

ATF APPRAISAL IN EMINENT DOMAIN CASES:

A REBUTTAL



Introduction

The article, “The Legality of the Across the Fence Appraisal Approach in Eminent Domain Proceedings” by Todd Amspoker, Esq. (Sep/Oct 2000 *Right of Way*) shows that there are still wide spread misconceptions about appraisal principles in general and about Across the Fence (ATF) methodology in particular.

Highest and Best Use

As in all appraisals, the fundamental principle in planning a corridor appraisal is that of Highest and Best Use. The concept of highest and best use is generally understood to mean:

The reasonable probable and legal use of vacant land or an improved property, which is physically possible, appropriately supported, financially feasible and results in the highest value to the land.

Implied within this definition is a recognition of the contribution of that specific use to community environment or to community development goals in addition to wealth maximization of individual property owners. Also implied is that the determination of highest and best use results from judgment and analytical skill: the use determined from analysis represents an opinion, not a fact to be found.

The basis for arriving at the highest and best use of the land lies in the market analysis and the economic concept of supply and demand. Generally, it is that use which, in a given time, anticipates the greatest land value that can be created, consistent with any restrictions imposed by its environment and the community in which it is located.

Highest and best use is that legal use which will yield to the property the highest present value. Further, it must be a use or combination of uses:

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1. Which is or will be permitted under existing or reasonably attainable zoning and/or other regulations;
2. For which there is an economic, social, and/or market demand;
3. For which the property is physically suitable or adaptable;
4. And which is harmonious with the nature and condition of existing neighborhood development.

Highest and best use is the foundation upon which the structure of the appraisal is erected and is the bedrock of the appraisal analysis and report. If, in the appraiser's opinion, the highest and best use of the site is for continued corridor operation, then ATF methodology is the correct method to be used. If the highest and best use is for a non-corridor use, then other appraisal methodology must be used.

Case Study

In the "Actual Case Study" (*City of Tracy v. The Westside Irrigation District*) cited in the article, the property being appraised was a small portion of a no-longer functioning irrigation ditch. The irrigation district's decision to appraise their parcel using ATF was apparently made on the grounds that the property was a public utility and was entitled to be valued on that basis. That decision was preposterous! The basis of an appraisal is highest and best use, not the type of ownership it is under. The site no longer had any use as a corridor and should have been appraised under net liquidation. But the district's inappropriate use of ATF appraisal methodology does not make the ATF approach invalid or illegal in eminent domain situations. [*Shaffer-Rahn note: Attempting to open a bottle with a sledgehammer instead of a bottle-opener doesn't make the hammer a useless tool.*] It simply means that a useful tool was used in an inappropriate manner.

In 1988, the Oregon Court of Appeals, in a decision¹ regarding the valuation of a transportation corridor had this to say about ATF methodology—

"The ATF method assesses the market value of separate, similar parcels located near the condemned parcel, determines a square foot value and applies that figure to the area of the condemned parcel. An "enhancement factor" is added to that value to arrive at the value of the parcel as a whole. Since the railroad's appraiser testified that the highest and best use of the land was as a railroad corridor, the ATF appraisal was admissible to show how the value of corridor property was determined in the market."

In 1989 the California Public Utilities Commission,² acting on a petition from the City of Vallejo concerning the valuation of a longitudinal easement on a corridor, ruled in favor of using ATF in the following language: "Issue 4 — Should the easement be valued as a whole or segment by segment? Southern Pacific Transportation's (SPT) appraiser valued the easement area in five segments while the City's appraiser valued the easement area as a whole... We believe that the segment method adopted by the witness for SPT and the City's earlier appraiser is the most appropriate and reasonable method to use in the circumstances with which we are faced. The evidence shows

that the corridor passes through distinctly different neighborhoods where the uses of the property differ between segments. We would expect that the fair market value of these different properties would vary from neighborhood to neighborhood."

The ATF methodology, as criticized by Mr. Amspoker, has been extensively tested, peer-reviewed, and is widely accepted by the appraisal profession as well as by buyers and sellers of these special-purpose properties.

Legal Objections

Under the heading "Legal Objections to Use of the ATF Approach," Mr. Amspoker points out that the fair market value depends on what the property owner (condemnee) has lost as opposed to what the taking agency (condemnor) has gained or avoided. Then he leaps into that quagmire which had previously been stirred by Dr. George Karvel in his article³ wherein Dr. Karvel concluded that the loss of value to the owner of a corridor resulting from a public utility's power of condemnation can only be measured using a before-and-after approach to value. If, in Dr. Karvel's opinion, the presence of a new easement caused no monetary or operational loss to the corridor owner, the public utility would be required to make only a nominal payment and not a value based on ATF.

