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Inequitable Valuation in Regulatory Takings Cases: Compensation That "Goes Too Far"

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Inequitable Valuation in Regulatory Takings Cases: Compensation That "Goes Too Far"

The Surface Mining Control and Reclamation Act of 1977 (SMCRA)[1] was enacted by Congress on August 3, 1977 primarily to provide a way to protect the environment from the harmful effects of surface coal mining while still allowing for the production of coal as a national energy source. On October 13, 1989 the United States Claims Court, in *Whitney Benefits, Inc. v. United States*,[2] held that the enactment of SMCRA totally eliminated the economic value of the plaintiffs' fee coal interest and constituted a taking under the Fifth Amendment of the United States Constitution. This note will trace the development of takings law cases in light of *Whitney Benefits*, concentrating on the current test for establishing a regulatory taking and the appropriate remedy if such a taking is found.

I. The Clause and Eminent Domain

The Just Compensation Clause[3] in the Fifth Amendment prohibits the government from taking private property for public use without just compensation. The requirement of just compensation applies directly to the federal government and is applied to the states through the Due Process Clause of the Fourteenth Amendment.[4]

Traditionally, the government takes private property by the process of eminent domain.[5] Under the power of eminent domain

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[1] Surface Mining Control and Reclamation Act of 1977 [hereinafter cited as SMCRA], Pub. L. No. 95-87, § 522, § 1 Stat. 445 (codified at 30 U.S.C. §§ 1201-1328 (Supp. III 1979)).

[2] 18 Cl. Ct. 394 (1989).

[3] "[N]or shall private property be taken for public use, without just compensation." U. S. Const. amend. V.

[4] *See* Webb's Fabulous Pharmacies, Inc. v. Beckwith, 449 U.S. 155, 160 (1980); Chicago, B. & Q.R.R. v. Chicago, 166 U.S. 226, 235-41 (1897). In addition, many state constitutions require compensation where property is taken. *See, e.g.* L. Tribe, American Constitutional Law § 9-2, at 458 n.6 (1978).

[5] *See, e.g.*, Housing Authority of Cherokee Nation of Oklahoma v. Langley, OK., 555 P.2d 1025, 1028 (1976); *see also*, Eaton, Real Estate Valuation in Litigation 404 (1982) ("eminent domain" is government's right "to take private property for public use").

the government acquires the affirmative right to physically occupy private property or obtain possession of the property from a private person through condemnation proceedings. The Just Compensation Clause requires that the government pay for property rights it acquires through eminent domain. The Supreme Court interpreted this constitutional guarantee of just compensation not as a limitation on the power of eminent domain, but as a condition of its exercise.[6]

One limitation upon the definition of a governmental taking is the requirement that the property be taken for a public use. Once this limitation is met, the government has unrestricted ability to obtain any private property.[7] This requirement is not a difficult hurdle for the government to pass, because "public use" has been liberally interpreted by the courts. However, the government is clearly prohibited from granting its taking authority to a private company simply to improve its own economic position.[8] In addition the government is prohibited from using the power itself to make money in strictly entrepreneurial activities.[9]

II. EMERGENCE OF REGULATORY TAKINGS

Prior to the landmark decision in *Pennsylvania Coal Co. v. Mahon*[10], physical invasion was necessary for a taking to occur.[11] In cases where the property owner was restricted in his or her ownership rights by legislative statutes or administrative regulations, the owner was not permitted to assert a governmental taking. Even if the owner was actually harmed more by these regulations than a property owner whose rights had been usurped by eminent domain, the owner was prohibited from asserting a taking. The government was protected in its actions by the "police power." Government police power is not specialized, rather it encompasses the right of federal, state and local gov-

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[6] Long Island Water Supply Co. v. Brooklyn, 166 U.S. 685, 689 (1897); *see* E. FREUND, THE POLICE POWER 541 (1904) where the author concludes that the compensation requirement has always been an element of the exercise of eminent domain in civilized societies.

[7] Berman v. Parker, 348 U.S. 26 (1954). Also, the "public use" requirement of the Taking Clause is "coterminous with the scope of a sovereign's police power."

[8] *See, e.g.*, NL Industries v. Eisenman Chemical Co., 642 P.2d 976 (Nev. 1982).

[9] *See* Webbs Fabulous Pharmacies, Inc. v. Beckwith, 449 U.S. 155, 163-64 (1980).

[10] 260 U.S. 393 (1922).

[11] *Id.*

ernments to enact legislation protecting the health, safety, morals or general welfare of the people within their jurisdiction.[12]

Although the government's police power is still recognized as a viable defense, *Pennsylvania Coal* put an end to the notion that the taking of property could never occur through mere legislation.[13] Justice Oliver Wendell Holmes acknowledged that, as members of a civilized and complex society we must all accept regulation and control by the governing body. However, he tempered that general rule by stating, "if regulation goes too far it will be recognized as a taking."[14]

Since *Pennsylvania Coal*, the Court has had difficulty articulating the point at which regulations "go too far." The Court has yet to articulate a clear standard for determining when such governmental activity should be considered a taking of property.

