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CONTEMPORARY REAL ESTATE APPRAISAL METHODS

Instructor: Professor James A. Graaskamp
University of Wisconsin School of Business

I. Basic Concepts and Definitions

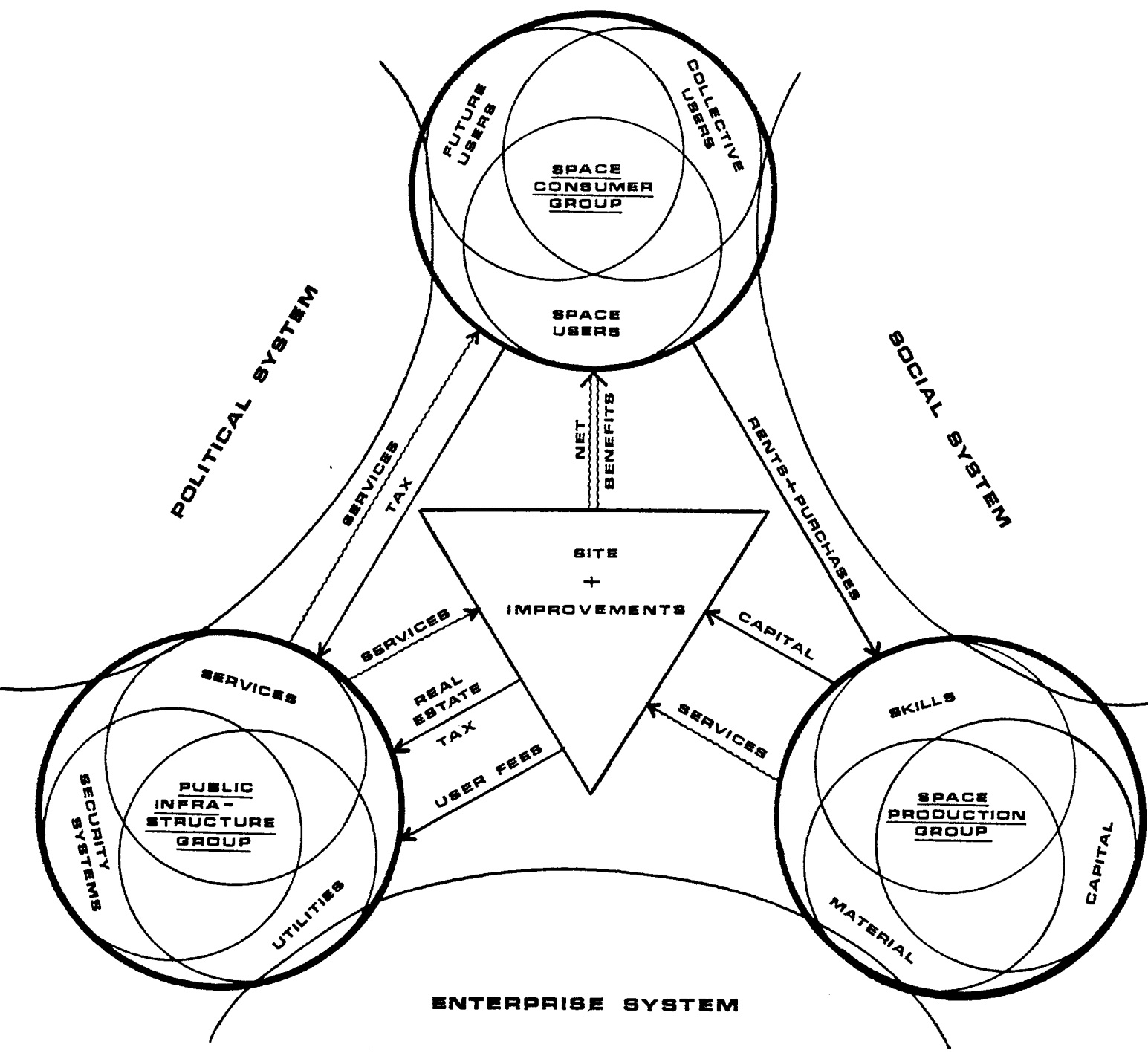
- A. Real estate is a tangible product - defined as artificially delineated space with a fourth dimension of time referenced to a fixed point on the face of the earth.
 1. Real estate is a space-time unit, room per night, apartment per month, square foot per year, tennis court hours, or a condominium for two weeks in January at a ski slope.
 2. To the space-time abstraction can be added special attributes to house some form of activity.
 3. Improvements from survey market to city layouts to structures define space.
 4. Legal contracts and precedents define time.
 5. Rights of use are defined by public values, court opinions.
 6. Private rights to use are those which remain after the public has exercised its rights to control, to tax, or to condemn.
- B. A real estate project is cash-cycle business enterprise which combines a space-time product with certain types of management services to meet the needs of a specific user. It is the process of converting space-time needs to money-time dimensions in a cash economy.
 1. A real estate business is any business which provides expertise necessary to relate space-time need to money-time requirements and includes architects, brokers, city planners, mortgage bankers, and all other special skills.
 2. The true profit centers in real estate are in the delivery of services and cash capital.
 3. Equity ownership is the degree to which one enterprise controls or diverts cash from another real estate enterprise.
 4. Public has direct ownership to the degree real estate taxes take a percentage of tenant income in excess of service cost.
 5. Consumer must view space as a total consumption system involving direct cost, surface cost, transportation cost and negative income of risk.
 6. The best real estate project is the one which has the lowest net present value of cost as the sum of cost to the consumer production sector and public sector.

- C. The real estate process is the dynamic interaction of three groups, space users (consumers), space producers, and the various public agencies (infrastructures) which provide services and capital to support the consumer needs. (See Exhibit 1)
1. Each of these three decision groups represent an enterprise, an organized undertaking. All are cash cycle enterprises constrained by a need for cash solvency, both short and long term.
 2. A desirable real estate solution occurs when the process permits maximum satisfaction to the consumer at a price that he can afford within the environmental limits of land while permitting the consumer, producer, and the government cash cycle to achieve solvency - cash break even at a minimum, after full payment for services rendered.
 3. Solvency of the total process, not value, is the critical issue.
 4. Land is an environmental constraint and not a profit center.
 5. Land provides access to a real estate business opportunity and is not the opportunity itself. Real estate business wants to control land to create a captive market for services.
- D. Land is the point where demand and supply forces find cash solvency. Location is a manufactured attribute. Site attributes are exploited to create location by analyzing:
1. Static attributes.
 2. Legal-political attributes.
 3. Linkage attributes.
 4. Dynamic attributes.
- E. Recognition of the fact that profit maximization must be limited by concerns for physical environment and community priorities for land use has resulted in redefinition of the most basic concept in appraisal; i.e. highest and best use, in the authorized terminology handbook sponsored by the American Institute of Real Estate Appraisers and the Society of Real Estate Appraisers. Compare the 1971 definition with that for 1975:

Highest and best use concept-

"A valuation concept that can be applied to either the land or improvements. It normally is used to mean that use of a parcel of land (without regard to any improvements upon it) that will maximize the owner's wealth by being the most profitable use of the land. The concept of highest and best use can also be applied to a property which has some improvements upon it that have a remaining economic life. In this context, highest and best use can refer to that use of the existing improvements which is most profitable to the owner. It is possible to have two different highest and best uses for the same property: one for the land ignoring the improvements; and another that recognizes the presence of the improvements.:

p. 57, Real Estate Appraisal Principles and Terminology, Second Edition, Society of Real Estate Appraisers 1971.



THE REAL ESTATE PROCESS

"Highest and Best Use: That reasonable and probable use that will support the highest present value, as defined, as of the effective date of the appraisal. Alternatively, that use, from among reasonably probable and legal alternative uses, found to be physically possible, appropriately supported, financially feasible, and which results in highest land value. The definition immediately above applies specifically to the highest and best use of land. It is to be recognized that in cases where a site has existing improvements on it, the highest and best use may very well be determined to be different from the existing use. The existing use will continue, however, unless and until land value in its highest and best use exceeds the total value of the property in its existing use. Implied within these definitions is recognition of the contribution of that specific use to community environment or to community development goals in addition to wealth maximization of individual property owners. Also implied is that the determination of highest and best use results from the appraisers judgement and analytical skill, i.e., that the determined from analysis represents an opinion, not a fact to be found. In appraisal practice, the concept of highest and best use represents the premise upon which value is based. In the context of most probable selling price (market value) another appropriate term to reflect highest and best use would be most probable use. In the context of investment value an alternative term would be most profitable use."

Real Estate Appraisal Terminology, Edited by Byrl H. Boyce, Ph.D. SRPA, Ballinger Publishing Co., Cambridge, Mass. 1975

- F. The purchase of a piece of real estate today involves the acceptance of a great many assumptions about the future. Those who take care to validate these assumptions in a period of transition as to public land use control tend to have the most successful investment.
 - 1. Business decisions today make explicit recognition of their assumptions and the need to act under conditions of uncertainty.
 - 2. Business risk is the difference between assumptions about the future and realizations, the proforma budget and the end of the year income statement.
 - 3. Risk management is the control of variance between key assumptions and realizations.
 - 4. An appraisal is a set of assumptions about the future productivity of a property under conditions of uncertainty.

- G. The concept of highest and best use of land was a commodity concept which did not consider externalities adequately. It is being replaced by concepts of most fitting use and the concept of most probable use.
 - 1. The most fitting use is that use which is the optimal reconciliation of effective consumer demand, the cost of production, and the fiscal and environmental impact on third parties.
 - 2. Reconciliation involves financial impact analysis on "who pays" and "who benefits" - thus the rash of debate on how to do impact studies.

3. The most probable use will be something less than the most fitting use depending on topical constraints imposed by current political factors, the state of real estate technology, and short term solvency pressures on consumer, producer, or public agency.
 4. Most probable use means that an appraisal is first a feasibility study of alternative uses for a site in search of a user, an investor, and in need of public consent.
- H. In seeking the most fitting and most probable use, the inner city planner and private property appraiser must interact to determine how community objectives and consumer - production sector solvency can be achieved simultaneously.
1. A real estate decision has only two basic forms. Either a site is in search of a use and consumer with the ability to pay, or a consumer, need or use with a defined ability to pay is seeking some combination of space-time attributes he can afford.
 2. The individual consumer with needs and a budget is the drive wheel.
 3. The public sector represents the community owned consumer service delivery system, seeking to minimize marginal cost to the consumer and average cost to the community at large.
 4. The production sector responds to a derivative demand for engineering and management expertise.
- I. Critiquing the form and adequacy of a real estate solution is analogous to the artistic concept of judging the success of an art object by relating form of the solution to the context to which it was created.
1. Context includes those elements which are fixed, given, or objectives and to which any solution must adapt.
 2. Form giving elements are those variables within the artists control, i.e. options or alternatives at a particular time.
 3. A solution is judged for its correctness or success in terms of the degree of fit of the form proposed to the context.
 4. Feasibility analysis is concerned with the degree of fit or the extent of misfit between a proposed course of action and the context within which it must operate or fit.
 5. Success therefore depends on how appropriately the problem is defined; testing feasibility depends primarily upon accurate and comprehensive definition of the context.

CONTEMPORARY REAL ESTATE APPRAISAL SEMINAR

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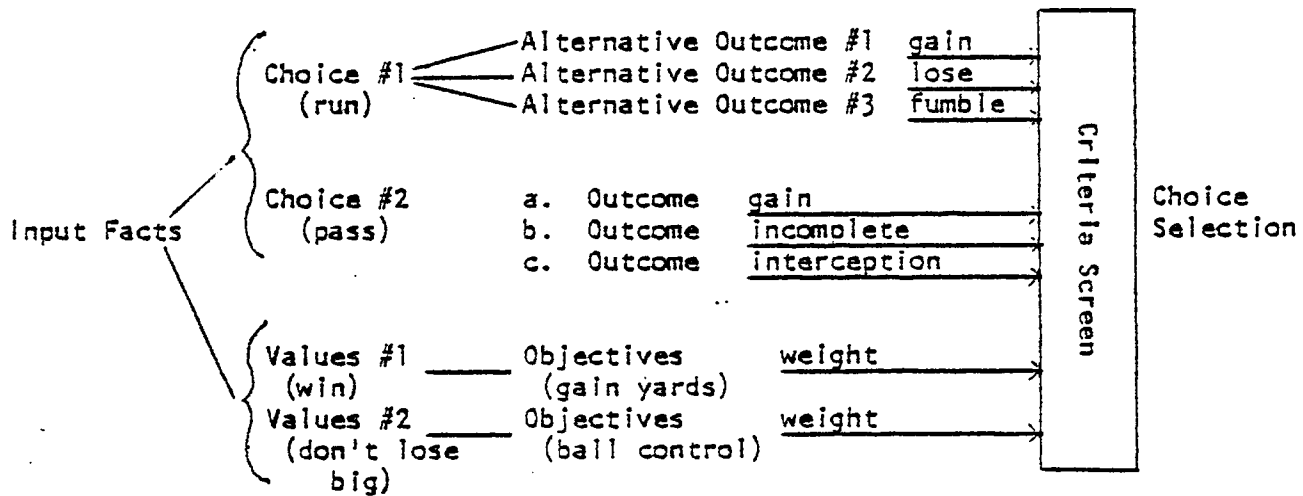
II. A Real Estate Appraisal - A Business Forecast

- A. Prof. Richard U. Ratcliff was the first of several urban land economists to critique traditional appraisal in light of current business forecasting methods and techniques. In effect Ratcliff describes an appraisal as a prediction about the price of a future transaction under conditions of uncertainty. Uncertainty is introduced because knowledge of the facts is less than perfect and future conditions unknown.

One approach to forecasting or reaching a decision is by modeling to structure facts and relationships in a manner appropriate to the decision process. Three types of models are common in real estate analysis:

1. Physical models = sand tables to understand site, building mass, and shape.
 2. Communication models = flow charts of industrial process or traffic patterns.
 3. Abstract or symbolic models = items with mathematical or logic concepts, $I/C = V$ is a symbolic model of the relationship between income productivity.
- C. In constructing any decision model there are six basic elements to be considered:
1. The decision to be made or the question to be answered.
 2. The data available with which a decision must be made.
 3. The theoretical relationships or logical structure which focuses the data on the problem.
 4. The interface between the analyst and the requirements of the model.
 5. The interface between the results of the model and the decision maker or client and their ability to comprehend and believe (credit ability is always more important than credit in real estate).
 6. The relationship between the economic significance of the answer and the cost to acquire the answer by using the model.
- D. In general, a decision requires that information be systematically organized to identify choices of action and the alternative outcomes from each choice. (See Diagram #1). At the same time facts help shape general values which in turn lead to explicit objectives, and then specific selection criteria.

Diagram #1



- E. The three approaches to value are models of how economic man might price a property to maximize his return and minimize his cost. It represents an historical compromise between three powerful groups in the early 1930's who really had different needs or questions about price.
1. Insurance company lenders wanted to lend less than cost to build - thus they emphasize the cost approach.
 2. Real estate brokers wanted to know what they could sell it for today, and therefore emphasize the market comparison approach.
 3. The FHA appraisal section was headed by a Michigan professor, Fred Babcock, who believed all property should be valued as a capital budgeting decision, i.e. as the present value of future net returns.
 4. To compromise they seized on Marshallian economics which said in the short run the market is out of balance and reveals market price. During the intermediate term, it reflects income value which cannot be forecast for the long run. In the long run, prices have tendency to equal cost of production.
- F. Since that time, writers have shown buyers are interested in many things besides maximum profit including minimum risk, compatibility with community, portfolio effects from taxes and diversification as well as subjective, qualitative satisfactions. Therefore, an appraisal model may seem to have the same question - What is the value of property - but in fact it represents multiple questions:
1. What is the nature of the decision to be served by the appraisal benchmark?
 2. What is the specific asset for which value is sought?
 3. What is the date for which value is relevant?
 4. What is the definition of value - theoretical structure - which focuses the data on the problem?
- G. Ratcliff points out a variety of value estimates or viewpoints which have significance in the appraisal of any specific property:

1. Vs - value to the owner or user.
2. Vc - cost of constructing a substitute property.
3. Vp - a probabilistic prediction of what the property will sell for.
4. Vo - price at which the property is offered for sale.
5. Vb - bid price by a prospective purchaser.
6. Vt - the price at which the property is actually sold, as an historic fact.

H. The Ratcliff viewpoint is just plain common sense. On page 14 of his text he states his premise:

"The fundamental concepts of value and price which are central to appraisal are at the heart of the social science of economics. Economic goods are valuable because of their utility (productivity) and scarcity. Thus in analyzing the value of a parcel of real estate, the starting point is with its inherent utility - the characteristics and qualities which can make it productive and desirable, and for which people are willing to pay.

"But price is set in the market place. To serve his client's needs, the appraiser seeks to predict the price at which the subject property will probably sell. Viewing the property as a package of potentially productive qualities, the appraiser must predict the outcome of the interaction of the market forces of demand and supply to which the property might be exposed and which could trigger a transaction from which market price will emerge.

"Economics is a behavioral science, descriptive of the economic behavior of people under various conditions. It is the appraiser's task to predict how people, both buyers and sellers, will behave with respect to the subject property when it is exposed for sale. People make values and determine prices."

I. An appraisal as a benchmark for decision requires the appraisal report to reflect the client's purposes for which an appraisal is sought. It is common sense that the more questions that an appraisal can serve, the more business potential there is; fair market value serves only a limited number of issues.

1. For the mortgage lender, the issue is the liquidating value or probability of future cash returns being adequate to repay the loan, interest, and cost, and the distribution of profit centers over time to maintain repayment incentive to the borrower.
2. For the courts eminent domain or assessment appeal, the statement of function leads to the definition of value as the jurisdictional market value.
3. A report for a would-be buyer or seller might lead to the definition of value as investment market value.
4. For most cases the appraiser would seek to determine the most probable selling price.

J. Investment market value is a term coined by Mack Hodges for the present value of future income receipts, considering a specific set of assumptions about the after tax cash flow of property and

requires some general description of the investment standards and tax status of buyers interested in a specific type of property, specifically income investment property. Investment value, which requires some detail about motivations of a probable or specific buyer, is a special case of the broader concept of "most probable sales price." (Vp)

- K. Most probable selling price is derivative of the theoretical work of Prof. Richard U. Ratcliff, William Kinnard, Paul Wendt, and others.
1. The quotable definition: "The most probable price is that selling price which is most likely to emerge from a transaction involving the subject property if it were to be exposed for sale in the current market for a reasonable time at terms of sale which are currently predominant for properties of the subject type."
 2. This approach makes the point conclusion explicitly a statement of the central tendency (mode, mean, or median) around which a transaction price is likely to fall. Thus it generally supplies a valuation as a range of prices within which a transaction would most likely occur, similar to but not necessarily a concept of statistical standard error. This range will be called a transaction zone.
- L. General format of RATGRAM Appraisal follows common sense logic:
1. Define the issue for which the appraisal is sought in order to select the appropriate definition of value.
 2. Analyze alternative uses of property to select most probable use as of date of appraisal.
 3. Infer from probable use the most probable buyer-type, financial motivations, and negotiation position.
 4. Define comparability and test applicability of three alternative approaches.
 - a. Preferred method is to infer buyer behavior from completed market transactions.
 - b. In the absence of sales, simulate buyer estimation methods and constraints.
 - c. Knowing nothing of buyers methods, fallback to normative approaches.
- M. In the contemporary approach, note:
1. Any method is judged on the reliability with which it predicts transaction price-not on intellectual elegance-robustness.
 2. Buyer-type is generally a class, but it could be a single buyer. The statistical market place assumption does not control.

3. There is no need that buyers be fully informed as the market may provide evidence that prices are being set by ignorance; there is no need that buyers have reasonable choices if the seller is enjoying a monopoly position.
 4. Finally it should be noted that the logical development from productivity analysis to selection of the appraisal report structures the form of the report.
- III. Since appraisal starts from what is known about a specific piece of property (Productivity Analysis, Chapter 2 in Ratcliff), it is similar to a feasibility report until one has determined the probable use and the probable buyer.
- A. Refer to Exhibit 2.
 - B. The traditional appraisal report always moves from the general to the specific, subject to a series of limiting conditions. Many of these special conditions are professional courtesy to avoid competition with other professions at the same time that one avoids paying the other professions and continues as a lone wolf in appraisal, controlling the customer, a psychological hang-up of real estate brokerage. Thus the appraiser avoids:
 1. Engineering factors
 2. Finance and taxation matters
 3. Title issues, surveys, etc.
 4. Legal character of leases, permits, and other contracts
 - C. At the same time the element of uncertainty, left implicit by a single number conclusion, is hedged by additional limiting conditions including the appraisal practice of ignoring politics, land use administration, and personalities.
 1. The practice of using limiting conditions has moved to the point where the appraiser supports consistency based on faulty premises rather than honesty as the reliability of a prediction
 2. Nevertheless, all an investor buys is a set of assumptions about future.
 3. Since risk is the variance between assumptions and realizations, how can the appraiser evaluate the probable productivity of the property without evaluating all the assumptions which can be made explicit.
 4. Thus the transaction zone or range of estimates together with other report writing techniques are intended to provide better methods of recognizing the need for tolerance in the decision process for the conditions of uncertainty which surround the appraisal estimate.
- IV. Ratcliff has been most comprehensive in statement of basic appraisal theory, many writers are contributing to the rethinking of the appraisal process and appraisal techniques. A number of selected readings by these other professional and academic critics have been included in the appendix of your workbook.

Exhibit 2

TRADITIONAL APPRAISAL AS A FICTIONAL SET OF FEASIBILITY ASSUMPTIONS

Feasibility Analysis

Will the project really work for a specific investor?

