
The owner lost fencing worth $500	The owner lost fencing worth $500
It will cost $750 to put fencing back	It will cost $750 to put fencing back
$250 extra needed to replace value of fencing lost	The owner wants $500 for the lost fencing plus $750 for a new fence
Total payment of **$750** for fencing	Total payment of **$1,250** ($500 Enrichment)
Depreciated value of fence plus increment in value to replace fence	*Payment for two fences: the existing fence and a whole new fence*

Furthermore, since compensation is based on the market value of the lost property, owners often cannot be "made whole" when it comes to intangibles not considered by the market, such as sentimental value or "blue sky" that is specific to an owner and not a property. Compensation must be for actual damages that are not dependent on conjecture or remote or speculative uses such as future plans.[3] This principle is the basis for supporting legitimate damages, including costs to cure.

Speculative Uses

Examples of remote and speculative uses could include claims of the loss of ability to add on to a building or add parking spaces. Other examples include:

- "I was going to build a Walmart" in the Middle of Nowhere
- Lost income from a ground lease to a national-credit drugstore that does not yet exist
- Loss of future parking on vacant land where no parking exists (frustration of plans)
- Obtaining a future irrigation permit
  - Basin Electric Power Co-Op, Inc. v. Cutler, South Dakota, 254 N.W.2d 143 (1977)
- Value as if the site was filled when it is not. "To permit such evidence would open a flood-gate of speculation and conjecture that would convert an eminent domain proceeding into a guessing contest."
  - Yoder v. Sarasota County, Florida, 81 So. 2d 219 (1955)
- "Highest and best use means the most advantageous use to which the property could actually be put without entering into speculation."
  - Ark. Model Jury Instr., Civil AMI 2007, November 2020 Update

The landowner should be no worse off and no better off monetarily than if the acquisition had never happened.[4]

6. Project Influence

Finally, valuation in condemnation must consider the impact on property values created by the project itself. Fair market value (or simply, "market value") is the measure of "just compensation" per the courts. The courts also believe that justice flows not just to the landowner but also to the public. The landowner's interest in property is protected by the Fifth Amendment, so every citizen should be paid what their property is worth.

However, when a public project is announced, the value of surrounding land may begin to increase due to speculation in the case of new roadway projects, or land value may decline in the case of project blight. Both scenarios are to be ignored by the appraiser. This does not mean that comparables located on the project must never be used, but they must be vetted to determine whether the project influenced the transaction.

The courts do not believe it is just that the government pay for the "enrichment" of landowners caused by the project for which the land is being acquired.[5] The sentiment is that the public should not be expected to pay for the value created by the project. Conversely, a governmental entity should not offer compensation based on a diminished market value caused by announcement of the property, since it is not fair to penalize the landowner for the project's negative reception by the market. "The resulting scope of the project rule, when properly applied, ensures fair results for both landowners and the public" (Uniform Appraisal Standards for Federal Land Acquisitions, 2016, p. 16). Project influence is often interpreted to require valuation of the whole property before the acquisition under a hypothetical condition that the project has not affected values in the neighborhood or simply considered as part of the Scope of Work. The Project Influence Rule is also known as the "Scope of the Project Rule" in federal land acquisitions (Yellow Book).

The key takeaway is the fair market value of property is to be paid to landowners as if the project did not exist, whether the impact is positive or negative.

To avoid project influence in the appraisal, the appraiser is advised to ask the comparable confirmation sources if the project was considered in the transaction, review public maps and public meeting minutes to determine when the project was known by the public, make market-based adjustments to project-influenced transactions after the date the project was announced or commenced, or seek comparables from similar neighborhoods. The standards for exclusion of transactions influenced by the project are not solely determined by the appraiser but are judicial decisions that can vary by court and circumstance (See Real Property Valuation in Condemnation (Appraisal Institute, 2018), (p. 86-87).

Exclusion of project influence from the appraisal may require selection of comparables from similar neighborhoods not impacted by the project, even though they are farther away from sales that are closer to the subject. Project influence can be difficult to understand and difficult to apply. It is highly advisable for the appraiser to retain documentation in the work file supporting project influence or the lack thereof.

PROJECT BLIGHT

In a real-world example of project blight, a highway project in the Dallas area had been announced and offers to landowners had begun. Then an economic downturn paused acquisitions, but tenants still knew the project was imminent. As a result, occupancies dropped from 80% to 20% along the corridor. When acquisitions resumed several years later and new appraisals were ordered, comparables were selected from similar markets not subject to project blight.

Conclusion

Other significant concepts must be addressed but can vary greatly depending on jurisdiction. For example, the appraiser may be required to define the larger parcel or select the appropriate economic unit. As previously mentioned, the valuation may require an appraisal of leasehold interests or business value. Although essential to understand, these practices are not as universally applicable across the United States.

Knowledge of these foundational concepts, their exceptions, jurisdictional variations and their application can have significant impacts on the appraised value. Accordingly, the right of way practitioner should invest in educational resources such as J. D. Eaton's *Real Estate Valuation in Litigation (ISBN-13: 978-0922154203),* the Appraisal Institute's *Real Property Valuation in Condemnation (ISBN-13: 978-1935328742), Fifty-State Survey: The Law of Eminent Domain (ISBN-13: 978-1614386063)* and IRWA education. Since there can be gray areas in their application the practitioner must be willing to consult state statutes, model jury instructions, local case law, legal counsel and peers to determine and how to employ them. Many state bar associations and independent attorneys publish works pertaining to the exercise of eminent domain in various states. As the proverb says, "in the multitude of counsel, there is safety." ✪

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[1]*Brown v. Legal Found. of Washington, 538 U.S. 216, 236 (2003)*
[2]*United States v. Chandler-Dunbar Co., 229 U.S. 53 (1913), Boston Chamber of Commerce v. Boston, 217 U.S. 189, 195 (1910)*
[3]*Omnia Commercial Co. v. United States, 261 U.S. 502, 513 (1923); A. G. Davis Ice Company, Inc. et al., Defendants, Appellants, v. United States of America, Plaintiff, Appellee, 362 F.2d 934 (1st Cir. 1966)*
[4]*Olson v. United States, 292 U.S. 246, 254 (1934)*
[5]*United States v. 428.02 Acres of Land, 687 F.2d 266, 269 (8th Cir. 1982)*
[6]*United States v. Miller, 317 U.S. 369 (1943)*

Other citations are available upon request.

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