

USE OF SUBDIVISION DEVELOPMENT ANALYSIS IN A CONDEMNATION CASE

By *Arthur C. Spalding**

When a person seeks to purchase a home, that person is likely to be concerned with a number of factors, which might include the community in which the home is located; the school district in which the home is located; the size of the home and the lot on which it is located; the physical condition of the home; the type, size and condition of other homes in the neighborhood; and the price of similar homes which have recently sold in the same neighborhood. An appraisal of a home would likely be based on an analysis that addressed such factors using what is known as the “sales comparison” method of appraisal. A person who seeks to purchase vacant land for development of multiple building sites, however, is not so concerned with the sale price of other vacant land parcels, except perhaps to use the same for negotiating strategy with the seller. The buyer of vacant land to be developed for multiple building sites is concerned with the number of lots that can legally and physically be developed on the vacant land; the cost of constructing roads, utilities and other improvements which are necessary for the development; the price that is likely to be obtained for the lots after they are developed; the demand for such lots; the length of time that will be necessary to sell all of the lots; and the profit that will be realized after all the lots are sold. An appraisal of vacant land based on an analysis of these factors is known as the “subdivision development” method or “subdivision development analysis”.

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Certain governmental bodies, including the Michigan Department of Transportation (“MDOT”), have sought trial court rulings that “subdivision development analysis” is inadmissible in a condemnation case in the state courts of Michigan. Such contention would seem no longer to be viable with the ruling in *MDOT v Weaver*¹ and the denial of MDOT’s application for leave to appeal to the Michigan Supreme Court.² An unpublished opinion of the Court of Appeals is, of course, not precedentially binding under the rule of stare decisis;³ however, *MDOT v Weaver* may be persuasive if cited because the opinion arguably satisfied certain of the requirements for publication.⁴ Denial of an application for leave to appeal, likewise, is not to be regarded as precedent,⁵ but in its Order of denial the Supreme Court stated that it was “because we are not persuaded that the questions presented should be reviewed by this Court.”⁶

The Fifth Amendment to the United States Constitution guarantees property owners the right to just compensation when a governmental body takes property for a public use. Every Michigan Constitution has had a similar clause and the current Constitution provides that “[p]rivate property shall not be taken for public use without just compensation therefor being first made or secured in a manner prescribed by law”.⁷

The Michigan Supreme Court has elaborated upon the meaning of the term “just compensation” under Michigan’s 1963 Constitution in the case of *Silver Creek Drain District v Extrusions Division, Inc.*⁸ In doing so, the Court focused on the historical establishment of the meaning of that term.

The meaning of “just compensation” cannot be discerned merely by a careful reading of the phrase. The words themselves, as the Court of Appeals found, just

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do not inform a court about the potential complexity and variety of factors to be considered in determining value.

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Throughout our history and clearly by the 1960s, it was uncontroversial that a determination of “just compensation” required the consideration of all the multiplicity of factors that go into making up value. In the nineteenth century, while summarizing just compensation and its meaning in American constitutional law, Michigan Supreme Court Justice THOMAS M. COOLEY, in his treatise *The General Principles of Constitutional Law in the United States of America*, said:

The rule by which compensation shall be measured is not the same in all cases, but is largely affected by the circumstances. If what is taken is the whole of what the owner may have lying together, it is clear that he is entitled to its value, judged by such standards as the markets and the opinions of witnesses can afford, and that this, except in extraordinary cases, must be the full measure of his injury.

The United States Supreme Court has had a similar and unvarying view of this matter, holding [1890 citation deleted] that the value of land must include “every . . . element entering into its cash or market value, as tested by its capacity for any and all uses” Then, again, in 1933, the Supreme Court held that “[t]he requirement that ‘just compensation’ shall be paid is comprehensive and includes all elements” [citations deleted]. The calculation is to “include any element of value that [property] might have by reason of special adaptation to particular uses.” [1934 citation deleted]. Yet again in 1956, the high court held that [j]ust compensation includes all elements of value that inhere in the property. . . .” [citation deleted].

Michigan’s understanding of just compensation has been identical in all relevant particulars.

