

# Public Utility Easements in Railroad Rights of Way

***When valuing public utility easements within a railroad right of way, an appraiser can employ several approaches to value. In this article, the series of mutually exclusive decisions prerequisite to selecting the most appropriate valuation technique is explored. A decision model is used to guide the reader as the author examines the status of a utility with regard to the right of eminent domain and discusses defining the larger parcel, selecting the corridor's highest and best use, and identifying the related valuation techniques.***

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In this article, the issues relevant to valuation of public utility easements in railroad corridors are discussed. On first examination, the problem and solution consist of valuing a partial interest in real estate. The adversarial interests of the parties, however, differ significantly regarding proper application of partial taking or condemnation valuation concepts. Areas of difference include right of eminent domain, value to buyer or seller, definition of the larger parcel, fee simple ownership, highest and best use, and "across-the-fence" (ATF) value.

Further, some right of way valuation models include application of questionable assemblage or corridor enhancement fac-

tors to determine corridor value. Although disputed, a useage or occupancy factor is often incorporated in lieu of before-and-after valuation to determine the value of the utility's right of way.

Relying on valuation theory, a schematic decision model was constructed to assist the appraiser in resolving the valuation problem (Fig. 1). The model is applicable in all corridor valuation situations regardless of the entity negotiating to acquire or maintain an easement in a preexisting right of way. Each decision point is discussed in the sections that follow.

## Public Utility or Private User

Valuation of easements in railway corridors first requires that the appraiser determine the lessee or buyer's right of eminent domain. The status of the user has a significant effect on the valuation approach and values determined, regardless of the appraisal assignment.

Generally, public utilities have the right of eminent domain and power of condemnation; private corridor users do not. This distinction is important in deciding

whether to adopt a valuation approach that measures value in terms of the buyer (taker) or seller (owner).

## Value to Buyer (Taker)

Private transportation-communication corridor users have few options but to obtain necessary easements by acquiring new rights of way, parcel by parcel (1). An alternative is to negotiate for an easement with owners of an existing corridor such as a railroad. The maximal value of an existing corridor easement to a private corridor user, though, is the cost of acquiring an easement for a new alternate route plus administrative, legal, and time costs of acquisition.

When acquisition costs of a new corridor are divided by the market value of an existing corridor, an assemblage factor or multiplier may be calculated. ATF sales, or sales of adjoining land, are used to establish the market value of the existing corridor.

John P. Dolman and Charles F. Seymour have reported values for such right of way assemblages as being "two to three times" the prevailing price of farm land acreage. . . . A higher multiplier (value) was reflected in urban areas. . . ." (2) From their own experience, multiples ranging from two to six were reported (3).

Dolman and Seymour maintain that it is important to

distinguish the "assemblage" costs incurred in assembling a new "custom corridor" from the usually lower enhancement factor realized in the sale of an already existing corridor.

In the market approach to enhancement factors, actual sales of existing corridors are researched and compared to ATF value on the date of the sale (4).

Summarizing corridor assemblage and enhancement factors may be calculated as follows:

### Corridor Assemblage Factor

$$\begin{aligned} & \text{Cost of "New" Corridor} \\ & + \text{Legal \& Admin. Costs + Time} \\ & \hline & \text{ATF Value of Existing Corridor} \end{aligned}$$

### Corridor Enhancement Factor

$$\begin{aligned} & \text{Actual Sale of Existing Corridor} \\ & \hline & \text{ATF Value of Existing Corridor} \end{aligned}$$

Each factor is presumed to represent a premium over the ATF value of an existing corridor. Also, assemblage factors are presumed to be greater than enhancement factors.

The assumption when valuing an existent right of way is that the corridor has

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some value in excess of the value of adjacent land. Justification for the assemblage or enhancement factor is found in the concept of plottage. Appraisers generally agree that small parcels combined into a larger one with greater utility result in a value greater than the sum of the parts.

**The status of the user of the railroad corridor has a significant effect on the valuation approach and values determined, regardless of the appraisal assignment.**

Value to the buyer based on the cost of alternative corridors or income to be earned is relevant to private entities. As-

semblage or enhancement factors may be used to establish the maximal negotiated price or rent to be paid by a willing and knowledgeable private user.

Regardless of the benefits to be derived or costs to be avoided, a public utility with the right of eminent domain is responsible only for the diminution in value or loss to the principal corridor occupant. The basis of the valuation measurement when a public utility with the right of eminent domain acquires an easement within an existing right of way is value to seller.

