

VALUING PROPERTIES IN TRANSITION



DIANE E. FEUERHERD chairs the litigation practice at Miller, Miller & Canby. She is an appellate and trial attorney, focusing on business, estate, real estate, and eminent domain litigation in the Maryland state and federal courts. She serves as a contributing editor for the Maryland State Bar Association's (MSBA's) Maryland Appellate Blog and is a contributing author to the treatise Appellate Practice for the Maryland Lawyer: State and Federal. She serves on the Appellate Judicial Nominating Commission for the State of Maryland, the MSBA's Judicial Appointments Committee, and the Board of Directors for the Maryland Bar Foundation. In addition, she is an Associate Member of the Owners' Counsel of America, a national network of experienced eminent domain attorneys who represent property owners.



ANDREW R. LINES, MAI, CRE, is a principal in CohnReznick's Valuation Advisory Services group where he specializes in real estate, affordable housing, cannabis, and renewable energy. Andrew leads a group of appraisers across the country performing valuations on a wide variety of real estate property types including residential, commercial, industrial, hospitality, and special purpose properties such as landfills, waste transfer stations, marinas, hospitals, universities, self-storage facilities, racetracks, CCRCs, and railroad corridors. He provides market studies, rent compatibility studies, and feasibility analyses for low- and mixed-income developments, due diligence for mergers and acquisitions of multi-state operational and early stage cannabis companies, preparation of impact studies and testimony at local zoning hearings in 15 states. He is experienced in the valuation of leasehold, leased fee, and partial interests and performs appraisals for all purposes including financial reporting (GAAP, IFRS, IRC), litigation (including eminent domain), and gift/estate planning. Andrew is a State Certified General Real Estate Appraiser in the states of Illinois, Indiana, Wisconsin, Maryland, Georgia, Florida, Ohio, New York, New Jersey, Arizona, Kentucky, Washington, and the District of Columbia.



JEFF TIBBALS is a co-founding partner of Bybee & Tibbals. He is an eminent domain attorney, focusing on obtaining just compensation for landowners in condemnation matters. The majority of Jeff's cases involve questions of constitutional law, including eminent domain and the Fifth Amendment promise of just compensation for the taking of private property for public use. Jeff has also served as a leader in South Carolina in the fight for access to justice for all citizens, as a member and chair of the South Carolina Bar Pro Bono Board. Learned in historic real estate title matters, Jeff has prevailed in trials to establish title to marsh for landowners who can trace a chain back to a King's Grant or grant from the State of South Carolina. Jeff earned the prestigious designation of CRE, as a member of the Counselors of Real Estate, a global organization of real estate professionals spanning numerous disciplines. For four years, Jeff chaired the Real Estate Litigation and Condemnation Committee of the American Bar Association's Section of Litigation. Jeff currently serves as the chair of the City of Charleston Boarding of Zoning Appeals, is a member of the James L. Petigru American Inn of Court, and serves as the South Carolina Primary Member of the Owners' Counsel of America.

INTRODUCTION¹

When real property subject to condemnation is within an area of urban renewal² or is underutilized, understanding the potential for a highest and best use that differs from a property's current use, as of the date of condemnation, is critical. This article will explore how to identify an underutilized property, provide practical and legal considerations for

counsel and appraisers as they approach the highest and best use for a property in urban renewal areas and prepare for trial, and discuss how and when urban renewal may (and may not) impact the maximum potential use of the subject property.

Urban renewal, whether it occurs organically or through government-driven development and

condemnation, evokes a discussion of gentrification of neighborhoods that remains a controversial subject, with the benefits of increased economic activity offset by a decrease in affordable housing and the displacement of residents or businesses who can no longer afford rising costs. This article seeks only to provide guidance so that appraisers, condemnors, landowners, and counsel can identify transitional areas in process and effectively evaluate just compensation in an eminent domain case.

IDENTIFICATION OF AN AREA IN TRANSITION

There are a number of signposts that lead to the identification of a neighborhood that may be in transition from a blighted area to one with burgeoning economic development and improved living conditions. These signs include:

- Rehabilitation projects in the vicinity;
- Growth of restaurant, bars, and retail stores that pop up in historically industrial areas;
- Increasing sales activity and property values;
- Government investment in infrastructure and updated facilities;
- Nearby brownfields redevelopment activity;
- Increasing residential population, particularly higher-income individuals or families, attracted by lower property values and rehabilitation opportunities;
- Official local and federal government policy findings supporting or encouraging urban renewal (e.g., tax incentives or zoning overlay designations).

