10-1-2005

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ARE PROPERTY OWNERS CONSTITUTIONALLY ENTITLED TO COMPENSATION FOR ENVIRONMENTAL REMEDIATION FUNDS?

Andrew Hysell*

I. SUMMARY & CONCLUSION.

In the case of Northeast Connecticut Economic Alliance, Incorporated v. ATC Partnership (Northeast II), the Connecticut Supreme Court upheld a superior court’s decision to consider the value of grants and third party remediation funds in the context of calculating just compensation for a condemnation of polluted property. Despite a contrary California appeals court decision, Northeast II’s conclusion is supported by law and fact. Because remediation funds have value to a disinterested buyer, they should increase property’s market value by an amount that includes reductions for any risks associated with rehabilitating polluted land. Takings law permits the consideration of prospective events to affect current property value if those events are reasonably likely to occur in the near future. If a market as a practical matter does not value remediation funds, courts may modify their analysis in order to avoid materially unfair compensation.

II. FACTS

The plaintiff in this case, the town of Windham, exercised eminent domain over a piece of real property known as Windham Mills, located within the town’s boundaries.¹ For over a century, the Windham Mills property was owned by American Thread and was

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¹ See Ne. Conn. Econ. Alliance, Inc. v. ATC P’ship (hereafter Ne. II), 861 A.2d 473, 483-84 (Conn. 2004).
used for the manufacture of textiles. The property suffered from significant pollution as a result. The Plaintiff, believing the property to be virtually worthless because of its environmental damage, filed a statement for compensation of one dollar for the “fair market value” (FMV) of the property. Defendant owner, ATC Partnership, disagreed with the property’s valuation and initiated suit.

After consideration, the superior court awarded the Defendant $1.675M and both parties appealed. On appeal, the Connecticut Supreme Court ruled that assessing a property’s FMV, including factors such as the effect of environmental damage and remediation costs, was within the purview of the trial court. However, the Northeast I majority held that the trial court erred as a matter of law in its exclusion of evidence of environmental damage and remediation costs from the calculation of the FMV. The Supreme Court rejected the categorical assertion that pollution under no circumstances alters the market price of real property. Therefore, the trial court could not dismiss the costs to cure environmental degradation without first examining the property in question.

The case was remanded to the superior court for a new trial. The trial court used the sales comparison approach to calculate the FMV of the property. According to the court, “for a sale to be ‘comparable,’ it should be of the ‘same kind’ as the subject property” with adjustments for any differences. To compare the

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2 See id. at 483.
3 See id.
4 See id.
5 See id. at 1080. The cost to cure could not be excluded automatically.
6 See id.
8 The comparative sales approach has long been an approved method for ascertaining the FMV of property. See Ne. Conn. Econ. Alliance, 2003 WL 553265, at *6 n.22.
9 See id; see also Sibley v. Middlefield, 120 A.2d 77, 80-81, n.22 (Conn. 1956). It is interesting to note that the American Jurisprudence Trials states that “the comparable sales technique is often impracticable” in the case of a polluted property due to factors like “the complexity of cleanup technologies, conflicting
property to clean land, the court included in its calculation the cost of ameliorating the property's pollution as instructed by the Supreme Court. The cost to cure was substantial and would have otherwise reduced significantly the FMV of the property. However, the superior court also made the following findings of fact:

1) A buyer would seek all potential funds available to defray environmental costs;

2) $3M had been approved in clean up grants and $200K had already been spent. American Thread had assumed liability for environmental cleanup under the Comprehensive Environmental Response, Compensation, and Liability Act (CERCLA) and;

3) Eighty percent of the property's environmental damage could be offset by potential remediation grants and third party contributions.

In the court's view, the combined value of the remediation grants available to a hypothetical buyer and possible third party contributions offset the remediation costs for the property. Therefore, the trial court added back the reduction of Windham Mill's market value caused by its pollution. Based on these sources of remediation, the trial court concluded the property's FMV at the time of the taking to be $1.75M. With ten years of interest—the time period of the litigation—the award totaled $4M.

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13 See id.
14 See id. at 9.
15 See id. at 8; see also Comprehensive Environmental Response, Compensation, and Liability Act, 42 U.S.C. §§ 9601-9675 (2002) [hereinafter CERCLA].
16 See id. at 9.
17 Ne. Conn. Econ. Alliance, Inc., 2003 WL 553265, at *9. The trial court found that 80% of remediation costs could be recovered by a hypothetical buyer.
18 Ne. II, 861 A.2d 473, 477 (Conn. 2004).
Plaintiff appealed, arguing that the inclusion of remediation grants and third party liability was improper. First, they claimed that remediation funds were too speculative to increase the market value of environmentally distressed property. A disinterested buyer would not pay more merely for a promise to money. Second, the Plaintiffs argued a private owner would be ineligible for the $3M grant awarded to the original ATC/Windham partnership. Because the FMV analysis considered a sale between private parties, only those grants available to a private party were relevant. Finally, the Plaintiff contended that the trial court mischaracterized potential third party contributions and remediation grants as rights running with the land as a matter of law. Because these funds were not a component of the property interest in a strictly legal sense, the Plaintiff contended that ascribing any value to them was improper.

The Connecticut Supreme Court rejected each of the Plaintiff's arguments and upheld the inclusion of remediation grants and third party contributions in the assessment of Windham Mills’ FMV. The Court found as a matter of law that the consideration by the superior court of “potential recovery of cleanup costs [both remediation grants and third party contributions] in calculating the property’s FMV . . .” was proper. In the Court’s view, “[Grant] moneys could only enhance the value of the property in the eyes of a reasonable prospective buyer.” Further, the fact that the trial court had made an error concluding that CERCLA liability “ran with the land” was deemed harmless because, even if the liability did not run with the land, “a variety of meritorious claims and defenses would [still] present legitimate issues for litigation” for a new owner. The Supreme Court therefore refused to find that the

19 See id. at 478.
20 See id. at 482.
21 See id.
22 See id. at 482, 487.
23 See id. at 488.
24 See id. at 486-87, 492.
25 See id. at 491.
26 See id. at 486.
27 Id. at 492
lower court’s inclusion of these factors was unreasonable. Finally, the Supreme Court considered the Plaintiff’s complaint that the $3M grant was available only to a public entity. The Supreme Court apparently agreed, but noted that a new buyer could enter into a similar public/private partnership. Because remediation grants would be accessible to a new buyer through such a partnership, the Supreme Court held that the lower court had acted “well within its discretion by considering the availability of state grant funds in the calculation of FMV.”

