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September 25, 2012

Mr. Gregory Forsythe, Chairman
Professional Board
International Valuation Standards Council
41 Moorgate
London EC2R 6PP
United Kingdom
CommentLetters@ivsc.org

RE: Request for Comments on the Discussion Paper "Valuation of Trade Related Property" dated August 1, 2012

Dear Mr. Forsythe:

Thank you for the opportunity to comment on the Discussion Paper "Valuation of Trade Related Property." On behalf of the Appraisal Institute, its Appraisal Standards and Guidance Committee ("ASGC") submits the following responses to the questions you posed in your request for comment dated August 1, 2012. Although the questions were posed so as to elicit response from individual valuation professionals and users of their services, we have responded using our collective knowledge of the normal course of business employed by our members.

Question 1a:

Are you familiar with the former GN12?

Response:

Some of our members are familiar with GN12.

Question 1b:

Is GN12 used in the valuations that you provide or receive?

Response:

We do not find that GN12 provides sufficient useful guidance. Specifically:

- The definition of "trade related property" is unclear because the phrase "trading potential" is unclear.
- The GN fails to stress that at the outset of any valuation it is critical for the valuer to determine just what is to be valued – the real property alone, or the going concern

(operation that uses the real estate.) The determination depends on what the client needs to have valued.

- Section 5.7 is inadequate. It states "the valuation conclusion may need to be broken down between the different asset components…." What is meant by "broken down"? It is important to distinguish between "allocation" and "separate valuation" of the different components. If a separate valuation, then *type of* value becomes an issue. If an allocation, then the basis for the allocation must be clear.

Question 2:

Do you consider that it is a) practical and b) necessary to define a distinct category of real property for valuation purposes based on the degree to which the buildings or any other structures are specialised?

Response:

No. It is more important for the valuer to recognize and identify (1) the type of value being sought, (2) the interest, and (3) the asset. The asset might be real estate or it could be the operating entity (going concern).

Question 3:

If you have answered yes to Question 2, do you consider that the term "Trade Related Property" adequately conveys the particular characteristics that may lead a valuer to adopt a different valuation method as compared to other types of property?

Response:

If a label is to be used, "Trade Related Property" appears to be appropriate.

Question 4:

If you have answered yes to Question 2, please also indicate the types of real property that should be included in distinct category.

Response:

We did not answer "yes" to Question 2. However, since this is a response from an appraisal organization, we believed it would be helpful to you to know that Appraisal Institute members generally include hospitality properties, restaurants, certain "convenience stores," nursing homes and other senior living facilities, hospitals, oil refineries, quarries, other mining operations, grain elevators, some self-storage facilities, certain resort properties, some sports arenas; the list is potentially endless.

Question 5:

If you have answered no to Question 2, are there any other characteristics other than the specialisation of the buildings or structures that you believe may require Trade Related Property to be separately categorised from other real property for valuation purposes?

Response:

Please see our response to Question 2.

Question 6:

Are you familiar with the “profits method” as outlined above to value TRP? If so please indicate the types of real property where you are familiar with its application.

Response:

It appears to us that this “profit method” is the same as the “income approach” used to value commercial properties, with the “hypothetical owner” being what we call the “typical buyer.” If this is so, then this discounted cash flow methodology is in broad use. However, other methodologies may be acceptable depending on the specific valuation problem.

Question 7:

What methods do you normally use to allocate value to the real property interest? Do you apply the same method regardless of the type of real property involved?

Response:

Any guidance developed needs to distinguish between “allocation” and “separate valuation” of the different components. If the objective is a separate valuation, then *type of* value becomes an issue, as does the competence of the valuer. [There’s a big difference between the questions “what is the value (as in value in exchange) of this item” and “how much does this item contribute to the value of the whole?”] If instead the objective is an allocation of the value of the “whole” among the components, there must be some logical basis for the allocation, depending on the intended use of the report.

When allocating the market value of the asset to its component parts, a generally accepted technique is to first develop the market value of the property as a whole, using the income approach and sales comparison approach, and then estimate the values of the non-real estate assets and deduct those from the value of the whole, leaving the value of the real property interest. The depreciated cost of the real property may also be used in the alternative or as a test of this methodology.

Question 8:

In your experience what sources of data are available to support the use of either the profits method or an allocation to the real property from the value of the business in occupation? How reliable are these?

Response:

Appraisal Institute texts, courses, and other publications are available in support of both methods and both are relied upon by members and others.

Question 9:

Do you consider that the general provisions in the IVSs concerning identification of the asset to be valued and clarification of the assumptions made about complementary or associated assets are sufficiently clear for application to TRP or do you believe that the IVSs should provide more specific guidance? If you believe that more specific guidance is required, please indicate the types of TRP where you believe that this is needed.

Response:

We believe that the general provisions of the IVS are sufficient, as the differences in valuing these assets lies in proper identification of the characteristics of the subject asset and the requirements of the intended use of the appraisal report. The valuation methods and techniques used are within the judgment of the professional valuer and are not different from those already addressed in the IVS. However, GN12 has deficiencies, as noted above.

Question 10:

Please indicate any techniques with which you are familiar for ensuring that the value of the real property interest excludes any value attributable to other assets.

Response:

Please see our response to Question 7.

Question 11:

Please indicate for what purposes you consider that a valuation of a TRP should be made on the assumption that it is part of a going concern and for what purposes it should be made on the assumption that there is no business in occupation.

Response:

It depends on just what is to be valued (the interest in the real estate alone, or the operation that uses that real estate) and the type of value being sought. Market value presumes a transfer of ownership. Upon that transfer, what happens as far as occupancy and use will depend on the circumstances, including the highest and best use of the real estate and the intent of the most probable buyer.

Question 12:

Do you agree that the value of the real property interest is affected by whether or not there is a business in occupation?

Response:

Again, it depends on just what is to be valued – the real property alone or the going concern. The nature of the physical characteristics of the real estate may contribute or detract from value of the real property.

Question 13:

If you are a user of valuation reports, in your experience, is the distinction between the business and the property interest normally clear from the reports that you receive?

Response:

We find that many valuation reports are not clear on just what is being valued (real property or going concern) and that the valuation approaches often confuse the two. For example, in the income approach, the income from the operation of the going concern is capitalized giving a value of the going concern, whereas in the cost approach clearly just the real property is being valued. Often it is not clear in the sales comparison approach what the comparables consisted of and so therefore what the indicated value represents. Federally regulated lenders in the United States are required to have TRP valuations include allocations of the final value conclusion into conclusions of value of any included personal and intangible property. These allocations are performed by the real property appraisers who valued the asset as a whole, and the support for these allocations is not always clear.

We trust that you will find our comments helpful. Please do not hesitate to contact me if you have any questions regarding these comments.

Sincerely,

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