Not all of these signs are visible in the initial stages of transition. However, in a geographic area with significant population growth, these changes can occur rapidly. Speculative investment boosts the momentum of such changes, which can often include covered land plays where interim uses may defray the costs of holding the property until redevelopment is imminent and where an eventual

sale of the property for such redevelopment would reflect a premium.

APPRAISAL CONSIDERATIONS

Often, a landowner will identify new opportunities for the use of his property. In many circumstances, the landowner has invested in real property in an area of renewal due to the opportunity of growth and increased economic conditions and income. Longstanding property owners are often keenly aware of changing conditions and property value increases and have already considered or planned a conversion of property to a more profitable use. Less frequently, condemnors and their appraisers share this vision, particularly in the nascent phase of transition.

In cases where an appraiser evaluates the opportunity for a change in highest and best use, she must be cognizant of several factors in order to make a proper valuation analysis. These factors include, but are not limited to:

- Physical characteristics;
- Environmental condition;
- Restrictive covenants or other legal restrictions upon use;
- Surrounding uses;
- Demographics;
- Zoning and reasonable probability of rezoning;
- Feasibility/market demand;
- Consistent use theory; and
- Interim uses.

Naturally, these factors are typically examined in the context of the well-known and studied highest and best use criteria: (i) physical possibility; (ii) legal permissibility; (iii) financial feasibility; and (iv) degree of profitability.³

When determining a reasonable probability of rezoning, appraisers may need to address specific criteria, whether by statute or in relevant and

binding jurisprudence. In Illinois, for example, the LaSalle/Sinclair Factors⁴ which detail the following hurdles that must be met in order to satisfy the requirements:

- The compatibility with the existing use and zoning of nearby property;
- The extent to which property values of the subject property are diminished by the existing zoning restrictions;
- The extent to which the proposed amendment promotes the public health, safety, and welfare of the municipality;
- The relative gain to the public, as compared to the hardship imposed upon the applicant;
- The sustainability of the subject property for the purpose for which it is presently zoned;
- The length of time that the subject property in question has been vacant, as presently zoned, considered in the context of development in the area where the property is located;
- The consistency of the proposed amendment with the comprehensive plan, and any adopted land use policies; and
- That the proposed amendment will benefit the needs of the community.

Other states have worded the criteria somewhat differently. For example, in Colorado, those factors include the following: (i) rezoning of nearby property; (ii) growth patterns; (iii) change of use patterns and character of the neighborhood; (iv) demand within the area for certain types of land uses; (v) sales of related or similar properties at prices reflecting anticipated rezoning; (vi) physical characteristics of the subject property and of nearby properties; and (vii) the age of the zoning ordinance.⁵

At minimum, any appraiser should include examples of similarly rezoned properties and an analysis of the factors that would provide support that a market participant would expect future benefits. This might be inferred via land sales or sales of buildings to be adapted for reuse under the proposed (and

reasonable) rezoning. In some cases where easily identified transactions are scarce or non-existent, more detailed supply/demand analyses might be necessary. Often the appraiser's investigation must involve consultation with not only the landowner and market participants, but also environmental consultants, local zoning officials, and other professionals.

Environmental issues merit special consideration in areas transitioning from industrial to commercial or residential. In many circumstances, particularly in properties zoned and used for heavy industrial purposes, contamination is present or has been remediated. If the former, the costs of remediation must be considered in any valuation analysis involving a change of use. If the latter, there may exist restrictions on certain types of uses, or contracts with state or federal environmental agencies which restrict certain uses.

The concept of consistent use theory is sometimes overlooked. In an area of urban renewal, some appraisers will identify a highest and best use of investment (i.e., holding the property awaiting a higher value),⁶ but omit the benefits or income of an existing use in a valuation analysis. Consistent use is "the concept that land cannot be valued on the basis of one use while the improvements are valued on the basis of another."⁷ However, using the example of a hypothetical property which serves as both a potato farm and waterfowl hunting grounds, while "it is a violation of the consistent use theory to value a parcel for two uses that are mutually exclusive, it is permissible to value a parcel for two uses that are not incompatible and can take place simultaneously."⁸ Thus, because a property can always be used for *something* in addition to holding as an investment, appraisers should examine other compatible uses, even if they believe a neighborhood transition makes it prudent for a landowner to hold until values ripen. Thus, the concept of interim use, which embraces the concept of dual highest and best uses, may be suitable in most neighborhood transition cases and should be explored.

