THE EMINENT AND INVERSE ENVIRONMENT – The Interplay Between Environmental Issues and Condemnation.

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By: Mary Colchin Johndroe,
Cantey Hanger LLP
Cantey Hanger Plaza
600 West 6th Street, Suite 300
Fort Worth, TX 76102
817-877-2810
mjohndroe@canteyhanger.com

1. Introduction.

I've been asked to discuss environmental issues in condemnations.

Interplay between environmental issues and statutory eminent domain (or condemnation) and inverse condemnation proceedings is VAST.

Not going to attempt to cover it all.

- just a few of the front burner issues.

The Texas Constitution provides that no person's property shall be taken, damaged or applied to public use without adequate compensation being made. TEX. CONST. art. I, § 17.

A statutory condemnation in Texas is brought under Chapter 21 of the Property Code.

In a statutory condemnation, the condemnor compensates the property owner before appropriating property. TEX. PROP. CODE § 21.042.

If the government appropriates property without first paying adequate compensation, the property owner may bring a claim for inverse condemnation to recover resulting damages. *City of Austin v. Teague*, 570 S.W.2d 389 (Tex. 1978).

In both, statutory and inverse condemnation, a pivotal issue is ***compensation due*** to the landowner

- which is typically measured by the difference in fair ***market value*** of the affected property before and after the taking.

Market value is:

> . . . the price which the property would bring when it is offered for sale by one who desires to sell, but is not obliged to sell, and is bought by one who desires to buy, but is under no necessity of buying it, taking into consideration all of the uses to which it is reasonably adaptable and for which it either is or in all reasonable probability will become available within the reasonable future.

Enbridge Pipelines (East Texas) L.P. v. Avinger Timber, LLC, 386 S.W.3d 256, 265-66 and n. 1 (Tex. 2012), *citing City of Harlingen v. Estate of Sharboneau*, 48 S.W.3d 177, 182 (Tex. 2001).

In Texas condemnation law, market value properly reflects ***all factors that buyers and sellers would consider*** in arriving at a sales price. *Sharboneau*, 48 S.W.3d at 185, *citing City of Austin v. Cannizzo*, 267 S.W.2d 808, 815 (Tex. 1954) (emphasis added).

Professional appraisers are hired to conduct appraisals resulting in opinions of land value and compensation due to the landowner.

Appraisers almost always include a provision in an addendum at the back of their appraisal report stating something like:

> **Assumptions and Limiting Conditions**
>
> In conducting this appraisal, we have assumed, except as otherwise noted in our report, as follows:
>
> . . .
>
> No environmental impact studies were either requested or made in conjunction with this appraisal, and we reserve the right to revise and rescind any of the value opinions based upon any subsequent environmental impact studies. If any environmental impact statement is required by law, the appraisal assumes that such statement will be favorable and will be approved by the appropriate regulatory bodies.
>
> . . .
>
> We accept no responsibility for considerations requiring expertise in other fields. Such considerations include, but are not limited to, legal descriptions and other legal matters, geologic considerations, such as soils and seismic stability, and civil, mechanical, electrical, structural and other engineering and environmental matters.
>
> . . .
>
> No studies have been provided to us indicating the presence or absence of hazardous materials on the site or in the improvements, and our valuation is predicated upon the property being free and clear of any environmental hazards.
>
> . . .

This, ladies and gentlemen, may signal the loss of a great opportunity

- for the condemnor, on the ***before*** taking value, and

- for the condemnee, on the ***after*** taking value.

Environmental contamination, costs of remediation, and perception in the marketplace most assuredly can influence the value of a property.

2. Evidence of Contamination and Remediation Is Relevant to Market Value in Condemnation?

A. Texas Courts Undecided.

Texas courts have not yet decided if evidence of environmental contamination, potential liability for contamination, and remediation costs is admissible as relevant to market value of property taken by condemnation. *Caffe Ribs, Inc. v. State*, 328 S.W.3d 919, 930 and n. 5 (Tex. App.—Houston [14th Dist.] 2010, no pet.)

In *Caffe Ribs*, the State condemned property which had been used to manufacture and store oilfield equipment resulting in environmental contamination. *Id.* at 921.

The prior title holder, Weatherford, had entered an Environmental Remediation Agreement accepting responsibility for performance of and payment for remediation. *Id.* at 922.

The trial court admitted evidence as to contamination, but not evidence of the Environmental Remediation Agreement. *Id.* at 923.