Once the trial court’s consideration of remediation was approved, the Supreme Court reviewed and concluded that the trial court’s conclusions of fact did not constitute an abuse of discretion. The Supreme Court held that the lower court’s valuation of these funding sources was reasonable. It refused to disturb the evidentiary findings of the trial court because of a “broadly inclusive approach endorsed...in the context of property valuation” that reflected “the deference” afforded to a trial court’s conclusions about issues in the context of determining FMV.

While the Northeast II decision deals only with the issue of compensation and does not address the scope of eminent domain, it will have the practical effect of reducing the frequency of takings. In Connecticut, an exercise of eminent domain over polluted property suddenly has the potential to be very expensive. As a result, the environmental policy underlying remediation grant programs and third party liability statutes like CERCLA could be frustrated. Municipalities may find themselves in the strange situation of compensating private owners for grant funds bequeathed to an owner from the public treasury. Governments therefore may choose to forgo development plans involving eminent domain due

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28 See id. at 492. The Court noted that the former owner was strictly liable for repayment of remediation costs under federal law.
29 See id. at 488, n.16.
30 See id.
31 See id.
32 See id. at 488, 492.
33 See id. at 488, 491. The trial court did not “abuse its discretion.”
34 See id. at 490-911.
35 See id. at 484.
36 State funding may be used for cleanup of polluted property.
to the expense despite a strong public interest supporting a particular condemnation. Further, legislatures may consider restricting existing environmental remediation grant programs, especially in instances involving possible future condemnations. If other states follow suit, similar effects could be seen around the country.

The significance of the *Northeast II* decision warrants a review of its conclusion and its underlying reasoning. The court did not provide an expansive explanation for its decision. Therefore, it is useful to consider the opinion of a different court that conducted an extensive analysis of valuation remediation funds within the context of a FMV calculation. The California Appeals Court’s decision in *Mola Development* excluded remediation from a FMV analysis. *Mola Development* involved the valuation of property for state taxation purposes, not compensation for takings. However, as the Plaintiffs in *Northeast II* realized, the basic model of a hypothetical market transaction is common to both a California tax assessment and a calculation of just compensation. Therefore, *Mola Development*’s rationale for the exclusion of remediation funds from FMV may be relevant to a takings analysis.

**III. ANALYSIS**

**A. Mola Development Corp. v. Orange County Assessment Appeals Board** holding: Remediation grants should not be considered in the calculation of FMV.

Prior to *Northeast II*, the question of whether the value of remediation funds may properly be included in the calculation of FMV for the purpose of a takings apparently had not been directly addressed by a court anywhere in the country. Without an authority to bolster their argument, the *Northeast II* plaintiffs relied upon a California appeals court decision regarding property valuation for taxation purposes to oppose the inclusion of remediation funds in the

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37 *Northeast II* essentially forces government to compensate a property owner for an expenditure of public funds via a bond program. Governments may rethink their remediation grant programs as a result.

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39 *Ne. II*, 861 A.2d 473, 485.
calculation of FMV.\textsuperscript{40} \textit{Mola Development} involved a taxpayer challenge of an assessment appeals board’s decision that included the value of environmental remediation funds in the valuation of polluted, non-income producing land for taxation purposes.\textsuperscript{41} The \textit{Mola Development} court disagreed with the board’s decision and rejected as a matter of law the inclusion of remediation funds because, in its view, those funds had virtually no market value and were legally distinct from the property.\textsuperscript{42}

The court began by first referencing California’s constitutional mandate to value property for taxation purposes according to fair market value.\textsuperscript{43} To ascertain a meaning for FMV, the court looked to the relevant California tax code prescription for assessing a property’s value for taxation purposes. Section 110, subdivision (a) of the California Tax Code defined FMV to mean “the amount of cash or its equivalent that property would bring if exposed for sale in the open market under conditions in which neither buyer nor seller could take advantage of the exigencies of the other, and both the buyer and the seller have knowledge of all the uses and purposes to which the property is adapted and for which it is capable of being used, and of the enforceable restrictions upon those uses and purposes.”\textsuperscript{44} The Court ultimately concluded that under this definition, remediation funds should not be included in a property’s FMV.\textsuperscript{45}

To reach its conclusion, the court first eliminated any potential policy arguments in support of remediation valuation on the grounds that anything beyond a rigid FMV analysis was constitutionally impermissible. The court noted that in California and other states, property valuation for taxation purposes was a strictly legal

\textsuperscript{40} See id. at 486.
\textsuperscript{42} See id. at 559.
\textsuperscript{43} CAL. CONST., Art. XIII, §1, (a) (“All property is taxable and shall be assessed at the same percentage of fair market value.”).
\textsuperscript{44} Mola Dev. Corp., 95 Cal. Rptr. 2d at 552 (quoting Cal. Rev. & Tax. Code § 11D(a) (Deering 2005)). Note the court assumed the constitutional fitness of this tax provision, not questioning whether the FMV formula defined in §110 was sufficient to ascertain the FMV requirement found in Article XIII of the California State Constitution.
\textsuperscript{45} See Mola Dev. Corp., 95 Cal. Rptr. 2d at 559.
Questions of whether a valuation model would promote the cleanup of polluted property generally or would ensure an owner recouped his reasonably expected investment were therefore irrelevant. The court went so far as to excuse itself preemptively from culpability for negative policy consequences resulting from its decision, reiterating the constitutional character of FMV precluded anything beyond a strict legal analysis.

*Mola Development* also concluded that remediation funds did not increase the market value of polluted land. That position is extreme in the sense that it rejects placing any value on what is essentially cash money available to a potential buyer. The court reached its determination in three steps. First, it focused exclusively on the risks and pitfalls of purchasing polluted property from the perspective of an objective buyer. These disadvantages included (1) the risk of partial or complete failure in an attempt to remediate, (2) the possibility of a property acquiring a negative “stigma” that remains despite the property’s rejuvenation, and (3) potential exposure to the “draconian realities of CERCLA liability.” In total, the court found these drawbacks so severe they cast serious doubt on the assertion that an ordinary buyer would pay more for polluted land that carried with it a right to remediation.