Furthermore, many market participants of properties—in the areas where the trend of development begins to be a more fundamental question in the highest and best use analysis of a particular site – will refer to income-producing sites as covered land plays. This reflects a perspective that existing and continuing income is strong enough to warrant a short-to-long-term hold, but where the majority of an investor’s return will be recovered upon sale for redevelopment. In these scenarios, capitalization rates for properties might be lower than average rates, as the overall rate must consider not only the year-over-year return, but also the return at the end of the holding period, which in cases like these would reflect a premium.

SPECIAL ADAPTABILITY OF LAND

Expanding the Scope

In a tax assessment appeal, the Supreme Court of Connecticut rejected the plaintiff’s claim that the trial court’s rejection of a more generalized highest and best use of the property (which contemplated other varying industrial uses) meant that the court had failed to consider the marketplace in determining highest and best use. It relied on the proposition that “the ‘special adaptability of land for a particular purpose’ will only be properly considered in valuation ‘if there is a reasonable probability that the land could be so used within a reasonable time and with economic feasibility.’”⁹ The trial court, based on findings that the facility was designed and constructed to the company’s specifications, and that continuing the current use was legally feasible and profitable, concluded that the highest and best use was narrower, for the continued present use by the company or similar entity.¹⁰ The court affirmed, citing two of its previous opinions regarding special adaptability of land in support.

Rebutting the Presumption of Current Use as Highest and Best Use

Affirming the district court’s ruling that the vacant property’s highest and best use was as a future commercial sand mining site, the Fourth Circuit Court of Appeals held that a landowner must show that

a proffered highest and best use which is different from the present use is “‘reasonably probable’ and that the probability has a real market value.”¹¹ The court, citing the seminal *Olson v. United States* opinion, stated that if an element affecting value depends on “‘events which, while within the realm of possibility, are not fairly shown to be reasonably probable [it] should be excluded from consideration for that would be to allow mere speculation and conjecture to become a guide for the ascertainment of value[.]’”¹² The landowner must show that the property has real potential for the suggested use, and also demonstrate market demand for property with such a use.¹³

INTERIM USE FOR TRANSITIONING PROPERTIES

The owner of a contaminated former industrial site in California claimed “interim use” value of fixtures and equipment, even though they were incompatible with the undisputed highest and best use of the property as a mixed commercial/retail development, arguing the existing use could have continued temporarily until the property was ready for development. A California Court of Appeal ruled that the claim ran “afoul of the basic proposition that ‘in eminent domain actions, elements affecting value which, while possible, are not reasonably probable, should be excluded.’”¹⁴ Vague generalities as to possible delays in development are not sufficient, and there was no identified obstacle or cause that would have been “reasonably likely to prevent or deter” the immediate commencement of the physical process of development.¹⁵ Explaining the consequences of permitting such an interim use claim, and the doctrine’s underpinnings which provided a basis for denial, the court opined as follows:

If defendant’s approach to ‘interim use’ were sustained, such a claim could apparently be submitted in *every case* where property with existing business-related improvements is taken for redevelopment to a higher and better use. After eliciting generalizations from its experts about possible delays in development, a landowner could recover the value of the real

estate at a higher and better use than the one he has made, while adding in a claim for fixtures and improvements which are incompatible with that use.

At its core the concept of interim use is intended for situations where property is *in the process of transition* from a less valuable to a more valuable use, e.g., from agricultural to residential development. The property is worth more because of its *future* use, but market forces may not yet have reached the point where it is economical to make the transition. The property is essentially held as an *investment* for eventual development to the higher use. During this period the continuation of the past, soon-to-be-displaced use is valuable for helping to defray the carrying costs that would otherwise be incurred by the buyer. (See Matteoni & Veit, *Condemnation Practice in Cal.*, *supra*, § 4.18, p. 106 [“Although the highest and best use may be reasonably near, development to that use may not be immediate.”]; ... *Mocco v. City of Jersey City (In re Mocco)* (1998) 222 B.R. 440, 457-458 [under New Jersey law, “interim use” means period during which property destined for higher use is “h[e]ld for future development” until “demolition and re-development is economically feasible”]; *Woods v. State* (1971) 317 N.Y.S.2d 782, 783 [36 App.Div.2d 572] [where condemned acreage was surrounded by developed land and was served by utilities, agricultural use on which condemnor’s expert based valuation was “properly rejected by the court except as an interim use”]; *Pascack Motel, Inc. v. State* (1972) 338 N.Y.S.2d 204, 206, italics added [award for interim use allowed, though reduced to reflect “income approach,” where appraisers agreed that highest and best use was “future development as a shopping center or modern high rise motel”].) This policy would not be served by permitting a landowner to assert a claim for “interim use” based on the mere suggestion that development to a higher and better use *might* or “could” be delayed by routine steps in the development process, without a concrete showing that the delay