### Value to Seller (Owner)

The principle that public utilities with the right of eminent domain have the power of condemnation is well established and accepted. Negotiations for purchase or rental of existent rights of way to a public utility are limited by the utility's status as a potential condemnor.

Acquisition attempts for public and quasi-public easements usually begin with negotiation efforts, but all parties are aware that the agency (utility) can and will resort to

authorized eminent domain proceedings if negotiations are not successful (5).

In addition to assembling the new corridor, parcel by parcel, or negotiating to use an existing corridor, public utilities may also condemn an existing corridor to acquire the necessary right of way. Because condemnation, real or probable, affects the valuation of an existent corridor, it is reasonable to expect standards of value in line with condemnation case law.

The most extensive valuation of railway corridors involved a Special Court's decision in the U.S. government's acquisition of 16,000 miles of rights of way to form Conrail (6). A summary of the Special Court's opinions was presented by William R. Perlik and David R. Johnson (7).

The court affirmed that "value to the owner not value to the taker . . . should determine the basic measure of just compensation" (8). Thereby,

the entire case proceeded on the basis that the condemnee must show what value he would have been able to realize from his property if it had not been taken for public

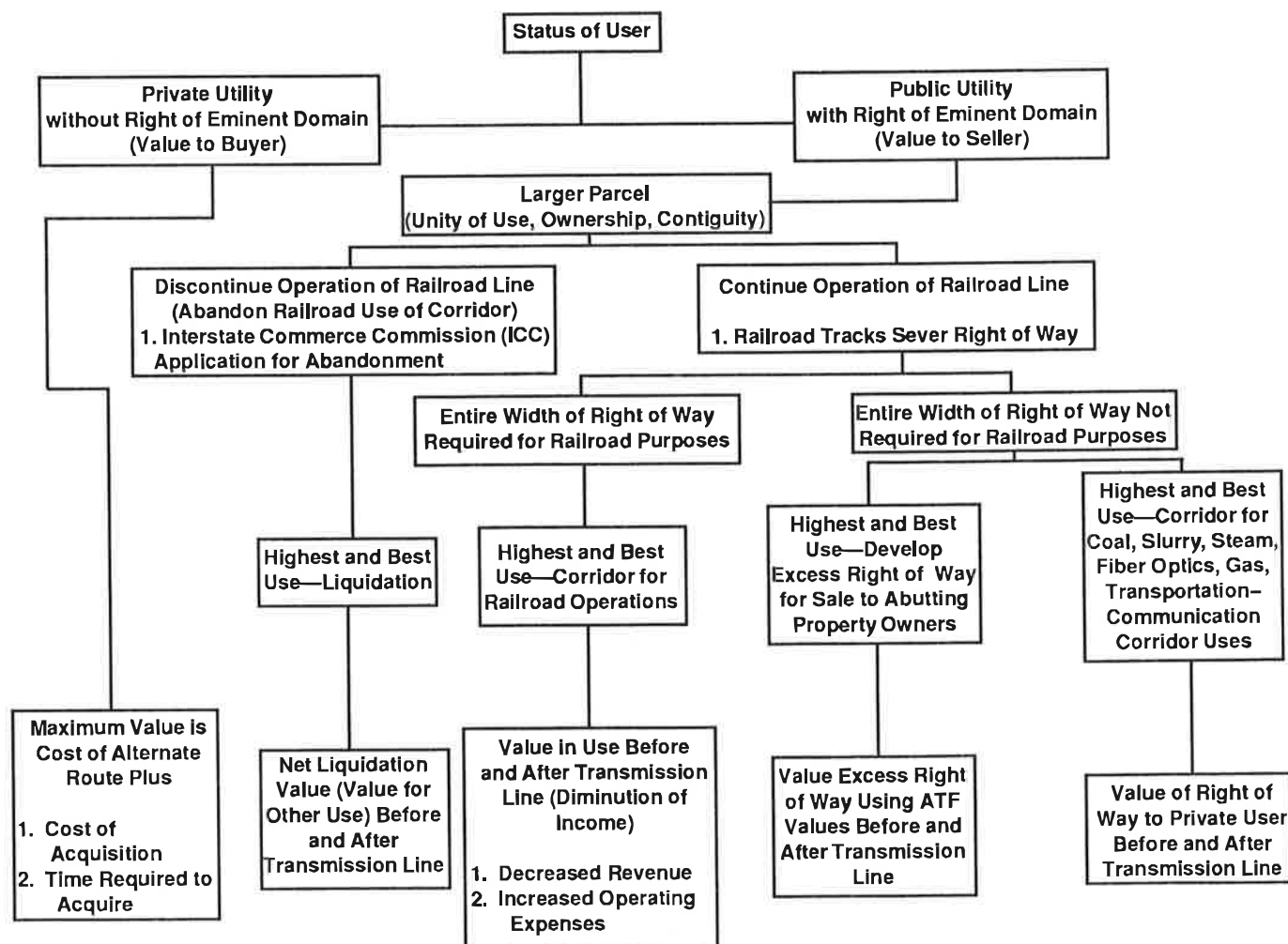


Figure 1. Decision-valuation model for valuing public utility easements.

use... compensation may not be established with reference to any "values" not capable of being sustained in the marketplace (9).

Further, the Special Court rejected the use of assemblage value, enhancement factors, and related multipliers.

The mere fact that right-of-way has been assembled is not significant *unless* there is nonspeculative likelihood of sales in the private marketplace for amounts higher than those that could be realized by disassembling the right of way and selling it as separate parcels (10).

Numerous opinions rendered by courts of jurisdiction have reiterated that property rights acquired in eminent domain proceedings be valued from the perspective of the value to the seller (owner). In *Otter Tail Power*, the legal principle is clearly set forth:

It must be borne in mind that the material consideration is not the benefit to be derived by the petitioner, but the damages sustained by the landowner. "It is the damage caused by imposing the easement on the land which the owner is entitled to receive." *Robbins v. St. Paul, Stillwater & T.F.R. Co.*, 22 Minn. 286. It makes little or no difference what benefit the petitioner may receive (citations omitted) and it is of little consequence whether or not the description furnishes data for an estimate of the value of such benefits (11).

In *Olson v. United States* the same rule was stated in the following language by the U.S. Supreme Court.