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46 *See id.* at 551-52. The *Mola Develop.* court noted that other state supreme courts, including those in Massachusetts and New Jersey, adopted a similar viewpoint. These state courts agreed that “considerations of public policy” were not meant for matters of property tax valuation because of the “constitutional mandated focus on value is a matter independent of public policy.” *See id.*, *see also* Inmar Assoc’n, Inc. v. Borough of Carlstadt, 549 A. 2d 38 (N.J. 1988) and Reliable Electronic v. Bd. of Assessors, 573 Ne. 2d 959 (Mass. 1991).

47 *See Mola Dev. Corp.*, 95 Cal. Rptr. 2d at 550.

48 “If environmental cleanup laws have the unintended consequences of lowering the market value of commercial real property for tax assessment purposes, then that is what they do, for better or worse.” *Id.* at 559-60.

49 “The idea that a prudent buyers might be willing to lessen the discount that they would demand on sale of the property in light of the fact that parties other than the seller might also have to contribute to the cleanup costs simply does not accord with market reality....” *Id.* at 557-58.

50 *See id.* at 553-54.

51 *See id.*

52 *See id.*

53 “[U]nder any standard pegged to what buyers and sellers do in an open market, it is almost impossible to imagine prudent buyers not demanding at least
Second, any value that polluted land in conjunction with remediation funds had above and beyond polluted land with no funds, the court explained, was purely subjective to the seller. According to Mola Development, an owner was ultimately “stuck” with the responsibility of pollution remediation, while a buyer had no corresponding obligation. The seller thus benefited from remediation funds in a manner that the buyer did not. The court cited an axiom of property valuation that market value must be assessed in a manner excluding the “peculiar circumstances of the seller.” The court viewed remediation funds as something outside the “value to potential purchasers generally, and the normal uses to which potential purchasers could put it.” Through the application of a strict FMV analysis—as the court insisted repeatedly was required under Article XIII—anything not valued by a regular buyer was irrelevant to assessing a property for taxation purposes.

Finally, the court rejected assessing a dollar value to remediation funds that a buyer would acquire and a seller would lose through the transfer of ownership of the contaminated property. The court considered the remediation funds an intangible interest that had no legal connection to the land. Therefore, even though the buyer would receive an extra benefit from remediation funds, the value of those funds was legally separate from the value of the property. The court analogized that giving a subsequent buyer indemnification through CERCLA was the equivalent of handing over the deed along with a “blank check.” The remediation funds

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a dollar-for-dollar deduction of cure costs-reduced, of course, to present value.” See id. at 554-55.

54 See id. at 558.
55 See id.
56 “Buyers only care that they don’t pay them.” Id. at 548.
57 See id. at 548-49.
58 See id. at 558 (quoting Pacific Mutual Life Ins. Co. v. Orange County., 187 Cal. App. 3d 1141, 1148). This principle is well established within the realm of calculating just compensation for takings.
59 See id. at 557.
60 See id. at 558-59.
61 See id. at 559.
62 See id. at 557.
available—the blank check—was a distinct property interest from the land and thus had no relevance to the property’s value.63

The Plaintiffs in Northeast II cited Mola Development’s conclusion as applicable to the assessment of FMV in a takings environment.64 They argued that because remediation funds were an entirely separate interest whose value was severely compromised in the eyes of a prudent buyer, a purchaser in a market transaction would not pay more than the polluted value for a property.65 Without market value, a potential remediation grant therefore should not be included in FMV the Plaintiff contended.66

As previously mentioned, the Connecticut Supreme Court flatly rejected Mola Development’s conclusion. The Court declared that it historically had taken a “broad view” of the factors relevant to FMV.67 According to the Court, evidence of both cost to cure and remediation funds therefore could be admitted within this broad scope and the trial court would then give it the “proper [evidentiary] weight.”68

At first, a reasonable person might find the idea of compensating an owner for remediation funds entirely unreasonable. However, after considering flaws in Mola Development’s hypothetical market transaction, it appears likely that markets would in fact value remediation. But, even if a market viewed remediation funds to lack any objective value, the principles of takings jurisprudence extend a FMV analysis beyond the confines of the California constitution. Issues of fundamental fairness can prompt a court to modify or abandon a FMV analysis in order to achieve just compensation.

B. Mola Development’s FMV analysis of polluted property mischaracterizes the interest of a hypothetical buyer and ignores the compulsion of a hypothetical seller to sell.

63 See id.
64 Ne. II, 861 A.2d 473, 486 n.18 (Conn. 2004).
65 See id. at 481-82.
66 See id.
67 See id. at 487 n.18 (citing Andrews v. Cox, 17 A. 2d 507 (Conn. 1941)).
68 See id. at 487 n.18.
1. The court incorrectly assumed that a hypothetical buyer only seeks clean land, therefore incorrectly concluding remediation funds are irrelevant to a FMV analysis.

Remediation funds should have objective value to a hypothetical purchaser interested in making profits because remediation tends to improve the value of polluted property. Funds, when used to implement environmental rehabilitation programs, usually improve the quality of land. For higher land quality results in improved uses and increased economic value. Short of a market failure, a self-interested buyer should consider the availability of remediation funds to add something to the value of polluted property. How can two polluted pieces of property—one with access to millions of dollars for its cleanup and the other with no claim to anything—be valued identically by a rationale market?

Acknowledging that remediation funds improve the value of land contradicts Mola Development's assertion that prior to their use the funds are worthless to a prospective buyer. This contradiction springs from an assumption central to Mola Development's FMV analysis: the court assumed a hypothetical buyer was only

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70 Wisconsin Brownfields Program reported a potential $227M increase in taxable property values from remediation grants and 507 acres of land returned to productive use. See BROWNFIELDS, INFO. ON THE PROGRAMS OF EPA AND SELECTED STATES, U.S. GEN. ACCOUNTING OFFICE, 67 (GAO-01-52) (Dec. 2000) [hereinafter Brownfields].

71 "Market failure is defined as the inability of markets to reflect the full social costs or benefits of a good, service, or state of the world. Therefore, when markets fail, the result will be inefficient or unfavorable allocation of resources." MARLIES WIERENGA, ELAW, A BRIEF INTRODUCTION TO ENVIRONMENTAL ECONOMICS 1 (Aug. 2003), available at http://www.elaw.org/assets/word/What%20is%20environmental%20economics%20%2D%202.doc (last visited Jan. 5, 2006).

interested in purchasing clean land. Based upon that misconception, the court reasoned that clean alternatives to the polluted property would virtually erase any market value for remediation funds. Because of the risks and costs associated with remediation, a reasonable buyer seeking clean land would ignore the existence of remediation funds and simply pick a clean alternative. Mola Development's narrow characterization of a hypothetical buyer's interests skewed its FMV analysis to the point where the court essentially concluded that access to free money was worth nothing.