In *Penn Central Transportation Co. v. New York City*,[15] the Court stressed that, in fact, it *could not* devise a set formula for determining when a regulatory taking has occurred. However the Court did suggest a set of factors that should be considered. These factors include the extent of the adverse economic impact to the property owner and the extent to which the government activity interferes "with distinct investment-backed expectations."[16] The more extensive the economic impact and governmental interference, the more likely it is that a taking will be found. Additionally, a taking will more likely be found if the "interference with property can be characterized as a physical invasion by government."[17]

No one factor determines the existence of a taking in a regulation case.[18] A court must look at the facts of each case to see how the property owner was impacted by the rule or regulation; thus each situation is evaluated on an *ad hoc* basis. Significant factors include the amount of capital the owner invested in the property, the reasonable expectation of property use that existed, whether the regulation was foreseeable, and what uses of the property and rights of the owner were left intact after the regulation.[19]

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[12] *See generally* E. CORWIN, LIBERTY AGAINST GOVERNMENT 88 (1948).
[13] *Pennsylvania Coal*, 260 U.S. at 393.
[14] *Id.* at 415.
[15] 438 U.S. 104 (1978).
[16] *Id.* at 124.
[17] *Id.*
[18] Kaiser Aetna v. United States, 444 U.S. 164 (1979).
[19] *Id.*

This approach was utilized by the court in *Whitney Benefits*.[20] The following is a summary of the *Whitney Benefits* facts that led the Claims Court to find a regulatory taking which warranted just compensation by the United States.

III. FACTUAL SUMMARY OF *WHITNEY BENEFITS*

Whitney Benefits, Inc. is a non-profit charitable company that owns coal in fee under 1,327 surface acres in Sheridan County, Wyoming. Most of the land is irrigated or subirrigated Tongue River alluvial valley floor [hereinafter AVF] making it valuable for farming.[21]

In 1974, Peter Kiewit Sons' Co. [hereinafter PKS], a mining corporation, leased the rights to mine coal in exchange for advance and operating royalties. By 1977 PKS had also purchased approximately 600 surface acres located above the coal it was leasing from Whitney Benefits.[22]

In 1976, PKS spent one million dollars for preliminary tests of its leased property and filed a permit application to begin coal production with the Wyoming Department of Environmental Quality [hereinafter DEQ]. The application was withdrawn in August of that year for procedural reasons, but PKS expressed an intent to refile.[23]

The enactment of SMCRA on August 3, 1977 effectively prohibited surface mining in the absence of a state-issued permit. The Act also explicitly provided that no permit or revision application should be approved by the state unless it could be shown that the proposed surface coal mining operation would "not interrupt, discontinue, or preclude farming on alluvial valley floors that are irrigated or naturally subirrigated . . . ."[24]

The coal in this case was physically located under an AVF which was significant to farming. Any attempt to mine the coal would preclude farming activity on or near the AVF. In compliance with SMCRA, Wyoming's DEQ would therefore be required to reject any application by Whitney Benefits or PKS to mine the coal.[25]

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[20] Whitney Benefits, Inc. v. United States, 18 Cl. Ct. 394 (1989).

[21] *Id.* at 396.

[22] *Id.* at 397.

[23] *Id.*

[24] *Id.* [*quoting* SMCRA § , 30 U.S.C. § 1260 (1982)].

[25] *Whitney Benefits*, 18 Cl. Ct. at 397.

In recognition of the inequity to coal producers, like Whitney Benefits or PKS, who had made substantial financial commitments before the Act's passage, SMCRA provided for an exchange of the affected property for federal coal. The plaintiffs took advantage of this exchange provision and reapplied to the DEQ in October of 1978. Whitney Benefits interpreted the Act to require obtaining a rejection by the DEQ in order to qualify for the exchange program.[26]

In January of 1979, Whitney Benefits' application was rejected by the DEQ for procedural reasons. Since 1982 the plaintiffs have been negotiating with the defendant concerning which property is to be exchanged.[27]

In 1983-84, the plaintiffs expended $130,000 to perform test drilling on a parcel of federal land considered for a possible exchange. The federal government proposed a different piece of land, called Hidden Water Tract, for an exchange. PKS rejected that offer as they had previously mined the area and were not interested in the coal that remained.[28]

On August 3, 1983, exactly six years after SMCRA's enactment, the plaintiffs filed a complaint under the Tucker Act and the Fifth Amendment, contending that SMCRA had stripped their property of all its economic use.[29] The U.S. Claims Court dismissed their action explaining that the exchange mechanism precluded plaintiffs from asserting a Tucker Act claim. Because SMCRA provided for just compensation on its face, the court reasoned that there was no unconstitutional taking of the property.[30]

The plaintiffs then filed a "citizen suit" in the U.S. District Court for the District of Wyoming seeking to compel an exchange.[31] The district court agreed that the government had unreasonably delayed compensation and directed the Secretary of the Interior to exchange federal coal equal in value to the plaintiffs' fee coal.[32]

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[26] *Id.* at 398.