Considerations that may not be reasonably held to affect market value are excluded. Value to the taker of a piece of land combined with other parcels for public use is not the measure of or a guide to the compensation to which the owner is entitled (12).

Further, value to alternative users who lack the power to condemn was rejected in *United States v. Miller*,

Since the owner is to receive no more than indemnity for his loss, his award cannot be enhanced by any gain to the taker. Thus, although the market value of the property is to be fixed with due consideration of all its available uses, its special value to the condemner as distinguished from other who may or may not possess the power to condemn must be excluded as an element of market value (13).

The concept of value to the seller is the appropriate basis of valuation when the buyer or lessee possesses the right of eminent domain. The stage of acquisition, whether it be negotiation, arbitration, or

eminent domain proceedings, does not alter this fundamental concept of value.

Whatever the valuation methodology employed, the values must be verifiable in the marketplace. It is also clear that when public utilities acquire or periodically seek to renegotiate rents for easements in pre-existing rights of way, the compensation paid is limited to the damages incurred by their occupancy.

The measurement of these losses requires identification of the larger parcel as well as before and after valuation to gauge the extent of damages.

### Larger Parcel

Before proceeding to value an easement in an existing corridor, the appraiser should obtain the legal description and physical measurement of the larger parcel, the easement area, and the land remaining unencumbered by the easement.

The larger parcel is "the portion of a property that has unity of ownership, contiguity, and unity of use" (14). Two issues relevant to the valuation of easements in railway rights of way are significant when defining the larger parcel. One is the pending or actual abandonment of the railway. The second is the condition of title within the larger parcel.

### Track Abandonment

Continued use of a railroad track for the movement of freight or passengers creates self-inflicted severance on the railroad's right of way. For valuation purposes, the right of way is divided by the presence and continued use of the tracks. The two sides of the right of way cannot be joined or, therefore, viewed as constituting the larger parcel. The larger parcel is that part of the right of way on the same side of the railroad tracks as the easement.

Severance by the railroad tracks results in lack of contiguity and prohibits unity of use. This obstacle to viewing the entire right of way as the larger parcel is overcome if the track has been abandoned or an Interstate Commerce Commission (ICC) application for abandonment has been filed. For the abandonment application to be approved:

- (1) The ICC must find that the public convenience and necessity (PC&N) permit abandonment and
- (2) no financially responsible party provides financial assistance, subsidy or purchase... (15).

Abandonment of the railway permits use

of a valuation procedure called "net liquidation value," which will be discussed later.