Contrary to the court's assumption that buyers only seek clean property, there are private parties interested in purchasing polluted land in hopes of rehabilitating and then either selling the property at a profit or putting the land to a higher economic use. While some purchasers will not have any interest in polluted land, others may actually seek out distressed property in hopes of making a profit through its acquisition and subsequent rehabilitation. Anything that makes environmental cleanup cheaper, or possibly even free, is of substantial value to such a developer. Polluted

73 "[O]ne under no 'exigencies' forcing it to bargain for the property, can save itself a tremendous headache simply by buying uncontaminated property." Id. at 553.
74 See id. at 552-54.
75 See id. at 553 (noting that the "draconian consequences" of CERCLA liability would literally scare away investors).
77 For example, a company seeking to build a corporate headquarters would not be interested in the delay or the speculation of remediation. However, a speculative developer, hoping to buy inexpensive land, rehabilitate it, and then construct condominiums, might actually seek out brownfields that have access to environmental clean up funds.
78 Remediated brownfields become useful for economic development - creating new jobs. See Jerome S. Chudzik, Graef, Anhalt, Schloemer & Associates, Inc., Brownfields And The Teeter-Totter Principle (2001), http://www.brownfields2002.org/proceedings2001/CV-07-01.pdf (last visited Jan. 5, 2006); see also Heather Todd, State environmental program helps owners raise value of property in short time, SAN ANTONIO BUSINESS JOURNAL, JULY 17, 1998, at 1 ("Created two years ago by the Texas Natural Resource Conservation Commission (TNRCC), the Voluntary Cleanup Program (VCP) is encour-
land that can be purchased for less than the price of clean land and be remediated through the expenditure of someone else's money should be valued above and beyond what the market will pay for polluted land sans funds.

The billions of dollars disseminated under federal, state, and local government remediation programs is convincing evidence that private markets value remediation funds. One Connecticut agency alone “provides up front cash grants up to $10 million to investors, developers and business owners who undertake redevelopment projects” of brownfields. The purpose of a grant under programs like these is to create an economic incentive for private investors to purchase a polluted property they otherwise would not. As these grants entice buyers to encumber themselves with less than environmentally pristine land, the logical conclusion is that remediation funds have some measurable, objective market value.

In Housing Authority v. Suydam Investors, the New Supreme Jersey court implicitly recognized that remediation funds, because they objectively improve polluted land, have market

aging the remediation of polluted land while simultaneously boosting the Texas real estate market.”), available at http://www.bizjournals.com/ sanantoniostories/1998/07/20/focus1.html (last visited Jan. 5, 2006); See also U.S. E.P.A., BROWNFIELDS REDEVELOPMENT EFFORTS ARE BIG IN THE HEART OF DALLAS 2 (“[B]rownfields restoration successes within Dallas include a former pipe manufacturing plant that became a pallet recycling facility, creating 35 jobs while retaining 60 others, and a former municipal landfill that was redeveloped into a 15-acre plaza for restaurant, hotel, and office/warehouse.”), available at http://www.epa.gov/brownfields/pdf/ss_dalla.pdf (last visited Jan. 5, 2006).

See U.S. E.P.A., BROWNFIELDS CLEANUP GRANTS (“Cleanup grants provide funding for a grant recipient to carry out cleanup activities at brownfield sites. An eligible entity may apply for up to $200,000 per site.”), available at http://www.epa.gov/oswer/cleanup/funding.htm (Last visited Jan. 5, 2006).


The Supreme Court held that polluted property should be valued as if its contamination had been removed. The condemner would have the option of initiating a separate action for clean-up costs and, hypothetically, these costs could be offset by remediation grants and third party contributions. The rationale for automatically valuing polluted land as clean and then requiring the government to sue for remediation, is the belief that remediation will in fact restore the land’s value.

Indemnification agreements can also “lessen the diminution in value associated with the contamination” by providing a source of funding to offset rehabilitation costs. If someone with the capacity to pay is legally required to remediate a property’s pollution, a buyer has access to resources from somewhere other than grants. In contrast, Mola Development viewed potential CERCLA liability as something a buyer would fear, noting that the statute can implicate subsequent nonpolluting owners in certain circumstances under a theory of strict liability. While the reach of CERCLA is not something to be trifled with, developers can take preemptive steps to protect themselves. In addition, buyers are able to take shelter within statutory carve-outs from environmental liability made contingent upon their purchase of a polluted property.

CERCLA liability, if assessed on a prior owner who has financial liquidity, in reality is an economic opportunity to a new owner. For example, in Northeast II, the prior owner-manufacturer had admitted liability under CERCLA. Instead of the law burdening the property, it provided the new owner with an additional source of remediation funding to help clean the property.

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83 See id. at 676.
84 See id.
87 See CERCLA, supra note 14, at 101(35) (“innocent landowners” exempted from liability).
88 See Brownfields, supra note 68, at 40. Massachusetts Brownfield Program “provides statutory liability protection to parties that did not cause or contribute to the contamination at a site.” Id. at 52, 59 (describing similar liability protection applicable in New Jersey and Pennsylvania for those who perform cleanups).
2. *Mola Development*’s FMV analysis involves a seller that is disadvantaged relative to a buyer.

The model hypothetical market transaction is a tool used by courts to calculate property value for purposes of compensation and taxation. The goal behind this valuation exercise is to reconstruct the kind of transaction that would occur naturally in a sale of private property within the context of a free market. To create a transaction that mirrors reality, a court must review past transactions as well as current market conditions. The court must then apply what it has learned from its review to the specific facts of the property’s value being adjudicated. In the analysis, the court essentially must put itself in the shoes of a buyer and seller and judge how they would bargain.\(^8^9\)

For the hypothetical transaction to mirror the market and generate an accurate property value, the relative positions of the buyer and seller must be balanced. The integrity of the market transaction therefore requires consideration of a willing buyer and a willing seller, neither of whom have any unusual advantage or vulnerability.\(^9^0\) A transaction where a seller is subordinated to a buyer fails to meet this standard. When the actions and interests of a seller are given less regard vis-à-vis the buyer, the judicial analysis will likely result in an undervaluation of the property.