[27] *Id.*

[28] *Id.*

[29] *Id.* (the complaint was filed in the U.S. Claims Court).

[30] *Whitney Benefits*, 18 Cl. Ct. at 398.

[31] *Id.* (the suit was filed pursuant to 30 U.S.C. § 1270 (1982) in the United States District Court for the District of Wyoming).

[32] *Whitney Benefits*, 18 Cl. Ct. at 398.

In response, the Secretary filed a notice of compliance with the court arguing that because it would originally have been uneconomical to surface mine the plaintiffs' property, the property was valueless and therefore no exchange was warranted. The Secretary stated that he offered an exchange of Hidden Water Tract in 1986, but the plaintiffs refused to accept it.[33]

In the meantime, the United States Court of Appeals for the Federal Circuit reversed and remanded the Claims Court's earlier dismissal, stating that the exchange provision was not determinative of whether SMCRA effected a taking of plaintiffs' property. Further proceedings were ordered and extensions were allowed to consider recent cases in takings law jurisprudence.[34]

On remand, the Claims Court held that enactment of SMCRA had totally eliminated the economic value of the plaintiffs' coal and constituted a taking under the Fifth Amendment.[35] The time of the taking was held to be August 3, 1977, the date SMCRA became effective, and the amount of the just compensation due the plaintiffs began accruing as of that date.[36] The court used the valuation method which incorporated a discounted cash flow approach to determine the fair market value of the coal on the date of the taking.[37] It further held that the plaintiffs were entitled to prejudgment interest.[38]

IV. AD HOC DETERMINATION

A. Property Interests

In determining whether a taking has occurred, a plaintiff must first demonstrate that he or she has a protected interest under the Constitution. Property interests themselves are not created by the Constitution but must arise from an independent source, such as state law.[39] It is settled law in Wyoming that an

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[33] *Id.* at 399.

[34] *Id.* The cases to be considered were: Nollan v. California Coastal Comm., 483 U.S. 825 (1987); Keystone Bituminous Coal Ass'n. v. DeBenedictis, 480 U.S. 470 (1987); and MacDonald, Sommer & Frates v. Yolo County, 477 U.S. 340, *reh'g denied*, 478 U.S. 1035 (1986).

[35] *Whitney Benefits*, 18 Cl. Ct. at 406.

[36] *Id.* at 407.

[37] *Id.* at 416.

[38] *Id.*

[39] *See* Board of Regents v. Roth, 408 U.S. 564, 577 (1972).

interest in minerals constitutes a property interest.[40] One's mineral interest is distinct from any interest in the surface land.[41] Thus Whitney Benefits' fee ownership in the coal under the AVF is a constitutionally protected property interest. Further, the U.S. Supreme Court has held that a lease interest is also property, and that an injured lessee has a property right requiring compensation.[42] Therefore, if PKS could demonstrate that it was harmed by SMCRA's implementation, it, like Whitney Benefits, could also recover for a taking in violation of the Constitution.

B. Character of the Government Action

The second consideration in a takings analysis is the character of the government's action that allegedly led to the claimant's injury.[43] If the government regulates to such an extent that the property interference approaches an actual physical invasion by the public, it is more likely that a taking will be found.[44] However, if the government action is justified as "aris[ing] from some public program adjusting the benefits and burdens of economic life to promote the common good,"[45] it will less likely be seen as a taking.[46]

In *Whitney Benefits*[47] the governmental action is Congress' enactment of SMCRA, a piece of social and economic legislation, the clear purpose of which was to protect the environment from the harmful effects of strip mining.[48] The Act is facially constitutional because it does not bar all beneficial use of coal-bearing land.[49] It only regulates the conditions under which coal

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[40] *Whitney Benefits*, 18 Cl. Ct. at 405 [*citing* Williams v. Watt, 668 P.2d 620, 624-25 (Wyo. 1983) and Skaw v. United States, 740 F.2d 932, 935-36 (Fed. Cir. 1984) (mineral rights are property subject to the Fifth Amendment's Taking Clause)].

[41] *Id.*

[42] A. W. Duckett & Co. v. United States, 266 U.S. 149 (1924).

[43] *Penn Central*, 438 U.S. at 124.

[44] *See* Loretto v. Teleprompter Manhattan CATV Corp., 458 U.S. 419 (1982) (Distinguishing the case from *Penn Central*, the court said a permanent physical invasion "does not simply take a single 'strand' from the 'bundle' of property rights: it chops through the bundle, taking a slice of every strand." *Id.* at 435).

[45] *Penn Central*, 438 U.S. at 124.

[46] *Id.*

[47] 18 Cl.Ct. 394.

[48] SMCRA § 102, 30 U.S.C. § 1202 (1982).

[49] Hodel v. Virginia Surface Mining & Reclamation Ass'n., Inc., 452 U.S. 264, 268 (1981).

production may be conducted and does not attempt to regulate any alternative uses for the property affected.[50] Furthermore, while strip mining has not been classified as a noxious use of property,[51] it is within Congress' power to reduce and limit its harmful effects whenever possible.

