

# APPRAISAL REVIEWS

The good, the bad and the ugly

(And we're not going to talk much about the good)



# Report Review – Part 1

THE  
GOOD



# A Good Report

- Follows Generally Accepted Appraisal Practices and Procedures.
- Follows appropriate guidelines
  - USPAP
  - IRS Regulations



# A Good Report

- Well written
- Easily understood
- Conveys the message you're intending to deliver to the reader.
- Logically leads the reader from the initial presentation of the data to the value conclusion.



# Report Review – Part 2

THE  
BAD

# A Bad Report

## Section 1 – Let's Talk English

- Incorrect Grammar
- Not-so-great Spelling
- Distracting Sentence structure
  - (i.e. is it a sentence?)
- Does not use Correct Punctuation
- Use the wrong word



# A Bad Report

- Let's see some examples
- In every example I used in this presentation, the city, appraiser, property size and any other identifying information has been changed to prevent disclosure of the actual owner.
- Other than that, the quotes are accurate.



# Grammar

- “The residence was a merely composed of homesteaders, miners, loggers and cattle and sheep ranchers.”



# Grammar

- “As mentioned several times throughout this review, the valuation of the subject property consisting of 40 acres and should have concluded from the fee simple valuation on page 155 at a value of \$110,000 based on the appraiser’s calculations.”



Is this a sentence?

- Skiing, fishing, hunting and hiking popular tourist activities.

Is this the word you want to use?

- “The subject property consists of two contiguous tracts which contain 41 acres and 76 acres, respectfully.”

# What are you saying?

- “The appraisers’ approach, which is labeled as Scenario “B,” the foregone development opportunity, is the before value, and that the after value, Scenario “A,” value of the raw land less the cost to remove the land from the flood plain, is the after value. In fact, Scenario “B” is not applicable, Scenario “A”, without deducting the cost to remove the land from the flood plain, is the before value, and there is no after value calculated.”

## Easily understood?

- “Indeed this area could to some extent also be thought of as The 100 Acre Woods exurban fringe, though that city’s own metropolitan area is so much smaller than the huge Metropolis conurbation that its economic influence is muted.”



# Punctuation

- Punctuation saves lives
- Consider the difference between these:
  - Let's eat, Grandpa!
  - Let's eat Grandpa!

# A Bad Report

## Section II -- The Technical Review

- Internal Consistency
- Support & Analysis
- Are the computations correct?
- If it said it followed USPAP, did it?
- Did they follow IRS Guidelines?
- Is the analysis / approach used recognized as generally accepted appraisal practices?



# Internal Consistency

- Information from one page should match the same information on another page.
- The subject property and the owner should remain consistent throughout the report.

# Follow USPAP

- “According to the public records... Title to the property was conveyed at a price of \$1,450,000 on December 25, 2000, which was subsequently recorded in Christmas County records at...”
- Less than 1 year later, appraiser I. M. Good appraised this property at \$200,000, with a Conservation Easement value of \$150,000.



# Follow USPAP

- Should the report have included a discussion of the prior sale?

# Follow USPAP

- Second Draft – same property
- I. M. Good added this: “It has been reported that the price paid regarding this transaction was severely inflated by an estimated \$1 million, and that fraud may have been involved. The actual price paid was closer to \$450,000.”
- Is this statement sufficient to comply with USPAP for a summary appraisal report?

# Does it Follow IRS Rules & Regulations?

- Use fair market value as the standard of value
- Consider the entire property before and after donation of the easement
- Consider Enhancement
- Follow accepted appraisal practices



# Report Review – Part 3

# THE UGLY



# Bias

- The subject property consisted of two 37-acre contiguous tracts in a subdivision.
- All properties in this subdivision were subject to a private covenant.
- Owner Mickey Mouse placed a conservation easement on the property in 2000.



# Bias

- Private covenant

- Only one residence and guest house per tract.
- Other structures limited to a garage and barn.
- Commercial or industrial facilities or activities are not permitted.

- Cons. Easement

- Only one residence and guest house per tract.
- Other structures limited to a garage and barn.
- Commercial or industrial facilities or activities are not permitted.



# Bias

- Sales – Before the easement
  - Appraiser I. M. Good included 13 sales from two subdivisions subject to the same private covenants; the price/acre ranged from \$10,000 to \$20,000.
  - The subject property, located in the superior subdivision, was purchased 1 year prior to the donation for \$20,500/acre.
  - I. M. Good concluded at the purchase price (\$20,500/acre).



# Bias

- Valuation – After the easement
  - There were two sales from the same subdivisions that had a conservation easement in place at the time of sale.
  - The first sale, located in the inferior subdivision sold for \$16,000/acre.
  - Other sales in that same subdivision ranged from \$10,000 - \$17,000/acre, with a median price of \$12,000.



# Bias

- The other property had a sale / resale occurring before and after placement of the easement.
  - Before \$12,000/acre
  - After \$16,500/acre
- Applying the time adjustment stated elsewhere in the report, the Before value = \$15,500/acre.



# Bias

- Based on this very limited information, how much impact on value is attributable to the conservation easement?
  - It has exactly the same restrictions as the private covenant attached to the property.
  - CE Sale #1 sold for \$16,000/acre (unencumbered sales ranged from \$10,000 - \$17,000; the median price was \$12,000).
  - CE Sale #2 had a before value of \$15,500, and an after value of \$16,500/acre (a 6% increase).



# Bias

- I. M. Good after valuation:
  - “Although the highest and best use does not change, there is a nuisance issue with the placement of an easement on each parcel... This loss can range from 0% to a high of 15%. This range is drawn from conversations with other appraisers and knowledgeable people in the land trust business.”