In the case before it, *Mola Development* applied a hypothetical transaction to gauge FMV that put a seller in an inferior position relative to a hypothetical buyer. Courts have characterized a "willing seller" to be one that is under no duress to sell, including the *Mola Development* court itself.\(^9^1\) However, *Mola Development* was not true to its own rhetoric, applying a transaction where the seller was forced to offer his property for sale prior to the use of remediation funds. Because the court refused to permit any valuation of remediation funds prior to their use, the transaction used by

\(^9^0\) 60 AM. JUR. Trials 447 §5 (2005).
\(^9^1\) See Mola Dev. Corp. v. Orange County. Assessment Appeals. Bd., 95 Cal. Rptr. 2d 546, 547 (2000) (a transaction must consider a seller who is not under ‘any compulsion’ to sell); see also Olson 292 U.S. at 257.
Mola Development was one where a “buyer could take advantages of the exigencies of the other.” The seller suffered from an exigency—the inability to remediate prior to the sale within the context of a hypothetical marketplace that did not value remediation funds.

Mola Development rationalized any unfairness of its valuation formula by claiming it could not rightfully consider issues of public policy in a narrow FMV legal analysis. What the court misunderstood was that its FMV formula—regardless of any public policy issues—failed to meet the basic requirements of a self-interested market transaction. The timing of the valuation preempted the expenditure of remediation funds and therefore the model transaction essentially featured a seller under duress. As such, the seller’s position was the very proverbial barrel that neither party is supposed to find themselves over in a voluntary transaction. Because the hypothetical market transaction applied by the court was flawed, its ability to render an accurate FMV was compromised.

The effect of the seller’s exigency is acute when viewed in the case of Windham Mills. ATC Partnership, in the court’s view, had likely access to substantial sums of remediation funds both through a state grant and established third party CERCLA liability. A rationale actor, assuming a market would not value those funds at all, would first use them to ameliorate pollution before it sold the property. Mola Development’s own argument that a hypothetical buyer would not view remediation funds as having value supports the proposition that any self-interested seller would first clean up polluted land with free money before putting it on the market. Not doing so, in the opinion of the Northeast II plaintiffs, made a large parcel of land worth one dollar.

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92 Mola Dev. Corp. 95 Cal. Rptr. 2d at 547-48.
93 See id. at 551.
94 See id. at 547-48.
95 Hous. Authority v. Suydam Investors, 826 A.2d 673, 680-81 (N.J. 2003) (New Jersey court interprets 5th Amendment and New Jersey state constitution to require a market transaction where neither the seller or buyer are “under any compulsion to act.”)
96 Northeast II, 861 A.2d 473, 478 (Conn. 2004). How a future event can be considered is explained later.
3. Risk should not act to bar the valuation of remediation funds, but should instead reduce their worth to a hypothetical buyer and thereby reduce compensation to the owner.

*Mola Development* argued that, even if there was some expectation of improvement in the quality of polluted real property, no reasonable buyer would pay extra for polluted land even with access to remediation funds due to the risk and uncertainty associated with remediation attempts and possible residual stigma. This assertion has some validity because a prudent buyer, without any accommodation, might find the risk and administrative hassles of buying polluted property prohibitive, even with access to remediation funds. However, risk alone does not automatically deter a buyer if a discount in price is offered to offset potential downsides of remediation. A discount for risk essentially makes the existence of that risk more palatable to investors.

Markets adjust for risk through discounting instead of simply jettisoning transactions. The practice of discounting for risk and inconvenience is seen when bad loans are purchased for pennies on the dollar by collection agencies and high insurance premiums are issued for equally high-risk drivers. In a similar fashion, if remediation funds exist to clean fouled land and such expenditure would likely increase the land's value, a rationale market should ascribe *some* value to those funds. The risks associated with a planned remediation project should not automatically preclude its consideration, but instead reduce to a degree its impact on the property's value. It is reasonable to assume a buyer would pay

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97. See *Mola Dev. Corp.* at 318. See also Roger Beers, *Stigma Damages in Property Contamination Cases*, [http://www.rbeerslaw.com/stigma.html](http://www.rbeerslaw.com/stigma.html) (“Now they can't sell their property - except to speculators who are betting that the "stigma" will disappear with time.”).


99. Christopher Serkins, *See the Meaning of Value: Assessing Just Compensation for Regulatory Takings*, 99 *Nw. U. L. Rev.* 677, 691 (2005). (“[E]xpanding and contracting the anticipated development costs that would be necessary to create the property's highest and best use will shift the burden of those risks of development in a hypothetical transaction between a willing buyer
for the right to access remediation funds if given a deduction for the associated risks and expense of cleaning the property.

Courts have the ability to calculate a discount for risk and apply that discount to reduce a property’s highest economic value. For example, Christopher Serkins explains that where a condemned property’s highest value is calculated, future development of that property with a discount for risk can be considered.\textsuperscript{100} Serkins notes that the property’s best use value should deduct both the costs of development as well as \textit{the risks associated with development} [italics added], including “environmental hazards, cost overruns, unscrupulous contractors . . .”\textsuperscript{101} In other words, “[t]he baseline rules about who bears development risk are reflected in the property’s fair market value, and therefore affect compensation.”\textsuperscript{102}

\textbf{4. Intangible factors that are not part of land in a legal sense frequently affect the market value of real property.}

\textit{Mola Development} did entertain the possibility that under some circumstances, polluted land with a right to remediation funds might fetch a nominally higher price than simply polluted land standing alone.\textsuperscript{103} Therefore, in order to justify the complete exclusion of remediation in light of the possibility of some market value, the court stressed the “separateness” of the funds in a legal sense from the land itself.\textsuperscript{104} In \textit{Mola Development’s} view, the funds were a distinct legal interest and therefore could not properly be characterized as part of the property.\textsuperscript{105} Because the funds were

\textsuperscript{100} See \textit{id.} at 690.

\textsuperscript{101} See \textit{id.} at 691; see \textit{id.} at 692.

\textsuperscript{102} See \textit{id.} at 691. \textit{See also id.} at 692.


\textsuperscript{104} See \textit{id.} at 558-59.

