

# ■ An Introduction to Eminent Domain

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Eminent domain is the power of a government agency or limited types of private companies (such as utilities) to involuntarily acquire private property rights in exchange for the payment of just compensation. Condemnation laws involve complicated legal and valuation issues. Providing a nuanced discussion of those issues that differentiates between the procedural and substantive requirements of each state would require a treatise, not an article. Therefore, this article provides a general introduction to the laws of one exemplar state — Michigan. In many instances, the general concepts described in this article are more broadly applicable. Most important, this article illustrates just compensation issues that may not be identified by property owners confronted with a potential taking.

## General Procedural Issues ■ ■ ■

In Michigan, the Uniform Condemnation Procedures Act (“UCPA”)<sup>1</sup> provides procedures that condemning authorities must follow both before filing and during an eminent domain lawsuit. It also provides substantive benefits to property owners.

Before an “agency,”<sup>2</sup> which can include both government and private entities such as utility companies, can file a lawsuit, it must tender a “good faith offer.” A good faith offer identifies the amount of just compensation the agency is willing to pay. In order to prepare a good faith offer, the UCPA authorizes the

agency to enter the property, but only after notifying the owner and providing the opportunity to accompany.<sup>3</sup> The agency may also obtain financial records.<sup>4</sup>

Michigan is a quick-take state. This means the agency obtains title to the property before just compensation is ultimately determined, although it must pay its good faith offer to the property owner at the outset of a lawsuit.<sup>5</sup> The agency must complete the taking once an owner answers the complaint and cannot dismiss the lawsuit if it believes that the just compensation awarded is excessive.

The UCPA entitles owners to interest on any unpaid just compensation from the date the agency receives possession of the property to the date payment is received.<sup>6</sup> This typically entitles the owner to reimbursement of attorney fees calculated on a contingency basis,<sup>7</sup> and payment of the owner’s reasonable expert fees.<sup>8</sup>

While the good faith offer process is followed fairly consistently in many jurisdictions, Michigan is one of the most generous states when it comes to reimbursement of attorney and expert fees.

<sup>1</sup> MCL 213.51 *et seq.*

<sup>2</sup> MCL 213.51(c).

<sup>3</sup> MCL 213.54(3).

<sup>4</sup> MCL 213.55(2).

<sup>5</sup> MCL 213.57-213.59.

<sup>6</sup> MCL 213.65.

<sup>7</sup> MCL 213.66 (3).

<sup>8</sup> MCL 213.66 (1).

## Just Compensation in Condemnation Cases ■ ■ ■

While the courts often use lofty platitudes, asserting that “nothing can be fairly termed just compensation which does not put the party injured in as good a condition as he would have been if the injury had not occurred,”<sup>9</sup> there are limitations imposed. Alternatively, there are factors that affect just compensation that may not be readily apparent to a lay person. Condemnation has been acknowledged to be a highly technical area of the law. Therefore, this article addresses a few of the more important concepts in the three primary categories: real estate, fixtures and business damages.

### Real Estate-Based Just Compensation

Before valuing property, it is important to identify the property at issue. The UCPA defines a “parcel” as “an identifiable unit of land, whether physically contiguous or not, having substantially common beneficial ownership.”<sup>10</sup> For example, just compensation for the acquisition of a parking lot with a different legal description than the building that it services would include payment for the building’s diminished value. The reasonable potential of assembling multiple properties that increases the value of the disparate parts may also be considered. For example, owners of property acquired for Comerica Park and Ford Field, home fields for the Detroit Tigers and Lions, were entitled to assert a higher value based on the potential assemblage of the neighborhood for the three downtown casinos that were proposed at the time.<sup>11</sup>

The Stadia acquisition also illustrates the “Scope of the Project Rule,” which essentially requires that any effects — whether positive or negative — caused by the contemplation of the project be disregarded when valuing property.<sup>12</sup> In the Stadia cases, significant evidence demonstrated that casino interests were in the process of assembling options — with the blessing of the Detroit government — and were only relocated when the Detroit Lions decided to move downtown. As such, the acquisition reflected the value of the property under a highest and best use of assemblage for casino development. The Scope of the Project Rule provides basic fairness to both agencies and owners. If, for example, announced plans to construct a new interchange in an area that had previously been farmland caused values to escalate

in anticipation of commercial use, it would be unfair to the agency to force it to pay more. If the uncertainty surrounding a project stifled development, it would be unfair to pay owners less.

