Bundle Of Rights Theory Applied To Valuation Of Easements And Rights-Of-Way

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A long time ago it was an accepted fact that a man's home was his castle. That is to say, he could do whatever he desired with his property. He, and he alone, owned it and could control its use, misuse or non-use. He had the right to occupy it and deny occupation to others. He could build what he liked or destroy what had already been built. He could enter it at will or depart from it at will. He could allow others to occupy it, but only with his concurrence and agreement.

This was not only true of the surface, but also was considered to apply equally to the soil below the surface, right down to the very centre of the earth. Similarly, he completely owned all of the space above his property. In fact if his earthly property boundaries were, for example, in the form of a square, then the extent of his ownership was an almost limitless inverted pyramid, with the apex at the centre of the earth and the base of the pyramid somewhere out in infinite space . . . beyond imagination.

Ownership -- Bundle of Rights

To illustrate this concept of ownership let's consider a bundle of sticks. This bundle of sticks represents the complete package of man's original concept of ownership. Each stick represents one of the rights included in the overall package: The right to enter; the right to use for any purpose; the right to improve in any fashion; the right to deny entrance to others; the right to permit entrance by others; the right to rent or lease for fixed terms; the right to build whatever he wants; the right to demolish a building; the right to grow trees or crops of any kind; the right to cut down trees; the right to sell or part with his ownership; and so on. In addition he has the right not to do any of these things.

The small known world of man expanded, many years ago, as new lands were "discovered." Such discoveries were usually made by individuals or groups of individuals on behalf of a King or a country. Huge areas of land were claimed in the name of the King. The bundle of sticks was taken over by the King. Later, perhaps in return for services rendered, the King granted to selected individuals, a tract of land here, or a tract of land there - sometimes small - sometimes large. And so it was with the continent of North America. The King gave away a bundle.

However, the *entire* bundle of rights was seldom, if ever, granted. Usually there was a holdback. Perhaps the grant of ownership stipulated that such grant would only continue subject to certain services being provided to the King upon demand, or subject to certain periodic payments of goods, or perhaps of rent.

The new owner didn't really have complete unconditional ownership and control of the land forever and ever. His package was something less than complete. One or more of the rights of absolute ownership had been conditionally removed. Let's subtract two sticks from the bundle.

In law however, and in the eyes of the people of the land, he was still the owner . . . i.e. the owner of something less than absolute ownership. His "home" or his "castle" had lost just a little of its stature, and if he failed to meet his commitments, he could lose it.

Civilization Marches On

With the advance of civilization, owners of land started to make demands upon the King, through his governing bodies. They wanted protection from marauders - which meant the provision of soldiers or police. They demanded protection from the ravages of fire - which meant fire fighter or fire brigades. These and many other services cost money - money which, it was deemed, should come from those requiring the services. That was fine, as far as it went. But what if an owner refused to pay his share. The answer was obvious. Take back the "ownership" of the land. And so it came to pass that the owner would only be permitted to continue his ownership of the package, provided that he met these commitments, later to be called TAXES.

In more modern times it is recognized that there are a number of governmental limitations on the rights of ownership, and these are briefly as follows:

The Right of Taxation

As mentioned above, different levels of government - Federal, Provincial (Canada), State (USA), municipal (cities, towns, villages, etc.) - have passed laws which require the owner to make payment of taxes at various times and for various reasons. Failure to make payments when demanded, or within certain time limits,

can result in loss of ownership. Take another stick away from the bundle.

The Right to Police

As populations became more concentrated, it became necessary for the Government to pass laws to control the use of property for the good of others. Health, building and zoning laws were passed. Take another stick from the bundle.

The Right to Expropriate Or Condemn

With the advance of our modern society, it was found that sometimes certain public projects required the use of privately owned property. Initially, it was only necessary to haggle with the owner as to price and the property could be purchased. However, some owners didn't want to part with part or all of their property, and the proposed project was held up or even prevented from going forward, so the government passed laws to allow them to expropriate or condemn the property for public use. In other words, the government (at various levels) could take away the ownership of the property. Of course, they had to pay compensation to the former owner.