\textsuperscript{105} See \textit{id.} at 557-59.
not a legal right running with the land, a separate contract would be required to bequeath them to a purchaser. 106

The flaw with this argument is that many intangible factors—characteristics that do not run with the land in a legal sense—have been recognized by courts to affect the market value of real property. 107 Future zoning changes and the likely prospect for development, while not legal rights in any sense, amount to value in the eyes of a buyer. 108 If a market ascribes additional value to a piece of land, that fact in and of itself warrants inclusion. The ethereal nature of a factor that removes it from the basket of rights formally associated with a piece of real property is therefore irrelevant. It should be included in the FMV analysis because what the market will bear for the property has increased as a result of its existence.

Consider a private party wishing to purchase a piece of land and assume normally polluted property is worth $10 per acre. However, this particular brown field has a near certain claim to a $1M grant that, when spent over the course of one year, will likely render the land suitable for residential development. As developed property, the land is worth $1000 per acre. A rational buyer with a desire to develop would measure risks and costs and then, based on calculations, ascribe some additional value to polluted land for its claim to the $1M.

C. Articulating a legal rationale for the inclusion of remediation funds to assess just compensation.

Based upon the preceding analysis of the arguments underlying the Mola Development decision, it is apparent that a hypothetical market transaction should not, as a rule, exclude the value of remediation funds. Remediation funds have the potential to improve the objective value of land. This potential improvement is foreseeable and any risk associated with its achievement can be

106 See id. at 557.
107 See id. at 557-58.
108 See Peter Rock Assoc. v. Town of North Haven, 756 A.2d 290, 335 (Conn. 2000) (citing Minicucci v. Comm’r of Transp., 559 A.2d 216 (Conn. 1989)).
discounted. Ultimately, the potential to improve land with remediation funds is an opportunity for a disinterested buyer to make money and the fact that the remediation funds are not part of the land legally does not preclude their valuation within the context of a market transaction.

Upon concluding that a market should value remediation funds, the next step is to integrate that understanding into existing takings jurisprudence. Two issues previously discussed need to be addressed. First, future remediation is an event that has not occurred at the time of takings. It is necessary therefore to consider how takings law treats future events in determining just compensation. Also, not every market is efficient. In the case of an inefficient market, remediation funds may be undervalued. It needs to be resolved what flexibility a Connecticut court has beyond a strict FMV analysis.

1. Just compensation and how courts define it.

The Fifth Amendment's just compensation clause bars government action that has the effect of "forcing some people alone to bear public burdens which, in all fairness and justice, should be borne by the public as a whole."\(^\text{109}\) The United States Supreme Court has held that just compensation requires that "no private property shall be appropriated to public uses unless a full and exact equivalent for it be returned to the owner,"\(^\text{110}\) with the qualification that a property owner "be made whole but is not entitled to more."\(^\text{111}\) To ensure fair compensation is paid, the property's best, most lucrative use is considered.\(^\text{112}\) However, an owner's own par-


\(^{111}\) Olson v. United States, 292 U.S. 246, 255 (1934); see also U.S. v. General Motors Corp., 323 U.S. 373, 379 (1945) ("[T]he owner must be put in as good position pecuniarily as if his property had not been taken.").

\(^{112}\) 60 AM. JUR. Trials 447 §8 (2005).
ticular special purpose that cannot be translated into objective value for a hypothetical buyer is removed from consideration.\footnote{General Motors Corp., 323 U.S. at 383 (describing a business person's good-will as not translatable to another and therefore not affecting market value); see also U.S. v. Commodities Trading Corp., 339 U.S. 121, 130 (1950) ("The general rule has been that the Government pays current market value for property taken, the price which could be obtained in a negotiated sale, whether the property had cost the owner more or less than the price.").}

The Connecticut Constitution has also been interpreted to provide similar protections in the context of takings, requiring that "just compensation" be paid where a person is deprived of real property through a governmental exercise of eminent domain.\footnote{See U.S. CONST. Amend. V; see also CONN. CONST. art. I, §11.} Connecticut courts have adopted a measure of FMV that mirrors federal and other state jurisprudence, saying valuation equals a market transaction where "a willing buyer would pay a willing seller based on the highest and best possible use of the land assuming that a market exists for such an optimum use."\footnote{Gray Line Bus Co. v. Greater Bridgeport, 449 A.2d 1036, 1042 (Conn. 1982); see also Ne. II, 861 A.2d 473, 481-82 (Conn. 2004) (noting that the probability of property being put to its most valuable use is also considered).} In addition, "the loss to the owner from the takings, and not its value to the condemner, is the measure of damages to be awarded in eminent domain proceedings."\footnote{See Ne. II, 861 A.2d at 481-82.} The court also has said just compensation requires that a market value be paid for a property that evaluates the land's best use at the time of the taking.\footnote{See Melillo v. New Haven, 732 A.2d 133, 136 (Conn. 1999); see also Tuchman v. State, No. CV030472731S 2003, WL 22078674 at *13 (Conn. Super. Ct. 2003); see also Tuckel v. Town of Southbury, 172 A. 222, 223-24 (Conn. 1982) ("Both the Connecticut and the federal constitutional provisions limit the right to compensation to those instances in which there has been a taking of property.").}

When presented with both state and federal takings claims, the Connecticut Supreme Court has chosen not to differentiate between the protections afforded by the United States Constitution and those found in Article First, §11 of the Connecticut Constitution.\footnote{See Melillo v. New Haven, 732 A.2d 133, 136 (Conn. 1999); see also Tuchman v. State, No. CV030472731S 2003, WL 22078674 at *13 (Conn. Super. Ct. 2003); see also Tuckel v. Town of Southbury, 172 A. 222, 223-24 (Conn. 1982) ("Both the Connecticut and the federal constitutional provisions limit the right to compensation to those instances in which there has been a taking of property.").} In \textit{Melillo v. New Haven}, the court upheld a finding that the rights afforded by §11 were sufficient to provide just compensation to claimants, effectively rendering redundant the party's concurrent
assertion of a Fifth Amendment takings violation. The Melillo court’s conclusion is significant because the takings clause of the Fifth Amendment is applicable to the states through the Fourteenth Amendment. A trial court recently applied Melillo to hold that both the federal and state constitutional compensation rights are coterminous.

