

Environmental Law

Environmental Cleanup in Real Property Valuation

Key issues that must be considered when determining a property owner's liability

By James M. Turteltaub

Environmental contamination can have a significant impact on the just compensation received by a property owner in a condemnation case. The treatment of environmental contamination present on condemned property was established by the New Jersey Supreme Court in *Housing Authority of the City of New Brunswick v. Suydam Investors, LLC*, 177 N.J. 2 (2003) and *New Jersey Transit v. Cat in the Hat*, 177 N.J. 29 (2003). These decisions hold property owners liable for environmental remediation costs incurred by the condemnor after the property is condemned. The Court's decision in *Suydam* also established a bifurcated process, which separates the assessment of environmental remediation liability from the determination of just compensation for the condemned property as if the property had been remediated. The Court's decision in *Cat in the Hat*, which permits condemnors to reserve the right to recover present or future costs of remediation from



Turteltaub is a partner at Carlin & Ward of Florham Park. He argued the Suydam case before the New Jersey Supreme Court.

condemnees without being subject to the defenses of res judicata, collateral estoppel, and the entire controversy doctrine.

The appropriate assessment of environmental costs has been evolving since the decisions in *Suydam* and *Cat in the Hat*. There are certain key issues that must be considered

when determining the property owner's appropriate liability.

The first consideration is the highest and best use underlying the property's valuation in the condemnation proceedings. This use may differ from the condemnor's intended use of the property. This is significant because the use of the property effects the appropriate remediation and associated cost. For example, an industrial use could permit the encapsulation of contamination and filing of a Declaration of Environmental Restriction or "deed notice" providing record notice of any conditions or restrictions on the use of the site due to site contamination. (N.J.A.C. 7:26E-8.1 et seq.) A residential use may require the removal of all contamination from the site. The difference in costs could be substantial. The crux of the problem is the proper amount of remediation to be ascribed to the condemned property where the highest and best use is industrial and the condemnor's planned use is residential.

No case has ruled specifically on this particular just compensation issue of whether a property owner's liability should be limited to the amount necessary to clean the property to the use underlying the property's valuation as if remediated. If the property is condemned for a residential use but valued as an industrial property, then the cost of cleanup should be assessed based on remediating the property for an industrial use. If the cleanup cost of the property was held to the more stringent residential standard, the property owner would in essence be required to pay a portion of the condemnor's project cost.

When property is condemned for an industrial

use and valued based on residential highest and best use, this raises a more complicated question. Because the condemnor is only entitled to recover the costs of environmental remediation, the issue is whether the property owner should be assessed the lower actual cost of cleanup or the higher estimated cost of cleanup as per the residential standard.

Another issue complicating the proper assessment of environmental remediation costs is the time required to complete the remediation. A property owner could choose to clean contamination pursuant to a plan completed over several years. In contrast, the condemning agency may need to expedite the cleanup to proceed with its public project. This would increase the net present value of the cleanup costs over a longer remediation. Although not addressed by the courts, the constitutional mandate to provide just compensation should preclude the property owner from bearing the increased present value of the costs resulting from the condemnor's accelerated cleanup.

The determination of appropriate cleanup cost assessment is more complicated when the condemned property is part of a larger cleanup consisting of an assemblage of properties in the same project. Segregating the cleanup costs among the properties could be difficult. It may be necessary to review work records, disposal logs, remedial action work plans, and details of the overall area remediation in order to ascertain the appropriate remediation cost. In these cases, allocation disputes may be costly to resolve.

Establishment of appropriate remediation costs can be complicated further when the costs are estimated by a municipality's designated private redeveloper. Permitting a municipality to delegate environmental testing and the preparation of cost estimates could create a conflict. Private redevelopers are generally motivated by profits. Those profits would be enhanced by reducing property acquisition costs. Given the profit motivation, a private redeveloper might inflate the environmental remediation cost estimates.

These issues will most likely be the sub-

ject of future litigation in which the courts will resolve these and other issues. Recent cases have provided some guidance. For example, the Tax Court's decision in *Metuchen I, LLC v. Borough of Metuchen*, 21 N.J. Tax 283 (Tax Ct. 2004), addressed the valuation using the net present value of estimated environmental costs. In *Metuchen I*, the taxpayer sought to reduce its assessment by the cost of required environmental remediation. In calculating the proper assessment, the Tax Court deducted the net present value of the remaining cleanup costs discounted over the projected cleanup period. The Tax Court also made a deduction for the entrepreneurial overhead and profit associated with the cleanup costs. *Metuchen I* demonstrates how the projected time to complete the cleanup would impact the assessment of environmental liability.

Another relevant aspect of *Metuchen I* was the Tax Court's treatment of a proposed deduction in property value for the "stigma" of environmental contamination. This deduction is similar to the valuation of property "as if remediated" in accordance with the *Suydam* decision. In *Metuchen I*, the Tax Court did not permit a deduction for "stigma" because of a lack of proofs. The Tax Court found the appraiser's opinion to be a "net opinion" and cited his failure to isolate the impact of "stigma" in his comparable sales from the cost to remediate those properties. This opinion demonstrates the difficulty appraisers will have when making the claim that "stigma" reduces the property's value.

In *New Jersey Meadowlands Commission v. Thirteen Group, LLC*, BER-L-7752-02 (Nov. 29, 2006), the New Jersey Meadowlands Commission (NJMC) acquired an open landfill that was inactive for almost 40 years. NJMC estimated the cost to close the landfill was in excess of \$24 million. Notwithstanding the presence of the open landfill, NJMC's complaint contained a waiver of any claim NJMC had against the property owner for potential environmental claims. That waiver did not extend to third parties. The property owner then appraised the property as if the

landfill were remediated. NJMC rebutted this appraisal by seeking to present evidence of the cost to remediate the landfill remediation at trial. Following *Suydam*, the court would not permit NJMC to introduce evidence of cleanup costs. Instead, NJMC was permitted to amend its complaint and seek the costs of remediating the landfill in a separate proceeding.

Borough of Paulsboro v. Essex Chemical Corporation (A-6577-05T5), decided on July 13, addressed issues related to the valuation of a condemned closed landfill site. The property owner objected to the taking by claiming the borough's offer of just compensation did not properly value the property (N.J.S.A. 20:3-6). The condemnor's offer of just compensation was based on an appraisal which deducted an amount to reflect the property's limited utility caused by the closed landfill. Relying on *Suydam*, the property owner argued the landfill constituted an environmental condition which should have been valued as if remediated. The property owner was concerned that the borough might be permitted to deduct the cost to deconstruct and clean the closed landfill in the valuation proceeding and then recover that amount in a cost recovery proceeding. The court doubted the borough could deconstruct the landfill and, if it did, whether the property owner would be liable for that cost under *Suydam* and *Cat in the Hat*. Therefore, based on the possibility the landfill could limit the property's utility, the court found the borough's appraisal satisfied the bona fide negotiations requirements set forth in N.J.S.A. 20:3-6.

Balancing the property owner's obligation for environmental remediation costs with the right to just compensation is complex. The correct cost allocation depends on the specific facts of each case. Practitioners should use qualified environmental experts and real estate appraisers with a strong knowledge of the environmental laws to help achieve the best result. Although many of the disputes will be resolved by negotiated settlements, the complexities of this subject will require additional guidance from the Court. ■