Conversely, "[t]o make it commercially impracticable to mine certain coal has very nearly the same effect for constitutional purposes as appropriating or destroying it."[52] It is clear that the state has the power to regulate property without payment of compensation, yet if the regulation goes too far a taking may be found.[53] In performing the balancing test to resolve the character of the governmental action in *Whitney Benefits*[54] the court held that the restrictions put on the plaintiffs' coal went "too far."[55] Although this result is certainly within the court's discretion, it conflicts with the recent trend[56] to refuse compensation for similar types of regulation.

In regulatory takings cases, courts are much more likely to find a taking from a state-imposed restriction depriving a property owner of "all beneficial use" of his property.[57] The defendant in *Whitney Benefits* attempted to suggest that because the plaintiffs could perform underground mining to extract their coal, mine other minerals instead of the coal, or farm and ranch the surface property, there were important alternative uses for the property.[58] However the court held that underground mining was not feasible as an alternative use for the property.[59] The

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[50] *Id.*

[51] *See, e.g.*, Mugler v. Kansas, 123 U.S. 623, 668 (1887) ("A prohibition simply upon the use of property for purposes that are declared . . . to be injurious to the health, morals, or safety of the community, cannot . . . be deemed a taking . . . ."). It is well recognized that one cannot be viewed to have a property right to engage in "noxious conduct". The illegalization of the manufacture and sale of dangerous drugs or of a polluting activity are therefore never considered to be infringements of property rights. I personally question if strip-mining should not be included as a "polluting activity", but thus far the courts have not categorized it as such.

[52] Pennsylvania Coal Co. v. Mahon, 260 U.S. 393, 414 (1922).

[53] *Id.* at 415.

[54] 18 Cl. Ct. 394.

[55] *See supra* text accompanying notes 13-14.

[56] *See* Keystone Bituminous Coal Ass'n. v. DeBenedictis, 480 U.S. 470 (1987) (where the court refused to compensate when the landowner could utilize other aspects of his property).

[57] First English Evangelical Lutheran Church v. Los Angeles County, 482 U.S. 304, 311 (1987).

[58] *Whitney Benefits*, 18 Cl. Ct. at 405.

[59] *Id.*

court also correctly pointed out that the other alternative uses are not related to coal rights and that it was the loss of coal rights that was affected by the Act.[60] The fact that the plaintiffs could use other property they own to gain a profit did not excuse the government for rendering the coal property useless.[61]

C. *Economic Impact and Investment Backed Expectations*

The third consideration in the takings analysis consists of examining the situation from an economic perspective, both before and after the impact of the regulation. A court must note any adverse economic impact[62] suffered by the plaintiff, especially if such adverse impact is caused in part by investment-backed expectations.[63] If some negative impact is shown, the government is required to compensate the claimant, even if the regulation only temporarily deprives an individual of his or her property rights.[64] However, the property owner still bears the burden of showing a substantial deprivation[65] not within the protection of the state's "police power" to regulate.[66] Additionally, it may be a requirement that the regulation was reasonably unexpected by the property owner. The remedy for the actual negative economic impact will be more fully explored in the next section.

D. *Just Compensation*

1. *The Tail Wagging the Dog*

Once a court has established that there was a regulatory taking, the Constitution demands that the government entity pay

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[60] *Id.*

[61] *Id.*; *but see First English Evangelical*, 482 U.S. at 304.

[62] *Penn Central*, 438 U.S. at 124.

[63] *Id.*

[64] *First English Evangelical*, 482 U.S. at 318.

[65] *Pennsylvania Coal Co.*, 260 U.S. at 415. *See also* Kirby Forest Industries, Inc. v. United States, 467 U.S. 1, 14 (1984):

> . . . while most burdens consequent upon government action undertaken in the public interest must be borne by individual landowners as concomitants of 'the advantage of living and doing business in a civilized community", some are so *substantial* and *unforeseeable*, and can so easily be indentified and redistributed, that "justice and fairness require that they be borne by the public as a whole".

[66] *Id.*

just compensation for the period beginning on the date the regulation first effected the taking and ending on the date the government entity chooses to end the regulation.[67] It has been suggested that the same principles for determining the proper measure of just compensation ordinarily applied in formal condemnation proceedings and physical invasion cases should be applied in cases of permanent or temporary takings.[68] However, there have been problems in determining the proper amount of compensation due an owner in a regulatory taking.

The same theory of compensation that exists for eminent domain cases exists for regulatory takings: when the public, through governmental action, substantially infringes on private property rights, it should take the burden of paying for the public benefit from that private individual and spread these costs among the whole of society. This theory is premised on the recognition that it is patently unfair to force an individual to suffer alone for the benefit of everyone else.[69]

Unlike an eminent domain situation,[70] regulators face uncertainty whenever they propose to implement any new restriction on land use such as zoning ordinances,[71] land-development prohibitions[72] or environmental legislation such as SMCRA.[73] It is certainly more difficult for a complainant to prevail in an inverse condemnation proceeding[74] and recover damages to the

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[67] San Diego Gas & Electric Co. v. City of San Diego, 450 U.S. 621, 653 (1981) (Brennan, J. dissenting).