would probably appear, to a hypothetical buyer and seller, sufficiently likely and lengthy to support a price enhancement based on “interim use.”¹⁶

HOTEL REDEVELOPMENT

The Fifth Circuit’s opinion in *Whitehouse Hotel Ltd. P’ship v. Comm’r of Internal Revenue* concerned the allowable amount of a charitable-contribution deduction claimed by Whitehouse for donating a historic-preservation façade easement on the historic Maison Blanche building in New Orleans.¹⁷ Whitehouse’s appraiser, Richard Roddewig, determined that the highest and best use of the Maison Blanche and Kress buildings in both the before- and post-donation conditions was as a Ritz-Carlton hotel, an all-suites hotel, and retail on the bottom floors. The Commissioner’s appraiser, Dunbar Argote, concluded that the highest and best use of the Maison Blanche building was a mixed non-luxury hotel and retail complex.

The Tax Court did not explicitly rule on which determination was correct but did not accept Roddewig’s opinion, a decision the Fifth Circuit found was capable of two interpretations: (i) that even if the highest and best use was as a Ritz-Carlton, that had no effect on value; or (ii) a non-luxury hotel was the highest and best use. As to the former, the Fifth Circuit instructed the Tax Court to reconsider on remand whether luxury-hotel developers operate in a national marketplace and are willing to pay more than local market demands, the theory espoused by Roddewig. On the latter possibility, the court held that “the relevant question would be whether there was a ‘reasonable possibility’ that the property would be developed into a non-luxury hotel.”¹⁸ Before the easement was granted, Whitehouse had contracted with Ritz-Carlton, and procured architectural plans, to convert the buildings into a Ritz-Carlton hotel, and the Tax Court was instructed to consider, or reconsider if a ruling was made on, the validity of Argote’s opinion that many hotel projects in similar stages of development never come to fruition.¹⁹

GOVERNMENT SUBSIDIES AND INCENTIVES

In an appeal of a condemnation award to the New York Court of Appeals, the primary issue was whether the possibility of obtaining a limited-profit housing subsidy, under New York's Mitchell-Lama Law, could be considered in determining the highest and best use.²⁰ The trial court determined that the highest and best use of the subject parcel was as a subsidized high-rise apartment site, and the city contended on appeal that the subsidized use could not be considered because the government is involved in awarding such subsidies. The appellate court disagreed, stating that "[t]he fact that governmental activity is required to achieve a use does not necessarily disqualify the use from consideration."²¹ The example of awards based on uses requiring government issuance of zoning variances, when "the granting of such variances was reasonably probable[,] " was cited in support.²² The court held that if the granting of such a subsidy is shown to be reasonably probable, "and upon proof that such a project could or would have been constructed upon the subject premises in the foreseeable future but for the appropriation," then nothing prevents a lower court from making such a finding.²³

CASE STUDY—CS MEETING STREET

On August 25, 2017, the South Carolina Department of Commerce, Division of Public Railways, (Condemnor) filed a Notice of Condemnation in Charleston County, South Carolina, seeking to take an entire parcel owned by CS Meeting Street, LLC (Landowner), in conjunction with the construction and operation of a Navy Base Intermodal Facility and associated railway lines, in Charleston. The amount of just compensation offered by the Condemnor was \$1,705,500 for the parcel which totaled 3.17 acres of land. As of the date of condemnation, the property was vacant and was being leased by Landowner to an electric power company for a vehicle and equipment laydown yard in connection with a utility project. The subject property was located in an historically industrial area called The Neck (the narrowing lands north of peninsular Charleston) and had been used for commercial purposes since at least the late 1930s. In the 1950s, a gas station

operated on the property, and later, the property was used as a trucking terminal with services that included truck repair, service, and body shop operations. This business ceased in the 1990s and the property had remained idle for the most part for many years prior to the condemnation.