Appraisers should note that pending applications for abandonment are unlikely to

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be approved if the line is earning a profit. In addition, claims of planned abandonment are insufficient to override the fact that an operational rail line severs its own right of way and restricts the larger parcel to one side of the railroad tracks.

### Title

To protect themselves and inform readers of their report, appraisers usually insert the following statement in the transmittal letter.

No responsibility is assumed for the legal description or for matters including legal or title considerations. Title to the property is assumed to be good and marketable unless otherwise stated (16).

Although the assumption and disclaimer are valid, appraisers of railroad rights of way should be aware that the railroad's title to right of way is generally anything but clear. Not only may marketability be questioned, but also the "unity of ownership" required to define the larger parcel.

Title problems are often the rule. They are a result of the means by which railroads assembled their right of way, including failure to record necessary documents.

Use of the right of way in many instances has been acquired by deed, easement, and condemnation, with and without reversionary clauses to the grantor, heirs, and assignees (17). Parts of the right of way may also have been acquired by grant of Congress, adverse possession, and prescription.

The status of title should be determined by legal counsel: the railroad may not have the right to convey title for other use; continuity of ownership is at question; and, minimally, there will be a cost to cure any defects of title discovered.

The cost to cure is a necessary expense affecting value, particularly when the valuation method and defined area of the larger parcel require unity of ownership. Consideration should also be given to an ICC ruling that held that the railroad should not receive any compensation for real property for which it does not hold marketable title (18).

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### Easement Area

An easement may be described as square feet of occupancy within the railroad right of way. The easement may also be surveyed and drawn on maps of the corridor. The easement area, however described or drawn, does not preclude all alternative uses. In other words, an easement typically does not require 100% use of the air rights, surface, or subsurface of the land.

For example, an electric transmission line consists of a series of towers, tower pads, and overhead wires. The area occupied by the towers and pads is a taking of all the rights of use. Alternative uses are also precluded for some distance around each tower. Overhead transmission lines, in contrast, allow many uses beneath them such as agricultural pursuits, parking, highways, and construction of residential, commercial, or industrial space (zoning and building codes permitting).

The limitation on construction beneath transmission lines is a result of either electric utility policy or building codes. In Minnesota, building codes permit construction beneath transmission lines but the structures must have a 2-hour fire roof. The added cost of a 2-hour fire roof reduces the value of the affected site by the same amount.

After defining the larger parcel, the appraiser needs to recognize that the value of the easement area includes:

- The value of the land occupied by towers and pads and land precluded from any alternative use for some minimal distance around each tower.

- The increased cost, or loss, of use beneath the transmission line and within the easement area
- Severance damages to that part of the right of way bounded by the railroad tracks (19) and easement area

Use adjacent to the towers, beneath the transmission line, or in unencumbered areas will be defined by whatever places the greatest constraint on the alternate use, whether it be building codes, zoning, state health and safety standards, or the electric utility. Loss of use may be measured by applying the before-and-after rule of appraisal.

### Before-and-After Rule

Application of the before-and-after rule requires that the appraiser first value the larger parcel at its highest and best use without the easement in place. The remainder is then valued giving full consideration to the railroad's capacity to continue using the encumbered area subject to the rights of the beneficial estate (20).

The remainder in the case of an electric utility transmission line is the entire larger parcel less the area occupied by towers and pads. The area occupied by the tower and pads precludes all alternative use to the subservient estate and is therefore essentially a fee taking.

**Application of the before-and-after rule requires that the appraiser first value the larger parcel at its highest and best use without the easement in place.**

The difference between the before and after values represents the monetary loss to the railroad. It also represents, monetarily, the allocation of the bundle of rights between the electric utility easement and the remainder of the railroad right of way. The monetary loss may also be expressed as a percentage of the before value. When the value of the electric utility easement (loss to the railroad) is expressed as a percentage of the before value of the larger parcel, the label "usage factor" is often applied.

In efforts to reduce the time and cost of appraisal, the usage factor has been, at times, subjectively estimated at 15% to 80% of fee simple value. General assumptions regarding easement value (usage factors) should be avoided. The usage factor must be measured using before and after valuations. "The appraiser should be careful . . . to avoid estimating easement values as a percentage of fee simple value. . ." (21). Easement values may range from nominal to 100% of the fee value and may only be determined by direct before and after valuations.

The approach to value may include measures of value in use, net liquidation value, ATF values, and value to private right of way views. Which value approach to employ is a function of the appraiser's highest and best use analysis.