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Thus, in our law, “just compensation” was a legal phrase of art in 1963 that meant, and still means, that the proper amount of compensation for property takes into account all factors relevant to market value.⁹

As the Michigan Supreme Court explained in *In Re Widening of Gratiot Avenue*¹⁰:

“Many technical rules have been promulgated for determining value, none of which is important. The determination of value is not a matter of formulas or artificial rules, but of sound judgment and discretion based upon a consideration of all the relevant facts in a particular case.” The

Court, in *Silver Creek Drain District*,¹¹ emphasized that it had reiterated the general rule found in *Dep't of Transportation v VanElslander*,¹² where it described what is relevant to just compensation as “any evidence that would tend to affect the market value of the property as of the date of condemnation” The Michigan Court of Appeals has stated in *State Highway Commission v Minckler*:¹³ that “. . . fair market value is found by considering and evaluating all the factors and possibilities that would have affected the price which a willing buyer would have offered to a willing seller for the land under the circumstances.” Jury instructions used in Michigan trial courts for many years have, in part, defined “*market value*” as buying property “with knowledge of all of the uses and purposes to which it is adapted” and “*highest and best use*” as “the most profitable and advantageous use the owner may make of the property”.¹⁴ Thus, we see that the range of evidence that is admissible to demonstrate “*just compensation*” is indeed the consideration of all the multiplicity of factors that make up the value of property.

In *MDOT v Weaver*, the expert witnesses/appraisers for both the Weavers and MDOT agreed that the highest and best use of the Weavers’ vacant land was for subdivision development. They all testified at trial that such a venture was not speculative. They all agreed that streets and utilities already existed that would obviate the need for their construction. The trial court allowed the Weavers’ expert witness to testify as to the value of the Weavers’ property using subdivision development analysis. The trial court denied MDOTs two pre-trial motions in limine. MDOTs first motion in limine, for which the trial court conducted an evidentiary hearing, sought to preclude the admissibility of subdivision development analysis as a matter of law. In response, the Weavers offered the testimony of an expert appraiser, who was a member of the Appraisal Institute (MAI), regarding the reliability of the “principal and method” of subdivision development analysis. The trial court denied both of MDOT’s pre-trial motions in

limine. The Court of Appeals, in its per curiam opinion, affirmed the trial court's rulings that subdivision development analysis is admissible through an expert appraiser in a condemnation case and specifically held that “. . . to the extent that [one] argues the subdivision development method itself is improper, [that] argument has no merit”.¹⁵

A trial court's decision to admit or exclude evidence is reviewed by an appellate court for an abuse of discretion.¹⁶ Relevance is the threshold of admissibility and evidence is relevant if it has any tendency to make the existence of any fact that is of consequence to the determination of the action more probable or less probable than it would be without the evidence.¹⁷ Thus, any evidence that would tend to affect the market value of the property as of the date of condemnation is relevant.¹⁸

The Appraisal of Real Estate, 12th Ed., recognizes that subdivision development analysis can provide useful and reliable information if appropriate steps are taken to assure that it is based upon adequate factual data. *Subdivision Analysis*, published by the Appraisal Institute in 1993, recognizes subdivision development analysis as a legitimate form of analysis to determine the raw land value of proposed subdivisions.

In *MDOT v. Weaver*, MDOT asserted that a majority of jurisdictions throughout the country have held that appraisals using subdivision development analysis should be inadmissible in evidence in condemnation cases. For example, MDOT quoted from the Virginia Supreme Court in what is perhaps the most cynical statement by an appellate court that this writer has encountered:

The trial court cannot be too careful in excluding evidence of this character, as witnesses can always be found who will, in their imagination, cover the most hopelessly unmarketable vacant land in the neighborhood with apartment houses filled with desirable tenants, and with the aid of a little figuring, capitalize the prospective net income at ten times the actual value of the land.¹⁹

In contrast, the Sixth Circuit Court of Appeals has recognized the legitimacy of subdivision development analysis.