[68] *Id.* at 653, 657, 658-9 (Brennan, J., dissenting).

[69] *First English Evangelical*, 482 U.S. at 318 ("It is axiomatic that the Fifth Amendment's just compensation provision is designed to bar Government from forcing some people alone to bear public burdens which, in all fairness and justice, should be borne by the public as a whole.") (*quoting* Armstrong v. United States, 364 U.S. 40, 49 (1960).

[70] This is the most often cited reason to avoid holding a taking has occurred in regulatory cases.

[71] Agins v. City of Tiburn, 447 U.S. 255, 257 (1980).

[72] MacDonald, Sommer & Frates v. Yolo County, 447 U.S. 340 (1986).

[73] Hodel v. Virginia Surface Mining & Reclamation Ass'n., Inc., 452 U.S. 264 (1981).

[74] San Diego Gas & Elec. Co. v. City of San Diego, 450 U.S. 621, 638 n.2 (1981) (Brennan, J. dissenting) (citations omitted) According to Justice Brennan:

> The phrase 'inverse condemnation' generally describes a cause of action against a government defendant in which a landowner may recover just compensation for a "taking" of his property under the Fifth Amendment, even though formal condemnation proceedings in exercise of the sovereign's power of eminent domain have not been instituted by the government entity. . . [I]t is the landowner, not the government entity, who institutes the proceeding.

same extent he would be entitled to under other types of takings. For example, in *Agins v. Tiburon*[75] the court held that a property owner, suing for money damages on the theory of inverse condemnation because his land had been allegedly taken by a zoning ordinance substantially limiting the use of his property, could challenge the constitutionality of the ordinance and its application to his property through the procedure of mandamus or declaratory relief. However, the court declared that "the use of inverse condemnation with its imposition of money damages upon the public entity would, in our view, unwisely inhibit the proper and necessary exercise of a valid police power."[76]

Agins limited the practical victory for a prevailing plaintiff since monetary damages were not thought to be an appropriate remedy for regulatory takings. However, the Supreme Court broadened the possibility for a plaintiff's success by clarifying the test for determining when such a taking had occurred. It stated "[t]he application of a general zoning law to particular property effects a taking if (1) the ordinance does not substantially advance legitimate state interests, or (2) denies an owner economically viable use of his land."[77] Instead of requiring both factors to establish a taking, *Agins* allowed for recovery when only one prong was satisfied.

It seems that *Keystone Bituminous Coal Association v. DeBenedictis*[78] and *Whitney Benefits*[79] both followed the *Agins* rationale. In *Keystone*, the Court held that neither prong was satisfied and thus there was no taking.[80] The court in *Whitney Benefits* held that both prongs were satisfied, and thus a taking was found. Interestingly, in both cases the regulation in question affected rights associated with coal mining, but the conclusions of the respective courts are contradictory.

The result in *Keystone* is probably the most practical, although the test used was the broadened one put forth by *Agins*.

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[75] 24 Cal.3d 266, 598 P.2d 25, 157 Cal Rptr. 372 (1979), *aff'd* 447 U.S. 255 (1980).

[76] *Agins*, 24 Cal. 3d at 278 (On appeal the United States Supreme Court affirmed the state court's decision that no taking had occurred. Agins v. Tiburn, 447 U.S. 255 (1980)). The Supreme Court expressly refused to consider whether "a state may limit the remedies available to a person whose land has been taken without just compensation." *Agins*, 447 U.S. at 263.

[77] *Agins*, 447 U.S. at 260 (citations omitted).

[78] 480 U.S. 470 (1987) (considering the constitutionality of a state act similar to the statute struck down in *Pennsylvania Coal*, 260 U.S. 393 (1922)).

[79] 18 Cl. Ct. 394 (1989).

[80] *Keystone*, 480 U.S. at 501.

Perhaps a better approach would be to balance both prongs of the *Agins* test. In a situation where a property owner is denied the economic use of his land, but the regulation substantially advances legitimate state interests, the government will have to come forward with full compensatory relief.

Theoretically, this is what the Constitution demands for a fair and just result. Practically, however, such a result could create substantial financial burdens on government, particularly at the state and local levels. Furthermore, the government might be reticent to enact proper, helpful legislation for fear of opening itself up to huge[81] claims for compensation from allegedly affected individuals. Understanding the potentially destructive outcome of such a situation, state and local courts will tend to find no abrogation of the claimant's economic interest in his property. Perhaps they will hold that no taking has occurred in order to eliminate the need to pay just compensation, when the issue of just compensation should only be considered after it is decided a taking has occurred.