1. Objectives - decision standards provided by client decision process
 - a. Maximize spendable cash of total enterprise
 - b. Subjective gratification of specific individual
 - c. Adaptation to enterprise management specialties and weaknesses
2. Aggregate market potential opportunity identification
3. Merchandising analysis (Defining competitive edge) and specific user profile
4. Legal-political context
 - a. All legal constraints on site, seller, buyer and user are considered
 - b. What is legal is qualified by what is political
5. Physical-technical constraints are examined in terms of what might be
6. Impact on environment and community specifically forecast
7. Financing from buyer viewpoint considering all profit centers
8. Income tax advantages or disadvantages affecting spendable cash
9. Actual cash revenues and expenses forecasted for each period of time horizon
10. Limiting assumptions of solution
 - a. Identification of potential variance and sensitivity of objectives to alternative futures
 - b. Responsibility allocated among sources of expertise
 - c. Budget & purpose of study edits information scope
 - d. Format of analysis determined by structuring of data to lead to desired conclusion or recommendation

Appraisal Analysis

What would the project sell for if it did work for a typical investor?

1. Objectives - decision standards provided by theoretical framework
 - a. Maximize economic surplus of individual parcel
 - b. Prudent behavior of economic man
 - c. Average management to isolate return to land & capital
2. Aggregate market potential business climate
3. Merchandising comparison (Defining standard competitive substitute)
4. Legal-political context
 - a. Legality assumed
 - b. Limited to site use rather than regulations on probable user as alternative buyers are assumed
5. Physical-technical constraints are studied as is or in terms of conventional uses
6. Impact on environment and community assumed acceptable within existing permitted uses
7. Financing from lender viewpoint considering only net income line and below
8. Income tax not considered except implicitly recognized in market comparison
9. Revenues and expenses generally normalized and projected on linear trend for standard period
10. Limiting assumptions of solution
 - a. Average outcome without qualification as to alternative futures
 - b. Responsibility denied for other areas of expertise
 - c. Date of appraisal edits information scope
 - d. Format of analysis defined by model of fair market value appraisal report

- A. Much commentary on appraisal can be divided between those who would just as soon scrap the historical textbooks and language of appraisal (a la Ratcliff and Graaskamp), and those who would simply like to refine present dogma and techniques of appraisal report content (Wendt and Smith).
- B. While the rebels attack theory head-on with the romantic notion of toppling the temple of principles built in Chicago, the more pragmatic politicians are realistically chipping away at the stone tablets from within traditional institutions.
- C. A few argue that the change in appraisal method represents a shift from deductive logic based on principles to inductive forecasting tools capitalizing on observed behavior. A parody of scientific method versus theory and reason.
- D. Some of the other issues in debate relate to the following topics:
 - 1. What is function of appraisal?
 - a. Benchmark of value
 - b. Predict transaction price under conditions of uncertainty
 - c. To answer a question of a client
 - 2. What is the standard of professionalism?
 - a. Format (profession vs. institution)
 - b. Tools and techniques
 - c. Standards of business conduct
 - d. Reliability of results
 - 3. What is the frame of reference of real estate productivity?
 - a. The parcel
 - b. The individual investment interest
 - c. The community
 - d. The collective interest of society

COFFEE BREAK

CONTEMPORARY REAL ESTATE APPRAISAL REPORT

Suggested Outline

1/1/78

Letter of Transmittal

1. Brief statement of appraisal issue
2. Definition of value applied
3. Value conclusion (qualified by financing, terms of sale, and range of probable transaction zone as appropriate)
4. Sensitivity of conclusion to critical assumptions
5. Property observations or recommendations
6. Incorporation by reference of limiting assumptions and conditions

Table of Contents

List of Exhibits

Digest of Facts, Assumptions, and Conclusions

1. Property type
2. Property location
3. Property ownership
4. Determinant physical attributes
5. Controlling legal-political attributes
6. Pivotal linkage attributes
7. Marketable dynamic attributes
8. Most probable use conclusion
9. Most probable buyer profile assumed
10. Initial probable price prediction and central tendency
11. Adjustment of preliminary value estimate for external factors or market position of parties
12. Testing of corrected probable price for consistency with most probable buyer objectives
13. Final value conclusion and range of error estimate as appropriate

I. Appraisal Problem Assignment

- A. Statement of issue or circumstances for which appraisal is intended to serve as a decision benchmark and date of valuation
- B. Special problems implicit in property type or issue that affect appraisal methodology and definition of value
- C. Special assumptions or instructions that are provided by others
- D. Definition of value, which is the objective of appraisal analysis and disciplines appraisal process
 1. Selected definition and source
 2. Implicit conditions of the definition
 3. Assumptions required by relevant legal rulings
- E. Definition of legal interests to be appraised
 1. Legal description and source
 2. Permits, political approvals, and other public use entitlements
 3. Fixtures or personalty to be included with sale
 4. Specific assets or liabilities excluded as inconsistent with issue or premise of appraisal

II. Property Analysis to Determine Alternative Uses

A. Site Analysis

1. Physical (static) site attributes (size, shape, geology, slope, soil hydrology, etc.)
2. Special site improvements (wells, bulkheads, irrigation systems, parking surfaces with unique salvage or re-use characteristics, etc.)
3. Legal-political attributes (applicable federal, state and local zoning, covenants, easements, special assessments, or other land use codes and ordinances, etc.)
4. Linkages of site (key relationships to networks, populations, or activity centers that might generate need for subject property)
5. Dynamic attributes of site (perceptual responses of people to site in terms of anxiety, visibility, prestige, aesthetics, etc.)
6. Environmental attributes of site as related to off-site systems or impact areas.

B. Improvement Analysis

1. Physical (static) attributes of improvements, cataloged by type, construction, layout, condition, structural flaws, etc.
2. Mechanical attributes (brief statement of heating, ventilating, air conditioning, electrical, plumbing, and fire or safety systems in terms of limitations on use or efficiency)
3. Special structural linkages to off-site elements (tunnels, bridges, adjoining structures, etc.)
4. Legal-political constraints on use of existing improvements (federal, state and local building codes, fire codes, conditional use procedures, neighborhood associations, and inspection liens of record for violations).
5. Dynamic attributes of existing improvements (impressions created by type, bulk, texture, previous uses, past history, or functional efficiency)
6. Current uses and tenancies of improvements, if any
7. Environmental impact attributes of improvements on environs

E. Identification of Alternative Use Scenarios for Subject Property

1. Marketing existing uses of property as is
2. Renovation of existing property and marketing improved space
3. Redirection of existing property to alternative tenancies and uses
4. Replacement of existing improvements or program with new uses

III. Selection of Most Probable Use

A. Comparative Analysis of Alternative Uses

1. Testing and ranking alternative-use strategies for legal-political compatibility
2. Testing alternative-use scenarios for fit to physical property attributes within reasonable cost to cure
3. Selection of scenarios that justify market research

B. Analysis of Effective Demand for Selected Uses

1. Search for rents and income potentials of scenario space-time products
2. Screen and rank market targets
3. Apply income-justified residual investment approach to rank economic power of alternative market scenarios
4. Evaluate marginal revenue, marginal investment risk trade-offs

C. Summary Matrix for Selection of Most Probable Use Scenario

1. Physical fit
2. Legal-political risk
3. Strength of market demand
4. Adequacy of available financing
5. Revenue and cost assumptions risk

IV. Prediction of Price for Subject Property

A. Specification of Most Probable Buyer Type Implied by Most Probable Use

1. Criteria motivations of alternative buyer types
2. Selection of most probable buyer type as basis for prediction of a sales transaction with logic for ranking of alternatives
3. Specification of essential site, improvement, financial, or key decision criteria of principal alternative buyer types

B. Explanation of Appraisal Methodology for Prediction of Probable Purchase Price

1. Preferred method: to infer buyer behavior from actual market transaction and market data available from sales by comparable buyers of acceptable alternative properties
2. In the absence of adequate market sales data, the alternative method selected for simulation of probable buyer decision process
3. If market influence of simulation is impossible, select normative model such as investment value, or cost to replace

C. Search for Comparable Market Sales Transactions

1. Unit of comparison
2. Method of comparison
3. Explanation of search parameters
4. Investigation of sale transaction circumstances
5. Evaluation for comparability
6. Definition of predominant terms of sale
7. Source of comparative adjustments

D. Determination of Suitability of Existing Market Data for Inference of Value for Subject Property

1. Where data is adequate, selection of market comparison method to estimate value
2. Where data is lacking or misleading, selection of alternative valuation method and reasoning
3. Conclusion leads to E or F

E. Simulation of Probable Buyer Decision Process If Market Comparison Approach Is Inconclusive or Impossible

1. Source and explanation of simulation model
2. Schedules of simulation assumptions
3. Range of alternative simulation value predictions (sensitivity analysis)

(OR) F. Selection of Normative Model of Buyer Behavior

1. Investment model
2. Cost-to-replace model
3. Nonquantitative decision models

G. Computation of Most Probable Price and Standard Error of Prediction

H. Correction of Preliminary Value Estimate for External Factors

1. Identification of conditions relative to date of appraisal not present in market comparison assumptions
2. Specification of political contingencies that might upset normal appraisal assumptions of substitution
3. Identification of any violation of conditions in the definition of value by the appraisal methodology
4. Indication of adjustment necessary to preliminary probable price estimate or
5. Explicit statement that no adjustment is necessary

I. Test of Most Probable Price or Value Conclusion by Means of:

1. Comparison to values derived from selected alternative appraisal methodology
2. Demonstration of achievement of objectives of most probable buyer minimum selection criteria
3. Measurement of fit of financial cash requirements to market rents, lender ratios, or other relevant constraints
4. Comparison to decision criteria appropriate to issue (financial ratios required by mortgage lender, comparative assessments of similar property for the tax appeal board, rates of return in alternative investments, construction prices for similar property, or whatever demonstrates consistency with statement of the issue)

V. Appraisal Conclusion and Limiting Conditions

A. Definition of Value and Value Conclusion of the Report

B. Certification of Independent Appraisal Judgment

C. Statement of Limiting Conditions That Establish:

1. Contributions of other professionals on which report relies
2. Facts and forecasting under conditions of uncertainty
3. Critical assumptions provided by the appraiser
4. Assumptions provided by the client
5. Controls on use of appraisal imposed by the appraiser

Appendices

Maps, data sets, only if referred to in the text. These data collections would slow down the reader if included as an exhibit and are secondary to the argument in the body of the report.

CONTEMPORARY REAL ESTATE APPRAISAL SEMINAR

Concept of Most Probable Buyer Type/Most Probable Price

- V. Ratcliff Theory would place as much emphasis on behavior of prospective buyers or investors as on the operating behavior and characteristics of a property. Appraisal is trying to predict how people, buyer and seller, will behave in the future, converting a decision to a mutually acceptable price.
- A. Each party is operating under certain assumptions and constraints:
1. Buyers assume they will have to pay no less than some specific price, that others are bidding for the property, that they cannot afford to pay more than a certain amount of income for shelter or business location, or that a desired use requires a specific set of attributes.
 2. Sellers assume buyers see the property in the same way they do, that the property has some inherent value and utility, and that its just a matter of time before some fish can be found to pay the asking price.
- B. The definition of value selected by the appraiser also assumes certain motivations for buyer and seller which typically are a matter of convenience for the appraiser but often a significant source of error in the prediction of price. While the wording on fair market value differs slightly, the following conditions are always assumed to prevail:
1. Competitive market conditions.
 2. An informed buyer and seller.
 3. No undue pressure on either party.
 4. "Rational" or prudent economic behavior by both buyer and seller.
 5. A reasonable turnover period.
 6. Payment consistent with the standards of behavior of the market.
 7. Market Value looks at the transaction from the point of view of the buyer.
- C. However, a buyer is integrating and comparing a property more to a personal set of needs than to a property alternative which is only roughly similar to another in function and potential.
1. For example, a commercial office building developer seeks a site with a minimum number of construction problems, an optimum shape, and maximum rental value. On the other hand, the committee buying a home office site for an insurance company or bank will emphasize visibility and location at the expense of almost any development cost and despite any reduction in rental value for re-use.
 2. A young couple may buy an old house because it is run down and in need of renovation in order that the initial cost is low and the opportunity for creating equity is greatest, while the seller is selling because of irritation with the fit of the structure to his lifestyle or because he has reached the end of his lifecycle in that location.

3. One man's floor is another man's ceiling.
 4. Therefore, the eventual sales price at which two parties will agree is arranged within a zone of expectations and requirements reflecting the assumptions of each party. Indeed some transactions are designed so that the final price is determined later based on whose assumptions prove to be more correct in a speculative situation.
- D. Both buyer and seller enter negotiations with a subjective value expectation (V_s) which is a constraint in bargaining for the property.
1. "The actual selling price will usually represent a compromise between what the buyer would have paid if necessary and what the seller would have taken as a last resort." p. 13, Ratcliff.
 2. Therefore, the appraisal must take more than just the buyer viewpoint of the transaction or the appraisal will not be of a value that reaches the minimum the seller can or would accept.
- E. This leads then to the concept of a transaction zone around a point which is the central tendency of bargaining, a point we call most probable price. Notice the assumptions of most probable price may be somewhat more acceptable in terms of pragmatic realism than those of fair market value.
1. Subjective value (V_s) is a figure with which buyers and sellers enter the market as a constraint in the bargaining. The actual selling price will represent a compromise between what the buyer would have paid if necessary and what the seller would have taken as a last resort.
 2. In residential work, where there are many sales, the transaction zone may be defined statistically as the standard deviation of the estimate.
 3. The possible variance or error in the estimate of probable sales price may be intuitive by the appraiser.
 4. The zone may be defined by the logic of bargaining positions. The seller wants to cover his debt and broker fees; the buyer assumes a certain value in a new use less remodeling costs, less a cushion for unexpected costs and profit.
 5. In the cast of investment properties, sensitivity analysis may define the range of alternative outcomes.
 6. There may be certain conditions which cannot be known by the appraiser but which would change his estimate as to what the buyer or seller would accept; the appraiser may define the transaction zone as the range between optimistic and pessimistic impacts of external events.
- F. The important function of the transaction zone is to alert the reader of the report:
1. To the fact that an appraisal value is not a certainty but a prediction of a future hypothetical business event.
 2. Present value is the purchase of a set of assumptions about the future and therefore value depends on which set of assumptions the buyer and seller "buy."
 3. The reliability of a prediction is important in using probable price as a benchmark for a decision; reliability is less important in assessment than in investment, conservatism more important. in lending than in equity investment, etc.

VI. ^{Three} ~~Two~~ Basic Methods of Appraisal

As you know, Ratcliff concludes that most appraisals are concerned with prediction of a future event, a transaction price. Since an appraisal method is a forecasting tool, forecasting is best done with some past experience. Failing that, the best method is simulation of the real estate market process.

- A. Given reliable information on past market behavior, the preferred method of appraisal is to process the data, statistically if possible, to derive a prediction of future price behavior under given conditions and with means for estimating the reliability of the prediction.
 - 1. Statistical prediction if possible.
 - 2. Statistical rules for definition of a data set at the least.

- B. Should market data be unavailable or inconclusive, the appraiser is forced to resort to the second method of appraisal, namely the construction of a real estate market model of factors which reflect his understanding of how buyers and sellers might behave.
 - 1. The income approach and the cost approach are submodels of how an investor is supposed to behave.
 - 2. After tax investment models are another submodel of market behavior, but while these may measure demand from the buyer's viewpoint, it may not measure the minimum price expected by the seller who also has a tax model to consider. In using the second approach, the appraiser must be very careful to indicate price on the supply side representing minimum expectations (V_s) of the seller.

- C. Should there be no sales and no way to verify how buyers would review the specific property (utility case-rate base or kilowatt production?), then the appraiser falls back to normative methods.
 - 1. Normative means what the buyer would do if he were as smart as the appraiser and motivated only by a desire to maximize wealth.
 - 2. The traditional income approach on the cost approach are normative models unless it can be proven buyers behave accordingly.
 - 3. After tax cash flow models are normative models until it can be shown how these models value property.

CONTEMPORARY REAL ESTATE APPRAISAL SEMINAR

VII. Inferring Future Price From Sales Data

- A. For residential properties there are often many sales of similar properties so that powerful statistical tools can be brought into play, such as multiple regression, factor analysis, etc. However, the simple average can also lend itself to statistical inference.
- B. Dispersion is the variation or scatter of a set of values. Measures of dispersion are needed for the following basic purposes:
 - 1. To gauge the descriptive reliability of averages.
 - 2. To serve as a basis for control of the variability itself (such as rejecting a comparable that lies outside a certain range).
 - 3. To summarize facts, both an average and a measure of dispersion should be presented.
- C. When dispersion is small, then the selected average is a typical value in that it closely represents the individual values in the set and it is reliable in that it is a good estimate describing the typical case in the population. It is a useful generalization. Conversely, an average with very great dispersion is not very descriptive of the data set and may be a misleading generalization.
- D. Measures of dispersion include:
 - 1. A range
 - 2. The quartile deviation
 - 3. The mean deviation
 - 4. The standard deviation
- E. Consider the data on some apartment site land sales in Madison provided in Exhibits 1, 2, and 3. The range is the difference between the largest and smallest values of the variable:
 - 1. \$5.60 - \$6.50 per square foot of land or 90¢
 - 2. \$1970 - \$2208 per dwelling unit built or \$238
 - 3. \$3.72 - \$4.23 per square foot of gross building area or 51¢
 - 4. \$1226 - \$1327 per total number of rooms built or \$101
- F. Exhibit #3 shows the mean and the standard deviation of the mean.
- G. Quartile deviation must be applied to group data which are ranked from high to low. First the data is divided at the median and then each half of the data is split in half once again. Consider the net rentals of older supermarkets under existing leases provided in Exhibit #4.

Exhibit #4

CUMULATIVE FREQUENCY DISTRIBUTIONS
Supermarket Net Rents for 214 Stores in Chain X

(1) New Rent per Square Foot	(2) Number in Class with Lower Limit Shown	(3) Number Earning Less	(4) Number Earning as Much or More
\$2.25	2	0	214
2.35	23	2	212
2.45	49	25	189
2.55	63	74	140
2.65	45	137	77
2.75	25	182	32
2.85	3	207	7
2.95	4	210	4
3.05	<u>0</u>	<u>214</u>	<u>0</u>
Total	214	1051	875

H. In the full array of data, the value of Q_1 and Q_3 are found to be \$2.50 and \$2.70, meaning 1/4 of the properties generate less than \$2.50 a square foot and 1/4 exceed \$2.70 per square foot while the middle half fall between these values. The quartile deviation is then $(2.70 - 2.50)/2$ or 10¢, or stated another way the range of the second and third quartile is about 10¢ per square foot.

VIII. When comparable sales have only one dimension, such as net lease-able area or number of rooms, a direct mean and some of the squares dispersion test is possible. However, usually it is necessary to consider a variety of factors and discover how price changes relative to the net differences of each property. Linear regression is one such method.

A. Ratcliff in Chapters 6 and 7 demonstrates a point system which ranks properties and is then weighted by buyers priorities. The weighted points are then compared to unit price. This system may be too elaborate for houses but can be demonstrated on a variety of commercial properties.

B. Consider the evaluation of vacant industrial land in Exhibits 5, 6, and 7.

1. Point system should be kept simple. 1-3-5 indicates below average, average, and above average.
2. If the appraiser is capable of making more careful distinctions between comparable properties, he can use a ten point scale such as 0, 4, 6, 8, 10 for each item, being careful not to change scales.
3. Many small judgments are better than large rough adjustments because of the theory of off-setting errors. Too big a range in scoring implies drastic differences between the worst and the best.

4. Note that Exhibit 7 provides an objective scale for most factors so that the reader can understand the score. The weights in this case were corroborated in the narrative of the report from a 1968 study by Real Estate Research Corporation.
- C. All calculations for establishing the "a" and "b" factors for linear regression appear in Exhibit #8 and are charted in Exhibit #9.
- D. An example using restaurant sites in Madison is provided in Exhibits 10, 11, and 12.
- E. An example of a single family appraisal is provided in Exhibits 13, 14, 15, and 16.
- F. A fourth example comparing old store buildings in downtown Madison will be provided in a demonstration appraisal.

EXHIBIT #1

Basic Information of residential Multi-Family Land Sales Comparables

Factors	420 W. Wilson No. 1	219=N. Frances No. 2	102 N. Franklin No. 3	434 W. Mifflin No. 4	427 W. Main No. 5
Sales Price	\$ 84,950	\$48,000	\$86,900	\$160,000	\$53,000
Sales Date	'73	'72	'72	'72	'72
Type of Deed	WD	WD	WD	WD	WD
Volume and Page	403/510	346/561	334/ 23	337/215	342/113
Grantor	R.A. Paape Co. Inc.	Work of God, Inc.	Brown, Emily	Voss, Rob't	Miller + wife
Grantee	Hillmark, Dev. Corp.	Hillmark Corp.	Courtyard Assoc.	American United Investment	Hillmark Corp.
Land Area	13,068	7,920	15,246	26,400	8,712
Zoning	R-6	R-6	R-6	R-6	R-6

All have city services, sidewalk and street improvements
 No adjustment for time required as residential economics would not permit inflation of land prices.

Sandwich Research, Inc.