The State challenged the landowner's appraiser's comparable sales as not comparable because they involved parcels that were not contaminated. *Id.*

The State put on evidence of a plume of underground solvents and chemicals which were carcinogens and that some of these cancer-causing chemicals were migrating offsite. *Id.*

The State's environmental engineer opined that the property's soil and groundwater were contaminated and that it would take eight (8) years to remediate. *Id.* at 925.

The State's appraiser discounted the value of the property before the taking using a discounted cash flow analysis, considering cleanup of the property would take eight (8) years. *Id.*

And the jury's verdict was unquestionably affected, with the judgment resulting in the landowner being ordered to pay the State back $2.87 million.

However, the admission of contamination evidence was not challenged on appeal, so the Court did not need to and did not decide whether it was admissible. *Id.* at 930.

The Court simply held that once evidence is admitted relating to contamination and concerns about potential liability, then a third party agreement to pay costs associated with contamination is also relevant and admissible in determining what a hypothetical buyer would pay a hypothetical seller for the property. *Id.*

B. Majority Rule.

Although Texas case law has not specifically addressed these issues in the context of eminent domain, courts in at least thirteen (13) other states have determined the admissibility of evidence of environmental contamination and remediation of property taken in condemnation. *Caffe Ribs*, 328 S.W.3d at 930 and n. 5, *citing Moorhead Econ. Dev. Auth. v. Anda*, 789 N.W.2d 860, 877-884 (Minn. 2010) (collecting cases).

In *260 North 12th Street, LLC v. State of Wisconsin Dept. of Trans.*, 792 N.W.2d 572, 579 (Wis. Ct. App. 2010), the Court held that ***evidence of environmental contamination and the costs of remediation is relevant to fair market value*** and, therefore, relevant to a determination of just compensation in eminent domain proceedings.

The *260 North 12th* Court noted that its holding was consistent with the majority rule in the United States. *Id., citing* 4 NICHOLS ON EMINENT DOMAIN, sec. 13.10 at 13.96 (3d ed. 2007).

C. *Minority Rule.*

The *Anda* Court, while recognizing the "inclusion approach" of the majority of states, adopted the "exclusion approach." *Anda*, 789 N.W.2d at 877.

Some courts following the exclusion approach ***exclude all evidence of contamination***, while others have more specifically held that evidence of remediation costs is inadmissible, but property taken should be ***valued as remediated***, as opposed to being clean and never contaminated. *Id.* at 878 (citations omitted).

The *Anda* Court adopted an exclusion approach with modifications, holding that evidence of contamination and remediation may be admissible, but that evidence of remediation costs was not admissible, and that property taken in condemnation should be valued as remediated. *Id.*

The Court held that evidence of the reduction in value of the property caused by stigma attributable to environmental contamination was admissible. *Id.* at 883.

D. Application of USPAP.

Texas courts have recognized that the Uniform Standards of Professional Appraisal Practice ("USPAP") require appraisers to consider the effect on a property's value of various factors to which the property is subjected and that Texas law requires appraisers to abide by USPAP in making appraisals. *Avinger*, 386 S.W.3d at 266, *citing* TEX. OCC. CODE §§ 1103.002, .005, .154, .201, and .405.

USPAP accounts for contaminated property valuation with its Advisory Opinion 9: The Appraisal of Real Property That May Be Impacted by Environmental Contamination.

Advisory Opinion 9 cautions appraisers that, to comply with USPAP in the appraisal of a property that may be impacted by environmental contamination, the appraiser should insure that he/she meets the:

- ETHICS RULE
  - *An appraiser must perform assignments with impartiality, objectivity, and independence, and without accommodation of personal interests . . . . An appraiser must not communicate assignment results* with the intent **to mislead or to defraud**.

- COMPETENCY RULE
  - *An appraiser must: (1) be competent to perform the assignment; (2) acquire the necessary competency to perform the assignment; or (3) decline or withdraw from the assignment. . . .*

- Standards Rule 1-1(a): *In developing a real property appraisal, an appraiser must: (a) be aware of, understand, and correctly employ those recognized methods and techniques that are necessary to produce a* ***<u>credible appraisal</u>****;*

- Standards Rule 1-2(e): *In developing a real property appraisal, an appraiser must: (e)* ***<u>identify the characteristics of the property that are relevant to the type and definition of value and intended use of the appraisal</u>****. . . .*

- Standards Rule 1-2(f) and (g): *In developing a real property appraisal, an appraiser must: (f) identify any* ***<u>extraordinary assumptions</u>*** *necessary in the assignment; and (g) identify any* ***<u>hypothetical conditions</u>*** *necessary in the assignment.*

- Standards Rule 1-3(b): *When necessary for* ***<u>credible assignment</u>*** *results in developing a market value opinion, an appraiser must: (b) develop an opinion of the highest and best use of the real estate.*

- Standards Rule 1-4: *In developing a real property appraisal, an appraiser must collect, verify, and* ***<u>analyze all information necessary for credible assignment results</u>****.*

3. **Environmental Stigma Damages in Texas**.