Use of the property for trucking facilities resulted in soil contamination, caused by nine underground storage tanks, four above-ground storage tanks, and a documented oil spill on the property. Groundwater monitoring wells were installed in the 1990s, and prior to closing on its purchase, Landowner's affiliate entered into a Voluntary Cleanup Contract (VCC) with the South Carolina Department of Health and Environmental Control (DHEC). In connection with the VCC, a Declaration of Covenants and Restrictions was recorded, which placed certain restrictions on the property, including a use restriction which prohibited residential, agricultural, outdoor recreational, child day care, and adult day care uses on the property.

Meanwhile, the character of the surrounding area was quickly and drastically changing as a result of rapid growth in the Charleston area and a lack of available land for housing and development. As stated in Landowner's appraisal report:

Today Morrison Drive has taken on a new identity as NOMO. It has become a trendy chic location with retail, restaurants and now, apartments. It is accessible and has parking. Properties in NOMO were red hot starting in 2015 and have exhibited tremendous value appreciation. Even with substantial value increases the price of NOMO property is a bargain compared to downtown Charleston.

...

2016 and 2017 are now to the immediate subject neighborhood what earlier years were to NOMO. In a short two to three years most of the available properties in NOMO have been absorbed. There has been an inexorable south to north growth trend in Charleston for the last 100 years and there is no signs that the

north/south trend will change. The immediate subject neighborhood is the next area to be the beneficiary of this trend and already shows signs of transition from industrial/service businesses to more retail, restaurants, office and residential.

The property was zoned GB, General Business, in the City of Charleston. However, the city was actively promoting a change to UP, Upper Peninsula zoning, a new zoning designation enacted in 2015, which, according to the city, was:

incentive based offering height and density bonuses in exchange for added community benefits such as workforce housing, public open space, renewable energy, electric vehicle charging stations, transportation improvements, stormwater management improvements, green infrastructure, and achieving building certification programs for a high performing building.

...

The Upper Peninsula Zoning District is a new base zoning district (not an overlay) designed specifically for the Upper Peninsula. It encourages responsible growth and sustainable development. It allocates density in appropriate areas. It protects the character and livability of the existing residential neighborhoods. It encourages public and private investment and spurs economic development. It implements recommendations of City plans.²⁴

Based upon the city's policy decision to encourage rezoning of properties in The Neck to the newly adopted UP zoning district, his consultations with city planning and zoning officials, and his well-studied and supported view of market demand, Landowner's appraiser determined that there existed a reasonable probability of a zoning change for the property to UP.

Landowner had originally contracted to purchase the property in 2015 with the intent to develop it as a self-storage facility. However, due to the rapidly

changing conditions, its vision for the property changed. Landowner had been active in the local real estate market, including other properties in The Neck, and had commissioned comprehensive marketing and feasibility studies for multifamily residential use on other property holdings. Landowner perceived the potential for a mixed-use or multi-family development prior to condemnation and was in the process of rezoning the subject parcel to UP zoning at the time of the condemnation.

During litigation, Landowner retained the same firm that had done the multi-family marketing studies for its other projects in order to analyze whether the subject property would be suitable for such as use. Landowner engaged the firm and one of its founding principals to serve as an expert witness in the case. The market analysis determined that a multi-family development was feasible for the subject property, and that a:

young, single demographic who isn't highly affluent (most likely due to working in the service industry or at an entry level job) will be the primary target market. The subject site's proximity to Historic Downtown Charleston, as well as nightlife found further up the Peninsula, convenient location to a variety of job cores, and relative affordability will be highly appealing to this target demographic.

While the marketability study proved to be favorable, and the appraiser had determined reasonable probability of a zoning change to UP, the hurdle of the restrictive covenants imposed upon the property due to environmental contamination remained. Landowner engaged an environmental consultant specializing in brownfields redevelopment who had worked for DHEC from 1977 to 2008, and served as Program Manager, Environmental Health Manager Brownfields/Voluntary Cleanup from 2000 to 2008. After studying the history of the site, the protections put in place through the VCC, the current site conditions, and the covenants themselves, the environmental consultant opined that multi-family development could be accomplished on the property. More

specifically, she found that, based upon her review of the information, discussions with DHEC officials, and experience, the property was eligible for a modification of the restrictive covenants, and that it was reasonably probable that the property could be used for multi-family purposes so long as certain protective site improvements were made in connection with the construction of the project.