2. *Fair Market Value*

The basic principle for determining the amount due an individual whose property has been taken is contained in the statement by Justice Holmes that the test is "what has the owner lost, not what has the taker gained."[82] The courts look to the market value of the property taken to affix a value on what the owner has lost.[83] Additionally, a court will look to the value of the property at its "highest and best use."[84] In most cases, this value is determined by the "fair market value on the date it is appropriated."[85]

The fair market value is "what a willing buyer would pay in cash to a willing seller."[86] Traditionally, courts have looked

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[81] For example, in *Whitney Benefits* the court held the claimants were entitled to $60,296,000.00 plus pre-judgement interest on that amount. *Whitney Benefits*, 18 Cl. Ct. at 416. *See Agins*, 447 U.S. at 260 (threat of monetary damages has "chilling" effect on adoption of innovative zoning).

[82] Boston Chamber of Commerce v. Boston, 217 U.S. 189, 195 (1910).

[83] Note, *Valuation of Conrail Under the Fifth Amendment*, 90 HARV. L. REV. 596, 598 (1977).

[84] *Id.* at 599.

[85] *Kirby*, 467 U.S. at 10 [citing United States v. 564.54 Acres of Land, 441 U.S. 506, 511-513 (1979)].

[86] United States v. Miller, 317 U.S. 369, 374 (1943).

at the basis of a fair rental value for the property,[87] interest on the property's market value,[88] or actual damages incurred because of the deprivation of use[89] in situations where it is difficult to determine a fair market price at the time of the takings or "would result in manifest injustice to owner or public . . . ."[90]

The Supreme Court has stated that the market test is not definitive, but rather the overall standard is to be governed by equitable principles of fairness.[91] However, it is not proper to compensate any expenditures for appraisal fees[92] nor is it proper to obtain a remedy based on replacement cost of the property.[93]

The value is to be determined at the time of the taking,[94] and if there is a delay between the time of taking and the time of payment, the owner is also entitled to interest on the value of the property from the date of the taking.[95] The compensation may also be adjusted if the value of the property changed materially during any delay.[96]

Generally, the court will rely on an appraiser's estimation of the fair market value that he or she obtains by the market, reproduction cost, or income capitalization method of appraisal.[97] The market method is the most common way to appraise property affected by eminent domain. However, this may not be the most appropriate method of evaluation for land use regulatory cases because the size and quality of the lands are typically different.[98] One commentator points out that in using the income capitalization approach, the courts determine a value of projected net earnings attributable to income-producing property to calculate present value.[99]

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[87] This is a good measure to use in temporary takings cases. Kimball Laundry Co. v. United States, 338 U.S. 1 (1948).

[88] *See* Nemmers v. City of Dubuque, 764 F.2d 502 (8th Cir. 1985).

[89] This compensates for lost profits.

[90] *Kirby*, 467 U.S. at 10, n.14 [*quoting* United States v. Commodities Trading Corp. 339 U.S. 121, 123 (1950)].

[91] United States v. Fuller, 409 U.S. 488 (1973).

[92] United States v. Bodcaw Co., 440 U.S. 202 (1979) (per curiam).

[93] United States v. 564.54 Acres of Land, 441 U.S. 506 (1979).

[94] *Kirby*, 467 U.S. at 10.

[95] *Id.*

[96] *Id.*

[97] *See* United States v. 100 Acres of Land, 468 F.2d 1261, 1267-68 (9th Cir. 1972), *cert. denied*, 414 U.S. 822 (1973); *In re* James Madison Houses, 17 A.D.2d 317, 323-24, 234 N.Y.S.2d 799, 806 (1962).

[98] Note, *Inverse Condemnation: Valuation of Compensation in Land Use Regulatory Cases*, 17 SUFFOLK U.L. REV. 621, 642-43 (1983).

[99] *Id.* at 643. *See generally* UNIF. EMINENT DOMAIN CODE § 1110 (1974) (explaining

a. Fair Market Value as Determined in Whitney Benefits

In Whitney Benefits, the court rejected the defendant's contention that the proper method for determining the fair market value of the coal is the comparable sales approach.[100] In this method, the appraiser "uses sales and purchases of properties that reasonably resemble the subject property with respect to time, place, and circumstances."[101] In order for this method to work, there must be comparable property that was bought by a willing buyer and sold by a willing seller.[102] The court found that there was no such property available for comparison.[103]

Instead, the court decided to use a discounted cash flow (DCF) approach by "valuing the property based on the discounted stream of income the property is capable of producing over its useful economic life."[104] This method (called the "Boyd Plan" because it represented the name of the plaintiffs' appraiser who submitted the plan) uses the DCF analysis based on the capitalization of the projected income stream to value the coal.[105] The Court described in detail the factors considered in its adoption of the Boyd Plan for valuation in the instant case.

The method used by the court in *Whitney Benefits* evaluated the amount that a willing buyer would have paid for the property interest at the time of SMCRA's enactment.[106] In determining

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capitalization of income).