Federal and state courts use the FMV analysis to meet the constitutional standard of just compensation. The quantitative FMV analysis helps distill the more theoretical notion of just compensation into a more practical form in order to ascertain payments for specific government takings. While the “fair market value of property on the date it is appropriated” is the rule for calculating compensation, “other measures are employed only when market value is too difficult to find or when its application would result in manifest injustice to owner or public.” Courts often use one of three types of FMV calculations. The comparable sales approach is the most commonly used and, as its name indicates, compares sales of similarly situated property to estimate value for the seized land. If the comparable sales approach is impracticable, the court will use a reproduction cost or capitalization approach.

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119 Melillo, 732 A.2d at 143-44, n.28; see also Santini v. Connecticut Hazardous Waste Management Service, 342 F.3d 118, 126-27. (2d Cir. 2003) (noting the Melillo decision as effectively barring both a state and federal takings claim). See Miller v. Town of Westport, 842 A.2d 558, 559 (Conn. 2004). (citing Palazzolo v. Rhode Island, 533 U.S. 606, 617 (2001). Therefore, in other words, because states must comply with the dictates of the 5th Amendment takings clause, a finding that a state constitutional takings procedure is sufficient to pay just compensation for the seizure of property implies at least parity between the federal and state right.


124 "The instances in which market value is too difficult to ascertain generally involve property of a type so infrequently traded that we cannot predict whether the prices previously paid, assuming there have been prior sales, would be repeated in a sale of the condemned property." U.S. v. 564.54 Acres of Land,
The reproduction formula, or cost approach, starts from scratch and rebuilds the property, calculating the cost of doing so minus any depreciation. The capitalization approach takes an income producing property and capitalizes its future income to derive a present value. The formula selected and applied by the court is dictated by a property’s characteristics to ensure accurate valuation.

Depending upon the formulae used to assess FMV, prices being paid for real estate in a relevant market, improvements to the property, and possible economic uses for the land are considered. However, FMV may also be affected by additional factors, some of which may be purely idiosyncratic to the property itself. It is therefore understood that “an owner’s compensation depends so much on the facts of a case that no rigid formula is appropriate.” Practically speaking, this means that in the course of a trial a court must sift through data and analysis presented by both parties on the issue of valuation, processing that information through a formula of its choice in order to reach a judicial determination of FMV. In order to calculate an accurate FMV and provide constitutionally required “just compensation,” trial courts are bequeathed broad discretion to admit and establish the relevancy of evidentiary factors.

2. The “time of taking” requirement of a takings analysis does not preclude the prospective consideration of pending events in


127 See 56 AM. JUR. POF 3d 419, §16.
128 For example, comparable sales of real estate may not be available for certain unique properties.
129 26 AM. JUR. 2D Eminent Domain § 310 (2005).
130 See Ne. II, 861 A.2d 473, 482-83 (Conn. 2004) ("[E]ach parcel of property is in some ways unique...").
132 When there is no relevant market for the property, the valuation method can be on that is simply “just and equitable.” MODEL EMINENT DOMAIN CODE §1004(a).
133 See Eminent Domain, supra note 129; see also N.E. II, 861 A.2d. at 484-85.
the valuation of property when those events are likely to occur in the reasonably near future.

Assuming that remediation has value once applied, it must be resolved whether a seller can receive compensation for its expectation of retaining the land long enough to remediate it. The Supreme Court addressed and rejected the notion that, as a general rule, a seller has the "right of retention." The Court held in *Commodities Trading Corp. v. U.S.* that pepper acquisitioned by the Government from a private investor need not be given additional value to compensate for the investor's intent to speculate on increased postwar prices and therefore to hold onto the goods. The Court acknowledged that FMV could be higher than current prices "because a buyer anticipates future rises in prices." However, because projecting future prices was much too speculative and would discriminate against dealers of perishable goods, the Court held the general rule, short of "exceptional circumstances," did not include a right to retention.

However, some future events affecting value can be factored into the price of a piece of property. The Supreme Court has held that a property's valuation can "include market value it may command because of the prospects for developing it to the 'highest and best use' for which it is suitable." The Court subsequently specified that future pecuniary worth must be established "with certainty sufficient to persuade a purchaser of the business to pay for its capitalized value." The Fifth Circuit found this to be the case because "a hypothetical...buyer will purchase land with an eye to not only its existing use but to other potential uses as well." A party must show a reasonable probability that the land is both physically adaptable for such use and that there is a need or

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135 See *id.* at 126.
136 See *id.* at 126-28.
139 *U.S. v. 125.07 Acres of Land, More or Less*, 667 F. 2d 243 (1st Cir. 1981) (quoting *U.S. v. 320.0 Acres of Land, More or Less, Ect*, 605 F.2d 762, 781 (5th Cir. 1979)).
demand for such use in the reasonably near future.\textsuperscript{140} The U.S. District Court for the District of Maryland found admissible expert testimony as to an estimated date (roughly three to four years after the time of the taking) when the property could be put to its best and most profitable use, since this expert opinion was "sufficiently non-speculative and reliable."\textsuperscript{141}

The Connecticut State Supreme Court has concurred with federal courts on this matter, holding that future change, if reasonably probable and not merely speculative, may be considered in the determination of FMV of property taken by eminent domain.\textsuperscript{142} For example, consideration of a future, reasonably probable zoning change ought to be considered as it affects the present value of property.\textsuperscript{143} Other states have agreed. Evidence has been held to encompass "relevant facts at the time of the taking" and "may include those that have a bearing on an available future use of the property."\textsuperscript{144}

The American Jurisprudence Trials (AJT) also endorses the consideration of a reasonably probable future use to determine FMV and specifically notes that remediation fall into this category. The AJT states "if a third party’s liability for cleanup has been or is likely to be established [emphasis added], or if a state fund will pay for the cleanup, the market—and the courts—may disregard direct cleanup costs in determining property value."\textsuperscript{145} AJT’s approach uses the term “likely” to screen out speculative funds and retain only remediation funding that is probable at the moment the land is seized. If the reasonable probability of a future use can be established, that use in turn can be factored into the property’s value for compensation purposes. The door is open to taking heed

\textsuperscript{140} See U.S. v. 341.45 Acres of Land, 633 F.2d 108 (8th Cir. 1980).
\textsuperscript{142} Robinson v. Westport, 610 A.2d 611, 612-13 (Conn. 1992); see also Tandet v. Urban Redevelopment Comm’n, 426 A.2d 280, 284-85 (Conn. 1979).
\textsuperscript{143} See Peter Rock Assoc. v. Town of North Haven, 756 A.2d 290, 293 (Conn. 2000) (citing Minicucci v. Comm’r of Transp., 559 A.2d 216 (Conn. 1989)).
\textsuperscript{145} 60 AM. JUR. Trials 447 §30 (2005).
of a seller's planned use of remediation funds contingent upon meeting the reasonableness test.