### Highest and Best Use

The *Dictionary of Real Estate Appraisal* provides three definitions of highest and best use (22). Two definitions state that the "use" should be reasonable and probable and result in or support the highest present value.

Consequently, determination of the highest and best use of a railroad right of way excludes any use that is speculative or lacking verification in the marketplace. Further, the basis for measuring the effect of a utility easement on a railway corridor must have a higher present value than alternative uses. There are four alternative uses from which the appraiser may select highest and best use for a railroad corridor. They include liquidation; continued operation of the railroad and exclusive use of the corridor for rail purposes; sale of excess right of way; and use of excess land as a transportation-communication corridor.

Each use is mutually exclusive; that is, whatever the highest and best use, it has only one related valuation approach and precludes others of lesser value.

### Net Liquidation Value (NLV)

When the appraiser has determined that railroad operations have been abandoned, liquidation of the corridor is the only viable alternative. Liquidation may be accomplished by selling the corridor intact for nonrail use or, alternatively, disassembling and selling for ATF values.

Nonrail corridor user's demand for intact corridors is minimal, and sales of intact corridors are practically nonexistent. The

lack of comparable sales of intact corridors precludes valuation by means of market comparisons.

**The loss of value to the owner resulting from a public utility's power of condemnation can only be measured using a before-and-after approach to value.**

When valuing abandoned corridors, an NLV approach is most often employed:

The net liquidation value, for the highest and best use for non-rail purposes . . . shall be determined by computing the current appraised market value of such properties for other than rail transportation purposes, less all cost of dismantling and disposition of improvements necessary to make the remaining properties available for their highest and best use and complying with

applicable zoning, land use and environmental regulations (23).

In summary, the right of way is divided into segments based on adjoining land use. Appraisal values are based on ATF prices consistent with zoning, building, and environmental codes. Each segment is adjusted for size, shape, access, topography, and so forth.

The sum of the values for each segment of the corridor is also adjusted to account for selling and administrative costs. The value of the corridor is further reduced for the cost of restoring the corridor to its highest and best use (removing railroad tracks, ties, ballast, and bridges), plus any salvage value.

The final adjusted value is then discounted to net present value (NPV) to reflect the time to liquidate each segment of the corridor.

The two leading cases which have established the legal principles and appraisal procedures to be used in establishing NLV for non-rail use are Lake Geneva Line (3) and the CNJ Opinion (4)" (24).

Inasmuch as acquisition or renegotiation of a utility easement in a railway corridor does not preclude alternative uses, and a

public utility has the power of condemnation, NLV is measured before and after the transmission line. The value of the easement is the difference between the before and after values. The public utility is responsible for the diminution in value as measured by the difference in the before and after appraisals.

### **Value in Use**

Presuming that the highest and best use for the corridor is for continued rail operations and the entire width of the right of way is necessary for railroad purposes, the appraiser must then base the valuation on value in use; that is, continued operation of the railway.

Diminution of value resulting from a public utility's occupancy of the railroad right of way can occur only through the railroad's loss of revenue or increases in operating expenses. The loss of value to the railroad, or the value of the easement, may be measured by documenting the loss of revenue or increased costs of operation. The change in profitability may then be capitalized to estimate the easement value. In effect, documentation of revenues lost or increased operating costs is a measurement of the difference in the railroad's profitability before and after electric transmission lines, towers, and pads.

### **Value of Excess Right of Way**

When the railroad continues to operate and the entire corridor is not required for railroad purposes, the highest and best use may be to sell excess right of way to abutting property owners or developers. This value approach is similar to determining NLV.

The differences are that the railroad is continuing operations, the track severs the corridor, and the excess land is approximately one-half the size of the entire corridor width. Excess land lies on the same side of the tracks as the easement and excludes the statutorily required distance from the centerline of the tracks (25).

In this value approach the excess corridor is segmented. ATF prices are employed, and the value of the easement is set using before and after measurements. The public utility is responsible for the diminution in value of excess corridor land occasioned by the presence of the electric transmission line, towers, and pads. Additional damages may be supported if revenue loss or increased operating cost can also be documented.

## Value Transportation-Communication Corridor


When the railroad continues operation, the highest and best use of excess land may be as a transportation-communication corridor. The measures of value must be found in actual sales or rental of existing corridors to other users.

The diminution of value caused by the public utility's easement will be reflected in reduced rental rates or purchase prices by other users. The absence of verifiable market transactions often precludes this approach to value.