While it may be true that a new easement may not encumber or unnecessarily interfere with an existing present corridor use, to say that the easement does not encumber or interfere with the underlying land value is another matter. Given the changes in technology and industry in the past 30 years, who could have predicted the multiplicity of users we now find on transportation corridors. Value is generally defined as the present worth of future rights to benefits or income. The presence of a new easement may have a major impact on some future use and directly impact the underlying value of the land. Moreover, the fact that at the present moment the railroad has not made use of all the right-of-way does not preclude it from future full utilization and compensation predicated upon that contemplated full use.⁴

The fact that someone is not using their land fully at the moment does not give another party the right to come on the property and use it for only a nominal payment. This concept flies in the face of the Federal and State Constitutions and the whole idea of just compensation. In any condemnation proceedings, the condemnee is entitled to just compensation based on the highest and best use of the property, regardless of whether or not it is then being fully devoted to that use.⁵ Further, if an owner is making only a minor use of the premises, he cannot be deprived of his value for a major use if that use is

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authorized and gives it a higher market value, irrespective of whether the owner does or does not utilize the property for the purposes which give it its major use.⁶

The often cited case of *San Diego Land etc. Co. v. Neale*, (1888) 78 Cal. 63, states at pages 68 and 69 that:

“... in many instances, as in the case before us, there is no actual demand or current rate or price, either because there have been no sales of similar property, or because the particular piece is the only thing of its kind in the neighborhood, and no one has been able to use it for the purposes for which it is suitable and for which it may be highly profitable to use it. In such case, it has been sometimes said that the property has no market value, in the strict sense of the term.” (*Chicago N.W. RY v. E.R.R.*, 112 Ill. 607, *Lake S. & M.S. RY v. C.&WJ. R.R.*, 100 Ill. 33; *St. Louis R.R. v. Chapman*, 38 Kan. 307.) And, in one sense this is true.

But it is certain that a corporation

could not for that reason appropriate it for nothing. From the necessity of the case the value must be arrived at from the opinions of well-informed persons, based upon the purposes for which the property is suitable. This is not taking the “value in use” to the owners as contra-distinguished from the market value. What is merely taken into consideration are the purposes for which the property is suitable, as a means of ascertaining what reasonable purchasers would in all probability be willing to give for it, which in a general sense, may be said to be the market value. And in such an inquiry it is manifest that the fact that the property has not previously been used for the purpose in question is irrelevant.

Comparable Sales

In the same section of the article, Mr. Amspoker raises possible objections to comparable sales, which could be used by the condemnee’s appraiser to support the ATF value of the easement. As mentioned in the article, the ATF

approach is based on the premise that the corridor land should be worth as least as much as the land through which it passes.

The reasoning behind this premise is, absent the corridor, the land constituting the corridor would be part of the adjacent land parcels and would have the same market value.

In *People ex rel. Dept. of Public Works v. Auburn Ski Club*, 241 Cal. App. 2d 781, 784-86 (1966), hearing by the Supreme Court denied, the appellate Court held that the admission of evidence of “comparable sales,” which in fact were not very comparable, was permissible “Because of the peculiar circumstances described above— the sui generis character of the subject (ski slope) property and the impossibility of obtaining other market data.” These are the same circumstances that have resulted in the acceptance of the ATF methodology in right-of-way negotiations.

Traditional Approaches to Value

The three traditional appraisal approaches: sales comparison, income, and cost may not always be applicable when dealing with transportation corridors. Following is a brief discussion of each approach as they apply to the appraisal of special purpose properties.

Sales Comparison Approach

This approach is based on the principle of substitution, which holds that a prudent person will pay no more for a given property than the cost of a comparable and equally desirable substitute. The technique provides a value indication through comparison of the subject with similar or like properties that have recently sold after application of appropriate units of comparison and after making adjustments to the sales prices of the comparables based on the various elements of comparison.

Transportation corridors are special purpose properties; that is, properties that are devoted to or are available for utilization for special uses not usually found in the traditional real estate market.

Existing transportation corridors are

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not commonly bought and sold in the market and, where sales have taken place, many times the basis of the sale is "administrative settlement" rather than economic analysis of corridor sales. Even when there are corridor sales available for comparison, they are seldom in the same geographic area as the subject. This can result in a dramatic difference in the corridor value; obviously, a corridor through Los Angeles or Denver would have a higher land value than a corridor through Hayes, Kansas or Elko, Nevada. For these reasons, the Sales Comparison Approach may not always be usable in the traditional manner.

Income Approach

The principle of substitution underlies this approach (as it does the other two approaches to value) together with the concept of anticipation, which is the perception that value is created by the expectation of benefits to be derived in the future.

After gross income and expenses are estimated, the residual income of the property is converted or capitalized into a lump sum present value. This is accomplished from dividing net income by a market-derived capitalization rate or a capitalization rate of return for similar properties.