- “It is to be remembered that the property being taken is an undivided tract of 6.9 acres of unimproved land that may be suitable for subdivision and the question is what is the fair market value of such a tract. Account must be taken of all factors which would be considered by a prospective purchaser, including, *inter alia*: (1) Cost of subdivision including loss of land for streets and utility easements, platting and surveying expense, road and street improvements; [and] (2) Cost of holding the property while it is being subdivided and sold, briskness of demand, etc.”²⁰
- “There is some authority for the proposition that valuation based on the lot method of appraisal should never be admitted in condemnation cases involving unimproved raw land. [Treatise citation omitted]. The Government would apparently have us adopt such an exclusionary rule in this case. We think the better view, however, is that a lot method appraisal can be admitted in appropriate cases if the proponent offers credible evidence of the costs of subdivision – e.g., the expense of clearing and improving the land, surveying and dividing it into lots, advertising and selling, holding it, and paying taxes and interest until all lots are sold. [citation omitted]. Juries in condemnation cases should be permitted to consider any factors ‘that might fairly be brought forward and given substantial weight in bargaining between an owner willing to sell and a purchaser desiring to buy.’ [citation omitted]. The potential value of land if subdivided could well be considered by a willing buyer and a willing seller where subdivision is a reasonable possibility and the costs of subdivision are not speculative or uncertain.”²¹

If property has value for sale as building lots, it would be a very harsh rule which would deny the owner the benefit accruing by reason of having property so favorably located. It is proper that each case should be considered under its own peculiar circumstances. Exceptional circumstances will modify even the most carefully guarded rule.

It has also been argued that testimony by an expert appraiser using subdivision development analysis was deemed inadmissible in Michigan courts, as a matter of law, in a condemnation case in Michigan more than 80 years ago. *City of Detroit v Hartner*.²² In *Hartner*, the City of Detroit condemned property owned by the Hartners for use as a municipal park. At

trial, the Hartners offered witnesses who projected a plat of the acreage to show its present value for the purposes for which it could be used. The trial judge instructed the jury that there were certain contingencies that must arise before the owner realizes on it, such as marketing costs, investment, improvements and many other things. Review of the jury instruction given by the trial judge and quoted by the Supreme Court is essential to the understanding of the holding.

Now the rule of law is this: What is the present full, fair market price of the property for the best use it can be used. Now the owners of this property are entitled to the present, full, fair, market price of the property for the best purposes for which it can be used, and, as I said before, I think it can be fairly inferred in this case that its best use is to plat it and sell the lots at retail. In other words, it will bring more money from that than from any other use they can put it to. Now that is what they claim.

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In placing a value upon this property, you place the value just as you find it now, contemplating all the purposes for which it can be used best, giving it the value that it would sell for under this test, contemplating the best use that can be made of it.

The purpose of allowing the witnesses to go on and project into the future a plat of the acreage out there was to show not only the present value, but to show its present value for the purposes for which it could be used. Now you can readily see that when a man has ten acres of land and he is going to plat it, there are certain contingencies that must arise before he realizes on it. There is the cost of putting it on the market. There is the investment. There are many things that you cannot tell just how they will turn out. Maybe they will be this, and maybe they will be that. It is, to some extent, more or less of a speculation as to just exactly what a man would realize in dollars and cents at a certain period when he has put in improvements and changed the character and aspect of his property up there. So you see, gentlemen of the jury, if you roam off into that field, you are in a field of uncertainty. You should only take that testimony and that projected platting and selling and the income from it, to ascertain what you would pay for it in its naked state as acreage before you started to do it. Therefore, when the question was asked, what is that worth an acre now as it stands for the purposes for which it can be used best, platting, --- that is the basis of your calculation.²³

The Hartners claimed this jury instruction was too narrow. The Supreme Court, however, stated that “The rule seems to be well settled in accordance with the instruction given by the trial judge”²⁴

Based on the testimony of their witnesses, the Hartners had sought an award of \$208,000. Such testimony, as reflected in the instruction to the jury by the trial judge, included the “cost of putting it on the market,” “the investment,” “many things that you cannot tell just how they will turn out” and “improvements [which] changed the character and aspect of his property.”²⁵ The jury decided that the Hartners were entitled to only \$116,341.51. The Hartners, not the City of Detroit, appealed the jury verdict, claiming that they were losing the benefit of platting the property themselves, selling it and receiving the profits of such sales. The Supreme Court noted that the jury had apparently considered and rejected the Hartners’ appraisal and, in a unanimous opinion, held that “The compensation awarded by the jury is within the evidence submitted and cannot be disturbed. We find no reversible error.”²⁶

Quoting from *Pennsylvania Railroad Co v Cleary*,²⁷ the *Hartner* opinion further explained that the jury’s proper role was to determine “what a present purchaser would be willing to pay for [the property] in the condition it is now in.”²⁸ As the Court in *Cleary* stated: “it is the tract, and not the lots into which it might be divided, that is to be valued.”²⁹

