

Just Compensation for Contaminated Land

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When a government agency or private party involuntarily takes your property (a proceeding called eminent domain or condemnation), you are entitled to receive "just compensation" for the property. In North Carolina, "just compensation" is defined as the "fair market value" ("FMV") of the property taken, or the price a seller is willing to accept and a buyer is willing to pay for the property on the open market and in an arm's length transaction without duress.

In order to determine the FMV, the party that is taking your property will hire an appraiser who will inspect and appraise the property. The appraiser will gather information regarding the area where your property is located, the history of your property, recent sales of nearby comparable property, and other information that may be relevant to determining the FMV of your property.

What happens if, during this process, the appraiser discovers information that shows that there is contamination on your property? Can the appraiser consider this information in determining the FMV of your property? What effect, if any, does the contamination have on the amount of "just compensation" you will receive for the taking of your property?

Inclusion or Exclusion?

The issue of how to treat evidence of environmental contamination when determining just compensation appears to be an issue of first impression in North Carolina. However, other state courts have considered this issue and an analysis of those cases indicates that two divergent approaches have emerged.

One group of states has held that evidence of environmental contamination, including the cost of remediation, is admissible during the condemnation process (the "Inclusion Rule"). Courts in California, Connecticut, Kansas, Michigan, Oregon, Tennessee, and Florida have adopted this Inclusion Rule. These courts have held that environmental contamination affects the FMV of the property and is, therefore, relevant to determining just compensation. These courts also conclude that the exclusion of contamination evidence would result in inaccurate awards and force the condemning party to pay more for the property than it is worth.

Other states have adopted a rule that excludes evidence of contamination (the "Exclusion Rule"). Courts in Illinois, Iowa, New Jersey, Minnesota, and New York have concluded that valuing the taken property as contaminated is unfair to the property owner because the value of the property is often reduced dollar-for-

dollar by cleanup costs.

The courts in Illinois and Iowa exclude all evidence of contamination while the courts in New Jersey, Minnesota, and New York have adopted a "Modified Exclusion Rule," holding that, although evidence of cleanup costs is inadmissible, the property taken should be valued as "remediated." Based on an analysis of all of these cases, it appears that the Modified Exclusion Rule adopted by the courts in New Jersey, Minnesota, and New York is most likely to be fair to both the land owner and the condemning party.

The Inclusion Rule May Subject a Landowner to Double Liability

The Inclusion Rule may unfairly subject the landowner to double liability because environmental laws and condemnation proceedings may overlap in a way that penalizes the property owner twice. Under the Inclusion Rule, evidence of contamination and remediation costs will result in the property being valued as contaminated, which often reduces the FMV of the taken property dollar-for-dollar by the actual or estimated cost of remediation.

At the same time, the property owner may be held liable for the contamination under environmental laws and be required to pay the costs of cleaning up the property. The Inclusion Rule also has the effect of providing the condemning party with a windfall because the condemning party pays a discounted price for the property due to the contamination but then receives the property in a cleaned condition after remediation.

Although North Carolina courts have not ruled on whether the Inclusion, Exclusion, or Modified Exclusion Rule applies, the risk of double liability is very real in North Carolina because the environmental laws in North Carolina assign liability to property owners for contamination.

Other Reasons the Inclusion Rule May be Unfair to a Landowner

Another reason the Inclusion Rule may be unfair to a landowner is the difficulty of assessing the FMV of contaminated property. Finding comparable parcels to arrive at an estimate of value is problematic because each piece of property is unique and the effect of contamination on each piece of property is different. As a result, traditional expert testimony as to FMV based on comparable sales might not be available. Because the FMV of contaminated property is difficult to estimate and including evidence of contamination may subject a property owner to double liability, excluding evidence of cleanup costs in condemnation proceedings appears to be the better approach.

The Inclusion Rule also may be unfair to a landowner because it may allow the condemning party to use the condemnation process to circumvent procedures that have been established for recovering cleanup costs. A contamination action has procedural safeguards that allow a landowner to contest liability for the contamination, bring third-party actions against former owners, and assert certain defenses.

However, in a condemnation action, a landowner is not able to join other potentially responsible parties in the action or assert defenses that could be asserted in a contamination action. In addition, evidence relating to how the contamination occurred and who may be responsible is not relevant in a condemnation action. If the condemning party is permitted to introduce evidence of cleanup costs in a condemnation action, it will deprive the landowner of procedural due process rights and unfairly permit the condemning party to recover cleanup costs from the landowner without proving the landowner's liability for the contamination.

The Exclusion Rule Avoids Double Liability

The Exclusion Rule, on the other hand, acknowledges the liability of the property owner to clean the property under environmental laws while avoiding a discounting of the value of the property due to the contamination. If cleanup costs are not admissible, the property owner will have the obligation to clean the property but will not be forced to surrender the property to the condemning party at a reduced price. Thus, excluding evidence of contamination and remediation greatly diminishes the risk that a property owner will face double liability for contamination that existed on the property at the time it is taken.

The Modified Exclusion Rule - A Balanced Approach: Remediated, Not Cleaned

While it appears that the inclusion of evidence of cleanup costs may be unfair to a landowner, establishing the FMV of property as "clean" may result in inaccurate awards and force the condemning party to pay more for the property than it is worth. For this reason, a more balanced approach may be to value the property as "remediated" rather than as clean. In other words, just compensation for contaminated property should be the FMV of the property after remediation. This approach is consistent with the Modified Exclusion Rule that has been adopted in New Jersey, Minnesota, and New York.

Clean property has never been contaminated. Remediated property, in contrast, is property that has gone through a process to remove the contamination. Although the contamination has been removed, the property may have developed a reputation as being contaminated. Even if a property has been cleaned, fear of discovering additional contamination and the accompanying liability may reduce a property's value to prospective purchasers. For this reason, the FMV of remediated property can be different from property that has never been contaminated and a balanced approach would suggest that the property should be valued as "remediated."

Therefore, even though evidence of cleanup costs should be inadmissible, under the Modified Exclusion Rule the proper valuation of contaminated property that has been taken should be the FMV of the property as "remediated" as opposed to its FMV as "contaminated" or its FMV as if it were "clean."

So, for a balanced approach, in an action where contaminated property is condemned, just compensation should be the FMV of the property as remediated, and evidence of contamination of the property should be considered only to the extent necessary to determine if there is any loss of value to the property due to the reputation of the property as being contaminated.

Conclusion

When a government agency or private party takes private property from you involuntarily, it will make you an offer of just compensation and tell you it represents the FMV of the property it is taking from you based on an appraisal it has obtained.

If your property is contaminated, the condemning party may try to discount the value of the property based on the estimated costs of cleaning up the property. Keep in mind that you do not have to accept the condemning party's valuation of your property and that there are sound procedural, substantive, and policy arguments that can be made for rejecting an offer which is based on the inclusion of cleanup costs.

So, don't be worried when the party taking your property threatens to file a lawsuit against you. Instead, you should consult with an attorney who is experienced in the area of eminent domain or land condemnation law concerning your legal rights. A good eminent domain attorney will be able to effectively identify your

potential damages and help you select necessary experts to prove what you are due for just compensation. The attorney also will help you negotiate with the entity taking your property and can take your case to trial if a settlement is not reached.

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