The same powers of expropriation (condemnation) were also given to quasi-governmental bodies and in many cases to large privately owned companies such as railroads, electricity companies, gas companies and so on. Take another stick from the bundle.

The Right of Escheat

It sometimes happened that a property owner died without leaving any heirs and without leaving a will. Rather than have all the neighbours scrambling to take over the ownership of the property, the Government decided that, in such a case, the ownership of the property would revert to the Government. This is referred to as escheat. Take yet another stick from the bundle.

Real Property Concept

I am trying to establish the concept that modern day ownership of property embraces a great many rights, but not absolute rights, to the property. The package we know as "ownership" has many limitations thereon, of a hereditary or governmental character. This package is now represented by the bundle of sticks that remains; still a substantial bundle, but much reduced from the original "castle" that was owned by King Arthur, or given to one of his Knights. Even so, the package is still a substantial bundle, and still includes: The right to use (subject to governmental controls); the right to enter (more or less without restriction); the right to lease (subject to perhaps the need to register the lease); the right to improve (subject to governmental controls); the right to deny entrance to most others (but not certain governmental inspectors, etc.); the right to demolish a building (but not if it has been declared a historic site, etc.); the right to grow trees and crops (but not necessarily the right to cut down trees); the right to sell or part with ownership (subject perhaps to capital gains tax); and so on. In addition the right not to do any of these things except you could for example be forced to demolish a dangerous structure, or to remove a structure which constituted a health hazard.

Market Value

And so we come to the basis of almost all valuation, including most easement and right-of-way valuations, namely market value. For the purpose of this talk I do not propose to delve too deeply into the many facets of market value, or the many definitions of market value. There is however one definition to which I would like to refer and leave with you for your consideration:

"The highest price estimated in terms of money which a property will bring if exposed for sale in the open market allowing a reasonable time to find a purchaser who buys with knowledge of all the uses to which it is adapted and for which it is capable of being used."

This definition was, I believe, first set out in a legal decision in a condemnation case in California, and has been extensively used in the United States and also in Canada. It is a good definition, in that it qualifies to a considerable degree the situation and circumstances, or terms of reference, under which the estimate of value is being made.

Right-Of-Way

For what purposes would someone require a right-of-way? The following, though not a complete list, embraces most of the uses with which we as members of the American Right of Way Association are familiar: Roadways; electricity transmission lines; gas pipelines; water mains; sewers; rights of access to another property; footpaths; and others. As I said, the list is not all embracing and there may be omissions, but this is not important for the purpose of this talk.

Fee Versus Easement

Some of the above uses could be for public or quasi-public purposes, but some could be for private purposes, acquired by negotiation or acquired by expropriation or by negotiation under the "cloud of expropriation."

Some of the above rights-of-way could entail the acquisition of the fee in the land, i.e. the whole residual bundle of rights in the possession of the former owner. Some, however, may be more in the nature of easements, to take only specified uses of the land, but still leave certain rights belonging to the former owner. In other words, the bundle is split -- part remains with the former owner, and part (of the bundle, that is) is conveyed to the person or party, government body or utility company, or whatever, that desires to make those specified uses of the land.

At this point this question arises. "Just how many sticks does the acquiring party require? Does he (the acquirer or purchaser) require only a few sticks, or does he require a lot of sticks?" Naturally the more he requires, the fewer will remain to the owner of the fee. Also, I submit, the more he takes, the more he will have to pay as the price of acquisition. If he takes the whole bundle (and it is an entire taking, not a partial taking) then he will presumably have to pay, as a minimum, the market value of the property at the date of taking. If the property was being used for business

purposes, he may have to pay more than market value, and I will touch on this later. Sometimes the taking of only a small number of rights can leave the owner with very little utility in the balance, and he may be required to take the entire interest.

The main point that I am making is that the former owner had in his possession a bundle of rights (represented by the bundle of sticks), and he is being asked or forced to part with some or all of those rights. He must be compensated commensurate with the number of rights taken from him. If he had already parted with some of his rights (e.g. by way of lease or by a former grant of an easement) then the measurement, or the measurement base, i.e. the bundle he starts with, is that much smaller to begin with. This must receive consideration. Whatever the size of the bundle he starts with, this bundle presumably has a measurable market value, and that generally is the starting point in the calculation or estimate of the value of the number of rights that are being taken away from an owner.