The *Hartner* opinion clearly drew the distinction between “that testimony and that projected platting and selling and the income from it, to ascertain what you would pay for it in its naked state as acreage before you started to do it”,³⁰ and simply the valuation of lots that a speculator “might be able to realize out of a resale in the future.”³¹

While not specifically describing it as such, *Hartner* was dealing with testimony based on subdivision development analysis, while *Cleary* was dealing with the valuation of lots that would

result from a platting. In effect, *Cleary* was dealing only with the revenue side, while *Hartner* dealt with both the revenue and expenses associated with lot development. Neither court specifically addressed the issue of “profits”, which are sometimes discussed in opinions from other jurisdictions, but the deduction of “entrepreneurial profit,” as is suggested by *The Appraisal of Real Estate*, is an extension of *Hartner* which favors a condemning body.

The *Hartner* trial court allowed the jury to consider subdivision development evidence. Such decision was sustained by the Michigan Supreme Court. The holding in *Hartner* is consistent with the subsequent holding of the Michigan Supreme Court in *VanElslander* and *Silver Creek Drain District*, which opinions broadly interpret the evidence which may be offered in a condemnation case to include all elements of value that inhere in the property and any evidence which tends to affect the market value of property.

It has been argued that the opinions in *Dep’t of Conservation v Connor*³² and *State Highway Commissioner v Snell*,³³ both citing *Hartner*, stand for the proposition that the development approach is *per se* inadmissible. In *Connor*, the trial court admitted evidence concerning the resale value of timber found on property being acquired via condemnation. The Supreme Court noted that the defendant/property owner’s experts’ testimony was less than credible, surmised that the jury may not have believed the defense’s obviously inflated calculations, but nevertheless found that the jury’s verdict was within the acceptable limits (i.e., lower than the defendants’ experts, but higher than the plaintiff’s). Therefore, like the *Hartner* Court, *Connor* affirmed the decision of the jury which had heard and rejected the evidence concerning development analysis.

Snell simply misreads *Hartner*. In *Snell*, the property owner sought to introduce development analysis testimony regarding the cost of building a service road. Summarizing the

Hartner decision, *Snell* noted: “The [*Hartner*] court did not allow the jury to consider the various costs involved in platting and developing the property.”³⁴ Such statement was not correct. The *Hartner* jury was allowed to consider all of the subdivision development analysis testimony at trial and its decision was upheld on appeal.

It has been claimed that the Court of Appeals acknowledged MDOT’s interpretation of *Hartner* in *City of Detroit v King*.³⁵ Such claim is incorrect. The Court of Appeals, in *King*, merely acknowledged that the City made an assertion based on *Hartner*, but the Court proceeded to say “... this is not such a case.”³⁶

The Michigan Rules of Evidence, and those cases examining the use of expert testimony, support the proposition that an appraisal of vacant land, based upon subdivision development analysis, should be placed before a jury, whose responsibility it is to determine how much weight and credibility the testimony is afforded. MRE 702 governs the admissibility of expert testimony and the trial court’s “gatekeeping” role and grants the trial court the discretionary authority, reviewable for its abuse, to determine reliability in light of the peculiar facts and circumstances of the particular case.³⁷

Although market participants cannot foresee the future, it is unrealistic to believe that market participants do not attempt to prognosticate the future when estimating the value of real property. One would never purchase income producing property if a belief did not exist as to the quantity and quality of an expected future income stream. Nor would a knowledgeable vacant land developer ever consummate a purchase of vacant land without considering and evaluating all of the elements of subdivision development analysis. To argue otherwise is to ignore market reality. Subdivision development analysis recognizes that market participants, although not omniscient, would consider the entire mass of information affecting the market value of the

property prior to a transaction. Likewise, expert testimony in a condemnation case must examine all the relevant information.