> Courts and commentators, for a variety of reasons, are not supportive of income capitalization as a measure of value. *See* A.G. Davis Ice Co. v. United States, 362 F.2d 934, 936-37 (1st Cir. 1966) (projected net earnings or lost profits too speculative because depend on variable factors such as taxes, economic conditions, competition, labor, or knowledge of owner); 4 SACKMAN, (citation omitted) (reasons for rejecting income capitalization appraisal in eminent domain cases include conjecture concerning value of human efforts). *But see* City of Revere v. Revere Constr. Co., 285 Mass. 243, 249, 189 N.E. 73, 75 (1934) (holding when net income related to location, rather than skill, can be considered); . . . .

Id. at 643, n. 106.

[100] *Whitney Benefits*, 18 Cl. Ct. at 408.

[101] *Id.*

[102] *Id.* (*citing* United States v. Miller, 317 U.S. 369, 373-74, *reh'g denied*, 318 U.S. 798 (1943)).

[103] *Id.*

[104] *Id.*

[105] *Whitney Benefits*, 18 Cl. Ct. at 408.

[106] *Id.* at 410 ("[I]n its Plan, the Boyd Company performed a full independent analysis of the 1977 coal market and concluded that a willing buyer would have assumed that it could sell Whitney coal for $13.13 per ton.").

this value, the reasonable annual production rate,[107] the price of the coal,[108] and capital and operating costs[109] were estimated, based on both information obtained by an industry publication,[110] and expert testimony about such matters for similar area mines.[111]

The court discounted by eleven percent the valuation amount obtained.[112] This discount percentage was chosen because it was found that the rate generally applied in the coal industry in 1977 fell in the range between eight and twelve percent.[113] Additionally, a ten percent discount rate was used in BLM's Guide to Federal Coal Property Appraisal[114] and the NRET (BLM's Northwest Regional Evaluation Team) had previously used a ten percent rate to value Whitney Coal for exchange purposes.[115]

Apparently, the court in *Whitney Benefits* was also relying on the defendant's own previous valuation assessment of the property in issue. The court mentions several times that the figures found at each stage are comparable or even conservative when compared with the government's earlier documentation of its negotiations with the plaintiffs.[116]

The defendant argued that the Boyd Plan was too speculative,[117] and that it compensated for lost profits.[118] The defendant further asserted that lost profits are clearly not compensable in

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[107] *Id.* ("[T]his court finds that such [a] purchaser likely could secure utility coal contracts for 2 million tons of coal per year and industrial coal contracts for an additional 500,000 tons.").

[108] *Id.*

[109] *Id.* at 413 (These costs would include expenditures related to labor costs at the mine, mine development drilling, laboratory costs, legal accounting, marketing, administrative services, insurance expenses, property taxes, SMCRA's reclamation fee, unit price costs of capital expenditures, etc., less work already done by PKS.).

[110] *Whitney Benefits*, 18 Cl. Ct. at 411 n.15 (The publication is *Coal Week*).

[111] *Id.* (*i.e.* Sheridan County, Wyoming).

[112] *Id.* at 412-13 (This figure was increased one percent due to risk factors associated with the proposed production: "Whitney was undeveloped; the proposed 4 million ton per year production rate might take several years to reach; a buyer of Whitney might not be able to acquire additional surface land; DEQ might not approve the Boyd Plan's river diversions; DEQ might not approve the Boyd Plan's final impoundments; and the price of coal might decrease over time.").

[113] *Id.* at 412.

[114] *Id.* (quoting the Appraisal Guide: "In general, the use of a discount rate adjustment to account for risk is not recommended because of overwhelming subjectivity involved in selecting the risk premium.").

[115] *Whitney Benefits*, 18 Cl. Ct. at 412.

[116] *See id.* at 411-13.

[117] *Id.* at 410.

[118] *Id.* at 409.

regulatory takings cases because lost profits "would be compensation for value added to the property taken by the plaintiffs' location and goodwill, their management skill, and all the potential risks and opportunities that make up the concept of profit."[119] They are "derived from business activities [that] depend to a greater extent upon the amount of capital invested and the good fortune, business skill and management with which the business is conducted [rather] than . . . the land itself."[120]

The distinction between compensation based on lost profits, and the compensation awarded the plaintiffs in *Whitney Benefits* is unclear. The court stressed that because the case involved coal reserves, the valuation could only be measured by the coal's ability to produce income.[121] It is true that the coal is not valuable unless it can be extracted and utilized.[122] However, the method used in this case seems to go beyond the mere capitalization of speculative income. The Boyd Plan looks at the market for Whitney coal in 1977 and provides a list of buyers that would have used the coal. This compilation is not reliable because, in addition to the quality and proximity of the coal, the buyers would presumably buy Whitney coal based on considerations such as the seller's reputation and ability to conduct the deal properly. In fact, the managerial skill of the seller might completely outweigh the quality of the coal as an indication of how much, if any, coal was sold to these buyers.