At this point I would lilke to make it quite clear that, insofar as I am concerned, market value is never a positive figure, it is never "determined," it is always "estimated." Its accuracy or reliability is only as good as the individual who makes the estimate, and only as good as the reliability of the facts and data used by that individual, and only as good as the degree of professional skill applied to the interpretation of those facts and data.

Already we can see that the valuation of a right-of-way is not a simple matter, but is filled with these complications: Those requiring consideration of the starting point (market value of the owner's bundle of rights); those relating to the number of rights to be taken from the owner, and relating to the number of rights to remain with the owner; and those regarding the nature of the intended use to be made of the right-of-way. I intend to come back to this latter problem later.

Urban, Rural, Rurban Property

There can be, and usually is, a considerable difference in the valuation of urban property and the valuation of rural property, and I am not speaking only about the difference in dollar amounts. The whole procedure and the whole basis is generally different. Most of my appraisal life has been spent in dealing with urban property, and I try to avoid getting involved with rural valuation problems.

In a similar way, it naturally follows that the valuation of a right-of-way is also quite different when dealing with urban versus rural problems.

There is also a third category of property which I will refer to as rurban property, which falls broadly speaking, in between. This class consists of those areas of lands on the fringe of developed urban areas that are approaching the time when such lands will become "ripe" for development. The Borough in which I work (Borough of Scarborough) forms part of the Toronto Metropolitan Area. There are six Boroughs in all, and we have a two tier form of Municipal Government. Scarborough has a population of more than 400,000 persons and is increasing by about 20,000 to 25,000 persons per year, plus associated amenities such as stores, schools, churches, etc. We have the only substantial area of vacant land remaining in Metro, much of it still farmland.

Taking Of The Whole Versus Partial Taking

To complicate the problems of valuations of rights-of-way still further there is the difference of the procedures of valuing an entire property versus the problems of a partial taking. In point of fact, however, it should be recognized that the taking of an easement, or a right-of-way in the nature of an easement, in itself, constitutes a partial taking. Also, when only part of a property is required for an easement, we may have a double effect to consider - i.e. the loss in value to the area within the easement, and the loss in value, if any, to the remaining portion of the owner's lands outside the easement area. In such cases the appraiser may find himself involved in the measurement of what is referred to as "injurious affection," i.e. the loss in value to the land outside the easement or right-of-way area, caused by the construction of the particular undertaking for which the easement or right-of-way was acquired. This is a somewhat specialized subject, and I will not attempt to discuss it in any depth here, but knowledge of the subject is essential for the valuation of this type of problem.

Easements and rights-of-way are rarely of a private nature, but are normally acquired by an Authority with powers of expropriation or condemnation. Even though the easement or right-of-way is acquired by negotiation, without the need to resort to expropriation, it must never be forgotten that these negotiations are conducted under the "cloud of expropriation," and in all fairness, the owner should be given all of the benefits that he would have had under the law, if he was being expropriated. An appraiser/negotiator should never try to take advantage of an owner because of his lack of knowledge of the Laws of Expropriation.

This means that if the individual conducting the negotiations is to properly perform his task, he must have some knowledge of expropriation or condemnation law, and furthermore, must have some knowledge of how the Courts have interpreted that law. This is, perhaps, not too important in the case of the taking or acquisition of an entire property, i.e. the entire bundle of rights, but it is most important in the case of a partial taking, i.e. the taking or acquisition of part of an owner's property. As I have explained, a right-of-way in the nature of an easement constitutes the taking of only part of the owner's property rights, and this matter of having knowledge of the law of expropriation is therefore most important.

Expropriation Law In Ontario

We in Ontario are somewhat fortunate in that we have basically only two acts with which to concern ourselves in acquiring land under

expropriation, or under the cloud of expropriation - namely the Provincial Expropriation Act, that applies to all levels of Government or Expropriating Authorities below the Federal level, and the Federal Expropriation Act applicable at the Federal level. The provincial act, unfortunately for us, is slanted very strongly in favour of the property owner. So much so, that a property owner has very little to lose by fighting the Expropriating Authority all the way. He is guaranteed payment of his legal and appraisal fees, even if he loses a case before the Courts. It's tough, but that's the way it is.