EXHIBIT #2

Vacant Land Market Comparison
Residential Use Land Price: Mean

Comparable Sales

Factors	420 W. Wilson No. 1	219 N. Frances No. 2	102 N. Franklin N. 3	434 W. Hifflin N. 4	427-31 W. Main No. 5	Mean (X) 1-5
Sales Price	\$84950	\$48000	\$86900	\$160000	\$53000	\$432850
Date of Sale	'73	'72	'72	'72	'72	
Land Area (sq.ft.)	13068	7920	15246	26400	8712	71346
No. of Dwelling Units Built	43	24	43	73	24	207
Total Gross Bldg.	20070	12670	24364	43040	10900	111044
Total # Rms Blt.	65.5	38	65.5	130.5	40	339.5

Mean Land Price - \$/per:

1. Square Ft. of Land	\$6.50	\$6.06	\$5.60	\$6.06	\$6.08	\$6.06
2. Dwelling Unit Blt.	\$1976	\$2000	\$2020	\$2192	\$2208	\$2079
3. Total Gross Bldg. Floor Area	\$4.23	\$3.79	\$3.79	\$3.72	\$4.86	\$4.08
4. Total # Rms Blt.	1297	1263	1327	1226	1325	1288

Exhibit 3

Vacant Land Market Comparison
Multi-Family Residential Use Land Price
Mean & Standard Deviation

	Comparable	Land Price/ Comparable Unit	$\bar{X}-X$	$(\bar{X}-X)^2$	Mean Deviation $MD = \frac{\sum \bar{X}-X}{n-1}$	Standard Deviation $S = \sqrt{\frac{\sum (\bar{X}-X)^2}{n-1}}$
Land Price Per:						
Sq. Ft. of Land (Row #1, Ex. #6)	1	\$6.50	.44	.19		
	2	6.06	0	0	$\frac{.92}{4}$	$\sqrt{\frac{.44}{4}}$
	3	5.60	.46	.21		
	4	6.06	0	0		
	5	6.08	.02	.04	\$.23	\$.33
Total		\$30.30	.92	.44		
Mean (sum x_i 's) n		\$ 6.06				
No. of DU Built (Row #2, Ex. #6)						
	1	1976	53	2809		
	2	2000	29	841	$\frac{433}{4}$	$\sqrt{\frac{62341}{4}}$
	3	2020	9	81		
	4	2192	163	26569		
	5	2208	179	32041	\$108	\$249.68
Total		\$10396	433	62341		
Mean		\$ 2079				
Total Gross Bldg. Area Built						
	1	4.23	.15	.02		
	2	3.79	.29	.08	$\frac{1.87}{4}$	$\sqrt{\frac{.92}{4}}$
	3	3.79	.29	.08		
	4	3.72	.36	.13		
	5	4.86	.78	.61	\$.465	\$.48
Total		\$20.39	1.87	.92		
Mean		\$ 4.08				
Total No. Rooms Built (Row #3, Ex. #6)						
	1	1297	9	81		
	2	1263	25	625	$\frac{172}{4}$	$\sqrt{\frac{7440}{4}}$
	3	1327	39	1521		
	4	1226	62	3844		
	5	1325	37	1369	\$43	\$43.13
Total		\$6438	172	7440		
Mean		\$1288				

EXHIBIT #5

Industrial Land Sales Selected as Comparables
to MG & E Subject Parcel

	Date of Sale	Price	Public Record	Square Feet	(Acres)	\$/Sq. Ft.
1. MATC	6/8/67	\$108,750	Confirmed by MATC Finance Director	152,460	(3.5)	.71
2. MATC	1/23/67	75,000	Vol.828,p.280	81,828	(1.88)	.92
3. Gorman	12/20/65	17,500	Vol.436,p.463	21,060	(.48)	.83
4. Holfman	6/5/64	15,000	Vol.779,p.558	17,050	(.39)	.88
5. Garrett	5/31/63	12,000	Vol.758,p.226	13,932	(.32)	.86
6. Madison Transit	1/4/68	55,000	Vol.4,p.358	211,701	(4.86)	.26
7. Madison Trust	12/28/66	45,000	Vol.828,p.204	67,900	(1.56)	.66
8. NW Mutual	9/9/66	117,500	Vol.824,p.144	138,521	(3.18)	.85

EXHIBIT #7

Quality Scores & Weight Per Category

1. Size (Marketability Factor)	<u>Weight</u>
0 - 1 acre = 5	20
over 1 - 3 = 4	
over 3.5 - 10 = 3	
over 10 - 20 acre = 2	
over 20 acre = 1	
2. Accessibility to all areas (in terms of distance and time) 1-5 where 5 = premium + 3 = average	20
3. Visibility from major artery 1-5	15
4. Availability of sewer/water at site 1-5	15
5. Availability of rail 1-5	10
6. Soils and topography	<u>20</u>
	<u>100%</u>

Exhibit 16

Table of Scores for Comparable Properties

	<u>1</u>	<u>2</u>	<u>3</u>	<u>4</u>	<u>5</u>	<u>6</u>	<u>7</u>	<u>8</u>	<u>Subject</u>
Size	3	4	5	5	5	3	4	4	1
Access	4	4	4	4	4	2	3	3	4
Visibility	5	5	5	5	4	1	1	2	5
Sewer/water	5	5	5	5	5	2	5	5	5
Rail	1	1	1	1	3	1	2	2	4
Soils	2	3	2	2	2	4	5	5	1

<u>Feature</u>	<u>Weight</u>	<u>Weighted Ratings</u>								<u>Subj</u>
		<u>1</u>	<u>2</u>	<u>3</u>	<u>4</u>	<u>5</u>	<u>6</u>	<u>7</u>	<u>8</u>	
Size	20	60	80	100	100	100	60	80	80	20
Access	20	80	80	80	80	80	40	60	60	80
Visibility	15	75	75	75	75	60	15	15	30	75
Sewer/water	15	75	75	75	75	75	30	75	75	75
Rail	10	10	10	10	10	30	10	20	100	40
Soils	20	40	60	40	40	40	80	100	100	20
Total		340	380	380	380	385	235	350	365	310
Price/Sq. Ft.		.71	.92	.83	.88	.86	.26	.66	.85	

EXHIBIT #8

Least Squares Regression

Model $Y = a - b X$
 where $Y =$ estimated land value per square foot
 $X =$ weighted quality ratings

Comparables	Y	X	Y ²	X ²	XY
1	.71	340	.504	115600	241.400
2	.92	380	.846	114400	349.600
3	.83	380	.689	114400	315.400
4	.88	380	.774	114400	334.400
5	.86	385	.740	148225	331.100
6	.26	235	.068	55225	61.100
7	.66	350	.436	122500	231.000
8	.85	365	.723	133225	310.250
	$\Sigma = 5.97$	$\Sigma = 2815$	$\Sigma = 4.779$	$\Sigma = 1007975$	$\Sigma = 2174.25$

Step 2: Compute mean of Y and mean of X

$$\bar{Y} = \frac{\Sigma Y}{n} = \frac{5.97}{8} = .746$$

$$\bar{X} = \frac{2815}{8} = 351.875$$

Step 3: Compute ΣY^2 , ΣX^2 and ΣXY

$$\begin{aligned} \Sigma Y^2 &= \Sigma Y^2 - n(\bar{Y})^2 \\ &= 4.779 - 8(.746)^2 \\ &= 4.779 - 8(.557) \\ &= 4.779 - 4.452 \\ &= .327 \end{aligned}$$

$$\begin{aligned} \Sigma X^2 &= \Sigma X^2 - n(\bar{X})^2 \\ &= 1007975 - 8(351.875)^2 \\ &= 17446.873 \end{aligned}$$

$$\begin{aligned} \Sigma XY &= \Sigma XY - n\bar{X}\bar{Y} \\ &= 2174.25 - 8(.746)(351.875) \\ &= 2174.25 - 2099.99 \\ &= 74.26 \end{aligned}$$

Step 4: $b = \frac{\Sigma XY}{\Sigma X^2} = \frac{74.26}{17446.873} = .004256$

EXHIBIT #8 continued

Step 5: $a = \bar{Y} - b\bar{X}$

$$= .746 - .004256 (351.875)$$

$$= -.7517$$

Hence $Y = -.7517 + .004256 (X)$
 $Y_n = -.7517 + .004256 (310)$
 $= .56765$ say .57

Step 6: Compute standard error

$$S_{y.x} = \sqrt{\frac{\sum y^2 - b \sum xy}{n-2}}$$

$$= \sqrt{\frac{1327 - .004256 (74.26)}{8-2}}$$

$$= \sqrt{\frac{.10949}{6}}$$

$$= \sqrt{.001825}$$

$$= .042719$$
 say \$.04

Step 7: Compute r^2

$$r^2 = \frac{\sum xy}{\sum x^2 \sum y^2}$$

$$= \frac{74.26}{(17446.873)(.327)}$$

$$= .9665$$

EXHIBIT #10

Basic Information on Restaurant-Commercial Land Sale Comparables

	Barnaby's East	Barnaby's West	Bud's West	Pigs Ear East	Marc's Big Boy South	Marc's Big Boy East
Sales Price	\$92,000*	\$89,000	\$75,700	\$91,000	\$87,500	\$85,000
Sales Date	10-6-70	6-30-70	6-29-71	5-20-72	9-3-69	3-15-68
Type of Deed	Lease with Option	WD	WD	WD	WD	WD
Volume & Page	209-455	184-75	264-173	344-385	130-463	15-108
Grantee	Barnaby's Inc.	Barnaby's Inc.	Clyde Chamberlain	Poole, Inc.	B & G Realty	B & G Realty
Area	38,211	32,900	45,236	141,570	38,327	30,237
Zoning	C-2	C-3-L	C-3-L	M-1	C-2	C-2
Principal Business Frontage	E. Washington Ave.	Mineral Point & Grand Canyon Roads	Odana Rd.	Cottage Grove Road & Atlas Avenue	S. Park Street	E. Washington Ave.
Position on Block	Inside lot	Corner lot	Inside lot	Corner lot	Corner lot	Inside lot

All have city services, Pigs Ear did not have curb and gutter
 No adjustment of time required as restaurant economics would not permit inflation of land prices.

EXHIBIT #11

Attribute Point and Weight Comparison
Of Restaurant-Commercial Land Sales and Subject Property

(See Exhibit #8)	Barnaby's East	Barnaby's West	Bud's West	Pigs Ear East	Marc's Big Boy South	Marc's Big Boy East	Subject
30 *Site	Points Wgt'd Pts						
Shape	5	1	5	3	5	3	5
% Usable	3	3	5	5	5	5	1
Site Preparation	3	1	5	5	5	5	5
Visibility	3	5	5	3	5	3	3
Access							
Left & Right Turn	5	5	5	3	3	3	1
Frontage Road	3	5	5	1	5	5	5
Total	<u>18</u>	<u>20</u>	<u>25</u>	<u>20</u>	<u>28</u>	<u>24</u>	<u>20</u>
Weight	540	600	750	600	840	720	600
50	Linkages						
Traffic Volume	5	5	3	3	5	5	3
Supportive Retail/Serv.	5	5	3	1	1	3	1
Proximity to Multi-Family Residential	1	5	5	1	3	3	3
Proximity to Employ.	3	3	3	1	1	5	3
**Interstate-Beltline	<u>2</u>	<u>1</u>	<u>1</u>	<u>3</u>	<u>2</u>	<u>2</u>	<u>1</u>
Total	<u>15</u>	<u>18</u>	<u>15</u>	<u>9</u>	<u>12</u>	<u>18</u>	<u>11</u>
Weight							
20	Image						
Development Activity	5	5	3	1	1	3	1
Prestige of Street Address	<u>5</u>	<u>5</u>	<u>3</u>	<u>1</u>	<u>3</u>	<u>5</u>	<u>1</u>
100	Total	10	10	6	2	4	8
		<u>200</u>	<u>200</u>	<u>120</u>	<u>40</u>	<u>80</u>	<u>160</u>
	*Scale 1,3,5 Except **	<u>1490</u>	<u>1700</u>	<u>1620</u>	<u>1090</u>	<u>1520</u>	<u>1190</u>

EXHIBIT #12

Determination of Linear Regression
 Weighted Mean Value of Land/sf
 Commercial-Restaurant

Comparable	1 Land \$/sf	2 Total Wgtd. Pts.	3 (Land \$/sf) ²	4 (Wgtd.Pts) ²	5 (3 x 4)
	Y _i	X _i	Y _i ²	X _i ²	X _i Y _i
1	\$2.40	1490	5.76	2220100	3575
2	2.73	1700	7.45	2890000	4641
3	1.67	1620	2.79	2624000	2705
4	.64	1090	.41	1881000	698
5	2.28	1520	5.20	2310400	3466
6	2.81	1780	7.90	3168400	5002
TOTAL	\$12.53	9200	29.51	15093000	20087
Mean	(Y)=\$2.09	(X)=1533			

Calculations of Mean, Standard Deviation

$$\begin{aligned} \text{Sum } y^2 &= Y^2 - n(Y)^2 \\ &= (29.51)^2 - 6(2.09)^2 \\ &= 845 \end{aligned}$$

$$\begin{aligned} \text{Sum } x^2 &= X^2 - n(X)^2 \\ &= 1509300 - 6(1533)^2 \\ &= 993366 \end{aligned}$$

$$\begin{aligned} \text{Sum } xy &= XY - n(x)(Y) \\ &= 20087 - 6(1533)(2.09) \\ &= 863 \end{aligned}$$

$$Y' = a + bX_{\text{subject}}$$

$$b = \frac{\text{Sum } xy}{\text{Sum } x^2} = \frac{863}{993366} = .00087$$

$$a = (Y) - b(X) = \$2.09 - .00087(1533)$$

SALES PRICE/SUBJECT SITE

$$Y' = a + bX_{\text{subject}}$$

$$= -\$.76 + .00087(1190) = \underline{\$1.80}$$

STANDARD DEVIATION

$$S_{xy} = \frac{\text{Sum } y^2 - b(\text{Sum } xy)}{n-2}$$

$$= \$ \underline{.15}$$

EXHIBIT #13

Buyer Characteristics in Dudgeon School Area

1. 636 Crandall Street
 Married couple, 27 years old - one year old child - college degrees - salary \$10,000 per year
 Valued protected play area for child, convenient location on bus line, remodeled kitchen, house with character within price range and possibility to build equity. They are having home rewired and doing minor maintenance required themselves. Financed with a conventional mortgage and second mortgage from state VA
 Relative importance of buyer factors reported by interviewer:

Physical condition	10
Interior space	25
Mechanical equipment	10
Location & neighborhood	25
Financial operating burden	25
lot	5
	100

2. 821 Minakwa
 26 year old couple, no children - project manager - college degree \$10,000 salary.
 Primary motivations were: house had more character and value than a new house for the same price, location for bringing up children, mechanicals in good condition and fireplace. Lot was considered a drawback.

3. 3120 Gregory
 Man and wife in mid -forties, no children - needed three bedrooms with full dining room and 2-stories high, wanted a two car garage but settled for one. Preferred west side for convenience and more value appreciation.
 Purchased house expecting to repaint entire building.
 Buyer reported purchase price of \$24,000

4. 2455 Mohawk Dr.
 Married couple, 27 years old, no children, both work with college educations. Husband gave major weight to structural soundness, neighborhood appeal, and location near bus line and beltline.
 Wife gave preference to wooded neighborhood and outdoor yard, and space utilization inside. Mechanical and storage were given only medium emphasis.

5. 645 Sheldon St.
 28 year old married couple, no children, college educated.
 They preferred home with garage, fireplace, close to bus line, and on west side between campus, square and Hilldale. Wanted garden.
 Physical condition was rated highly, exterior appearance was not important. Lot size was more important with mechanical and interior condition less important.

6. 1510 Whenona Drive
 Married couple (approximately 30) - 2 children, ages 3 and 5 - college degrees - father, \$10,000; wife works as a nurse.
 Couple emphasized structural soundness as they expected to remain in house more than 10 years and possibly add a room at the rear. They wanted good sized rooms and visual appeal or character of an older home in a stable neighborhood. Valued location for convenience and stability of value and knew other young couples were moving in with plans to fix up their homes, too. They did not expect mechanical equipment to be modern in an old home and expected to update the kitchen eventually.
 Off-site factors were taken for granted except for bus which wife used every day for work.

821 Minakwa St.

3120 Gregory

645 Sheldon St.

636 Crandell St

628 Crandell St

640 Knicherbock

657 Knicherbock

SUBJECT

<u>Features</u>	Weight	Rating / Weighted Ratings							
		821 Minakwa St.	3120 Gregory	645 Sheldon St.	636 Crandell St	628 Crandell St	640 Knicherbock	657 Knicherbock	SUBJECT
Location & Neighborhood	25	2/50	6/150	4/100	2/50	2/50	4/100	4/100	2/50
Lot	5	2/10	4/20	4/20	6/30	4/20	4/20	4/20	4/20
Financial Burden	15	4/60	2/30	4/60	6/90	4/60	4/60	4/60	6/90
Exterior Architecture	15	4/60	4/60	4/60	6/90	6/90	6/90	6/90	4/60
Mechanical	10	2/20	2/20	4/40	6/60	6/60	4/40	4/40	6/60
Physical Condition	10	2/20	4/40	4/40	4/40	4/40	4/40	4/40	4/40
Interior Attractiveness	20	2/40	2/40	4/80	4/80	6/120	6/120	6/120	4/80
TOTAL	100	260	360	400	440	440	470	470	400
PRICE		\$26,300	\$24,500	\$23,800	\$22,900	\$22,900	\$21,900	\$21,900	???

Ratcliff Linear Regression

EXHIBIT #15

$$Y = a + bx$$

$$b = \frac{n(\sum xy) - (\sum x)(\sum y)}{n(\sum x^2) - \sum(x)^2}$$

$$a = \frac{Y - b(\sum x)}{n}$$

$$n = 7$$

The number of comparables.

$$\sum Y = 164,200$$

The sum of the seven actual prices paid for the comparables.

(\$26,300) + (\$24,500) + (\$23,800)...

$$(\sum y) = 164,200$$

$$(\sum x) = 2840$$

The sum of the total weighs for the comparables.

(260) + (360) + (400) + (440) + ...

$$(\sum xy) = 65,916,000$$

(260)(26,300) + (360)(24,500) + ...

$$(\sum x)(\sum y) = 465,328,000$$

(2840)(164,200)

$$\sum(x)^2 = 8,065,600$$

(2840)²

$$(\sum x^2) = 1,186,200$$

(260)² + (360)² + (400)² + (440)² + ...

$$b = \frac{7(65,916,000) - (465,328,000)}{7(1,186,200) - (8,065,600)} = -16.467619 \approx -16.5$$

$$a = \frac{164,200 - (-16.5)(2840)}{7} = 30,151.428 \approx \$30,151.$$

$$Y = a + bx$$

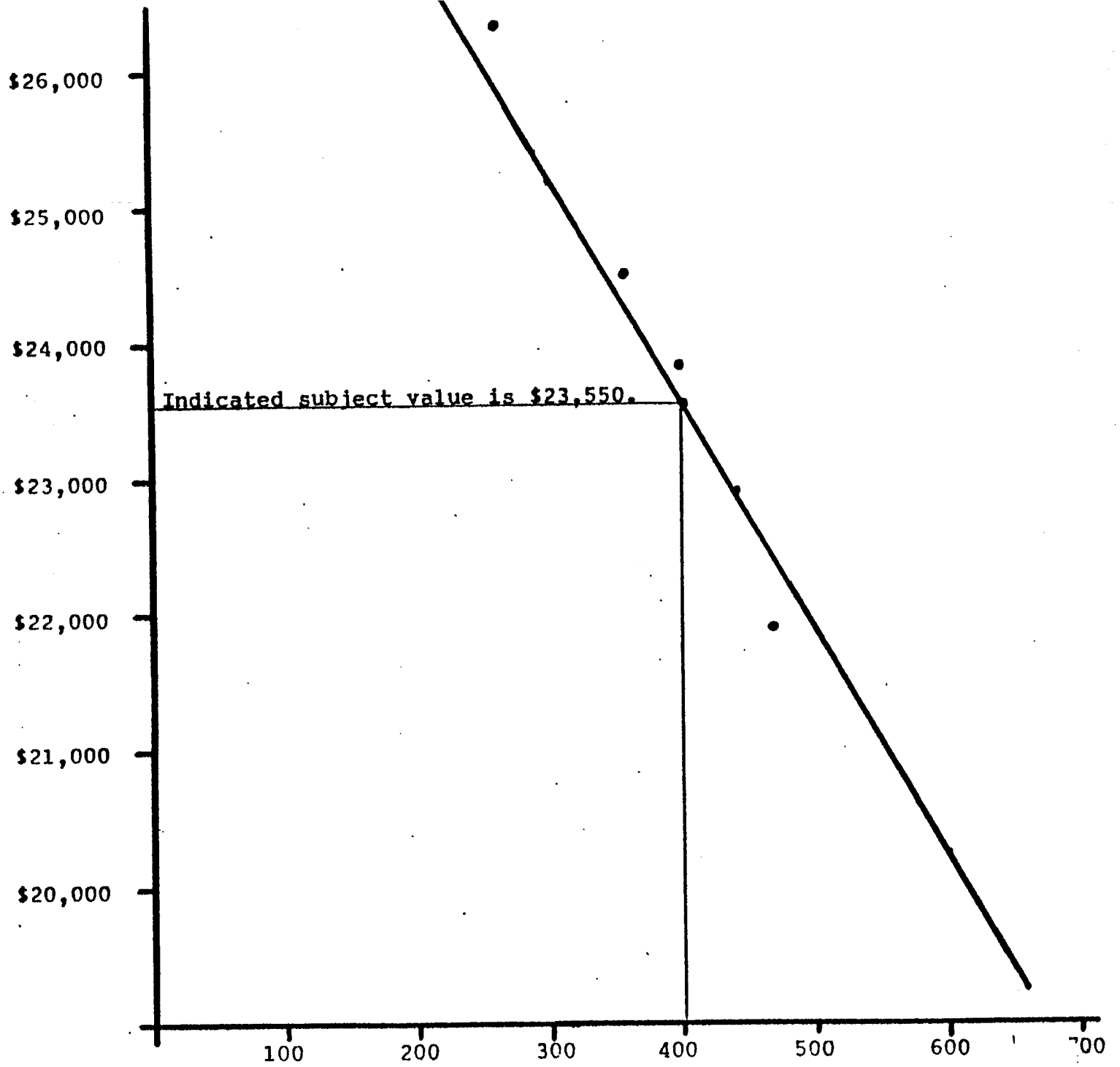
$$Y = 30,151 + (-16.5)(x)$$

'x' for the subject property was 400

$$Y = 30,151 + (-16.5)(400)$$

$$Y = \$23,550$$

EXHIBIT #16



Date of Inspection_____

Name of Inspector_____

VILLAGE OF MAPLE BLUFF
DANE COUNTY
WISCONSIN

SINGLE FAMILY RESIDENTIAL INFORMATION FORM

1. _____ Tax Parcel Number
2. _____ Property Owner
3. _____ Street Number
4. _____ Street Name

LAND DATA

5. _____ Previous Lot Sale Price
6. _____ Previous Lot Sale Date
7. _____ X Geocode
8. _____ Y Geocode
9. _____ Neighborhood Number
(01-18)
10. _____ Lot Square Feet
(rounded to nearest 500 ft.)
11. _____ Lot Front Feet
(rounded to nearest foot)
12. _____ Lot Depth
(rounded to nearest foot)

13. _____ Lot Subdividable
 (smaller of A, B,
 A & B apply only to unplatted-uncertified lots)

0 = No

CONDITIONS WHICH MUST
 BE MET:

A = Unplatted = $\frac{\text{Lot area} - 40,000 \text{ sq.ft.}}{\text{Gross Lots } 25,000 \text{ sq.ft.}}$
 (round down to next integer value)

B = Net = $\frac{\text{Lake frontage} - 100 \text{ ft.}}{\text{Additional Lots}}$
 (round down to next integer value)

1. All lots must have no less than 40' of street frontage or a single driveway (apron) easement.

2. Platted vacant lots (within a parcel) will be treated as buildable if, separately or in combination, the total area is \leq 14,000 SF, and conforms to condition #1.