The faithful application of the "time of takings" requirement reins in attempts to compensate for speculative future events. Under the Windham Mills scenario, at the time of the taking, ATC Partnership had the right to funds because of its ownership of the property being seized. ATC had acquired a grant and had begun to spend it. In addition, liability for the property's remediation had been assumed by American Thread, the prior owner of the property. The future value that would otherwise be realized by the seller comports with the time of taking requirement if it is evidenced that the remediation funds are in hand and/or a right to third party contribution is secure at the time of the taking.

3. Unlike Mola Development's interpretation of Article XIII of the California constitution, takings jurisprudence considers issues of fairness in the valuation of property that permits a court to modify, or even reject, the application of a FMV analysis.

A court has the power to modify the use of a FMV standard if an otherwise fundamentally unfair valuation would occur. In contrast to Mola Development's assertion that public policy was irrelevant to valuation in the context of property taxation under the California constitution, the United States Supreme Court has held that the public policy issue of fairness can be considered in compensating for a takings.146 The United States Supreme Court stated clearly that "manifest injustice to an owner or the public" may justify a valuation of land being taken through a means other than FMV.147

States have echoed that compensation ultimately must meet some minimum of fairness and have modified otherwise strict FMV analysis as a result. For example, an Arkansas court held that

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147 See id. A modification of, or a substitution for, a FMV analysis is necessary in order to avoid unfairness—or if traditional FMV models are unable to calculate a value for a particular property.
information discovered about property after the time of the taking could be admitted to evidence on the grounds that to do so otherwise would be "a harsh rule." Arizona has read into the phrase "just compensation" the understanding that a method for determining valuation must not be "unfair." In addition, the New Jersey Supreme Court has accepted reasonable alternatives to the three traditional valuation methodologies—reproduction, comparative, and capitalization—when these usual formulas have proven inadequate to measure a specific property.

The Connecticut Supreme Court has adopted a rule that "just compensation is an equitable [question] rather than a strictly legal or technical one," elaborating that "other measures may be appropriate when the fair market value measure of damages does not fully compensate the owner." Conversely, the court has not viewed the adjudication of FMV in a takings situation as separate from the realm of policy matters. In Arthur v. Town of Southbury, the Connecticut Supreme Court cited "political choices and settlements" being outside "its competence" in the case of the town's decision to discontinue a highway. The court held that it would "stay its hand" and defer to "a local administrative response" before it would assess what compensation was proper. Connecticut superior courts have applied these principles to ensure that wrong doers not benefit under an assessment of FMV and that an owner be compensated fully under the doctrine of "fair compensation."

152 See id.
153 Arthur v. Town of Southbury, 449 A.2d 1001, 1009-10 (Conn. 1982).
154 See id. See Ne. II, 861 A.2d 473, 477 (Conn. 2004) ("[T]he question of what is just compensation is an equitable one rather than a strictly legal one.")
155 City of Bristol v. Tilcon Minerals, Inc., No. CV9705722192004, WL 1462628, at *4-6 (Conn. Super. June 9, 2004) (quoting U.S. v. Virginia Electric Co., 365 U.S. 624, 636 (1961) ("[I]t would be manifestly unjust to permit a public authority to depreciate property values by a threat...[of the construction of a governmental project] and then take advantage of this depression in the price which it must pay for the property' when eventually condemned.")
Remediation grants and the right to third party payments can be permissibly included in FMV, even if valueless in the eyes of a private buyer, if the court believe that not doing so would be substantially unfair to the owner. Assuming the existence of a market failure that renders remediation funds valueless to an objective buyer and the lack of a seller's ability to first remediate property as an abrogation of the "hypothetical" market transaction where neither party is disadvantaged, a sufficient basis exists for the court to modify the FMV analysis to include some value for remediation funds. A fundamentally unfair assessment of value would otherwise jeopardize a property owner's right to just compensation.

D. Calculating the Present Value of Property subject to remediation funds.

Based on the preceding analysis, environmental remediation funds should not be excluded from FMV calculations as to do so may result in less than fair and just compensation for condemned property. Because profit-seeking purchasers would likely consider access to remediation funds to varying extents depending upon the facts specific to a case, a hypothetical FMV analysis should not automatically rule them out. Further, a court can, through the doctrine of fair compensation, ensure that the FMV transaction does not involve the exploitation of an exigency of the owner/seller. There may be many situations where remediation funds would be in fact worthless in an open market. However, the trial court should make that decision on a case-by-case basis rather than simply excluding all funding sources as a matter of law.

To gauge the FMV of remediation funds as applied, a trial court would first have to determine whether remediation would generate, with a reasonable probability in the reasonable future, an economically advantageous use. If not, the remediation funds would be irrelevant under a FMV and could only be considered if

*also* City of Hartford v. Rozas, 1999 WL 492597 at *2 (Conn. Super. June 30, 1999) ("[F]airness dictates that we go back to 1995 when the subject was capable of producing income in order to determine the value of the subject property.").
the Court found their exclusion much more than nominally unjust to the owner. If remediation would create future economic value, then the value created by each remediation dollar would be assessed. Resources allocated to remediation could generate more or less than one dollar in property value per dollar spent. Therefore, the improvement that results from the expenditure of the remediation resources, not the monetary value of the remediation funds themselves, is relevant to FMV. Any future value that would result from remediation should be capitalized to ascertain its current worth.

Second, there may be a possibility that a remediation attempt will fail completely and an appropriate discount for that risk is appropriate. Even if successful, a residual market stigma may attach to a previously polluted property after remediation. The court would need to assess, based upon expert testimony as well as the nature of the pollution, both the likelihood of market stigma attaching and the lingering financial effect of such prejudice. For example, a former uranium enrichment facility would be a candidate for an enduring and highly prejudicial market stigma, while an abandoned gas station would not. Finally, for an income producing property that would essentially need to go “out of commission” in order for the remediation to progress, a court could calculate loss of income during periods of remediation. Taken together, these factors would help determine the value of remediation funds to a hypothetical objective buyer.