Briefly the Provincial Act (and the Federal Act too) require(s) compensation to be based on market value. For this purpose, market value is defined as "the amount that the land might be expected to realize if sold in the open market by a willing seller to a willing buyer."

In addition to Market Value, an expropriated owner may be entitled to: damages attributable to disturbance; damages for injurious affection; and damages attributable to any special difficulties of relocation.

It is also spelled out that injurious affection means a reduction in value to remaining land arising out of the acquisition or construction of the works or the use of the land acquired, and also personal or business damages resulting from the construction of the works, or the use of the land expropriated. And to conclude this brief summary of Ontario Expropriation Law, an Expropriation Authority also has to pay damages for injurious affection if it occurs, even though no land is taken from an owner. In this regard, however, the onus is on the owner to establish and prove injurious affection.

The Ontario Act also spells out that when part of the land of an owner is taken, and when such part would not in itself be normally a marketable parcel of land, then the compensation shall be measured by the difference between the value of the owner's property "before" the taking, and the value of the owner's interest "after" the taking. It is not difficult to see that this provision is likely to apply to the appraisal of nearly all rights-of-way, easements or rights-of-way in the nature of easements. (Keep in mind, of course, that I am speaking of the valuation of land being acquired from a private owner, and not the valuation of a strip of land already used for an easement or right-of-way.

My purpose in outlining the above requirements is that these requirements must also be kept in mind by an appraiser or negotiator during negotiations conducted under the "Cloud of Expropriation."

Easement Document — Terms And Conditions

In the valuation of compensation for the acquisition of an easement, or of a right-of-way in the nature of an easement, it is of the utmost importance that full consideration be given to the actual terms and conditions to be incorporated into the easement document. I find it strange that this often gets overlooked at the negotiation stage, in spite of the fact that restrictions will almost certainly be imposed on the use of the land afterwards. Keep in mind that there will be two land uses to consider.

First, the uses by the authority acquiring the easement. Usually this is fairly obvious and will include not only the use for the construction of the undertaking but also the right to enter on the land for the maintenance of the works, or for the reconstruction of the works. Nevertheless, the rights of the acquiring authority should be studied, since these constitute the "bundle" to be acquired and priced or valued.

Second are the uses or rights remaining to the owner of the fee. In most cases, these will be written into the easement document in a negative manner. In other words, the owner will retain his former rights except for those rights that he will convey, and subject to a number of things that he will be asked to covenant not to do - e.g. not to construct a building on the easement land; not to grow trees thereon; not to change the contours without agreement, and so on. These again are rights which he is giving up.

In some cases, and these are exceptions to the general rule, the owner may demand, and the acquiring authority accept, special conditions that will merit consideration in the valuation. For example, I have come across cases where a land owner (a quasi-governmental body) insisted that there be a provision in the easement document, whereby, should the grantor at some future date require the use of the land, then the grantee is required to relocate the works at its own expense. In such cases, I submit that the so called "permanent" easement is merely a "licence to occupy," and should be valued as such. It certainly cannot be treated as a permanent easement, since the right to use that particular parcel of land could be of a temporary nature.

Conclusion

Unfortunately, many people in Ontario, and I believe in Canada and the U.S. also, seem to have a fixed idea that land for easements and for rights-of-way should always be valued at 50 percent of the market value of the land over which the easement is being acquired. *I submit to you that this is totally wrong. I submit to you that each individual easement and each individual right-of-way must be looked at as the acquisition of one or more of the rights of the owner.* You must consider the value of the bundle of rights owned "before" the taking of the easement; you must consider the nature and value of the rights removed from the bundle; and you must consider the value of the bundle of rights remaining "after" the taking. The difference between the "before" and "after" valuations should in most cases, equate to the value of the easement or right-of-way.

I submit to you that the damages caused by the taking could vary anywhere from a low of 10 percent to a high of 90 percent. *Each problem must be studied as an individual problem, and each problem must be examined in the light of all the facts and circumstances.*