14. _____ Lot Oversized (but not subdividable)
 0 = under 65,000 sq.ft.;
 1 = oversize lot

15. _____ Lake Access Easement
 0 = No; 1 = Yes

16. _____ Shore Quality
 3 = inaccessible bluff/Dengel Bay
 2 = shallow
 1 = mud; 0 = no dominant problem

17. _____ Water Quality
 3 = odor; 2 = flotsam; 1 = weeds;
 0 = no dominant problem

18. _____ Lake Front Feet
 (rounded to nearest foot)

19. _____ Lot on Corner
 0 = No; 1 = Yes

20. _____ Lot on Cul-de-sac
0 = No; 1 = Yes
21. _____ Inside Lot
0 = No; 1 = Yes
22. _____ Lot Wooded
0 = Below average (0 to 3 major trees)
1 = Average wooded lot (4 to 7 major trees)
2 = Above average lot (more than 7 major trees)
23. _____ Lot View
0 = Commercial lot or railroad lot
1 = Average view
2 = Golf course or park view
3 = Water average (non-State Capitol view)
4 = Water superior (State Capitol view)
24. _____ Lot Topography
0 = Severe, non-usable slope
1 = Wet pockets
2 = Downsloping lot
3 = Level contour
4 = Upward sloping lot
25. _____ Adverse Influence
- | | |
|------------------------------|------------------------------------|
| 0 = None | 5 = Public property
or exposure |
| 1 = Contiguous lake easement | 6 = Railroad |
| 2 = Joint driveway | 7 = High traffic |
| 3 = Other (high lines, etc.) | 9 = Combination |
| 4 = Commercial property | |

If lot suffers from two adverse influences, enter the higher value.

SITE IMPROVEMENT DATA

26. _____ Tennis Court
27. _____ Outdoor Pool
28. _____ Patio
29. _____ Storage Shed
30. _____ Boathouse

- 31. _____ Seawall
- 32. _____ Indoor Pool
- 33. _____ Elevator
- 34. _____ Other Structure Name
- 35. _____ Other Structure Value
- 36. _____ Other Structure Name
- 37. _____ Other Structure Value
- 38. _____ Special Structures Total
(Sum of columns 26 - 37)
- 39. _____ Driveway
(score = style, material)

STYLE

MATERIAL

- 1 = Linear into garage-
back into street
- 2 = Linear with turn-
around space
- 3 = Circular
- 4 = Large with parking
space and turnaround
space
- 5 = Circular with parking
space

- 1 = Dirt
- 2 = Gravel
- 3 = Asphalt
- 4 = Concrete/Brick

- 40. _____ Neighborhood Foliage
 - 1 = New and raw
 - 2 = Some mature trees
 - 3 = Shady
- 41. _____ Landscaping
 - 1 = Little or none
 - 2 = Average
 - 3 = Above average
- 42. _____ Screening of Back
 - 0 = Little or none
 - 1 = Yes

43. _____ Screening of Front
0 = Little or none
1 = Yes

44. _____ Curb and Gutter
0 = No; 1 = Yes

45. _____ Sidewalk
0 = No; 1 = Yes

IMPROVEMENT DATA

46. _____ Previous Sale Price

47. _____ Previous Sale Date

48. _____ Year Built

49. _____ Era
0 = Pre-1910 3 = 1950-1969
1 = 1910-1929 4 = 1970 to present
2 = 1930-1949

50. _____ Square Feet Living Space

51. _____ Number of Stories
0 = Vacant Lot 1.6 = Multilevel
1 = 1 Story 2 = 2 Stories
1.3 = 1-1/2 Stories 2.3 = 2-1/2 Stories

52. _____ Roof
(score = style, material)

STYLE

1 = Gable
2 = Hip
3 = Mansard
4 = Gambrel
5 = Flat
6 = Single pitch

MATERIAL

1 = Gravel
2 = Asphalt shingles
3 = Wood shake/shingle
4 = Slate shingles
5 = Tile
6 = Metal

53. Exterior
- | | |
|-----------------------------|-------------------------------------|
| 0 = Concrete block | 6 = Part masonry/
stained boards |
| 1 = Wood siding/frame | 7 = Part masonry/aluminum |
| 2 = Stucco | 8 = Predominantly brick
vener |
| 3 = Stained boards/shingles | 9 = Predominantly stone |
| 4 = Aluminum siding | |
| 5 = Part masonry/frame | |
54. Garage Type
- | | |
|--------------------|---------------------------|
| 0 = None | 5 = 2-3 car detached |
| 1 = Carport | 6 = 2-3 car basement |
| 2 = 1 car detached | 7 = 2 car attached, small |
| 3 = 1 car basement | 8 = 2 car attached, large |
| 4 = 1 car attached | 9 = 3 car attached |
55. Building Style
- | | |
|---|--|
| 1 = Cottage | 6 = Good builder's
suburban/mansion |
| 2 = Pre-1940 | 7 = Architectural
contemporary |
| 3 = Standard builder's
suburban (Owner custom
obsolescence) | 8 = Architectural
traditional |
| 4 = Architectural modern | 9 = Architectural colonial |
| 5 = Pre-1940 remodeled | |
56. Basement Type
- | | |
|-------------|---|
| 0 = Slab | 4 = Partially exposed (opening on
grade at least one side) |
| 1 = Crawl | 5 = Exposed (raised ranch/bilevel-
English basement- window sill at grade) |
| 2 = Partial | |
| 3 = Full | |
57. Basement Condition
- | |
|---------------------------------------|
| 0 = No problem |
| 2 = Mild problem due to seepage/aging |
| 5 = Poor condition or no basement |
58. Appearance to Neighbors
- | |
|------------------------|
| 1 = Less attractive |
| 2 = Equally attractive |
| 3 = More attractive |
59. Quality
- | | |
|--|-------------------------|
| 0 = Uninhabitable | 5 = Well-maintained |
| 1 = Major mechanical or
structural problems | 6 = Maintained like new |
| 2 = Interior damage | 7 = New--standard |
| 3 = Exterior maintenance
required | 8 = New--custom |
| 4 = Average condition | 9 = New--deluxe |

60. _____ Enclosed Porch
0 = None 5 = Average glass
1 = Small screen 6 = Large glass
2 = Average screen 7 = Small glass, heated
3 = Large screen 8 = Average glass, heated
4 = Small glass 9 = Large glass, heated

61. _____ Total Number of Rooms

62. _____ Total Number of Bedrooms

63. _____ Total Number of Bathrooms
(sum of bathroom scores)

64. _____ Half
(Score = .5 for each)

65. _____ Three-quarter
(Score = .75 for each)

66. _____ Full
(Score = 1 for each)

67. _____ Bathroom on First Floor
0 = No
1 = Yes

68. _____ Total Number of Fireplaces

69. _____ Living Room
(score = size, layout)

<u>SIZE</u>	<u>LAYOUT</u>
1 = Small	1 = Poor
2 = Moderate	2 = Indifferent
3 = Large	3 = Good

70. _____ Dining Room

0 = None
STYLE
1 = At end of living room
2 = Dining L
3 = Full dining area
4 = Separate room

71. _____ Den/Library/Study

0 = None 2 = Average
1 = Small 3 = Large

72. _____ Kitchen Score

. Score = (Size * Type * Work area) + Eating space

73. _____ Kitchen Size

1 = Small
2 = Average
3 = Large

74. _____ Kitchen Type

1 = Single wall 4 = U-shaped
2 = Pullman 5 = L- or U-shaped with island
3 = L-shaped

75. _____ Kitchen Work Area

To calculate kitchen score use:

0 = Obsolete (.5)
1 = Dated (.75)
3 = Modern (1.00)

76. _____ Kitchen Eating Space

To calculate kitchen score use:

0 = None 0
1 = Counter/Stools .2
2 = Space for table/chairs .4
3 = Breakfast nook .6

77. _____ Family Room

(Score = location, size)

0 = None	
<u>LOCATION</u>	<u>SIZE</u>
1 = Poor	1 = Small
2 = Adjoining kitchen	2 = Average
3 = Fully separate and well located	3 = Large

78. _____ Recreation Room

0 = None
1 = Yes (Must have fully finished floor,
ceiling, and walls)

79. _____ Laundry Area Score

(Score = location * type)

80. _____ Laundry Area Location

LOCATION

- 1 = Basement
- 2 = At grade
- 3 = Second floor

81. _____ Laundry Area Type

0 = None

TYPE

- 1 = Exposed
- 2 = Enclosed closet
- 3 = Separate room

82. _____ Heating System Score
(Score = Fuel * Type)

83. _____ Heating Fuel

FUEL

- 1 = Electricity
- 2 = Oil
- 3 = Gas

84. _____ Heating Type

TYPE

- 1 = Old hot water - radiators
- 2 = Old low pressure steam - radiators
- 3 = Old hot water integrated with water heater
- 4 = Gravity hot air grills on floor
- 5 = Hot water-baseboards
- 6 = Forced hot air
- 7 = ~~Forced hot air-zoned~~ *Hot forced-air/water - Zoned*
- 8 = Multiple forced hot air units

85. _____ Electrical Service

AMPERAGE

- 1 = 30 amp.
- 2 = 60 amp.
- 3 = 100 amp.
- 4 = 125 amp.
- 5 = 150 amp.
- 6 = > 150 amp.

86. _____ Water Heater
Score = (Capacity, Fuel)

0 = With hot water heat system

CAPACITY OF UNIT

1 = 20 gal. 5 = 75 gal.
2 = 30 gal. 6 = 100 gal.
3 = 40 gal. 7 = 100+ gal.
4 = 50 gal.

FUEL

1 = Electric
2 = Solar
3 = Oil
4 = Gas

87. _____ Interior Circulation (Traffic pattern)

0 = Poor
1 = Moderately good
2 = Good
3 = Excellent

88. _____ Total Special Features Score
(Sum of all special features points)

SPECIAL FEATURES

1. _____ Front Exterior Entry
(Score = Sum of style and function)
 STYLE FUNCTION
0 = Single door -1 = Unprotected
1 = Double door 2 = Protected

2. _____ Front Interior Entry
(Score = Sum of points)
-3 = Entrance direct to living room
0 = Vestibule (hall entry)
1 = Foyer (enclosed entry)
2 = Spacious vestibule
3 = Spacious foyer

3. _____ Master Bedroom Suite
(Score = Sum of points)
1 = Extra closet space
2 = Dressing area
3 = Sitting area

4. _____ Living Room Extras
(Score = Sum of points)
-3 = Classical cathedral ceiling
0 = None
1 = Contemporary sloped ceiling,
 built-in cabinets
2 = Sunken multi-level, special natural
 illumination, deluxe woodwork

5. _____ Dining Room Extras
(Score = Sum of points)
0 = None
1 = Built-in china cabinet, break front/buffet
2 = Wet bar
3 = Deluxe built-ins

6. _____ Den/Library/Study Extras
(Score = Sum of points)
0 = None
1 = Built-in cabinets
2 = Deluxe woodwork

SPECIAL FEATURES (Continued)

7. _____ Kitchen Extras

(Score = Sum of Points)

- 0 = None
- 1 = Each built-in appliance, serving pantry/bar, direct access to outside, grill/BBQ, more than one sink area
- 3 = No window
- 2 = Below average window area
- 0 = Average window area
- 1 = Above average window area

8. _____ Family Room Extras

(Score = Sum of points)

- 0 = None
- 1 = Built-in cabinets, deluxe flooring, deluxe paneling, sloped ceiling
- 2 = Wet bar
- 5 = Kitchen facilities

9. _____ Number of Special Spaces

(Score = Sum of points)

- 0 = None
- 1 = Special woodwork/craft area
- 2 = Dark room
- 3 = Sewing, sitting, office areas, partially finished recreation room

10. _____ Recreation Room Extras

(Score = Sum of points)

- 0 = None
- 1 = Built-in cabinets
- 2 = Wet bar
- 5 = Kitchen facilities

11. _____ Household Extras

(Score = Sum of points)

- 0 = None
- 1 = Greenhouse - attached at window, special indirect lighting
- 2 = Security system
- 3 = Greenhouse - attached and walk-in, sauna
- 5 = Central air conditioning, grand spiral staircase

VILLAGE OF MAPLE BLUFF, DANE COUNTY
 SINGLE-FAMILY RESIDENTIAL TAX INFORMATI.G FORM
 AS OF JANUARY 1, 1980

460111

- 1 Tax Parcel Number
- 2 Property Owner
- 3 Street Number
- 4 Street Name
- 5 Previous Lot Sale Price
- 6 Previous Lot Sale Date
- 7 Geocode X
- 8 Geocode Y
- 9 Neighborhood Number
- 10 Lot Square Feet
- 11 Lot Front Feet
- 12 Lot Depth
- 13 Lot Subdividable
- 14 Lot Oversized
- 15 Lake Access Easement
- 16 Shore Quality
- 17 Water Quality
- 18 Lake Front Feet
- 19 Lot on Corner
- 20 Lot on Cul de Sac
- 21 Inside Lot
- 22 Lot Wooded
- 23 Lot View
- 24 Lot Topo
- 25 Adverse Influence
- 26 Tennis Court
- 27 Outdoor Pool
- 28 Patio
- 29 Storage Shed
- 30 Boathouse
- 31 Seawall
- 32 Indoor Pool
- 33 Elevator
- 34 Other Structure Name
- 35 Other Structure Value
- 36 Other Structure Name
- 37 Other Structure Value
- 38 Special Structures Total
- 39 Driveway
- 40 Neighborhood Foliage
- 41 Landscaping
- 42 Screening of Back
- 43 Screening of Front
- 44 Curb Gutter
- 45 Sidewalk
- 46 Previous Sale Price
- 47 Previous Sale Date
- 48 Year Built

PLSPRICE	0
PLSDATE	0
GEO X	0
GEO Y	0
NBRHD	5
LTSOFT	22500
LTFEET	202
LTDPTH	142
LOTSDIV	0
LOTOVSZD	0
LKACC	0
SHORE	0
WATER	0
LKFFT	0
LTCNR	1
LTCUL	0
LTINS	0
LTWOOD	1
LTVIEW	1
LTTPO	3
ADINF	5
TENCT	0
OUTPOOL	0
PATIO	200
STSHD	0
BTHSE	0
SEAWLL	0
INPOOL	0
ELEV	0
STCT1	0
VALUE1	0
STCT2	0
VALUE2	0
SPCTOT	0
DRVWY	14
NBRFOL	3
LNDSCP	3
CRBK	0
SCRFT	0
CRBGTR	0
SIDWLK	0
PSPR	0
PSDATE	0
YRBLT	1927

- 49 Era
- 50 Sq. Ft. Living Space
- 51 Number of Stories
- 52 Roof
- 53 Exterior
- 54 Garage Type
- 55 Building Style
- 56 Basement Type
- 57 Basement Condition
- 58 Appearance to Neighbors
- 59 Quality
- 60 Enclosed Porch
- 61 Total Number Rooms
- 62 Total Number Bedrooms
- 63 Total Number Bathrooms
- 64 Half
- 65 Three Quarters
- 66 Full
- 67 On First Floor
- 68 Total Number Fireplaces
- 69 Living Room
- 70 Dining Room
- 71 Den/Library/Study
- 72 Kitchen Score
- 73 Kitchen Size
- 74 Kitchen Type
- 75 Kitchen Work Area
- 76 Kitchen Eating Space
- 77 Family Room
- 78 Recreation Room
- 79 Laundry Area Score
- 80 Laundry Area Location
- 81 Laundry Area Type
- 82 Heating System Score
- 83 Heating Fuel
- 84 Heating Type
- 85 Electrical Service
- 86 Water Heater
- 87 Interior Circulation
- 88 Special Features Score
- 89 79 ASSESSMENT

ERA	1
SQFTLS	2180
STORIES	3
ROOF	14
EXTER	4
GARAGE	7
STYLE	8
BSMTYP	3
BSMTCND	5
APPEARS	1
QUALTY	3
PORCH	0
ROOMS	9
BDRMS	4
BATHS	1.75
HFBTH	0
THQBTH	1
FULLBTH	1
BTHIST	1
FPLAC	1
LIVRM	23
DINRM	4
DEN	1
KTCHSCR	1.15
KTCHSZ	1
KTCHTYPE	1
KTCHWRK	1
KTCHEAT	2
FMLYRM	0
RECRM	0
LAUNSCR	1
LAUNLOC	1
LAUNTYP	1
HTGSCR	6
HTGFUEL	3
HTGTYP	2
ELECTSRV	2
WTRHTR	44
INTCIR	1
SPFTSCR	4
79ASSESS	81,000

IMPROVEMENT DATA

MADISON, WI 53704

LAND DATA

PREVIOUS LOT SALE PRICE	0
PREVIOUS SALE DATE	0
GEOCODE	0
NEIGHBORHOOD NUMBER	5
LOT SQ. FT.*	22500
LOT FRONT FT.*	202
LOT DEPTH*	142
LOT SUBDIVIDABLE	No
LOT OVERSIZED	No
LAKE ACCESS EASEMENT	No
LAKE FRONT FT.	0
LOT ON CORNER	Yes
LOT ON CUL DE SAC	No
INSIDE LOT	No
LOT WOODED	4 to 7 major trees
LOT VIEW	Average view
LOT TOPOGRAPHY	Level contour
ADVERSE INFLUENCE	Public property

SPECIAL STRUCTURES AND SITE IMPROVEMENTS

TENNIS COURT	0
OUTDOOR POOL	0
PATIO	200
STORAGE SHED	0
BOATHOUSE	0
SEAWALL	0
INDOOR POOL	0
ELEVATOR	0
0	0
0	0
SPECIAL STRUCTURES TOTAL	200
DRIVEWAY	Linear, concrete
NEIGHBORHOOD FOLIAGE	Shady
LANDSCAPING	Average
SCREENING OF BACK	Little or none
SCREENING OF FRONT	Little or none
CURB AND GUTTER	No
SIDEWALK	No

*APPROX. USING VILLAGE MAP

PREVIOUS SALE PRICE	0
PREVIOUS SALE DATE	0
YEAR BUILT	1927
ERA	1910-1929
SQ. FT. LIVING SPACE	2180
NUMBER OF STORIES	2 Story
BUILDING STYLE	Architectural Traditional
ROOF	Gable, slate shingles
EXTERIOR	Stucco
GARAGE	2 Car attached, small
BASEMENT TYPE	Full
BASEMENT CONDITION	Poor condition
QUALITY	Exterior maintenance required
APPEARANCE TO NEIGHBORS	Less attractive
ENCLOSED PORCH	None
NUMBER OF ROOMS	9
NUMBER OF BEDROOMS	4
NUMBER OF BATHROOMS	1.75
HALF BATHS	0
THREE QUARTER BATHS	1
FULL BATHS	1
BATH ON FIRST FLOOR	Yes
NUMBER OF FIREPLACES	1
LIVING ROOM	Moderate size, good layout
DINING ROOM	Separate room
DEN/LIBRARY/STUDY	Small size
FAMILY ROOM	None
KITCHEN SCORE	1.15
SIZE	Small
TYPE	Single wall
WORK AREA	Dated
EATING SPACE	Space for table/chairs
RECREATION ROOM	No
LAUNDRY AREA SCORE	1
LOCATION	Basement
TYPE	Exposed
HEATING SYSTEM SCORE	6
FUEL	Gas
TYPE	Old low pressure steam
ELECTRICAL SERVICE	60 amp.
WATER HEATER	50 gal., gas
INTERIOR CIRCULATION	Moderately good
SPECIAL FEATURES SCORE	4
LAND	24,500
IMPROVEMENTS	56,500
1979 ASSESSMENT	81,000
LAND	24,500
IMPROVEMENTS	56,500
1980 ASSESSMENT	81,000

FACTOR	TYP	RATE	AVE.	S-DEV.
PSFR	0.	1.00	89213.	22432.
PSDATE	2.	0.05	3347.	1787.
NBRHD	1.	1500.00	750.	1500.
LTSOFT	1.	0.22	2173.	873.
LOTSDIV	1.	15500.00	0.	0.
LOTOVSZD	2.	-0.05	0.	0.
LKACC	1.	100.00	0.	0.
SHORE	2.	-0.02	0.	0.
WATER	2.	-0.02	0.	0.
LKFFT	1.	350.00	0.	0.
LTCNR	1.	-750.00	-750.	0.
LTCUL	1.	500.00	0.	0.
LTWOOD	2.	0.05	1873.	2165.
LTVIEW	2.	0.02	0.	0.
LTOPO	2.	0.03	0.	0.
ADINF	2.	-0.02	-6796.	5048.
SPCTOT	1.	1.00	0.	163.
ERA	2.	0.02	-749.	866.
SQFTLS	1.	15.00	150.	4963.
STORIES	2.	0.02	0.	0.
EXTER	2.	0.01	964.	1592.
GARAGE	1.	1000.00	1000.	1826.
STYLE	2.	0.01	596.	1971.
BSHTYP	2.	0.01	669.	779.
BSHTCND	2.	-0.02	-4926.	3444.
APPEARS	2.	0.03	-2676.	673.
QUALTY	2.	0.02	-1949.	2389.
PORCH	1.	600.00	-900.	600.
BDRMS	1.	1500.00	0.	1225.
BATHS	1.	4000.00	0.	2000.
FPLAC	1.	750.00	-187.	375.
DINRM	2.	0.02	749.	866.
DEN	1.	1000.00	750.	500.
KTCHSCR	1.	350.00	-814.	955.
FARM	1.	100.00	-2150.	1509.
RECRH	1.	2000.00	0.	0.
LAUNSCR	1.	300.00	-450.	714.
HTGSCR	1.	200.00	-1400.	1200.
INTCIR	2.	0.01	-305.	610.
SPFTSCR	1.	200.00	-250.	1310.
AVE ADJUSTED AMT			77930.	6747.
WEIGHTED AVE.			76000.	
INDICATED VALUE			76000.	