## Conclusion

In this article, a series of mutually exclusive decisions designed to lead the appraiser to an appropriate valuation model for a public utility easement in a railroad right of way was presented. Consideration must be given to the status of the utility with regard to the right of eminent domain. Evaluation of the larger parcel and highest and best use further limit selection of a valuation model. The issues of enhancement factors and usage factors have been found to lie outside the scope of public utility easement valuation.

Appraisers know that it is appropriate to value raw land, homes, office buildings, and shopping centers using comparable sales. It is also appropriate to use purchase prices and rental rates for easements in railroad rights of way to estimate an easement's value to a private enterprise. Although comparable sales are measures of value to a buyer or lessee in the open marketplace, they do not measure the value of the easement acquired by a public utility.

A public utility with the right of eminent domain serves the public good and therefore is given special consideration when acquiring land or easements for public purposes. Regardless of the highest and best use or valuation approach selected, a public utility with the power of condemnation is clearly only responsible for the diminution of value to the owner resulting from the easement. This loss of value can only be measured using a before-and-after approach to value. 

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## End Notes

1. John P. Dolman and Charles F. Seymour. Valuation of Transportation/Communica-

- tion Corridors. *The Appraisal Journal* (October 1978): 509-22.
2. Ibid., 513.
3. Ibid., 520.
4. Ibid.
5. Harold D. Albritton, Controversies in Real Property Valuation: A Commentary. Chicago: American Inst. of Real Estate Appraisers, 1982, pp. 123-24.
6. *In the Matter of the Valuation Proceedings Under Sections 303(c) and 306 of the Regional Rail Reorganization Act of 1973*, 439 F. Supp. 1351 (Sp. Ct. 1977) ("Cue Opinion"); 445 F. Supp. 994 (Sp. Ct. 1977) ("CMV Opinion"); Sp. Ct. Rptr. N38196 (Nov. 24, 1981) ("Rail Use Opinion").
7. William R. Perlik and David R. Johnson. Valuing Rights of Way: Lessons from "The Rail Case." *Right of Way* (February 1983): 8-13.
8. CMV Opinion at 1011-16.
9. Perlik and Johnson, 8.
10. Rail Use Opinion at 220: Perlik and Johnson, 9.
11. *Otter Tail Power*, 128 Minn. 415, 151 N.W. 198 (1915) at 199.
12. *Olson v United States*, 292 U.S. 246, 78 L. Ed. 1236, 1245 (1981).
13. *United States v Miller*, 317 U.S. 369, 375, 63 S. Ct. 276, 280, 87 L. Ed. 336, 343 (1943).
14. American Inst. of Real Estate Appraisers, *Dictionary of Real Estate Appraisal*. Chicago: American Inst. of Real Estate Appraisal, 1984, p. 179.
15. James D. Jennings, Railroad Right of Way Appraisal. *Right of Way* (October 1984): 4.
16. American Inst. of Real Estate Appraisers, *The Appraisal of Real Estate*. Chicago: American Inst. of Real Estate Appraisers, 1983, p. 519.
17. Herb Atkinson, Abandoned Railroad Rights of Way-Title Problems. *Right of Way* (December 1986): 8.
18. AB-1 (Sub-No. 70F), Chicago and Northwestern Transportation Co.—Abandonment Between Ringwood, Ill., and Geneva, Wis. (Lake Geneva Line), 363 I.C.C. 956 (1981), p. 5.
19. Maximum right of way required for rail purposes is often established by state law; i.e., Minn. Stat., Sec. 219.46, Subd. I: "... side clearance of not less than eight feet six inches from the center line of the track. ..." For valuation purposes, right of way beyond that boundary is available for other use and is referred to as excess right-of-way (see Fig. 1).
20. Albritton, 124.
21. Ibid., 127.
22. *Dictionary of Real Estate Appraisal*, p. 152.
23. Code of Federal Regulations, Section 1121.43(C) of CFR 1121, Title 49.
24. Jennings, 5, 7; (3) Chicago and Northwestern Transportation Co.—Abandonment Between Ringwood, Ill., and Geneva, Wis. (Lake Geneva Line): *Chicago and Northwestern Transportation Co. U.S.*, 678 F.2d. 665 (1982), (4) Central Railroad of New Jersey Opinion (CNJ Opinion), 571 F. Suppl. 1269, 1278-1302 (Sp. Ct. 1983).
25. See n. 19. Also, excess land is often synonymous with larger parcel.

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