# Bias

- I.M. Good averaged the two sales prices to arrive at an after value of \$17,000/acre. (I recognize that this isn't the average, but it is the conclusion I. M. Good reached in that report).
- This price was compared to the subject concluded before value of \$20,500/acre (based on the purchase price).
- I. M. Good concluded that the easement reduced the value of the property by 17%.



# Bias

- The sale/resale of a single property before and after placement of the easement resulted in a slight increase in value.
- Analysis of the other sale in relation to properties in the same subdivision showed no decrease in value.
- “Knowledgeable people” said 0-15% nuisance decrease.
- The appraiser concluded at 17% diminution.



# Case Study Facts

- This property contains 15 acres located near Dairyville (not in California).
- It is zoned for Agricultural uses; the current zoning allows for 1 residence.
- The property didn't have water rights.
- The Cowabunga County Master Plan indicates the subject area has possible poor yield wells.



# Case Study Facts

- Properties of this size in this area had historically been utilized as single – family equestrian estates.
- Dairyville had issued between 1 and 5 residential building permits annually for 4 years prior to the valuation date.

# Case Study – 1<sup>st</sup> Draft

- “The subject property before the CE is zoned A, agriculture... I have concluded that it is reasonably probable that the property will be annexed to the Town of Dairyville and rezoned to PD (planned development) at 8.76 units per acre. Therefore the land is valued as if annexed to the Town of Dairyville and rezoned to PD for residential uses, and adjusted for the cost to annex.”

# Case Study – 1<sup>st</sup> Draft

- The report did not contain any extraordinary assumptions or hypothetical conditions.

Do you think it should have?

# Case Study – 1<sup>st</sup> Draft

- “Current housing supply.. Is primarily rural residential homes on acreage parcels (35 to 100 acres) and values begin in the high \$400,000’s and some exceed \$1,000,000.”

# Case Study – 1<sup>st</sup> Draft

- “Building permits for new construction indicate there is not a significant amount of residential building activity. This is due to a lack of a supply of lots for entry-level housing and the high demand for such a product for those that cannot afford the acreage estates in the county. There is virtually no multi-family housing product in the town to accommodate residents with lower-income housing needs.”

# Case Study – 1<sup>st</sup> Draft

- DCF Analysis – no market support given for any of these numbers:
  - Average sale price \$175,000
  - 18% to the lot
  - 15% for profit
  - \$18,000 costs
  - Deduct \$1,500 / lot for platting

# Case Study – 1<sup>st</sup> Draft

- I. M. Good found 4 sales in two cities (15 – 20 miles away).
- The average number of Residential Building permits issued in prior 2 years:
  - City #1 averaged 700
  - City #2 averaged 1,150
  - Dairyville issued 1 - 2

# Case Study – 1<sup>st</sup> Draft

- “Therefore a significant adjustment is warranted for the location of sales when compared to Dairyville.”
- I.M. Good adjusted sales downward 50% for location without further discussion.
- No other adjustments were made.

# Case Study – 1<sup>st</sup> Draft

- Should there be any extraordinary assumptions / hypothetical conditions?
- Is it reasonable to assume intense residential development without any established water supply?
- Is it reasonable to assume re-zoning?
- Does a DCF analysis require support?
- Is it appropriate to make a 50% location adjustment without any market support?

# Case Study – 2<sup>nd</sup> draft

- “Therefore, the land is valued as annexed to the Town of Dairyville and rezoned to PD for commercial and residential uses, and adjusted for the cost to annex and rezone the property. This is an extraordinary assumption.”

# Case Study – 2<sup>nd</sup> Draft

- This time, the subject history included a sale occurring within 3 years prior to the valuation date, with \$500,000 allocated to the subject parcel.
- I.M. Good used the same sales data, with a 50% location adjustment as before.
- Unsupported DCF analysis arrives at same value conclusion.

# Case Study – 2<sup>nd</sup> Draft

- Some obvious flaws:
  - Entire property acquired less than 3 years prior to valuation date for \$500,000; the value conclusion was 164% higher, without explanation or reconciliation.
  - HBU analysis did not include an analysis of the actual historic market use in the area – What is the value of the subject property as large residential acreage?

# Case Study – 2<sup>nd</sup> Draft

- Some obvious flaws:
  - HBU section had beginning of DCF analysis, concluded at zoned land value of \$7,275 per lot before considering discounting. I.M. Good concluded at \$8,700 per lot after DCF analysis.
  - No support provided for the 50% location adjustment.

# Case Study – 3<sup>rd</sup> Draft

- Included extraordinary assumption that the land is valued as annexed to the Town of Dairyville and rezoned to PD (planned development).

# Case Study – 3<sup>rd</sup> Draft

- Expanded the discussion on location:
- “Dairyville has: a smaller population, lower income, fewer in-town new homes, a need for entry-level housing; which requires lower land cost.”
- “All of these items require downward adjustments. For now, we will apply downward adjustments of 50% and 75% and compare these indications with other indications.”
  - Editorial comment – I.M. Good didn’t do this comparison

# Case Study – 3<sup>rd</sup> Draft

- My favorite quote from this appraisal, after applying 50% and 75% location adjustments to the 4 unadjusted sales:
- “These numbers present an unreasonably wide range, but this is what the market seems to be.”

# Case Study – 3<sup>rd</sup> Draft

- “The fair market value conclusion must be compared to the purchase of the subject property on December 25, 2000 for \$500,000. The time between the purchase and our date of value was one of major growth in people and jobs, and the subject was planned and prepared for annexation. Although the spread in dollars and percentage is high, it is not unreasonable given the markets and our conclusion of highest and best use.”



Any Questions?

Thanks for listening.

I hope you were entertained!

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