4:46 460115 30 OLD SHORE RD
 51:246 4601325.24 372 WOODLAND
 23:139 4601212 236 LAKEWOOD BLV
 29:159 4601237 122 LAKEWOOD BLV

FACTOR	SUBJECT	4-AMT	ADJ	51-AMT	ADJ	23-AMT	ADJ	29-AMT	ADJ
PSPR	0.00	85000.00	85000.	72850.00	72850.	122000.00	122000.	77000.00	77000.
PSDATE	80.00	78.92	4604.	79.42	2125.	79.75	1525.	78.67	5133.
NBRHD	5.00	5.00	0.	3.00	3000.	5.00	0.	5.00	0.
LTSQFT	22500.00	14000.00	1870.	10500.00	2640.	17500.00	1100.	8500.00	3080.
LOTSDIV	0.00	0.00	0.	0.00	0.	0.00	0.	0.00	0.
LOTQVSZB	0.00	0.00	0.	0.00	0.	0.00	0.	0.00	0.
LKACC	0.00	0.00	0.	0.00	0.	0.00	0.	0.00	0.
SHORE	0.00	0.00	0.	0.00	0.	0.00	0.	0.00	0.
WATER	0.00	0.00	0.	0.00	0.	0.00	0.	0.00	0.
LKFFT	0.00	0.00	0.	0.00	0.	0.00	0.	0.00	0.
LTCNR	1.00	0.00	-750.	0.00	-750.	0.00	-750.	0.00	-750.
LTCUL	0.00	0.00	0.	0.00	0.	0.00	0.	0.00	0.
LTWOOD	1.00	1.00	0.	0.00	3643.	1.00	0.	0.00	3850.
LTVIEW	1.00	1.00	0.	1.00	0.	1.00	0.	1.00	0.
LTTDPO	3.00	3.00	0.	3.00	0.	3.00	0.	3.00	0.
ABINF	5.00	5.00	0.	0.00	-7285.	0.00	-12200.	0.00	-7700.
SPCTOT	200.00	200.00	0.	400.00	-200.	200.00	0.	0.00	200.
ERA	1.00	1.00	0.	2.00	-1457.	1.00	0.	2.00	-1540.
SQFTLS	2180.00	2400.00	-3300.	1940.00	3300.	2500.00	-4800.	1820.00	5400.
STORIES	3.00	3.00	0.	3.00	0.	3.00	0.	3.00	0.
EXTER	4.00	4.00	0.	1.00	2186.	2.00	2440.	5.00	-770.
GARAGE	7.00	8.00	-1000.	4.00	3000.	5.00	2000.	7.00	0.
STYLE	8.00	9.00	-850.	4.00	2914.	9.00	-1220.	6.00	1540.
BSMTYP	3.00	3.00	0.	1.00	1457.	2.00	1220.	3.00	0.
BSMTCMD	5.00	2.00	-5100.	0.00	-7285.	2.00	-7320.	5.00	0.
APPEARS	1.00	2.00	-2550.	2.00	-2186.	2.00	-3660.	2.00	-2310.
QUALTY	3.00	3.00	0.	5.00	-2914.	5.00	-4880.	3.00	0.
PORCH	0.00	2.00	-1200.	0.00	0.	2.00	-1200.	2.00	-1200.
BDRMS	4.00	4.00	0.	3.00	1500.	5.00	-1500.	4.00	0.
BATHS	1.75	1.50	1000.	1.50	1000.	2.50	-3000.	1.50	1000.
FPLAC	1.00	1.00	0.	1.00	0.	1.00	0.	2.00	-750.
DINRM	4.00	4.00	0.	3.00	1457.	4.00	0.	3.00	1540.
DEN	1.00	0.00	1000.	1.00	0.	0.00	1000.	0.00	1000.
KTCHSCR	1.15	1.50	-123.	4.90	-1313.	6.60	-1907.	0.90	87.
FAHRM	0.00	32.00	-3200.	22.00	-2200.	32.00	-3200.	0.00	0.
RECRM	0.00	0.00	0.	0.00	0.	0.00	0.	0.00	0.
LAUNSCR	1.00	1.00	0.	6.00	-1500.	2.00	-300.	1.00	0.
HIGSCR	6.00	6.00	0.	18.00	-2400.	10.00	-800.	18.00	-2400.
INTCIR	1.00	1.00	0.	1.00	0.	2.00	-1220.	1.00	0.
SPFTSCR	4.00	6.00	-400.	13.00	-1800.	5.00	-200.	-3.00	1400.

ADJUSTED AMOUNT	75002.	49782.	83128.	83811.
SELECTION INDEX	14662.	21172.	21227.	22803.

RUN PROPCD
 B.D. Filename? HBLOTS
 Output Filename? KB:
 Enter (start col), (num col), (start ln), (end ln)
 ? 1, 132, 1, 40
 Format Code Filename? PROPTY.CRD
 18 WITSA::KB63 PROPCD+BASIC RN 16(16)K+15K 47.6(+18.1)
 18 WITSA::KB63 PROPCD+BASIC BB(11R) 16(16)K+15K 48.6(+1.0)

Property card for vacant site

1980 PROPERTY CARD - PARCEL 4401124

IMPROVEMENT DATA

LAND DATA

PREVIOUS LOT SALE PRICE 0
 PREVIOUS SALE DATE 0
 GEOCODE 0
 NEIGHBORHOOD NUMBER 7
 LOT SQ. FT.* 8400
 LOT FRONT FT.* 81
 LOT DEPTH* 104
 LOT SUBDIVIDABLE No
 LOT OVERSIZED No
 LAKE ACCESS EASEMENT No
 SHORE QUALITY No dominant problem
 WATER QUALITY No dominant problem
 LAKE FRONT FT. 0
 LOT ON CORNER No
 LOT ON CUL DE SAC No
 INSIDE LOT No
 LOT WOODED 4 to 7 major trees
 LOT VIEW Average view
 LOT TOPOGRAPHY Level contour
 ADVERSE INFLUENCE None

SPECIAL STRUCTURES AND SITE IMPROVEMENTS

TENNIS COURT ?
 OUTDOOR POOL ?
 PATIO ?
 STORAGE SHED ?
 BOATHOUSE ?
 SEAWALL ?
 INDOOR POOL ?
 ELEVATOR ?
 ? ?
 ? ?
 SPECIAL STRUCTURES TOTAL 0
 DRIVEWAY ??
 NEIGHBORHOOD FOLIAGE ??
 LANDSCAPING ??
 SCREENING OF BACK ??
 SCREENING OF FRONT ??
 CURB AND BUTTER ??
 SIDEWALK ??

*APPROX. USING VILLAGE MAP

PREVIOUS SALE PRICE ?
 PREVIOUS SALE DATE ?
 YEAR BUILT ?
 ERA ?
 SQ. FT. LIVING SPACE ?
 NUMBER OF STORIES Vacant Lot
 BUILDING STYLE ??
 ROOF ?
 EXTERIOR ??
 GARAGE ??
 BASEMENT TYPE ?
 BASEMENT CONDITION ?
 QUALITY ??
 APPEARANCE TO NEIGHBORS ?
 ENCLOSED PORCH ??
 NUMBER OF ROOMS ??
 NUMBER OF BEDROOMS ??
 NUMBER OF BATHROOMS ??
 HALF BATHS ??
 THREE QUARTER BATHS ??
 FULL BATHS ??
 BATH ON FIRST FLOOR ?
 NUMBER OF FIREPLACES ??
 LIVING ROOM ??
 DINING ROOM ??
 BEN/LIBRARY/STUDY ??
 FAMILY ROOM ??
 KITCHEN SCORE 999.00
 SIZE ??
 TYPE ??
 WORK AREA ??
 EATING SPACE ??
 RECREATION ROOM ??
 LAUNDRY AREA SCORE ?
 LOCATION ?
 TYPE ?
 HEATING SYSTEM SCORE ??
 FUEL ??
 TYPE ??
 ELECTRICAL SERVICE ??
 WATER HEATER ??
 INTERIOR CIRCULATION ??
 SPECIAL FEATURES SCORE ??

LAND IMPROVEMENTS 2,500
 1979 ASSESSMENT 28,500

LAND IMPROVEMENTS 26,000
 1980 ASSESSMENT 24,000

BUS BB.RETRIE

D.B.FILE TO RETRIEVE DATA FROM >MPBLUF
 OUTPUT FILE >
 D.B.FILE MPBLUF: 540 RECORDS, 94 COLUMNS.
 NA
 COLUMN >18
 <, >, OR = (WHICH ONE) >>
 VALUE >0

NA
 COLUMN >51
 <, >, OR = (WHICH ONE) >>
 VALUE >0

MP
 NUMBER OF COLUMNS >12
 RPT.COL. 1 >1
 RPT.COL. 2 >3
 RPT.COL. 3 >4
 RPT.COL. 4 >10
 RPT.COL. 5 >18
 RPT.COL. 6 >50
 RPT.COL. 7 >62
 RPT.COL. 8 >63
 RPT.COL. 9 >88
 RPT.COL. 10 >89
 RPT.COL. 11 >90
 RPT.COL. 12 >91

DELIMITER (MAY BE NULL) >
 DO YOU WANT ALLIGNED COLUMNS? >Y
 POSITION TO BEGIN COLUMN 1, TXPARNUM>0
 POSITION TO BEGIN COLUMN 2, STRNUM>13
 POSITION TO BEGIN COLUMN 3, STRNAM>21
 POSITION TO BEGIN COLUMN 4, LTSQFT>39
 POSITION TO BEGIN COLUMN 5, LKFFT>49
 POSITION TO BEGIN COLUMN 6, SQFTLS>59
 POSITION TO BEGIN COLUMN 7, BRNS>69
 POSITION TO BEGIN COLUMN 8, BATHS>77
 POSITION TO BEGIN COLUMN 9, SPFTSCR>85
 POSITION TO BEGIN COLUMN 10, 79ASSESS>95
 POSITION TO BEGIN COLUMN 11, 80ASSESS>105
 POSITION TO BEGIN COLUMN 12, ZCHANGE>115

*Creation of list
 using DB/MPBLUF data
 file -- ordered by parcel
 number -- lake properties
 Col. 18 = >0 lake front ft.
 Col 51 = >0 selects only
 parcels with improvements*

TXPARNUM	STRNUM	STRNAM	LTSQFT	LKFFT	SQFTLS	BRNS	BATHS	SPFTSCR	79ASSESS	80ASSESS	ZCHANGE
46011	43	BURROUS RD	13500	90	1960	4	2.25	7	112000	121000	1.08034
4601100	309	LAKEWOOD BLVD	43500	100	4960	5	3.5	14	107500	234000	2.177
4601101	303	LAKEWOOD BLVD	182000	275	5820	6	5.5	21	324000	339000	1.9443
4601104	81	CAMBRIDGE RD	31000	89	3860	5	4	14	159000	175000	1.1004
4601105	49	CAMBRIDGE RD	59000	260	5750	8	6	21	257000	270000	1.0505
4601106	57	CAMBRIDGE RD	21500	100	2680	5	3.25	10	113000	140000	1.23894
4601107	49	CAMBRIDGE RD	17000	80	4240	5	5.25	17	142000	180000	1.11111
4601108	45	CAMBRIDGE RD	18000	80	3000	4	2.25	4	163000	143000	1
4601109	37	CAMBRIDGE RD	20300	80	2480	3	3.25	8	140000	160000	1
4601110	33	CAMBRIDGE RD	29500	77	3000	5	2.5	4	124000	154500	1.22419
4601111	29	CAMBRIDGE RD	24500	82	2640	6	3.5	10	141500	147000	1.03887
4601112	25	CAMBRIDGE CT	24000	91	3000	4	4.25	13	172000	179000	1.0407
4601113	23	CAMBRIDGE CT	13000	87	2420	4	2.5	7	135000	130000	.962963
4601114	17	CAMBRIDGE CT	87500	475	4440	6	6	16	328000	310000	.96875
4601117	11	CAMBRIDGE RD	15300	50	1780	3	1.5	2	95000	105000	1.10524
4601118	9	CAMBRIDGE RD	16000	78	3000	4	2.75	14	131000	144000	1.1145
4601119	5	CAMBRIDGE RD	14500	78	2340	4	2.75	5	120000	120000	1
4601120	3	CAMBRIDGE RD	17000	70	1580	3	1.5	8	105000	110000	1.04742
4601121	35	BAYSIDE DR	20000	72	2460	4	3	9	130000	141500	1.0885
4601123	27	BAYSIDE DR	19500	75	2900	5	3	7	153000	157500	1.02941
46012	51	BURROUS RD	23500	375	1740	2	1.5	12	142000	155000	1.09155
460120.7	1008	BAY DR	26000	100	2860	5	2.5	6	186000	189000	1.01613

RG
 COLUMN TO GROUP >91

I
 D.B.FILE MBCPY: 560 RECORDS, 96 COLUMNS.
 #P
 NUMBER OF COLUMNS >4
 RPT.COL. 1 >3
 RPT.COL. 2 >4
 RPT.COL. 3 >2
 RPT.COL. 4 >1
 DELIMITER (MAY BE NULL) >
 DO YOU WANT ALLIGNED COLUMNS? >Y
 POSITION TO BEGIN COLUMN 1 , STRNUM>10
 POSITION TO BEGIN COLUMN 2 , STRNAM>15
 POSITION TO BEGIN COLUMN 3 , PROPOW>32
 POSITION TO BEGIN COLUMN 4 , TXPARNUM>62

*Creation of list
 using DB MBCOPY
 data file which
 has been sorted
 by street name --
 all properties included*

STRNUM	STRNAM	PROPOW	TXPARNUM
1008	BAY DR	RAEMISCH, BRUCE & GREG	460120.7
8	BAYSIDE DR	BUTCHER, GORDON G	46019
23	BAYSIDE DR	BACH, FRANCIS H	46017.2
35	BAYSIDE DR	WHIFFEN, JOHN P & LORNA D	4601121
27	BAYSIDE DR	WESTON, JOHN C	4601123
3	BAYSIDE DR	HARPER, ALPHA S	46015
4	BAYSIDE DR	BRUDEN, PHILIP M & PATRICIA I	46018
7	BAYSIDE DR	SHELTON, WILLIAM E & CAROL	46016
15	BAYSIDE DR	FISHER, JEROME	46017
44	BURROWS RD	KLIPSCH, RICHARD W & MARCIA	46013.1
22	BURROWS RD	SHERRY, TOBY E	460112
48	BURROWS RD	BLAKE, PHOEBE	46013
51	BURROWS RD	HAIGHT, NANCY K	46012
43	BURROWS RD	ELA, DOROTHY A	46011
837	BUTTERNUT RD	VOLZ, GORDON	4601398
816	BUTTERNUT RD	TRAVERS, THOMAS G & MARY ANN	4601390
811	BUTTERNUT RD	HOBBINS, MEREDITH L	4601395
911	BUTTERNUT RD	LEIDEL, FREDERICK D	4601349
822	BUTTERNUT RD	SIEBRECHT, HARLAN & DIANE	4601389
840	BUTTERNUT RD	ORR, ELEANOR A	4601387
819	BUTTERNUT RD	BARRY, DAVID S & JANE	4601396
831	BUTTERNUT RD	WITTMAYER, ESTHER E	4601397
704	BUTTERNUT RD	HOLMES, GEORGE E	4601404.1
828	BUTTERNUT RD	STRUCK, VERNON C & GERTRUDE M	4601388
806	BUTTERNUT RD	BREDESON, DUANE	4601392
812	BUTTERNUT RD	VACARRO, JAMES A & SLYVIA	4601391
801	BUTTERNUT RD	BLANCKE, ROSEMARIE	4601468.1
902	BUTTERNUT RD	STEVENS, MYRON	4601362
708	BUTTERNUT RD	BLANCHAR, DONALD W	4601404.2
807	BUTTERNUT RD	HOPKINS, J D	4601394
801	BUTTERNUT RD	BLANCKE, ROSEMARIE	4601393
23	CAMBRIDGE CT	STICHA, PENELOPE G	4601413
23	CAMBRIDGE CT	STICHA, EDWARD H	4601113
29	CAMBRIDGE CT	SUHR, FREDERICK C	4601126
17	CAMBRIDGE CT	WHIFFEN, JAMES D & ARLIS E	4601114
25	CAMBRIDGE CT	FINDORFF, JOHN R	4601112
57	CAMBRIDGE RD	MAUTZ, BERNHARD M JR	4601106
33	CAMBRIDGE RD	MCGUIRE, R T	4601110
3	CAMBRIDGE RD	HARPER, JOHN & NANCY	4601120
92	CAMBRIDGE RD	HART, JOHN R	4601142
81	CAMBRIDGE RD	STEUER, JOSEPH T	4601104
109	CAMBRIDGE RD	HOVDE, RAYMOND	4601173
49	CAMBRIDGE RD	WESTON, CARL B	4601107
68	CAMBRIDGE RD	TORMEY, DR. WESTON	4601147
45	CAMBRIDGE RD	DIMOND, WALDO B	4601108
37	CAMBRIDGE RD	WHIFFEN, JOHN	4601109
29	CAMBRIDGE RD	SUHR, FREDERICK C & MARY E	4601111
118	CAMBRIDGE RD	KRUPP, JOSEPH & CYNTHIA J NEL	4601187
121	CAMBRIDGE RD	FRAZIER, ALBERT F JR	4601171
88	CAMBRIDGE RD	NOURSE, DENNIS	4601144
69	CAMBRIDGE RD	VILAS, H J FRANCIS	4601105
11	CAMBRIDGE RD	JENSEN, KAI	4601117
5	CAMBRIDGE RD	LIZON, ROBERT H & DOROTHY I	4601119
58	CAMBRIDGE RD	OSTBY, BYRON C	4601148
50	CAMBRIDGE RD	VARDA, JOHN P	4601150
38	CAMBRIDGE RD	SCHWARZ, FREDERICK C	4601152
--	-----	-----	-----

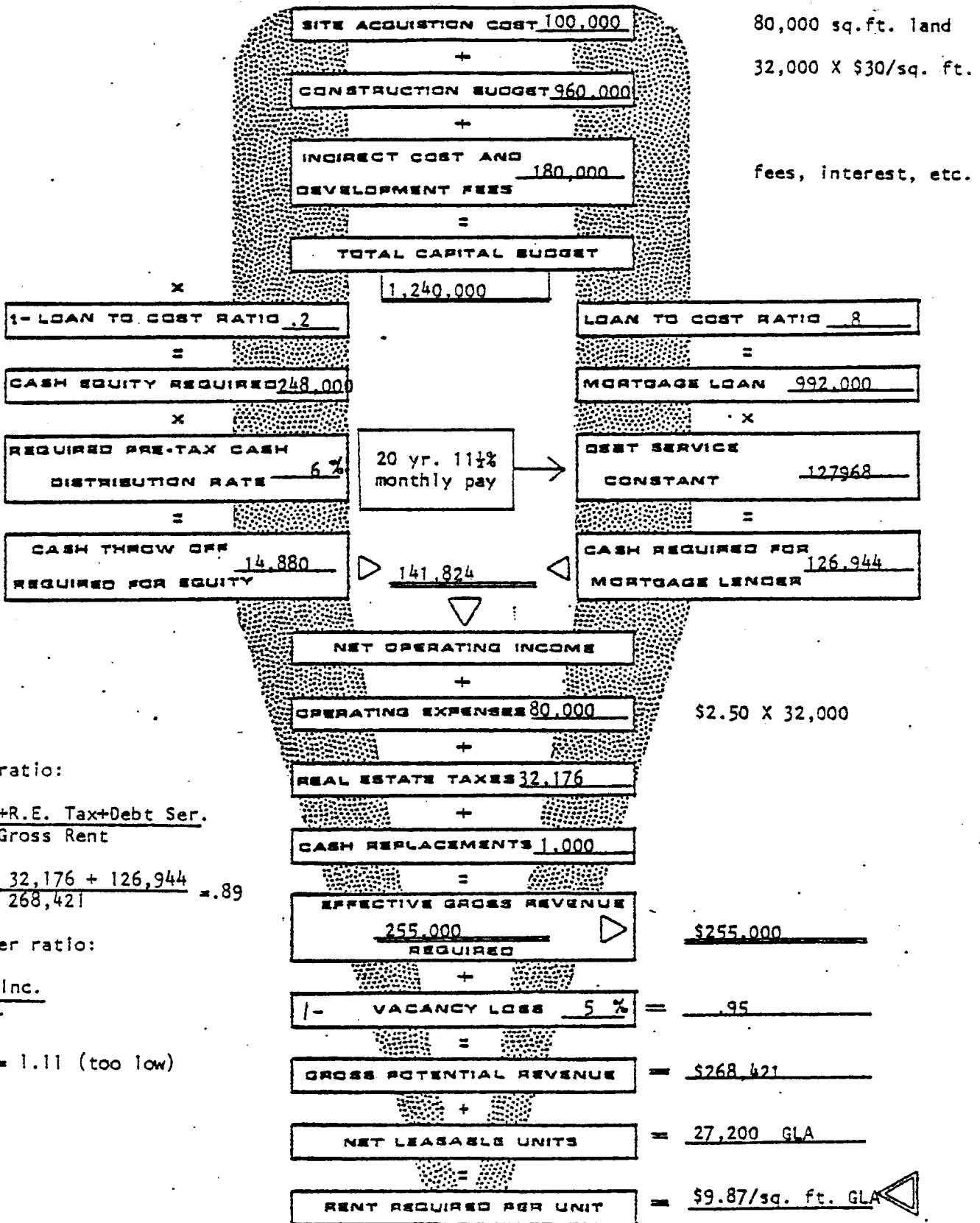
CONTEMPORARY REAL ESTATE APPRAISAL SEMINAR

IX. Investment Purchase Simulation

Investment simulation is useful to select most probable use, predict most probable price, or test the market comparison price prediction for fit to the profile of consumer objectives. Each requires a different level of data for application, depending on the type of property and the sophistication of investor-buyers in the market place.