While it is constitutionally prohibited, municipalities sometimes use restrictive zoning to depress values to allow future acquisition at a lower price.<sup>13</sup> The Scope of the Project Rule is part of the reason this type of conduct is not considered when appraising condemned property. Even in the absence of conscious attempts to stifle value to facilitate cheaper future acquisitions, if the reasonable possibility exists that the zoning classification of condemned property could have been changed creating greater value, rezoning may be considered.<sup>14</sup> Similarly, the possibility of obtaining a variance that increases value may also be considered.<sup>15</sup>

Certain types of properties that are not normally bought and sold on the open market are difficult to value when taken. In these instances, the property may be deemed a special-purpose property and just compensation would essentially indemnify the property owner for the loss of the property to them, as opposed to paying a market value that may be impossible to ascertain.<sup>16</sup> In these instances, the appropriate methodology is often a cost approach, whereby the underlying land and depreciated cost of the improvements are considered.

If a condemnation does not acquire all rights to an entire parcel, it is called a “partial taking.” In partial takings, the property owner is entitled to not only the value of the part taken, but also damages attributable to the remainder of the parcel. “The measure of compensation is the difference between 1) the market value of the entire parcel before the taking and 2) the market value of what is left of the parcel after the taking” with various factors including altered size, shape, access, grade, and zoning impacts considered.<sup>17</sup> Some items are not compensable like changes in traffic patterns<sup>18</sup> or the “general effects of a project” that are “experienced by the general public or by property owners from whom no property is taken.”<sup>19</sup> In valuing remainders in partial takings, it is assumed that the agency will use its newly acquired rights “to the fullest extent allowed by law.”<sup>20</sup>

Most of the concepts discussed in this section are derived from federal precedents. As such, the Michigan real estate issues described in this article have the greatest commonality with the laws of other states.

<sup>9</sup> *In re John C Lodge Highway*, 340 Mich 254, 262; 65 NW2d 820 (1954).

<sup>10</sup> MCL 213.51(G).

<sup>11</sup> *Detroit/Wayne County Stadium Auth v. Drinkwater, Taylor & Merrill, Inc*, 267 Mich App 625, 705 NW2d 549 (2005).

<sup>12</sup> MCL 213.70; MI Civ JI 2d 90.15.

<sup>13</sup> *Michaels v. Village of Franklin*, 58 Mich App 665, 674; 230 NW2d 273 (1975).

<sup>14</sup> *Highway Comm’r v. Eilender*, 362 Mich 697; 108 NW2d 755 (1961).

<sup>15</sup> *DOT v. VanElsander*, 460 Mich App 127; 594 NW2d 841 (1999).

<sup>16</sup> *In re Grand Haven Highway*, 357 Mich 20, 97 NW2d 748 (1959).

<sup>17</sup> MI Civ JI 2d 90.12.

<sup>18</sup> *State Highway Comm’r v Watt*, 374 Mich 300, 132 NW2d 113 (1965).

<sup>19</sup> MCL 213.70(2).

<sup>20</sup> MI Civ JI 2d 90.12.

## Fixtures and Personal Property

When property is acquired in Michigan, the owner or condemnee may elect to receive the value in place of fixtures. If the owner elects to move fixtures, just compensation includes the cost to detach, move, and reattach the fixtures at a new location (but not in excess of their value in place). Owners are also entitled to moving expenses for personal property.<sup>21</sup>

From an eminent domain perspective, a fixture is an item that is affixed to the realty and therefore condemned along with the realty. If an item will lose substantially all of its value upon removal from the condemned premises, it has been condemned and should be treated as part of the realty. Personal property is comprised of those items of furniture, minor equipment, and other non-realty assets that, although located in the condemned property, do not meet the definition of a fixture by many legal definitions but may in an eminent domain case. In eminent domain, something that is not physically attached may be a fixture if it is “constructively attached,” meaning that “even though it is not physically attached if it is a part of something else that is physically attached, and when the item, if removed, either could not generally be used elsewhere or would leave the part remaining unfit for use.”<sup>22</sup>

Determining what is or is not a fixture has been a problem for a very long time. The words fixture and affixed both imply some type of physical attachment, or annexation to the ground, a building or some other improvement. While annexation is one determining factor, the owner’s intended permanent use of an item is generally accepted to be the most important factor in concluding if that item meets the definition of a fixture.

The value in place of the acquired fixtures is determined by an appraisal that considers the assets as if fully installed, operating and providing utility to the owner’s business. Two approaches can be used to estimate Fair Market value in place: the cost approach and the sales comparison (or market) approach. Under the cost approach, the appraiser first estimates the cost to buy and install a new, identical asset, then deducts depreciation due to physical deterioration and obsolescence. Under the sales comparison approach, the appraiser investigates the amount that similar used assets are selling for in the open market, adjusts those prices for differences in characteristics (such as capacity, age or condition) and then adds the cost of freight, installation, and any other indirect costs required to put the asset into an operating condition. The cost approach can be applied to all types of fixtures, while application of the sales comparison approach is limited to assets that are commonly traded, such as lathes, milling machines, and other machine tools.