Supported by not only market data, but also the information and opinions provided by the city, DHEC, the feasibility/market expert and his study, and the environmental consultant, Landowner's appraiser opined that the highest and best use of the property would be for commercial and residential mixed uses. His appraisal report valued the property, and estimated the just compensation for the taking, at \$9,050,000. Although mediation ended at an impasse, the case ultimately settled prior to trial for \$4,500,000, as reflected in a publicly filed Consent Order of Dismissal.

WHAT IF THE CONDEMNATION PROJECT ITSELF IS URBAN RENEWAL?

While real estate development can be advanced solely by private actors, municipalities and other governmental taking authorities frequently employ eminent domain for urban renewal, in order to acquire property, stimulate redevelopment, or demolish blighted areas. When the condemnation project is urban renewal, the project influence rule is an additional consideration for determining highest and best use, particularly when evaluating the condemned property's redevelopment potential.

Under the project influence rule, "just compensation cannot include any enhancement or reduction in value that arises from the very project for which the property is being acquired."²⁵ As illustrated below, the rule is a two-way street, because the compensable value for the property can be neither increased nor decreased by the condemnation project:

For example, if the Government announces that it will establish a park on parcel A, then files an action to take parcel B adjacent to parcel

A, the Government should not have to pay for the increased value to [parcel B] following the Government's park announcement. Likewise, if the Government announces that it will establish a landfill on parcel A, the Government should pay the owner of parcel B the amount it was worth before the Government announced the landfill.²⁶

"While the project-influence rule may be neatly stated, it is not always so neatly applied."²⁷ The rule's exclusion does not apply, and just compensation must include any enhancement caused by an adjacent public improvement project, if: (i) "the property was not within the original scope of the project;" (ii) "the government failed to provide the public with adequate notice of the project's scope;" or (iii) "the landowner reasonably believed that subsequent government action removed the property from the project's scope."²⁸ Where the original scope of the project is enlarged at a later stage to include the subject property, any project-driven enhancement before this change is *compensable* to the property owner, whereas after the change, "any increase in value arising from the known fact that the lands probably would be condemned" are not compensable.²⁹ Determining whether the project influence rule applies, including whether and when the subject property is within the "scope of the project," is a question of law for the court, and not determined by the jury.³⁰

In the context of highest and best use, the project influence rule can impact several criteria, including potential property uses, land use restrictions, and market data.³¹ Zoning restrictions enacted to depress the value of property for the benefit of the condemning agency are excluded.³² However, when the property's highest and best use happens to be the same, so that the use supported by the condemnation project is also supported by the private marketplace, the project influence rule does not apply.³³

It is well-known that "[i]n Baltimore, condemnation drives urban renewal,"³⁴ frequently in one of two forms: (i) the city may acquire a single property

on a block of otherwise vacant buildings, in order to demolish the entire block, to remove blight in the hopes of redevelopment or open green space; or (ii) on a larger scale, the city uses long-standing urban renewal plans for entire neighborhoods or commercial corridors, often dating back to the late 1960s, to identify a broad area for property acquisition, even though the actual takings may occur slowly over time.³⁵

Below, a case study illustrates the role of the project influence rule in the highest and best use analysis within an urban renewal project.

In the Franklin Square neighborhood of West Baltimore, the city condemned the last remaining occupied property on an otherwise vacant block. Nearly 30 years prior, the property owner purchased two abutting rowhomes, to consolidate and renovate the first floor into a corner store with a commercial kitchen. After operating the store for several years, he leased it and turned to renovating the second floor into residential apartments. Across the street was a busy rowhome community, owned and recently renovated by private developers. There were no other food or grocery stores in the immediate area. But once the condemnation was announced, the owner lost his store tenant, attempted in vain to find a replacement, and then sought his own use and occupancy permit to reopen the store but was told by the city that there was “no point,” because the property was being taken by eminent domain. The city’s appraiser first determined the highest and best use of the property was residential only and valued the property at \$36,000.