The Income Approach is not usually employed to value transportation corridors. There is simply no way to apportion the revenue derived from a single segment or small portion of the integrated railroad system. A further deficiency of the Income Approach is that it gives no value indication of the available portions of the corridor outside the necessary railroad operating requirements, which could be used by other compatible users.

Cost Approach

The Cost Approach usually relates to properties improved with structures, and is a process in which the appraiser derives a value indication by estimating the current cost of reproducing or replacing the existing improvements, deducting accrued depreciation and finally adding the value of the land.

Depreciation is defined as the difference between the replacement or reproduction cost new of an item and its value in used condition. Land is valued by the Comparative Sales Approach wherein the site is considered vacant and available for its highest and best use, presumably consistent with existing usage.

In the classic sense, in the appraisal of special use properties, the land is appraised by the Sales Comparison Approach.

The Cost Approach is used to estimate the Replacement Cost New (RCN) of the improvements on the site. The RCN is then adjusted for depreciation, which is the difference between the replacement or reproduction cost new of an item and its value in used condition. It is the improvements that normally define the special purpose or use of the site such as a school, courthouse, hospital or a church.

In transportation corridors, it is the land and not the improvements that are unique and constitute the special use. Long, narrow strips of land which provide continuity between desirable endpoints are not ordinarily available in the usual subdivision of land uses. Therefore, the normal process of creating a transportation corridor is through assemblage and the cost approach includes both the acquisition of the necessary properties to create the corridor together with the normal project costs to make it useable. Those costs which can reasonably be anticipated in creating a corridor would include land, existing improvements, severance damages, relocation assistance, right of way clearance, legal and litigation fees, project and overhead costs including that giant

Cont'd on page 48

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President's Message

Cont'd from page 3

and uniform appraisal requirements of an acceptable appraisal, together with a uniform marketing of both to the general public. It was also agreed that these matters would be more thoroughly discussed at the NACAO meeting that the IRWA is hosting in San Antonio, Texas on March 15-18. The proposed merger between the ASA and NAIFA was not consummated.

The day prior to the commencement of the Appraisal Foundation meetings, Chair of the IPDC Howard Armstrong and I accompanied Susan Lauffer, Director of the Office of Real Estate Services (ORES), of the Federal Highway Administration (FHWA) and her Technical Services Team Leader, Richard Moeller, to a meeting with Z. Andrew Farkas, Ph.D., Director and Professor of the Morgan State University National Transportation Center and Fikru H. Boghossian, Ph.D., Dean of the Earl G. Graves, Morgan State University School of Business and Management, in Baltimore, Maryland. We discussed expanding their university's curriculum to include subjects such as the appraisal of partial takings for rights-of-way, relocation assistance, condemnation law and the Uniform Act Regulations (UAR), and the Uniform Relocation Assistance and Real Property Acquisitions Act (which the UAR's were based). Murray Piper, a graduate of Morgan State University, was also involved in the discussions; he offered to help get the courses developed and participate in lectures for the students. We were assured that Morgan State University was very much interested in doing what we had suggested, with assistance from the FHWA and the IRWA, and hoped to commence the development of such a curriculum by the spring semester.

Although this message turned out to be more of a report than a message, many important things happened that I wanted to relate to you. Thank you for being an IRWA member. ■

Armstrong

Cont'd from page 12

including updates on professional issues throughout the industry; legal decisions by the courts and rulings by governmental agencies that directly impact our profession. By giving our members the access to tools to improve their skills, we as an Association earn the designation of being the professional organization of choice for the right of way profession.

There are challenges for our organization in terms of administrative issues. The permanent location of our headquarters operation and the retention of qualified headquarters staff are also key elements of our continued success. Decisions regarding these important issues must be carefully studied; but when the studies are completed, we must take the bold steps to implement and support the actions taken.

The opportunities for our Association during this first decade of a new century are unlimited. We, as an Association, must ensure our focus is not solely on the success of our past actions, but what lies ahead. I pledge to each of you my untiring and dedicated efforts as a part of the International Executive Committee to guarantee our Association continues to improve in membership, in financial solvency and in professional recognition.

ATF Appraisal Rebuttal

Cont'd from page 17

project killer, environmental impact and mitigation. An analysis of these costs will assist the prospective right-of-way buyer in determining whether to locate on an existing corridor or to create a new one.

The Cost Approach indicates the upper limit of value for corridor transactions. The principle of substitution, as previously defined, is the basis for this approach to valuation and there is case law⁷ to support this approach for corridor valuation.

The three conventional approaches to value have limitations when dealing with corridor valuation. To accomplish the appraisal needs required for these special purpose properties, a hybrid variation of the Cost Approach and the Sales Comparison Approach has been

adopted by the Right-of Way industry. This variation, or "ATF" valuation, is based on the premise that the corridor land should be worth at least as much as the land through which it passes. Using this approach, the corridor is typically divided into segments or districts of similar utility based on the adjacent land use. Then the value of a typical parcel of adjacent land within the district is applied to that portion of the corridor to arrive at its market value. Finally, the values of each of the segments or districts of the corridor are added together to estimate the ATF value of the total corridor.