Generally, contamination of property via constituents exceeding state action levels is required to recover damages for contamination. *E-Z Mart Stores, Inc. v. Ronald Holland's A-Plus Transmission & Automotive, Inc.*, 358 S.W.3d 665, 673 (Tex. App.—San Antonio 2011, pet. denied).

In November 2012, the Fourteenth Court of Appeals ***affirmed stigma damages*** awarded for loss in market value resulting from prior contamination which had been remediated. *Houston Unlimited Inc. Metal Processing v. Mel Acres Ranch*, 389 S.W.3d 583 (Tex.App.—Houston [14th Dist.] 2012, pet. granted) (emphasis added).

The Texas Supreme Court heard oral arguments on the issue on December 5, 2013 in the case.

Process waste discharges from a metals finishing facility led to contamination of a stock pond on a neighboring farm property.

After the farm tenant complained its cattle had become ill, TCEQ tested the stock pond, documented that concentrations of hazardous metals in the stock pond exceeded state action levels, and required Houston Unlimited to investigate the contamination of its property and the stock pond and to prepare an environmental risk assessment.

Houston Unlimited took measures to stop further process waste discharges from its facility and undertook the required investigative work.

The investigation demonstrated that metals TCEQ previously detected in the stock pond no longer exceeded state action levels.

The environmental risk assessment, approved by TCEQ, concluded that there was no unacceptable risk to ecological receptors in the stock pond.

Mel Acres Ranch filed a lawsuit in Texas state court to recover loss of market value of its property caused by the contamination.

At trial, the jury held that Houston Unlimited was negligent in discharging pollutants, which proximately caused a loss of $350,000 in market value of the farm property.

In its appeal, Houston Unlimited argued that Mel Acres Ranch could not establish permanent damage to the property, which is a prerequisite to recovering for loss of market value, because the contaminants detected in the stock pond no longer exceeded state action levels.

Mel Acres Ranch argued that it could recover these ***damages for a permanent environmental stigma*** even if the contamination was only temporary.

Although the Houston Court of Appeals agreed that proving permanent damage was a prerequisite for the recovery of loss of market value, it held that the "permanent damages" do not need to be physical damage to the land, such as contamination above state action levels.

Rather ***a stigma resulting from even temporary contamination of a property (which would include contamination that has been remediated) may be a permanent damage for which loss of market value could be recovered***.

The Houston Court of Appeals held that the Mel Acres Ranch offered sufficient evidence to support the stigma-based loss of market value award.

Evidence of stigma included testimony by a real estate appraiser that: (1) TCEQ records of the contamination issue were publicly available; (2) the plaintiff would be required to disclose the contamination issue to avoid potential liability if it sold the property; and (3) there was a market perception of increased "environmental risk" associated with a contaminated property.

4. <u>Fear Damages in Condemnation in Texas.</u>

Texas courts have held that fear in the minds of the buying public is relevant to show diminution in value in condemnation when (1) there is a ***basis*** in reason or experience for the fear, (2) such fear enters into the ***calculations of persons who deal*** in the buying and selling of similar property, and (3) there is a ***depreciation of market value*** because of such fear. *Heddin v. Delhi Gas Pipeline Co.*, 522 S.W.2d 886, 888 (Tex. 1975) (emphasis added).

In *Heddin*, a gas transmission pipeline condemnation case, the Court held to establish a basis, it was incumbent upon the landowner to show either an actual danger or that the fear was reasonable. *Id.*

Proof of specific instances in which similar pipelines had ruptured was relevant to show fear of an actual danger reducing market value. *Id.*

5. <u>Cost to Cure Damages in Condemnation in Texas.</u>

In a partial takings case, the landowner may recover as damages the costs to ***cure any unsafe condition*** on the remainder necessitated by the taking. *Dallas County v. Crestview Corners Car Wash*, 370 S.W.3d 25, 42 (Tex. App.—Dallas 2012, pet. denied), *citing Interstate Northborough P'ship v. State*, 66 S.W.3d 213, 218 (Tex. 2001) (emphasis added).

In *Crestview Corners*, Dallas County took some property to widen a road, necessitating construction near some underground gas storage tanks.