At trial, and contrary to the project influence rule, the city used the facts that the store was closed and there was no current tenant to argue that the market value should be diminished. Several factors led the jury to reject the City’s argument, including: (i) the jury view, which presented not only the property but also its proximity to a thriving residential community in need of a corner convenience store; (ii) the owner’s sympathetic testimony and leasing records, which were summarized in the paragraph

above; and (iii) the owner’s competing appraiser. Ultimately, the jury awarded \$196,250.00.³⁶

CONCLUSION

While areas of transition can in some cases appear plain as day, other cases may require condemnors and landowners, and their respective counsel and appraisal experts, to dig into market characteristics and zoning in order to perceive change on the horizon. Often, questions may arise when a condemned property is on the fringe of a rapidly changing neighborhood. Ignoring the potential for change is a risk for condemnors, who may submit unreasonably low offers by failing to perceive a diamond in the rough. At the same time, a landowner or appraiser seeking to capitalize on transition must know the rules of the road and where the traps lie on reasonable probability of rezoning, environmental issues, and marketability. Finally, government-sponsored urban renewal projects present their own sets of challenges, particularly with the application of the project influence rule. A thorough understanding of these issues will aid in resolution and/or trial of your eminent domain case involving a property in transition. 🍀

Notes

- 1 This paper was prepared in conjunction with and submitted as part of the American Legal Institute’s Eminent Domain and Land Valuation Litigation CLE, on February 1, 2024.
- 2 Urban renewal is defined as “[t]he process of redeveloping urban areas by demolishing or repairing existing structures or by building new facilities on areas that have been cleared in accordance with an overall plan.” Black’s Law Dictionary (11th ed. 2019).
- 3 A property’s highest and best use must be analyzed using four criteria: (i) physical possibility; (ii) legal permissibility; (iii) financial feasibility; and (iv) degree of profitability. “Because most property is adaptable to several uses, the highest and best use is the physically possible, legally permissible, and financially feasible use that results in the highest value.” The Uniform Appraisal Standards for Federal Land Acquisitions (the “Yellow Book”), Section 4.3 (citing *United States v. 69.1 Acres of Land (Sand Mountain)*, 942 F.2d 290, 292 (4th Cir. 1991)).