In 1979-1980, David E. Lane, MAI, of Sacramento, California, conducted a nationwide survey of users and owners of "transportation/communication corridors" in order to ascertain the attitudes, policies and methods of valuation used by companies and people in the industry that deal daily with this special-purpose type of real estate. From among his many findings, we quote:

"The reasonableness of the Across the Fence method of valuation is manifested by its common use. Most purchasers and sellers of existing rights-of-way use ATF or some modified version of ATF methodology in arriving at negotiated settlements for rights-of way purchases. In cases where parties have refused this methodology and have arrived at values for negotiations through the use of the cost approach (replacement) or non-corridor valuation, it has resulted in polarization of views and ultimately litigation.

"The appraiser's contacts with public agencies, railroads, utilities and other corridor owners definitely indicated that the across the fence method of valuation was the most commonly acceptable and widely used method in reaching price agreement. There have been many agreements between public agencies and/or utilities based on this theory that have operated successfully for many years."

Transverse v. Longitudinal Takings

Finally, Mr. Amspoker listed several instances where a nominal award was made where a property was already burdened with a road easement; where there was no proof that property could

be used profitably; and finally, where the city took a street crossing over a railway that did not affect railway operations. There is no doubt that ATF methodology should not be used in these circumstances—the highest and best use of the property was non-corridor and using ATF was not appropriate. Again we emphasize that the misuse of the methodology by an appraiser or user does not invalidate the methodology. However, to take these limited and non-corridor instances and try to make them apply to longitudinal easements or takings on a transportation corridor stretches credulity to the breaking point.

In the 1978 case of *People v. Southern Pacific Transportation Co.*⁸, the appellate Court dealt with the issue of crossings versus longitudinal takings in these words “Plaintiff (State of California) also asserts that the defendant (Southern Pacific) is only entitled to nominal damages as a result of that diminished value. The case authority relied upon by the plaintiff in support of that assertion is inapposite; in each instance they involve transverse crossings which did not interfere with the railroad’s operation and are not applicable or similar to a longitudinal taking such as is presented in this instance. A similar claim was rejected in *Los Angeles v. Allen* (1917) 32 Cal. App. 553 at page 561, where the

court stated, “There is an important difference between the extension of a street crossing over a railroad track and a taking for the purpose of constructing a street longitudinally covering a right of way. The right to take longitudinally is very different from the mere right to cross, for in the one case the rights of the railway company are materially impaired, while in the other the taking is such that both uses can stand together.” In fact, it was SP policy for many years not to charge any fee for transverse crossings.

Conclusion

The ATF methodology for corridor evaluation has a long history, stretching back more than 80 years. Established by the I.C.C. as a means of making railroads account for their land holdings, ATF has been promulgated by some of this country’s most respected appraisers, it has been upheld in court, and is the predominant method used by both buyers and sellers in completing corridor transactions.

Like any other property, the highest and best use determines what methodology is used in corridor evaluation. In our experience, the great majority of corridor appraisals are for continued corridor uses and, if the highest and best use is for a corridor, the ATF methodology

provides a reasonable and acceptable solution to the valuation problem. ■

Rexford M. Shaffer, Jr. retired after 27 years as Chief Appraiser for the Southern Pacific Railroad. He is a past president of Chapter 2 and a past International President of the International Right of Way Association. He resides in Chico, California where he is a guest lecturer at California State University, Chico.

Arthur G. Rahn retired as Manager-Appraisals with the Union Pacific Railroad and is now an independent appraiser/consultant headquartered in Fairfield, California. He has a BS in accounting and a MBA in Real Estate. Mr. Rahn serves as a broad member of Chapter 2 and is a previous contributor to the Right of Way magazine.

NOTES

¹ DOT v. Southern Pacific Trans., (Or.App) 749 P.2d 1233

² City of Vallejo v. Southern Pacific Trans., California P.U.C. Application 88-07-021, filed July 18, 1988

³ Public Utility Easements in Railroad Rights of Way, Right of Way Magazine, April 1989, Page 5

⁴ Haley v. L.A. County Flood Control Dist. (1959) 172 Cal. App.2d 285, 290-292.

⁵ People v. Jones, 67 Ca. App. 2d 531 (1945) p537

⁶ City of Stockton v. Ellingwood, 96 Cal. App. 708 (205 p.228)

⁷ People ex rel. Dept. of Transportation V. Southern Pac. Transportation Co. (1978) 84 Cal.App.3d 315, 327.)

⁸ People ex rel. Dept. of Transportation v. Southern Pac. Transportation Co. (1978) 84 Cal App. 3d 315

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