The value in place is not meant to indicate what the fixtures would sell for on a liquidation basis. When assets are sold piecemeal to multiple parties, as is and where is (a transaction under the value premise sometimes referred to as value in exchange), the buyer not only ignores the value of foundations, piping, wiring and other components of installation, but also deducts the cost to deinstall and remove each fixture. In addition, specially designed and constructed equipment often has little to no value on the open market. Value in exchange might be useful to the condemnor, indicating the amount it might recover when it ultimately sells the acquired fixtures, but it does not help quantify the condemnee’s damages.

The fixture and personal property appraiser also estimates and reports the cost to detach, move, and reattach each fixture at a new location, which is generally assumed to be reasonably close to the condemned premises. Detach, move, and reattach costs are limited to value in place to avoid making the owner better off than before the taking. Thus, the owner of a very old, extremely large stamping press installed in a deep pit with a heavy foundation is not paid significantly more than the press is worth.

## Business Damages

In 1952, the Michigan Supreme Court held that the lost profits sought in the particular case before it were speculative.<sup>23</sup> Ultimately, that ruling has been expanded to bar all lost profits in condemnation cases, with the courts asserting that they are inherently speculative despite the fact that lost profits are recoverable in other contexts.<sup>24</sup> This is in fact a key difference between eminent domain matters and matters involving commercial damages outside of this context. While lost profits are barred in eminent domain matters, such damages are frequently awarded outside of the context of eminent domain, as long as such damages can be proven with a reasonable degree of certainty.

For example, while a business’s relocation after a taking may result in permanent and reasonably measureable increases in labor and transportation costs, and hence permanent decreases in profits, such damages are not typically recoverable as lost profits in an eminent domain matter. Further, courts often deny claims for damages associated with declines in revenue experienced by a business after a taking, as was the case in *City of Detroit v. Larned Associates*.<sup>25</sup> By comparison, such damages are often awarded in standard contractual and “business tort” matters.

However, instead of obtaining lost profits, businesses may recover the expenses that they incur to avoid lost profits. Recoverable costs to avoid business interruption include items such as

<sup>21</sup> *Wayne County v. Britton Trust*, 454 Mich 608; 563 NW2d 674 (1997).

<sup>22</sup> MI Civ JI 2d 90.20.

<sup>23</sup> *In re Slum Clearance*, 332 Mich 485; 52 NW2d 195 (1952).

<sup>24</sup> *In re Grand Haven Highway*, 357 Mich 20; 97 NW2d 748 (1959).

<sup>25</sup> *Detroit v. Larned Assocs*, 199 Mich App 36; 501 NW2d 189 (1993).

temporary increases in employee costs, costs of moving from the condemned property to a temporary location and then to a permanent location, expenses incurred to avoid losing customers, and increased expenses incurred at a new location.<sup>26</sup>

Such costs may have been incurred by the business as part of its efforts to mitigate (i.e., limit) the impact of taking on the business's ongoing profitability. In fact, compared to cases involving typical contractual and "business tort" damages, costs to mitigate may be of heightened focus in eminent domain matters. Given the established precedent that generally precludes business owners from recovering lost profits in eminent domain matters, business owners may have the increased incentive to incur significant time and costs to limit the ongoing impact to their business, as they may be unable to seek direct recovery of such losses.

In some instances however, property owners can be paid their going concern value if they are unable to relocate. One obvious example is a concession stand with a monopoly at a race track that was acquired and closed.<sup>27</sup> Where an entire neighborhood is demolished, as occurred with the General Motors Poletown facility, going concern value was allowed to a pharmacy in that neighborhood because the business could not be relocated.<sup>28</sup>

Calculating the impact on going concern value will often consider the but-for profit and Cash Flow generating ability of the business as an ongoing entity. Such an analysis may be done by a third-party appraiser or valuation expert. Similar to a lost profits analysis, the analysis will often consider the business's but-for revenues and costs absent the taking, giving consideration to the risk in achieving such Cash Flows. However, such damages are generally only recoverable in cases in which there is no reasonable means to relocate the business.

Michigan's business interruption rules are rather odd, particularly since eminent domain is treated inconsistently with other causes of action within Michigan. Therefore, rules in other states are most likely to deviate from Michigan's when it comes to this subtopic.

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<sup>26</sup> *Id.*; *Detroit v. Larned Assocs*, 199 Mich App 36; 501 NW2d 189 (1993); *Detroit v Hamtramck Cmty Fed Credit Union*, 146 Mich App 155; 379 NW2d 405 (1985).

<sup>27</sup> *Michigan State Highway Comm'n v L&L Concession Co*, 31 Mich App 222; 187 NW2d 465 (1971).

<sup>28</sup> *Detroit v. Michael's Prescriptions*, 143 Mich App 808; 373 NW2d 219 (1985).