3. *An Alternative Approach*[123]

Because of the problems encountered with a DCF approach in *Whitney Benefits*, a better solution might be to require the government to compensate PKS for its considerable financial outlay in connection with testing its leased interest and the proposed federal property exchange.[124] This reimbursement would

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[119] *Id.* (*distinguishing* Mitchell v. United States, 267 U.S. 341 (1925); Joslin Mfg. Co. v. City of Providence, 262 U.S. 668 (1923); and United States v. General Motors Corp., 323 U.S. 373 (1945)).

[120] *Id.* (*quoting* Cloverport Sand & Gravel Co. v. United States, 6 Cl. Ct. 178, 191 (1984)).

[121] *Whitney Benefits*, 18 Cl. Ct. at 409.

[122] *See* Note, *supra* note 83.

[123] An alternative approach is warranted because courts generally do not feel comfortable using income capitalization. *See supra* note 99.

[124] This would include $1 million from March 1976 and $130,000 from 1983, with interest paid on each amount from the date incurred.

only be afforded if the expenditures were reasonably based on PKS's investment-backed expectations,[125] and could be lowered by any amount the court found would be fair and just based on the nature of the property involved. The goal of this approach would be to put the lessor/owner in a position that resembles as closely as possible the position he or she was in prior to the attempt to realize any gains from the property.

The court should try to balance the necessity of the government imposed regulation with the potential value of the property without the impact of that regulation.[126] If the regulation was found to be of a paramount interest, no further compensation should be required.[127] If the necessity of the regulation did not substantially outweigh the property interest, the government should be required to compensate as if it had condemned the property through eminent domain and in fact, would be able to acquire title to any remaining interest after compensation was paid.

The difficulty would arise if the necessity of the regulation substantially outweighed the property interest, but was not one of the paramount[128] state interests. Perhaps in that situation a court could require that the property owner be awarded less than the market value[129] of his or her interest. The amount of compensation could be set by the court through its analysis of the fairest result for both the property owner and the public.[130]

Under this alternative, the lessee would probably never be fully indemnified, and based on the purpose of the regulation in question, the owner might or might not be fully compensated.[131] However, "just compensation" requires that the com-

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[125] A "reasonable investment-backed expectation" must be more than a "unilateral expectation or an abstract need." *See* Webb's Fabulous Pharmacies Inc. v. Beckwith, 449 U.S. 155, 161 (1980).

[126] For example, the prohibition of using the property in a "noxious" manner. *See supra* note 51.

[127] This seems only fair. If the regulation had a valid purpose and the property owner wished to condemn the property, he should be willing to give up all rights to it in return for compensation based on the fair market price of the property on the date of the taking.

[128] *See supra* text accompanying note 46.

[129] As determined by what a willing buyer would pay for the property, absent the regulation, on the day the regulation effected a taking.

[130] The Just Compensation Clause must be construed to demand fairness and justness for both the government and private property owners.

[131] This is acceptable in certain situations. *See* United States v. 564.54 Acres of Land, 441 U.S. 506, 511-12 (1979).

pensation paid by the government for taking property must be fair and just to both sides. In a world where governmental entities had unlimited fiscal resources, the equitable solution would be to compensate a particular owner or lessor for every interest he might have in property, including substantial emotional and psychological ties to a unique piece of land, or a particular profit-making potential based on the experience of the holder.[132]

However, in the real world, the government does not have unlimited reserves and the function of providing zoning laws and land use restrictions is a vital task our government must perform. It may be "unfair" to require one or a few persons to bear the burden of providing a benefit for society as a whole. Nevertheless, to a certain extent, it is the only realistic way to ensure that the state and local governments, in particular, do not abandon their duty to ensure that our environment is clean and safe, that our towns are not left to grow unchecked, and that the private landowner does not dictate for the whole populace what development will occur.[133]

CONCLUSION

The courts have recently begun to allow monetary compensation for inverse condemnation proceedings based on the regulatory takings theory. While this trend has been proper, in that some cases justify such awards, perhaps there should be a tighter limit on the valuation method employed in determining the amount of compensation paid. It is essential that courts continue to decide each of these cases on an *ad hoc* basis, both to establish whether a taking has in fact occurred and the proper remedy required of the government when its regulations cross the line and go "too far." In *Whitney Benefits*, the court properly found a taking, but chose to award compensation based on a method which might not be fair and equitable to both sides of the case. An alternative method was suggested, with the realization that such method left much to the discretion of each court. The

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[132] *But see* United States v. 564.54 Acres of Land, 441 U.S. at 511-12 (there is a difficulty in assessing the value an individual places upon a particular piece of property and because of the need for a clear, easily administrable rule governing the measure of "just compensation," the factors probably would still not be considered in valuation).

[133] The author realizes that the proposed alternative approach may not address all situations where a regulatory taking could occur.

courts appear to have recently leapt from one side of the fence in exclusively protecting the action of the government, to the other side in compensating property owners for what they *could* have gained from their property absent the regulation. This flip flop in the judicial approach to takings cases has been at the expense of the public, who must pay the compensation awarded through their government. A more balanced perspective would compensate the private owner on a more conservative basis while considering the competing interests of each side.

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