The landowner sought its costs to remove the storage tanks as part of the diminution in value of the remainder, which the Court allowed.

The landowner put on evidence that the tanks could explode as it was a safety hazard to have construction equipment close to the storage tank vent lines.

In fact, the landowner's attorney drew an analogy to a terrorist bombing and to Oklahoma City in his argument, to which type of argument from this particular attorney the Dallas Court of Appeals was obviously so accustomed that they deemed it improper, but minor.

6. <u>Inverse Condemnation in Texas</u>.

If the government appropriates property without paying adequate compensation, an owner may recover resulting damages in inverse condemnation. *Kopplow Dev. Inc. v. City of San Antonio*, 399 S.W.3d 532 (Tex. 2013).

Kopplow is a flooding case, in which the Texas Supreme Court held an inverse condemnation claim could be brought, despite that no flooding had ever occurred. *Id.* at 537.

The Court held it is enough to establish an intent to take when a governmental entity knows that ***harm is substantially certain to result*** from a specific act. *Id.*

An inverse condemnation may occur when the government ***physically appropriates*** or invades the property, or when it ***unreasonably interferes*** with the landowner's right to use and enjoy the property, such as by restricting access or denying a permit for development. *Westgate, Ltd. v. State*, 843 S.W.2d 448, 452 (Tex. 1992).

Physical taking may occur when regulatory action results in physical occupation of private property. *Lingle v. Chevron U.S.A., Inc.*, 544 U.S. 528, 538 (2005); *Mayhew v. Town of Sunnyvale*, 964 S.W.2d 922, 933 (Tex. 1998).

The Texas Supreme Court has held that landowners have a constitutionally-protected, compensable property interest in groundwater beneath their property. *Edwards Aquifer Authority v. Day*, 369 S.W.3d 814, 833 (Tex. 2012).

In *Day*, the Court held that State regulations cannot "unjustifiably" deprive landowners of the groundwater beneath their land. *Id.* at 843.

And, in *Edwards Aquifer Authority v. Bragg*, the Authority was held liable in inverse condemnation for denying permits for groundwater pumping and usage for irrigation of commercial pecan orchards. *Edwards Aquifer Authority v. Bragg*, 04-11-00018-CV, 2013 WL 5989430 (Tex.App.-San Antonio, November 13, 2013, no pet. h.).

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In *FPL Farming Ltd. v. Environmental Processing Systems*, FPL sued EPS for trespass based on subsurface migration of wastewater injected in a well permitted by TCEQ. *FPL Farming Ltd. v. Environmental Processing Systems*, 351 S.W.3d 306 (Tex. 2011).

FPL alleged that the injected wastewater migrated onto its property and contaminated its water supply. *Id.* at 307.

The Beaumont Court of Appeals had held that FPL had no common law cause of action for trespass because the TCEQ approved a permit allowing EPS to inject wastewater when information before TCEQ showed that EPS's waste plume was projected to migrate into the deep subsurface of the formation underlying FPL's property. *Id.* at 310.

The Texas Supreme Court reversed holding that a permit holder authorized to inject wastewater that could migrate to other property was not immunized from civil tort liability related to injections. *Id.* at 306.

An interesting footnote appears on p. 313 at note 6:

> **6.** FPL argued before this Court that should a government permit immunize a permit holder from trespass liability, the Injection Well Act would become a condemnation statute and the subsurface migration would be a government taking. Because we determine that a permit holder is not shielded from liability because he or she holds a permit, we do not reach FPL's constitutional concern.

Id. at 313 and n. 6.

However, regardless of a private party's potential tort liability, constitutional concerns remain.

The Injection Well Act, Chapter 27 of the Texas Water Code, governs the drilling and use of deep subsurface injection wells by TCEQ, as to wastewater generally, and by the Railroad Commission, as to wastewater related to oil and gas operations. TEX. WATER CODE §§ 27.001-27.105 (Vernon 2008 and Supp. 2013).

TCEQ has been held liable for a taking of water usage rights resulting in whooping crane deaths from the issuance of permits to private parties who made water withdrawals. *Aransas Project v. Bryan Shaw, et al.*, 930 F.Supp.2d 716 (S.D.Tex. August 28, 2013) (the "TAP" case).

The federal courts have imposed a form of "vicarious liability" on regulating governmental entities, as in the TAP case.

So, might governmental entities tasked with regulating groundwater or wastewater injection wells who issue permits resulting in migration onto other property and contamination of its water supply be liable for inverse condemnation?

Might they be liable upon issuance of permits when they know that harm is substantially certain to result?