- A. Do not confuse gross rent multipliers, net income multipliers, or market capitalization rates as investment simulation techniques. These are market comparison techniques. Sales price is being related to gross rents, net income, or indirectly to investment.
- B. The front door and back door approaches may be considered as the most basic method of investment simulation. Examples are provided in Exhibits 1-3; a second example of this method is provided in the demonstration appraisal case.
 1. The back door approach is used primarily to determine the most probable use.
 2. The front door approach is used to test a most probable price conclusion determined from the market place.
 3. The BFCF model was specifically designed as an after tax test of probable market price.
- C. Investment simulation requires proof that the most probable buyer group does in fact think in the format presented so that it is first necessary to define the appropriate simulation model and then define the elements as used by most probable buyers as well as the elements appropriate to the issue.
 1. Hotel owners may use house profit to determine the price to be paid for the hotel but fair market value for real estate tax appeals must define the income attributable to real estate.
 2. There are indirect controls on price, such as debt cover ratio required by lender, land value per unit allowed by FHA or state housing agencies multiplied by typical loan to value ratio, or recent developments in farm appraisal where computers will convert soil productivity and tillable acres to most probable gross income estimate.
 3. Income, expenses, and discount rate must be appropriate to the viewpoint in the probable use-probable investor scenario.
- D. The income attributable to real estate may require market rents for fair market value or contract rents and a lease management plan for investment value. However many rental structures are tied to business operations which are identified with the real estate but are not attributable to the real estate but rather to entrepreneurial management such as hotel operations, super regional shopping centers, or sand and gravel operations. It is useful to set up generalized rules which suggest the presence of non-real estate income:

**EXHIBIT I
LOAN TO COST RATIO APPROACH**



Default ratio:

$$\frac{\text{Op. Exp.} + \text{R.E. Tax} + \text{Debt Ser.}}{\text{Gross Rent}} = .89$$

$$\frac{80,000 + 32,176 + 126,944}{268,421} = .89$$

Debt cover ratio:

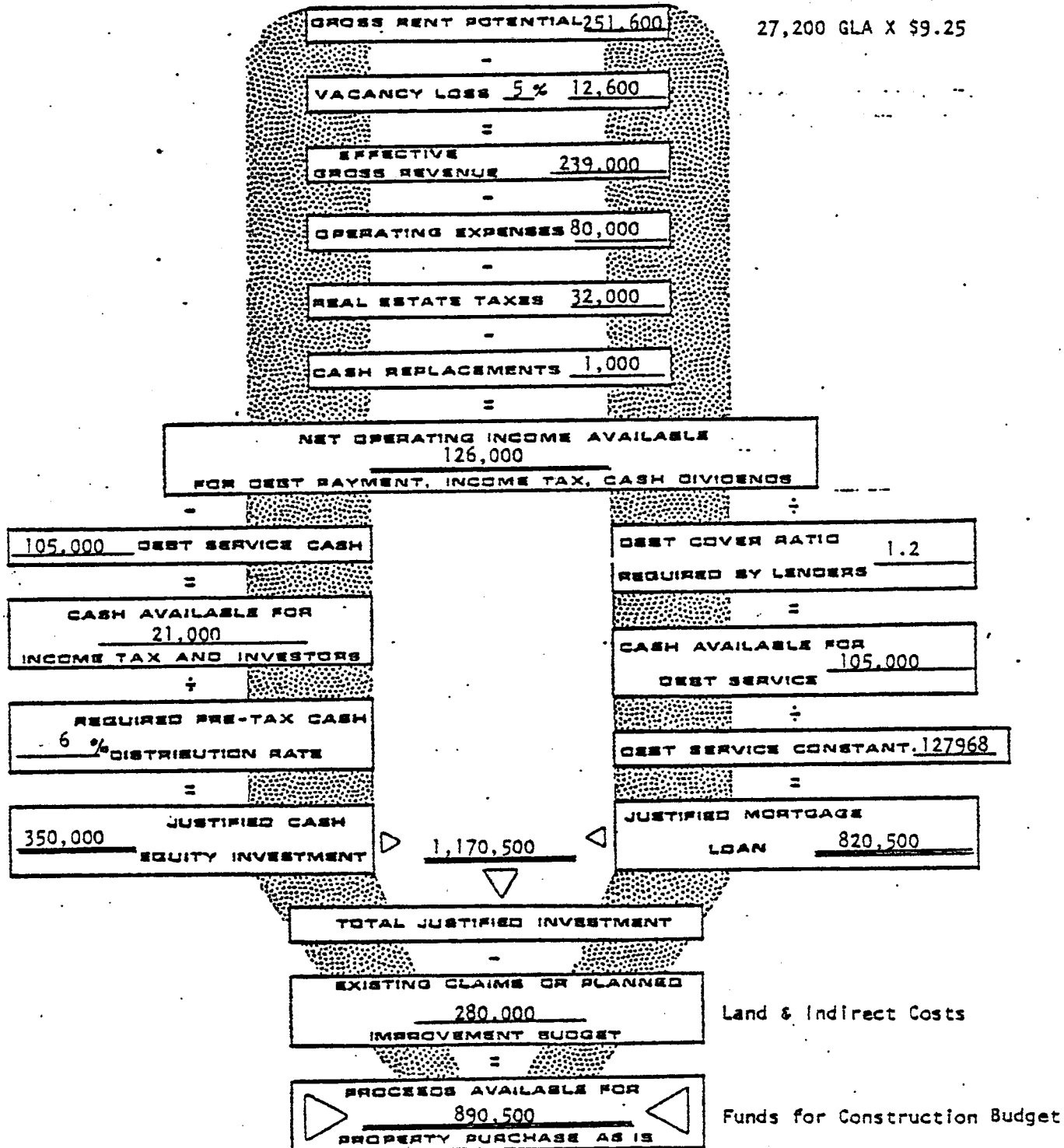
$$\frac{\text{Net Op. Inc.}}{\text{Debt Ser.}} = 1.11 \text{ (too low)}$$

$$\frac{141,824}{126,944} = 1.11 \text{ (too low)}$$

LENDER'S POINT OF VIEW

EXHIBIT 2

DEBT COVER RATIO APPROACH

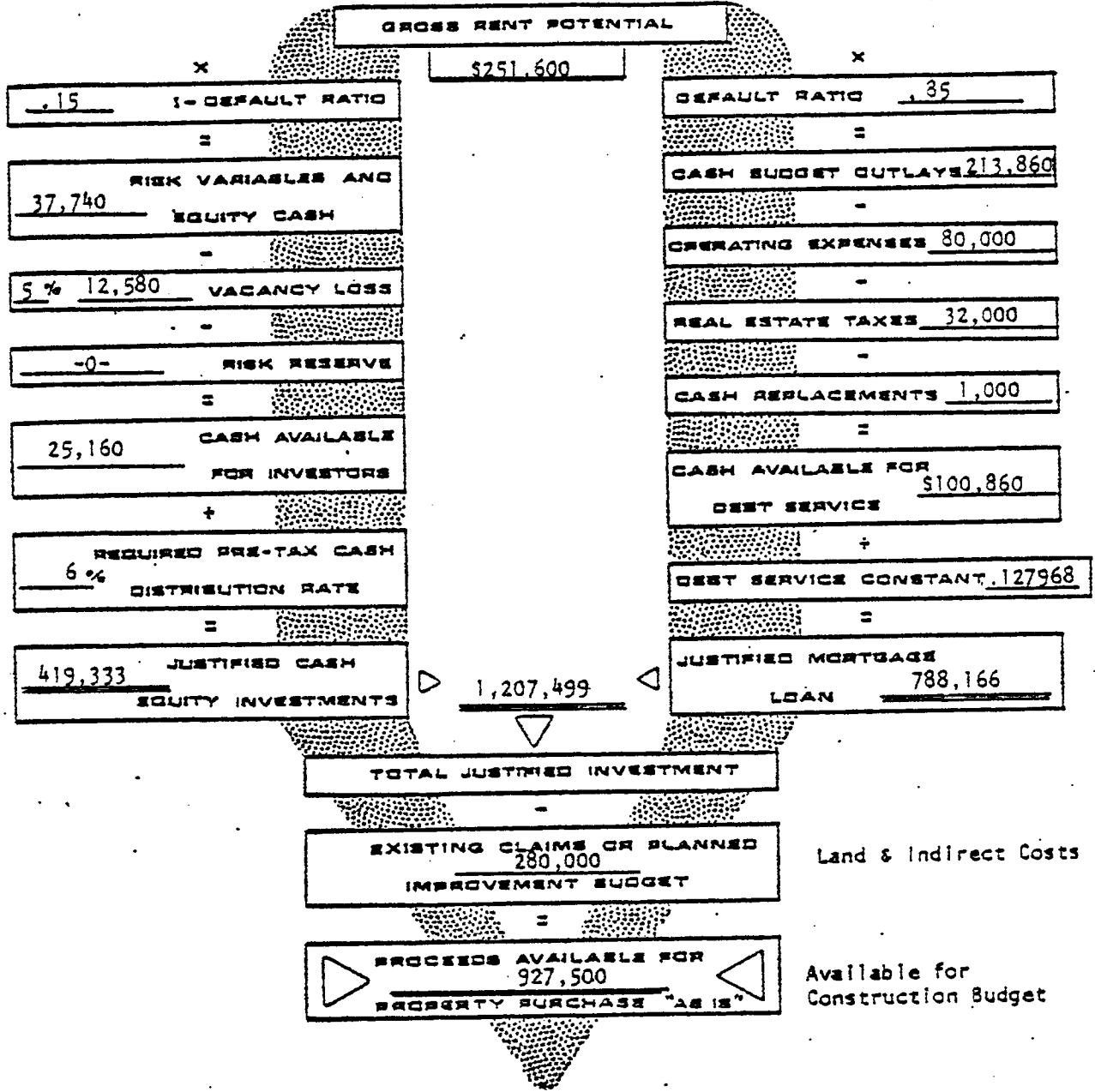


$\frac{890,500}{32,000} = \$27.80/\text{sq. ft. justified building budget}$

DEVELOPER'S POINT OF VIEW

EXHIBIT 3

DEFAULT RATIO APPROACH



\$37/sq. ft. of gross area for justified bldg. budget

1. Is the income from a retailing, service intensive business or from wholesaling of space (parking ramp vs. ramp operations or John Hancock Observation Deck or floor space rents)?
 2. Are entitlements that go with the land point specific or trans-portable? (permit to build a dam vs. a liquor license)
 3. Extraordinary features or services rather than customary (refrigerator stove may be customary but maid service is not)
 4. Ancillary rather than integral - such as janitorial service or utilities which could be contracted for from off-site contractors
 5. IRS classification as 1250 property or 1231 (real) or 1231 property (personalty).
- E. The operating expenses from the history of the building are not necessarily appropriate for a new buyer if the prudent management rule for fair market value or profile of the prospective purchaser for the most probable price may suggest changes in the modus operandi.
1. Currently manually operated elevators may be replaced by automated elevators.
 2. Budgets for kilowatt hours and BTU consumption may be modified downward by instituting improved procedure even though the cost per unit may be rising more than most expenses.
 3. Accounting systems of many owner occupied buildings are used to hide various items which may be weeded out including salaries to children, rent-a-plant, etc.
 4. Sale of a property may trigger reassessment and a whole new real estate tax, which leads to an interesting problem in circular reasoning since income value will be a function of real estate tax and the real estate tax is probably tied to value.
 5. It is necessary to read each lease to determine renewal options, the degree to which increased expanses can be passed through, or other concessions which may have been made which will cost money in the future. Ultimately expenses will need to be compared for normal level for that type of building and patterns analyzed.
- F. Exhibits 5-6 show the forecast of revenue, expenses, and deductions for non-real estate allocations for a hotel property.
1. Note that the estimate of occupancy is much more difficult than the determination of average rent per room per night.
 2. Note that projection for inflation may differ with specific items, such as utilities, labor, and supplies.
 3. Note that this appraisal was for a real estate tax appeal so that real estate taxes are not included in expenses.
 4. Note that a five year projection is about as far in the future as one cares to go.
 5. Except in the case of subdivisions, a short-term projection makes it necessary to have an assumption about real sale price.
- G. Discount rates must be chosen that are consistent with the treatment of income and the viewpoint of the appraisal.

Howard Johnson -
 Schedule of Projected Income and Expenses
 For the Years Commencing May 1, 1974-78

Exhibit 4-6

Period	1974-75	1975-76	1976-77	1977-78	1978-79
Occupancy (163 rooms)	68%	70%	71%	72%	73%
Revenue:					
Available Rooms	59,463	59,400	59,400	59,400	59,400
Occupied Rooms	40,463	41,580	42,174	42,768	43,362
Rate Average ¹	18.89	19.00	19.50	20.00	20.50
Room Revenue	764,450	790,020	822,390	855,360	888,920
Public Room Rental ²	7,116	7,200	7,200	7,200	7,200
Restaurant Rental ³	31,500	31,500	31,500	31,500	31,500
Telephone ⁴	(14,345)	(14,795)	(15,375)	(15,960)	(16,560)
Other Income ⁵	6,113	6,165	6,405	6,650	6,900
Room Service Commissions ⁶	1,635	1,850	1,920	1,995	2,070
Total Revenue	796,468	821,940	854,040	886,745	920,030
Operating Expenses:					
Payroll ⁷	166,180	164,390	170,808	177,349	184,006
Housekeeping ⁸	33,160	33,700	34,200	34,700	35,200
Adm. & Gen. ⁹	83,150	85,890	89,250	92,665	96,145
Adv. & Promotion ¹⁰	82,250	82,735	84,704	86,352	88,030
Utilities ¹¹	66,500	76,030	79,000	82,025	85,100
Repairs & Maintenance ¹²	16,550	13,500	13,500	13,500	13,500
Total Operating Expenses	447,790	456,245	471,452	486,591	501,981
House Profit	348,678	365,695	382,578	400,154	418,049
Misc. Interest Income	720	720	720	720	720
Gross Profit	349,398	366,415	383,298	400,874	418,769
Less: Insurance	10,314	9,926	9,926	9,926	9,926
Land Rental ¹³	7,680	7,680	7,680	7,680	7,680
Income to Furnishing ¹⁴	64,000	64,000	64,000	64,000	64,000
Income before RE Taxes and Debt Service to Land and Buildings	267,404	284,809	301,692	319,268	337,163

Sardworth Research, Inc.

Notes to Exhibit 4-6

1. Rate Average:

- The average room rate for the year ending April 30, 1975 was \$18.89. This was a \$.19 increase over the room rate for the period ending April 30, 1974, or about 1%. The increase was due in large part to standardizing room discounts for major clients and for functions requiring a large number of rooms.

2. Public Rooms:

- For the year ending April 30, 1975 the total dollar volume was \$7,116. In comparison, for the year ending December 31, 1974, the total volume was \$6,854. Public room rental was not found to be related to the level of occupancy or total revenues, thus it is assumed to be fairly fixed in character.

3. Restaurant Rental:

- The restaurant is leased to Howard Johnson's for a minimum rent of \$31,500, plus 5% of the amount of gross receipts which exceeds 20 times the minimum rental.

4. Telephone:

- Telephone revenues have averaged 3.4% of room revenues, compared with an industry average of 3.6% (Lodging Industry, by Laventhal, Krekstein, Horwath, and Horwath).
- Annual equipment lease payment is \$12,764.40.
- Net losses have average 1.8% of revenues. With increased occupancy, losses should not exceed 1.5%, comparable to national averages in Laventhal, Krekstein, Horwath and Horwath.

5. Other Income:

- Includes valet and laundry, vending sales, sundry sales, and 10% commission on banquet food sales. Vending has averaged 1/2 of 1% of total revenues. The remainder accounts for 1/4 of 1% of total revenues.

6. Room Service Commissions:

- 2% commission on restaurant bills and room service charged through motel plus 20¢/room service ticket, thus variable with occupancy.

7. Payroll:

- Actual and target results are 20% of total revenues.

8. Housekeeping:

- Averages have ranged from \$33,157 (December 31, 1974 closing) to \$33,775 (April 30, 1975 closing), or 4.06% to 4.27% of total revenues. Dollar amounts are fairly constant within a narrower range of occupancies.
- Includes commissions to travel agencies.

9. Administrative and General:

- For the year ending December 31, 1974 the total amount was approximately \$82,750, or 10.45% of revenues. The totals are comprised of expenditures the majority of which are variable in nature.
- Includes a 3% fee for management services.

10. Advertising and Promotion:

Schedule

		<u>1975-76</u>
Outdoor Sign		
Sign Co.	\$1625.50/mo.	
Advertising Co.	31.50/mo.	
Less: Howard Johnson's share	<u>(275.00/mo.)</u>	
Total	\$1377/month X 12 =	\$16,524
Promotions		1,500
Publications		7,200
Franchise Fee (5% of gross room receipts plus public room rentals)		39,537
Manager Expense and Promotion		3,475
Miscellaneous Advertising		2,500
Reservation Charge to Howard Johnson		<u>12,000</u>
Total		<u>\$82,736</u>

11. Utilities:

- The total is comprised of four elements: electric bulbs, electric current, fuel, and water. The total for the year ending December 31, 1974 was \$64,274 or 8.12% of total revenues.
- Interim rate increases by Gas and Electric commenced in June 1975. Electric increased 17.7% while fuel (gas) increased 7.33%. At present, additional proposed increases are being evaluated by the Public Service Commission which would become effective in 1976. Electric increases are proposed to be an additional 14.9% while gas is to increase 4.9%. Beyond 1976, increases are expected to be between 5% and 10% per year for both forms of energy.
- Utilities are not expected to exceed 9.23% of total revenues without a corresponding increase in room rates. Increases in utilities are expected to occur faster than any corresponding increase in room rates, thus it should be some time before the utility expense ratio will stabilize at approximately 9%.
- Year to date totals indicate the projections for 1975-76 are consistent with the above assumptions concerning the room revenue increase lag.

12. Repairs and Maintenance:

- Contracts

Plabocki Sign Repair Contract	\$1,060
Westinghouse Elevator Contract	3,336
Pellitteri Wast Removal	738

- Actual for year ending December 31, 1974 was approximately \$16,550.

- For the year 1975-76, the year to date totals indicate a decrease in expenditure. Such expenditures should remain fairly constant over the next five years.

13. Land Rent:

Monthly rental charges	\$1000
Less: Recovery from leased property	<u>(360)</u>
Net land cost per month	640

14. Furnishings and Other Assets:

Furnishings and Equipment

Furnishings and Equipment	\$251,120
Carpeting	60,490
Two Autos	9,480
Signs	9,967
Leasehold Improvements	<u>5,778</u>
Total per Audit	336,835

Factors Attributed to Furnishings

Rate of Return	9.0%
Recapture	10.0%
Personal Property Tax	4.5%

Income Equivalent of Recapture and Return to Equity

$336,835 + 336,835(9\% \times 10 \text{ years}) = 639,987$

$639,987 \div 10 = 63,999$ or 64,000

1. Straight capitalization presumes reserves in expenses for any item replaced before the end of the useful life. The Ellwood discount factor assumes reserves only for items replaced within the protection period.
 2. The FHA will provide a discount rate for the 2013 form which integrates the allowable cash on cash return to equity, mortgage insurance and debt service constant at the allowable interest rate.
 3. Investment analysis assumes only cash available for distribution is discounted after a decision to internally finance improvements has been reached. Reserves and expense policies must be kept consistent with resale assumptions in the scenario.
 4. Viewpoint gets tricky in terms of prudent investor vs. trader vs. institutional investor, all with different opportunity costs of money. Eminent domain appraisal is clearly from the viewpoint of the buyer but net liquidating value is from the viewpoint of the trustees and what he must do to protect himself against charges of waste (prudent man) or delay.
- H. Do not rely on overall rates from the market place since these are derivative of particular financing packages or engineered to suit past objectives of the parties

Exhibit 7

MC CLOUD B. HODGES, JR.
REAL ESTATE INVESTMENT, VALUATION AND COUNSELING
410 PINE STREET, SUITE 203
VIENNA, VIRGINIA 22180 703 - 281-5668

October 9, 1980

MEMORANDUM FOR several interested RE appraisers/counselors,
trial attorneys and academicians

Enclosed is an expanded and revised list of OARs and assessment/sales ratios which are self explanatory. This list is not a pure (random) sample by statistical rules. On one hand it is much larger than a sample need be, as it covers nearly 70% of all known property sales for the areas described, in the price range above about one-half million dollars, excluding MF apartment properties sold for condo conversion. On the other hand, it is possible that the 30% of investors-purchasers who, thus far, have not cooperated in furnishing data for this survey, may have shown slightly lower average OARs and A/S ratios.