- 4 LaSalle National Bank v. County of Cook, 12 Ill.2d 40, 145 N.E.2d 65 (1957); Sinclair Pipe Line Co. v. Village of Richton Park, 19 Ill.2d 370, 167 N.E.2d 406 (1960).
- 5 Eminent Domain and the Reasonable Probability of Rezoning: Why It Matters for a Property's Highest and Best Use, Sean Metherell, Faegre Drinker (Nov. 2, 2018). See also City of Brighton v. Palizzi, 214 P. 3d 470 (Colo. App. 2008).
- 6 Some courts have cast doubt on whether "holding for future development" can qualify as a recognized highest and best use in the context of a condemnation action. See, e.g., Dept. of Transportation v. Janssen, 339 N.E.2d 359, 361 (Ill. 1975).
- 7 J.D. Eaton, Real Estate Valuation in Litigation (2nd ed. 1995); see also The Appraisal Inst., The Appraisal of Real Estate, 46 (10th ed.1992); The Appraisal Inst., The Dictionary of Real Estate Appraisal, 72, (3d ed. 1993).
- 8 Eaton, supra note 7, at 115.
- 9 United Technologies Corp. v. Town of East Windsor, 262 Conn. 11, 22 (Conn. 2002).
- 10 Id. at 24-27.
- 11 U.S. v. 69.1 Acres of Land, More or Less, 942 F.2d 290, 292 (4th Cir. 1991).
- 12 Id. (quoting Olson v. U.S., 292 U.S. 246, 257 (1934)).
- 13 Id. at 293.
- 14 Emeryville Redevelopment Agency v. Elementis Pigments, Inc., 101 Cal. App. 4th 1083, 1111-12 (2002) ("A finding of compensable 'interim use' will ordinarily require concrete evidence of circumstances that could reasonably cause a buyer of the particular property at issue to view the presence of incompatible improvements as a net economic benefit rather than a net cost." (emphasis in original)).
- 15 Id. at 1112-13.
- 16 Id. at 1114-15.
- 17 615 F.3d 321 (5th Cir. 2010). Also at issue, but not relevant to the highest and best use discussion, was the easement's effect on Whitehouse's opportunity to build on top of the contiguous Kress building it also owned. The expert appraisers differed in opinion as to whether the easement prohibited such construction.
- 18 Id. at 336 (citing Olson, 292 U.S. at 256-57).
- 19 Id. at 336-37.
- 20 In the Matter of City of New York (Rudnick), 25 N.Y.2d 146, 148 (N.Y. Ct. App. 1969).
- 21 Id.
- 22 Id. (internal citations omitted).
- 23 Id. at 149. The appellate court ultimately reversed and remanded, ruling that, while "a court may properly base its determination of fair market value upon a subsidized use, if such use is reasonably probable," the reasonable probability that a subsidy would have been granted had not been established. Id. at 150.
- 24 <https://www.charleston-sc.gov/1686/Upper-Peninsula-Zoning-District>.
- 25 City of Boulder v. Fowler Irrevocable Tr. 1992-1, 53 P.3d 725, 727-28 (Colo. App. 2002). See United States v. Miller, 317 U.S. 369 (1943); United States v. Reynolds, 397 U.S. 14 (1970); Caffe Ribs, Inc. v. State, 487 S.W.3d 137, 143 (Tex. 2016) ("[N]either project enhancement nor project diminishment reflects true 'market value' – that is, what a willing buyer would pay a willing seller under market conditions ... The rule ensures that the condemnee is made whole, not placed in either a better or worse position than he or she would have enjoyed had there been no condemnation."); see also H. Dixon Montague and George Murphy, The "Scope" of the Project Influence Rule, SM006 ALI-ABA 377 (2007); Jack Sperber, Using the Valuation Rules as Tools to Win Your Case, 27 No. 2 Prac. Real Est. Law 5, 19-22 (March 2011).
- 26 United States v. 480.00 Acres of Land, 557 F.3d 1297, 1312 n.8 (11th Cir. 2009).
- 27 Caffe Ribs, Inc., 487 S.W.3d at 143.
- 28 United States v. 49.01 Acres of Land, 669 F.2d 1364, 1367 (10th Cir. 1982), quoting United States v. 2,353.28 Acres of Land, 414 F.2d 965 (5th Cir. 1969), United States v. 320.0 Acres of Land, 605 F.2d 762, 793 (5th Cir. 1979), John B. Hardwicke Co. v. United States, 467 F.2d 488, 490 (Ct. Cl.1972), and United States v. 172.80 Acres of Land, 350 F.2d 957, 959 (3d Cir. 1965). See also Miller, 317 U.S. at 377 (holding that if the "lands were probably within the scope of the project from the time the Government was committed to it," rather than "merely adjacent lands," then "the Government ought not to pay any increase in value arising from the known fact that the lands probably would be condemned").
- 29 Miller, 317 U.S. at 377. See also Reynolds, 397 U.S. at 21 (holding that in order to fall within the scope of the project, the property need not be "actually specified in the original plans for the project," but "need only be shown during the course of the planning or original construction it became evident that land so situated would probably be needed for the public use.").
- 30 Reynolds, 397 U.S. at 20 ("[I]t is for the judge and not the jury to decide whether the property condemned was probably within the project's original scope").
- 31 Sperber, supra note 25, at 20.
- 32 United States v. 480.00 Acres of Land, 557 F.3d 1297 (11th Cir. 2009) (joining the Second, Third and Fifth Circuits to hold that "[i]n order to have a zoning restriction excluded from a calculation of a property's value, a landowner must show that the primary purpose of the regulation was to depress the property value of land or that the ordinance was enacted with the specific intent of depressing property value for the purpose of later condemnation." (emphasis added)); see also United States v. Certain Lands in Truro, 476 F. Supp. 1031, 1036 (D. Mass. 1979) (finding extensive involvement of the federal condemning authority in the enactment of a local zoning provision in Cape Cod, agreeing with the property owner that "the federal government should not be allowed to profit from the decreased values which that bylaw effected," and holding that "any fluctuation in property value which has resulted from the three acre zoning provision is a fluctuation which is attributable to the federal project

itself and therefore that the three acre provision should not be considered in determining the fair market value of the land in question.”).

- 33 Sperber, *supra* note 25, at 21.
- 34 In Baltimore, Condemnation Drives Urban Renewal, *The Md. Daily Record* (Dec. 4, 2008), available at <https://thedailyrecord.com/2008/12/04/in-baltimore-condemnation-drives-urban-renewal/>.
- 35 Baltimore Dep't of Planning, Urban Renewal Plans, available at <https://planning.baltimorecity.gov/planning-plans/urban-renewal>.
- 36 *Mayor and City of Baltimore v. Kevin L. Davenport*, Circuit Court for Baltimore City, Case No. 24-C-18-005103.

@ALLICLE