How would a prospective buyer of vacant land, knowing the highest and best use was for subdivision development, value such property? How would a knowledgeable seller, knowing how a buyer could develop a property, establish a selling price? It is not unreasonable to surmise, under such circumstances, that both a knowledgeable buyer and a knowledgeable seller would utilize subdivision development analysis to assist them in arriving at the fair market value of the property for purposes of a transaction. The profit to be realized from such a development is extracted before estimating the land value. The “profit deduction” step is a necessary corollary to subdivision development analysis. To the extent that any owner of vacant land must accomplish the development of such property by sale to a “developer,” they have “lost” the so-called developer’s profit and it is not recoverable as just compensation in a condemnation case. Notwithstanding the loss of developer’s profit, property owners are entitled to receive the “highest” price the property will bring when sold to a buyer knowledgeable of all of the uses and purposes to which the property is adapted and for which it is capable of being used.³⁸

The Appraisal of Real Estate; Subdivision Analysis; opinions of the United States Supreme Court and the Sixth Circuit Court of Appeals; proper application of the Michigan Supreme Court’s opinion in *Hartner*; and now the opinion and orders of the Court of Appeals and Supreme Court in *MDOT v Weaver* all support the proposition that subdivision development analysis is recognized in Michigan as a reliable method to determine the valuation of vacant land that is best suited for development into a subdivision and that subdivision development analysis is admissible through an expert witness in a condemnation case.

ENDNOTES

¹ *Michigan Department of Transportation v. Weaver, et al.*, unpublished per curiam opinion of the Court of Appeals, issued June 27, 2006 (Docket No. 257798, 257799, 258087 and 258088)

² 477 Mich 997, 725 NW2d 668 (2007)

³ MCR 7.215(C)(1)

⁴ MCR 7.215(B)(3, 4, and 5)

⁵ MCR 7.321

⁶ *MDOT v Weaver* (Supreme Court Order)

⁷ Const 1963, art 10, §2

⁸ *Silver Creek Drain District v Extrusions Division, Inc.*, 468 Mich 367; 663 NW2d 436 (2003)

⁹ *Silver Creek Drain District* at 375-379

¹⁰ *In re Widening of Gratiot Avenue*, 294 Mich 569, 574; 293 NW 755, 757 (1940)

¹¹ *Silver Creek Drain District* at 379, footnote 14

¹² *Dep't of Transportation v VanElslander*, 460 Mich 127, 129-130; 594 NW2d 841 (1999)

¹³ *State Highway Commission v Minckler* 62 Mich App 273, 277; 233 NW2d 527, 529 (1975); , citing *US v Miller*, 317 US 369, 374; 63 S Ct 276, 280; 87 L Ed 336, 343 (1943) and *State Highway Commissioner v Eilender*, 362 Mich 697, 699; 108 NW2d 755, 756 (1961)

¹⁴ M CIV JI 90.06a; M CIV JI 90.09

¹⁵ *MDOT v Weaver* (Court of Appeals opinion at page 4)

¹⁶ *Craig v Oakwood Hospital*, 471 Mich 67, 76; 684 NW2d 296, 303 (2004)

¹⁷ *VanElslander* at 129

¹⁸ *VanElslander* at 130

¹⁹ *Fruit Growers v Alexandria*, 216 Va. 602, 608; 221 SE2d 157 (1976)

²⁰ *United States v 158.24 Acres of Land*, 696 F2d 559, 564 (8th Cir. 1982)

²¹ *United States v 47.3096 Acres*, 583 F2d 270, 271-272 (6th Cir. 1978)

²² *City of Detroit v Hartner*, 227 Mich 132; 198 NW 839 (1924)

²³ *Hartner* at 137-138

²⁴ *Hartner* at 138

²⁵ *Hartner* at 137-138

²⁶ *Hartner* at 139

²⁷ *Pennsylvania Railroad Co v Cleary*, 17 A 468; 125 Pa. 442 (1889)

²⁸ *Hartner* at 139

²⁹ *Hartner* at 138, quoting *Cleary*

³⁰ *Hartner* at 138

³¹ *Hartner* at 139, quoting *Cleary*

³² *Dep't of Conservation v Connor*, 316 Mich 565; 25 NW2d 619 (1947)

³³ *State Highway Commissioner v Snell*, 8 Mich App 299; 154 NW2d 631 (1967)

³⁴ *Snell* at 309

³⁵ *City of Detroit v King*, 207 Mich App 169, 523 NW2d 644 (1994)

³⁶ *King* at 184

³⁷ *Gilbert v Daimler Chrysler Corp*, 470 Mich 749, 780; 685 NW2d 391, 408 (2004); *Kumho Tire Company Ltd v Carmichael*, 526 US 137, 158; 119 S. Ct. 1167, 1179 (1999)

³⁸ *Consumers Power Co v Allegan State Bank*, 20 Mich App 720, 744-745; 174 NW2d 578, 591 (1969)