This study, consuming several hundred man-hours in visits to offices of investors and inspections of their properties, was initiated more than two years ago primarily to obtain market data for rebutting several ad valorem tax valuations of properties owned by my clients. But it is now evident, from the specific results of the study and from its sheer coverage, that it ought to serve as the basis for a new educational manuscript advocating modern methods of valuing investment classed property. The "OAR" capitalization method, regardless of how the OAR is derived or constructed, is quite crude, often erroneous, and therefore useless as applied to higher priced property valuations. It was made even more useless during the last year in which many institutional sources of long term, level payment mortgage loans have withdrawn or have changed their lending practices in order to share in part of the inflation-produced cash flow through additional interest and/or future capital gain.

The second enclosure, a revised edition of "Effects of Financing on Price and Value", should explain the main reasons for the variances in OARs shown in the first enclosure: financing and tax shelter. The other reasons for OAR variances are the buyers' anticipated future changes in net income and resale/exchange values. Some properties are expected to produce large profits, or their only profits, in the distant future, while others will be nominally profitable only in the short range. This reduces the "NOI" either as a first year or a "stablized" figure to a position of invalidity in the valuation appraisal practice.

Enclosures

McCLOUD B. HODGES, JR.
 REAL ESTATE INVESTMENT, VALUATION AND COUNSELING
 410 PINE STREET, SUITE 203
 VIENNA, VIRGINIA 22180 703 - 281-5668

Sample of investment-classed property resales in the Virginia and Maryland suburbs of Washington, D. C., showing the wide variations in the overall capitalization rate (OAR) and in the assessment/sale price ratio. For any property which was not sold for cash above new, market-rate mortgage financing, the price shown is the cash-equivalent price, being the sum of the equity cash and the balances of the mortgage loans after discounting the loans to their estimated cash liquidable values at dates of property sales.

The OAR is based upon the cash-equivalent sales price and the net operating income (NOI) produced in the first year following the date of sale. If a full year had not passed by the date of any datum sale analysis, the NOI is that which was budgeted by the new owners. The assessment/sale price ratio is based upon 100% market value assessment and the cash equivalent sales price. Supporting data for all property sales are contained in a separate, confidential listing with corresponding identification (ID) numbers.

<u>ID</u>	<u>Year of Sale</u>	<u>Kind of Property and Location</u>	<u>Cash Equiv. Price</u>	<u>OAR</u>	<u>Assmt/Sale</u>
100	1977	Garden apts., Fairfax Co.	440,000	.1298	118%
105	1980	Office Bldg., Fairfax Co.	467,074	.0856	118%
107	1978	Elevator apts., Montgomery Co.	474,389	.0942	148%
110	1978	Elevator Apts., Arlington Co.	559,800	.0857	71%
113	1978	Office Bldg., Montgomery Co.	585,126	.1324	133%
115	1977	Garden apts., Fairfax Co.	589,000	.1091	94%
120	1980	Office Bldg., Fairfax Co.	590,255	.0860	158%
125	1980	Office Bldg., Fairfax Co.	638,975	.1291	229%
130	1976	Garden Apts., Alexandria City	730,058	.1232	77%
132	1978	Office Bldg., Montgomery Co.	746,833	.0818	97%
135	1978	Garden Apts., Fairfax Co.	802,900	.1396	104%
140	1980	Garden Apts., Fairfax Co.	836,857	.0874	96%
141	1977	Garden Apts, Prince Georges Co.	850,000	.1012	87%
142	1978	Office Bld., Montgomery Co.	950,000	.0759	89%
143	1978	Elevator Apts., Prince Georges Co	994,808	.1151	101%
144	1978	Office Bldg., Montgomery Co.	1,010,865	.0868	59%
145	1980	Office Bldg., Fairfax Co.	1,120,209	.0957	112%
147	1979	Garden Apts., Prince Georges Co.	1,159,172	.1267	102%
150	1977	Office Bldg., Fairfax Co.	1,245,200	.1124	106%
155	1976	Garden Apts., Arlington Co.	1,395,000	.1019	103%

<u>ID</u>	<u>Year of Sale</u>	<u>Kind of Property and Location</u>	<u>Cash Equiv. Price</u>	<u>OAR</u>	<u>Assmt/ Sale</u>
157	1977	Shopping Cntr., Montgomery Co.	1,461,500	.0879	98%
160	1976	Garden Apts., Alexandria City	1,577,300	.1065	108%
162	1980	Garden Apts., Ann Arundel Co.	1,638,000	.1416	90%
163	1979	Garden Apts., Prince Georges Co.	1,716,505	.1290	101%
164	1979	Garden Apts., Prince Georges Co.	1,732,107	.1827	144%
166	1978	Office Bldg., Arlington Co.	1,751,835	.0645	90%
168	1976	Garden Apts., Fairfax Co.	1,879,250	.1248	123%
170	1976	Garden Apts., Fairfax Co.	1,960,835	.1140	114%
175	1975	Elevator Apts., Fairfax Co.	1,984,500	.1321	156%
180	1978	Elevator Apts., Falls Church	2,000,000	.0821	91%
184*	1977	Garden Apts., Montgomery Co.	2,113,500	.1192	115%
185	1980	Shopping Center, Fairfax Co.	2,144,706	.1081	125%
190	1975	Elevator Apts., Alexandria City	2,153,606	.0831	137%
195	1978	Garden Apts., Fairfax Co.	2,324,000	.1224	106%
200	1975	Garden Apts., Fairfax Co.	2,375,000	.0950	115%
205	1977	Elevator Apts., Arlington Co.	2,400,000	.0975	66%
210	1980	Office Bldg., Fairfax Co.	2,510,492	.1290	133%
225	1978	Garden Apts., Fairfax Co.	2,569,500	.1068	85%
300	1975	Elevator Apts., Alexandria City	2,558,669	.1234	93%
301**	1979	Garden Apts., Prince Georges Co.	2,960,244	N/A	131%
303	1975	Garden Apts., Alexandria City	2,789,190	.0775	122%
304	1978	Garden Apts., Prince Georges Co.	3,090,639	Neg.	95%
305	1979	Office Bldg., Montgomery Co.	3,100,000	.1221	78%
306	1976	Garden Apts., Fairfax Co.	3,117,300	.1056	165%
307	1977	Garden Apts., Prince Georges Co.	3,125,000	.1070	102%
310	1979	Garden Apts., Alexandria City	3,214,928	.1110	110%
315	1980	Shopping Center, Fairfax Co.	3,765,341	.1093	132%
317*	1977	Garden Apts., Prince Georges Co.	4,000,000	.0810	86%
318	1978	Garden Apts., Prince Georges Co.	4,100,000	.1439	97%
319	1979	Garden Apts., Prince Georges Co.	4,128,173	.0962	98%
320	1975	Garden Apts., Fairfax Co.	4,190,700	.1359	155%
323	1977	Elevator Apts., Montgomery Co.	4,796,255	.0790	154%

* Financed under FHA 223(f) rehabilitation and refinancing program.

** Nominal price shown. No information available on terms of sale or NOI in first year of ownership.

<u>ID</u>	<u>Year of Sale</u>	<u>Kind of Property and Location</u>	<u>Cash Equiv. Price</u>	<u>OAR</u>	<u>Assmt/ Sale</u>
325	1980	Garden Apts., Fairfax Co.	4,871,282	.1316	124%
328*	1978	Garden Apts., Prince Georges Co	5,426,138	.0921	116%
330	1980	Office Bldg Complex, Fairfax Co	5,529,031	.1071	110%
335	1979	Garden Apts., Alexandria City	6,296,800	.1345	113%
340	1980	Office Bldg., Fairfax Co	6,593,267	.1121	154%
344	1979	Garden Apts., Prince Georges Co	6,726,848	.1457	88%
345	1976	Garden Apts., Fairfax Co.	6,735,450	.1161	102%
352	1979	Elevator Apts., Montgomery Co.	8,189,554	Neg.	208%
354	1979	Office Building, Montgomery Co	8,850,000	.0862	120%
355	1979	Office Bldg., Arlington Co.	8,857,450	.0593	128%
360	1978	Office Bldg., Montgomery Co.	10,729,000	.1025	80%
365	1976	Elevator Apts., Fairfax Co.	12,819,124	.0936	99%
375	1978	Office Bldg., Fairfax Co.	14,957,334	.0881	89%
385	1979	Elev. & Gdn. Apts., Prince Geo.	18,866,955	.0674	72%

* Financed under FHA 223(f) rehabilitation and refinancing program.

EFFECT OF FINANCING ON PRICE AND VALUE

WHAT CAN A 4-PERSON PARTNERSHIP PAY FOR A 10-YR. OLD, GOOD QUALITY APARTMENT COMPLEX UNDER 3 DIFFERENT SETS OF FINANCING TERMS ?

FACTORS CONSTANT IN ALL 3 ANALYSES:

- NET INCOME BEFORE R.E. TAXES STARTS AT \$350,000 AND RISES ON A 4% SLOPE IN ACTUAL INFLATION \$.
- R.E. TAX RATE = .0121; ASSESSED VALUE = SALE PRICE.
- DEPRECIABLE ASSETS = 85% OF PRICE, 25 YR. LIFE, 125% S/L D.B.
- NO MAJOR CAPITAL REPLACEMENTS IN NEXT TEN YEARS.
- RESALE PRICE 10 YEARS LATER = \$3,662,000, CASH-TO-SELLERS
- OWNERS WILL REMAIN IN 50% FED. & 5.75% STATE INCOME TAX BRACKET DURING ALL 10 YEARS OF OWNERSHIP.
- OWNERS WANT 18% EQUITY YIELD (I.R.R.) AFTER INCOME TAX.
- 1978 TAX ACT GOVERNS INCOME, GAIN & ADD-ON TAXES.

VARIABLE FACTOR: FINANCING

1ST MTGE	\$1,479,786 Asmd. @ 7½%, 17 More Yrs.	New \$1,850,000 @ 13%, 30 Yr. Amort., Ballooning 10 Yrs.	None
2ND MTGE	\$1,500,000 DPMM @ 6% Int. Only, 10 Yrs.	None	
PRICE/VALUE	\$ 3 537 073	\$ 2 527 098	\$ 1 435 046
EQUITY CASH	557 287	677 098	1 435 046
AFTER-TAX CASH FLOW IN YEAR	1 2 3 4 5 6 7 8 9 10	\$ 85 460 86 244 87 085 87 960 88 849 89 730 93 655 97 373 100 867 912 938	\$ 88 738 92 103 95 555 99 081 102 664 106 289 112 136 117 879 123 503 1297 106
			\$189 003 193 988 199 054 204 196 209 411 214 695 221 293 227 890 234 488 2905 060
"O.A.R."	.0869	.1264	.2318

"Overall Rate" = Year 1 Net Income After R.E. Taxes ÷ Total Sale Price/Value

10/7/80

SEMINAR INSTRUCTOR

DR. JAMES A. GRAASKAMP, Ph.D., SREA, CRE is one of the most popular and dynamic real estate instructors in the U.S. today. His presentations reflect the rare combination of real world experience and academic achievement that has characterized him as one of the industry's "Original Thinkers".

He has served as Chairman of the Department of Real Estate and Urban Land Economics at the University of Wisconsin for over ten years. He is currently teaching advanced appraisal techniques and advanced feasibility studies.

In addition to his academic work, Dr. Graaskamp is President and founder of Landmark Research, Inc., a real estate research and appraisal firm. He is also co-founder of a general contracting firm, a land development company and a real estate investment corporation. His work includes court testimony as an expert witness, substantial and varied consulting and valuation assignments which include investment counseling to insurance companies and banks and other lenders, plus feasibility and financial analysis of nationally known real estate development projects for a wide variety of clients.

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SECTION I

PRINCIPLES OF CONTEMPORARY REAL ESTATE APPRAISAL:

ORIGINS, THEORY, AND APPLIED EXAMPLES

*Copy of Section I is found in VIII. H. 1.
"Contemporary Appraisal Seminar"*

SECTION II

CONTEMPORARY APPRAISING OF LARGE INCOME PROPERTIES
INCLUDING EFFECTS OF FINANCING, SUBSIDIES,
AND NON-REAL ESTATE PROFIT CENTERS

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SEMINAR CRITIQUE FORM

Contemporary Appraisal of Large Income Properties
Including Effects of Financing, Subsidies,
and Non-Real Estate Profit Centers

A One Day Seminar For
NORTHWEST CENTER FOR PROFESSIONAL EDUCATION

August, 1981

Presented by
Prof. James A. Graaskamp, CRE, SREA
School of Business, University of Wisconsin

I. Introduction

It is generally recognized that the real estate market is dependent on substantial amounts of credit to support effective demand so that real estate prices and perhaps values vary with the terms and supply of credit generally available in the marketplace. Indeed the old timers have seen the definition of fair market value gradually move away from the firm premise of cash to the seller to a somewhat more subjective condition of terms generally available in the market.

- A. The pressure of double digit inflation is eroding many of the appraisers' favorite simplifications of the market model:
1. The long term fixed interest mortgage, amortized from property productivity is gone.
 2. The simple division of income between the mortgage and the equity component is smothered in participating mortgages, limited partnerships, convertible mortgages and seller financing.
 3. As the government had removed general subsidies to real estate finance such as regulation Q, it has made greater use of specific interest subsidies to selected special groups.
 4. Real estate markets must be defined not only in terms of use, age, income, but also access to capital.
 5. Moreover, most properties exist in a 3-tier market, utility to house an activity, commodity and money speculation, and as part of a going concern.
 6. The 3-tier market can be further subdivided by the nature of permits or other entitlements that are site specific and define risk of a vested or non-vested opportunity.
- B. Volatile money market conditions and the widespread use of creative financing leave the appraiser in considerable difficulty in defining typical market terms, cash equivalent prices or the relationship of

fair market value to transaction price. Does the client want fair market price, most probable price, going concern value, contributory value, investment value, or liquidating value in event of delinquency and foreclosure.

- C. The impact of these elements is significantly different for problems involving:
 - 1. Income investment properties
 - 2. Economic development properties
 - 3. Multi-family residential properties
 - 4. Single family residential properties
 - D. The impact of financing in each situation requires that we go back to basics. The appraiser or his client must define:
 - 1. What is the function of the appraisal?
 - 2. Which rights are to be appraised? (Those that run with the establishment on the site, with the ownership position, or with fee simple title).
 - 3. Which definition of value is appropriate?
 - 4. How is productivity allocated to the agents of production?
 - E. Reference to Exhibit 1
 - F. Reference to definition of fee simple title in Exhibit 2
 - G. Reference to definition of fair market value in Exhibit 3 and compare to most probable price in Exhibit 4
- II. The Games People Play With Income Investment Property makes it very difficult to apply any one of the three approaches to value.
- A. Sales prices are engineered by accountants to some degree to shift asset values among various classifications for land, structure, personalty, intangibles, capital gains and losses and ordinary gains and losses, making market comparison anything but objective (not to mention adjustments for non-market financing discussed in Section III).
 - B. Similarly, the income approach has great difficulty in applying the truism that income value is the present value of income plus the present value of reversion.
 - 1. There is the problem of defining net operating income in terms of what is attributable to the real estate (aside from financing effect on cash throwoff).
 - 2. There is the problem of defining the net reversion to equity in an uncertain future (aside from financing effect on mortgage balance).

EXHIBIT I

Critical Issues Which Define Appraisal Process

Function of the Appraisal	Property Rights	Relevant Definition of Value	Allocation of Productivity	Buyer Motivation Presumed
Tax assessment	Fee simple private rights unencumbered	Fair market value	Income attributable to land and structures only	Purchase of economic productivity
Mortgage loan (non-participating)	Encumbered fee simple private rights plus additional rights pledged	Regulations - fair market value Underwriting - solvency price or liquidating value	Fixed income pledged from all sources less costs of creative management	Share of economic productivity contributed by capital
Mortgage loan (participatory)	Encumbered title plus non-vested interest in selected future revenues	Present value of all future cash flows	Variable income pledged plus share of reversionary interest	Share of economic productivity contributed by capital plus share in selected management returns plus positioning against devaluation due to changing conditions
Sale of an Investment	Encumbered title plus vested entitlements plus going concern profit center opportunities	Most probable price above minimum acceptable alternative opportunity	Return from land, structures, personalty, and selected entitlements	Increase in spendable cash Increase in liquidity value of estate Positioning to maximize probability of survival of benefits despite changing conditions
Purchase of Investments	Encumbered title plus positioning for access to entitlements	Most probable price within perceived peril point limit	land, structure, personalty, and intangible assets less profit centers for management	Increase in spendable cash Increase in liquidity value of estate Positioning to maximize probability of survival of benefits despite changing conditions
Going concern purchase of a business	Encumbered title plus positioning for access to entitlements plus reduction in risk for business start-up plus monopolistic market controls	Most probable price within perceived costs of alternative	Land, structure, personalty, and intangible assets and good will plus profit centers for management	Increase in spendable cash Increase in liquidity value of estate Positioning to maximize probability of survival of benefits despite changing conditions

EXHIBIT 3

(*The most probable price - new edition, Institute)
FAIR MARKET VALUE - The highest price in terms of money which a property will bring in a competitive and open market under all conditions requisite to a fair sale, the buyer and seller, each acting prudently, knowledgeably and assuming the price is not affected by undue stimulus.

Implicit in this definition is the consummation of a sale as of a specified date and the passing of title from seller to buyer under conditions whereby:

1. buyer and seller are typically motivated.
2. both parties are well informed or well advised, and each acting in what he considers his own best interest.
3. a reasonable time is allowed for exposure in the open market.
4. payment is made in cash or its equivalent.
5. financing, if any, is on terms generally available in the community at the specified date and typical for the property type in its locale.
6. the price represents a normal consideration for the property sold unaffected by special financing amounts and/or terms, services, fees, costs, or credits incurred in the transaction.

Source: P. 137, Real Estate Appraisal Terminology, Editor Byrl Boyce.

EXHIBIT 4

The most probable price is that selling price which is most likely to emerge from a transaction involving the subject property if it were to be exposed for sale in the current market for a reasonable time at terms of sale which are currently predominant for properties of the subject type.

Source: P. 8, The Appraisal of 25 N. Pinckney, Editor James A. Graaskamp.

*Not to be confused with most probable price in contemporary appraisal, which does not reflect an assumption of a competitive market with alternative, does not require ignoring of public bargaining position of the party, and which does not require cash to the seller if the market cannot have a transaction without seller financing.

3. There is the problem of selecting a conversion process which reduces income cash flows and reversionary cash flows to a single present value.
- C. Neither revenue, nor expenses nor debt service are constant over time anymore so that NOI/OAR is no longer a useful valuation model. Instead rents, vacancies, expenses, and financing must be staged using a spread sheet for both income and the reversion. Lenders may share in appreciation and owner and lender may share the risk of variable interest and the first principal payment.
- D. The definition of economic rent attributable to the real estate
1. Is income attributable to entitlements that go with fee simple title to the land and are point specific or to transportable permits?
 - a. For example - does liquor license go with the building? Is permit to build or maintain a dam assignable? Does right to management fee and brokerage fee go with general partnership or property?
 2. Is the real estate income from retailing of space or from wholesaling space?
 - a. Parking ramp lease versus parking space by the hour, observation deck versus ticket, condominium conversion fee versus apartment project investment.
 3. Is the income for extraordinary services or intangible assets rather than customary?
 - a. Maid service versus janitorial, shopping center premium for proximity or for joint merchandising and risk management.
 4. Ancillary to rather than integral with the project.
 - a. Can services be acquired off premises such as janitorial or utilities?
 5. IRS classification as 1250 property (real) or 1231 property (personalty) or Section 38 (tangible) or Section 1048 (intangible).
 6. Is income attributable to governmental agencies in exchange for contractual entitlements of control or use to the public interest for the term of the contract?
- E. Problem of defining or forecasting a reversion
1. Pricing real estate for utilitarian purpose, to buy access to service sales, or speculate in long term demand/supply commodity relationships of long term commodity/money ratios.
 2. Can the appraiser prove presence of necessary conditions for appreciation and amount of depreciation?
 - a. Rising net income
 - b. Falling interest rates
 - c. Falling investor expectations

3. When is appreciation speculative, non-vested and excluded from fair market value?
 4. Can the appraiser simulate alternative speculative gains for most probable price?
 5. When a premium is paid anticipating syndication of condominium conversion, should there be an adjustment for purchase of a business opportunity? Does fair market value include management fees for conversion?
- III. Case Study of an appraisal of a 50-year old high rise office building in the CBD with vacancy problems, utility problems and management problems.
- A. Revenues reflected loss of a major tenant (State of Wisconsin), lack of demand for retail space on the first floor, a soft market for B-class space, and a reluctance of management and tenants to use pass-throughs for operating costs.
 - B. It was necessary to do a spread sheet indicating a gradual reduction of vacancy loss, a gradual updating of existing leases with pass-through clauses, and investment in critical energy conservation.
 - C. Resale price is tied to projected net income and gross with a debt cover ratio and a cash-on-cash yield. Loan-to-value ratio is irrelevant. (See The Appraisal Journal, January 1981, DCR/R_e Cap Rate Tables for Today's Financing, p. 15.)
 - D. Our firm makes heavy use of the backdoor approach on MRCAP for valuation.

LUNCH BREAK

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EXHIBIT 21

SCALE FOR SCORING COMPARABLES ON IMPORTANT INVESTOR CONSIDERATIONS
FOR OFFICE/RETAIL SPACE IN MADISON C-4 ZONE

Parking 25%	5 = Ample private parking on site or available on contract within the same block. 3 = Limited parking on premises 0 = Little or no surface parking on premises.
Location 20%	5 = In the blocks of East and West Mifflin St. or North and South Carroll St., across from the Capitol Square 3 = In the blocks of North and South Pinckney St., across from the Capitol Square, or in the 100 block of West Washington, or adjacent to General Executive Facilities. 1 = Off of the Capitol Square
First Floor Retail Lease in Place at Time of Purchase 15%	5 = Strong lease in place. 3 = Strong lease in place for part of first floor. 0 = Lease expires in less than 6 months or vacant.
Need for Renovation of Office Space at Time of Purchase 15%	5 = No renovation required. 3 = Modest renovation required. 1 = Intensive renovation required.
Visual Quality of Office Entrance 10%	5 = Excellent design and location. 3 = Indifferent design and/or location. 1 = Poorly defined and/or adjacent to incompatible uses.
Vacancies in Existing Office Space at Time of Purchase 15%	5 = Less than 10% of net rentable area (NRA). 3 = More than 10% of NRA. 0 = Vacant

WEIGHTED MATRIX FOR COMPARABLE PROPERTIES

FEATURE/ WEIGHT	Rating/Weighted Rating						Subject 110 E. Main
	#1 30 W. Mifflin	#2 50 E. Mifflin	#3 16 N. Carroll	#4 123 W. Washington	#5 102 N. Hamilton	#6 212 E. Washington	
Parking 25%	5/1.25	3/.75	0/0	0/0	3/.75	3/.75	3/.75
Location 20%	5/1.00	5/1.00	5/1.00	3/.60	1/.20	3/.60	3/.60
First Floor Retail Lease In Place 15%	5/.75	5/.75	0/0	3/.45	3/.45	0/0	1/.15
Need for Renovation 15%	5/.75	1/.15	3/.45	5/.75	1/.15	1/.15	3/.45
Visual Quality of Office Entrance 10%	5/.50	3/.30	3/.30	5/.50	3/.30	3/.30	1/.10
Vacancies In Existing Office Space 15%	5/.75	0/0	5/.75	5/.75	0/0	0/0	1/.15
Total Weighted Score	5.00	2.95	2.50	3.05	1.85	1.80	2.20
Selling Price	\$2,555,500	\$850,000	\$615,270	\$2,896,000	\$330,000	\$472,000	X
Total Net Rentable Area (NRA)	65,000 sq. ft.	38,500 sq. ft.	35,725 sq. ft.	138,000 sq. ft.	28,000 sq. ft.	38,000 sq. ft.	74,000 sq. ft.
Price Per Square Foot (NRA)	\$39.30	\$22.10	\$17.20	\$21.00	\$11.80	\$12.40	
Price Per Square Foot of NRA <u>Total Weighted Score</u>	7.86	7.49	6.88	6.89	6.38	6.89	

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EXHIBIT 22

EXHIBIT 23

CALCULATION OF MOST PROBABLE PRICE USING
MEAN PRICE PER POINT EQUATION METHOD
(With Standardized Weighted Point Scores)

Comparable Property	Selling Price per NRA	Weighted Point Score	Price per NRA Weighted Point Score (x)
1	\$39.30	5.00	7.86
2	22.10	3.45	7.49
3	17.20	2.50	6.88
4	21.00	3.05	6.89
5	11.80	1.85	6.38
6	12.40	1.80	6.89
TOTAL			42.39

$$\text{Central Tendency (Mean = } \bar{x} \text{)} = \frac{\sum x}{n} = \frac{42.39}{6} = 7.07$$

$$\text{Dispersion (Standard deviation = } s \text{)} = \sqrt{\frac{\sum (x-\bar{x})^2}{n-1}} = \sqrt{\frac{1.38}{5}} = .525$$

where:

x	\bar{x}	$(x-\bar{x})$	$(x-\bar{x})^2$	n	$n-1$
7.86	7.07	.79	.62	6	5
7.49	7.07	.42	.18		
6.88	7.07	-.19	.04		
6.89	7.07	-.18	.03		
6.38	7.07	-.69	.48		
6.89	7.07	-.18	.03		
			1.38		

Value Range: $\bar{x} \pm s = 7.07 \pm .53$

Estimate of Value of Subject Property =

$$\text{NRA of subject} * \text{Weighted point score of subject} * (74,000 \text{ S.F.}) \quad (2.2)$$

$$[\text{Sample mean of price per NRA per total weighted score} \pm (\text{Dispersion} * t \text{ value})] \\ [7.07 \pm (.53 * t \text{ value})]$$

	Confidence Level	
	68% (t = 1.000)	90% (t = 2.015) @ n-1 = 5;
High Estimate: ¹	\$1,240,000	\$1,320,000
Central Tendency:	1,150,000	1,150,000
Low Estimate:	1,060,000	980,000

¹All value estimates are rounded.

Schedule of Rental Revenues¹ for the Period of April 30, 1980 Through April 29, 1985

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Occupancy as of April 30, 1980	Space Sq. Ft.	Annual Rent per Sq. Ft. ²	Lease Terms as of 4/30/80 ³	Annualized Gross Rental Revenues				
				4/30/80- 4/29/81	4/30/81- 4/29/82	4/30/82- 4/29/83	4/30/83- 4/29/84	4/30/84- 4/29/85
Lower Level & Roof								
B Level Vault-Vacant	700	3.00	--	\$ 2,100	\$ 2,100	\$ 2,270	\$ 2,270	\$ 2,450
B Level-Showroom & Office	4000	3.00	--	12,000	12,000	12,960	12,960	14,000
A Level-Storage	400	4.00	6/30/80	1,600	2,400	2,600	2,800	3,000
Honeywell Phone Box	--	--	--	600	600	600	650	650
Total-Lower Level	5100			\$16,300	\$17,100	\$18,430	\$18,680	\$20,100
First Floor								
Chez Vous-112	454	4.80	10/1/76 - 9/30/81	\$ 2,180	\$ 2,290	\$ 2,360	\$ 2,360	\$ 2,360
Chez Vous-114	1000	4.80	10/1/76 - 9/30/81	4,810	5,030	5,200	5,200	5,200
North Entry	2000	9.00	--	18,000	19,500	21,000	22,500	24,000
South Entry-Leaf & Ladle ⁴	3500	9.00	1/1/80 - 12/30/84	31,500	33,130	33,950	36,670	39,600
Total-First Floor	6954			\$56,490	\$59,950	\$62,510	\$66,730	\$71,160
Second Floor								
201 Vacant	150	6.50	--	\$ 970	\$ 970	\$ 1,050	\$ 1,050	\$ 1,140
202 State ⁵	600	6.70	7/1/79 - 6/30/80	4,020	4,320	4,320	4,670	4,670
203-4 Vacant ⁵	543	6.20	9/1/78 - 8/31/79	3,370	3,640	3,640	3,640	3,930
205-6 State	506	7.00	3/1/78 - 5/31/80	3,540	3,820	3,820	4,120	4,120
207-8 Homecrafts	386	7.20	1/1/79 - 12/31/81	2,780	2,850	3,000	3,000	3,080
209-10 State ⁵	451	6.25	11/1/79 - 5/31/80	2,820	3,040	3,040	3,280	3,280
211 Dr. Regez	219	7.00	--	1,600	1,730	1,730	1,870	1,870
212-14 Dr. Wierwill	700	6.50	4/1/78 - 3/31/81	4,570	4,900	4,900	4,900	5,210
215 Vacant	415	6.75	7/1/78 - 6/30/79	2,800	3,020	3,020	3,270	3,270
216 UPI	500	7.50	5/1/80 - 4/30/81	3,750	4,050	4,050	4,370	4,370
218-19 Rape Crisis Center	816	7.00	1/1/80 - 12/31/81	5,840	6,120	6,260	6,530	6,690
220-21 State ⁵	1400	6.25	12/1/79 - 5/31/80	8,750	9,450	9,450	10,200	10,200
Total-Second Floor	6686			\$44,810	\$47,910	\$48,280	\$50,900	\$51,830

EXHIBIT 24

Schedule of Rental Revenues¹ for the Period of April 30, 1980 Through April 29, 1985

Occupancy as of April 30, 1980	Space Sq. Ft.	Annual Rent per Sq. Ft. ²	Lease Terms as of 4/30/80 ³	Annualized Gross Rental Revenues				
				4/30/80- 4/29/81	4/30/81- 4/29/82	4/30/82- 4/29/83	4/30/83- 4/29/84	4/30/84- 4/29/85
Third Floor								
301 Vacant	150	5.75	--	\$ 860	\$ 860	\$ 930	\$ 930	\$ 1,000
302-3 State ⁵	1179	5.75	--	6,780	7,320	7,320	7,900	7,900
304 State ⁵	230	6.70	--	1,540	1,660	1,660	1,800	1,800
305-8 State ⁵	942	6.70	--	6,300	6,800	6,800	7,360	7,360
309 The Journal Co.	232	7.20	9/1/79 - 8/31/80	1,810	1,880	1,970	2,030	2,120
310-11 State ⁵	456	6.70	--	3,050	3,300	3,300	3,560	3,560
312 Vacant	234	5.75	--	1,340	1,450	1,450	1,570	1,570
313-14 Dr. R. Meng	482	7.20	6/1/79 - 5/31/80	3,490	3,730	3,750	4,000	4,030
315 Vacant	731	6.70	10/1/79 - 9/30/80	5,000	5,080	5,310	5,480	5,630
316-19 Wisc. Builders Assoc.	1091	7.00	1/1/80 - 12/31/80	7,810	8,180	8,360	8,730	8,940
320-24 Vacant	1363	7.00	--	9,540	10,300	10,300	11,130	11,130
Total-Third Floor	7090			\$47,520	\$50,560	\$51,150	\$54,490	\$55,040
Fourth Floor								
401 Vacant	150	6.40	--	\$ 960	\$ 960	\$ 1,040	\$ 1,040	\$ 1,120
402 Furst, Carlson Inc.	648	6.40	5/1/79 - 4/30/80	4,350	4,370	4,700	4,730	5,090
403-11 State	2147	6.75	1/1/80 - 12/31/81	14,500	14,880	15,670	16,100	16,960
412 Vacant	202	6.40	--	1,290	1,290	1,400	1,400	1,500
413-14 Wisconsin Alliance of Cities	679	6.80	--	4,980	5,020	5,420	5,420	5,850
415 State ⁵	259	7.00	3/1/79 - 2/28/81	1,830	1,940	1,970	2,100	2,130
416-19 State ⁵	1370	6.00	vacated 6/30/80	8,220	8,880	8,880	9,590	9,590
420-20a State ⁵	560	6.70	vacated 6/30/80	3,750	3,750	4,050	4,050	4,370
421-22 State	300	6.70	vacated 6/30/80	2,010	2,010	2,170	2,170	2,340
423-24 Ed Konkol	340	6.60	9/1/79 - 8/31/80	2,240	2,240	2,420	2,420	2,620
Total-Fourth Floor	6655			\$44,130	\$45,340	\$47,720	\$49,020	\$51,570

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EXHIBIT 24 -- Continued

Schedule of Rental Revenues¹ for the Period of April 30, 1980 Through April 29, 1985

Occupancy as of April 30, 1980	Space Sq. Ft.	Annual Rent per Sq. Ft. ²	Lease Terms as of 4/30/80 ³	Annualized Gross Rental Revenues				
				4/30/80- 4/29/81	4/30/81- 4/29/82	4/30/82- 4/29/83	4/30/83- 4/29/84	4/30/84- 4/29/85
<u>Fifth Floor</u>								
501 E. C. Barton	150	7.60	--	\$ 1,240	\$ 1,270	\$ 1,270	\$ 1,380	\$ 1,380
502 Vacant	842	7.50	--	6,310	6,820	6,820	7,360	7,360
503-5 Vacant	810	7.50	--	6,070	6,070	6,440	6,800	6,800
506-19 State	3922	6.25	11/1/79 - 10/31/83	24,500	24,500	24,500	30,590	31,770
520 State-Bd. of Aging	555	6.70	7/1/79 - 6/30/81	3,950	4,000	4,270	4,330	4,940
521-22 Dr. Coryell	339	7.20	7/1/79 - 6/30/80	2,440	2,690	2,740	2,920	2,950
523-24 Green Bay Press Gazette	337	7.60	9/1/79 - 8/31/82	2,560	2,690	2,760	2,760	2,760
Total-Fifth Floor	6955			\$47,070	\$48,040	\$48,800	\$56,140	\$57,960
<u>Sixth Floor</u>								
601 Vacant	150	6.70	--	\$ 1,000	\$ 1,000	\$ 1,080	\$ 1,080	\$ 1,170
602-4 State ⁵	1473	6.00	vacated 6/30/80	8,840	9,540	9,540	10,300	10,300
605 Vacant	204	6.40	--	1,300	1,300	1,410	1,410	1,520
			to 6/30/80					
606-10 State	1000	6.70	then mo. - mo.	7,370	7,500	7,500	8,100	8,100
611 The Evjue Foundation	286	7.00	vacated 11/30/80	2,000	2,000	2,160	2,160	2,330
612-14 State	647	7.50	11/1/79 - 10/31/83	4,850	4,850	4,850	5,080	5,240
615 Tenney Bldg.	344	7.00	--	2,400	2,400	2,600	2,600	2,800
616 John Barsness	850	6.00	3/1/79 - 2/28/81	5,170	5,520	5,590	5,950	6,020
617 Bill Ward	250	6.70	vacated 5/31/80	1,940	2,120	2,120	2,300	2,300
618-19 State	494	8.00	vacated 5/31/79	3,950	3,950	4,270	4,270	4,610
620-24 Vacant	1262	6.70	--	8,450	9,130	9,130	9,860	9,860
Total-Sixth Floor	6960			\$47,270	\$49,310	\$50,250	\$53,110	\$54,250
<u>Seventh Floor</u>								
701 Lawton & Cates	150	5.75	6/1/79 - 5/31/83	\$ 930	\$ 970	\$ 1,100	\$ 1,050	\$ 1,090
702-19 Lawton & Cates	5417	5.75	6/1/79 - 5/31/83	33,600	35,100	36,450	37,850	39,160
720-24 Vacant	1106	7.00	--	7,740	7,740	8,360	8,360	9,030
Total-Seventh Floor	6673			\$42,270	\$43,810	\$45,910	\$47,260	\$49,280

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EXHIBIT 24 -- Continued

Schedule of Rental Revenues¹ for the Period of April 30, 1980 Through April 29, 1985

Occupancy as of April 30, 1980	Space Sq. Ft.	Annual Rent per Sq. Ft. ²	Lease Terms as of 4/30/80 ³	Annualized Gross Rental Revenues				
				4/30/80- 4/29/81	4/30/81- 4/29/82	4/30/82- 4/29/83	4/30/83- 4/29/84	4/30/84- 4/29/85
Eighth Floor								
801 Wisconsin Radio News	150	7.00	to 6/30/80	\$ 1,050	\$ 1,050	\$ 1,130	\$ 1,130	\$ 1,220
802-5 State	1536	7.55	to 10/31/83	11,600	11,600	11,600	12,060	12,520
806-7 Dr. Mannis	470	7.50	9/1/79 - 8/31/80	3,840	4,000	4,000	4,210	4,320
808-22 State	4580	6.00	7/1/79 - 6/30/80	27,480	36,620	37,100	37,100	39,580
823-24 Dr. Boyle	339	7.60	9/1/79 - 8/31/80	2,780	2,800	3,040	3,120	3,120
Total-Eighth Floor	<u>7075</u>			<u>\$46,750</u>	<u>\$56,150</u>	<u>\$56,870</u>	<u>\$57,620</u>	<u>\$60,760</u>
Ninth Floor								
901 Millman & Robertson	150	8.00	1/1/80 - 12/31/80	\$ 1,230	\$ 1,300	\$ 1,340	\$ 1,400	\$ 1,400
902 Wisc. Ins. Alliance	864	7.00	6/1/79 - 5/31/80	6,400	6,480	6,910	7,000	7,000
903-6 Mulcahy & Wherry	980	8.00	1/1/79 - 12/31/81	8,070	8,530	8,750	9,210	9,210
907 Robert Uehling	225	8.00	4/1/80 - 3/31/81	1,810	1,960	1,980	2,110	2,110
909-10 Larry Hall	700	6.00	6/1/79 - 5/31/80	4,520	4,550	4,870	4,900	4,900
911 Dr. Schweltz	248	7.75	1/1/79 - 12/31/80	1,920	1,970	2,060	2,140	2,230
912-19 Devine Insurance	2580	7.00	4/1/80 - 3/31/83	18,060	18,060	18,180	19,350	19,350
921 State	575	7.00	vacated 7/1/80	4,020	4,350	4,350	4,700	4,700
922-23 Judicial Commission	355	6.50	5/1/79 - 4/30/81	2,300	2,500	2,500	2,700	2,700
924-25 Dr. Rundell	339	7.20	6/1/79 - 5/31/80	2,650	2,680	2,860	2,880	2,880
Total-Ninth Floor	<u>7016</u>			<u>\$50,980</u>	<u>\$52,380</u>	<u>\$53,800</u>	<u>\$56,390</u>	<u>\$56,480</u>
Tenth Floor								
1001 Victor Lind	150	6.80	11/1/79 - 10/31/80	\$ 1,050	\$ 1,200	\$ 1,250	\$ 1,300	\$ 1,350
1002 Wisc. Assoc. of Indep. Colleges	864	6.50	1/1/80 - 12/31/80	5,760	6,050	6,190	6,480	6,650
1003-4 Wisc. Cannery & Freezers	756	8.00	5/1/79 - 4/30/80	6,050	6,050	6,530	6,530	7,050
1005-8 Boelter Co.	911	6.80	12/1/79 - 11/30/80	6,370	6,650	6,880	7,200	7,400
1009-10 Vacant	455	6.50	--	2,950	3,190	3,190	3,450	3,450
1011-13 Dr. Doll	727	6.65	6/1/79 - 5/31/80	5,230	5,270	5,640	5,670	6,100
1014 Vacant	229	6.25	--	1,430	1,430	1,540	1,540	1,670
1015-18 State	1616	7.50	11/1/79 - 10/31/83	12,120	12,120	12,120	12,600	13,090
1019-21 Vacant	680	6.70	vacated 2/29/80	5,380	5,440	5,870	5,910	6,350
1022 Herb Walsh	171	8.00	12/1/79 - 11/30/80	1,420	1,490	1,490	1,540	1,600
1023-24 Dane Co. Advocate for Battered Women	331	7.20	8/1/79 - 7/31/80	2,610	2,680	2,840	2,900	3,070
Total-Tenth Floor	<u>6890</u>			<u>\$50,370</u>	<u>\$51,570</u>	<u>\$53,540</u>	<u>\$55,120</u>	<u>\$57,780</u>
Annual Totals for	74,054 sq. ft.			<u>\$493,960</u>	<u>\$522,120</u>	<u>\$537,260</u>	<u>\$565,460</u>	<u>\$586,210</u>

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EXHIBIT 24 - Continued

Notes to Schedule of Rental Revenues for the
Period of April 30, 1980 Through April 29, 1985

¹The annualized gross rental revenue for the period from April 30, 1980 through April 29, 1981 is consistent with the actual lease terms, if at market rents, as of April 30, 1980. Increases in rents are assumed to take place according to lease terms and conditions; an increase of 8 percent is used at lease renewal dates. This factor was taken from a survey of office rent increases in Class B buildings on and near the Capitol Square in Madison and is the current rate used by the Tenney Building manager.

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²The annual rental market rate is given as of April 30, 1980. Only one tenant in Rooms 909-10 is considered to be below market rent at \$4.73/square foot; therefore the rent for this space is calculated at a market rate of \$6.00/square foot. Market rents are also imputed to spaces used by the building owner.

³Of the 87 rental space units in the Tenney Building as of April 30, 1980, there are 62 leases in place, but 54 of those terminate between 1980 and 1982. Only eight have leases that extend beyond April 30, 1982.

⁴The Leaf and Ladle Restaurant began its lease of 3500 sq. ft. of the first floor retail space on January 1, 1980. The restaurant had closed its door by October 1, 1980, and the remodeled space is once again on the market. The rental rate of \$9.00 with an annual escalator of 8% per year commencing in the second year is considered comparable for the area. A most probable investor might consider an escalator based upon a percentage of gross sales to encourage rental of this space if restaurant use is most likely; the projected revenues probably would not increase as rapidly as forecast.

⁵The state has given notice that it will vacate these spaces by June 30, 1980.

Schedule of Vacancies by Floor and by Lease Terms for
the Period of April 30, 1980 Through April 29, 1985

	Space Sq. Ft. ²	% Vacant	Annual Rental Rate Per. Sq. Ft.	# of Months Vacant	Projection Period				
					4/30/80- 4/29/81	4/30/81- 4/29/82	4/30/82- 4/29/83	4/30/83- 4/29/84	4/30/84- 4/29/85
<u>Lower Level & Roof</u> ¹									
B Level - Vault	700	100	3.00	12	\$ 2,100				
	700	100	3.00	12		\$ 2,100			
	700	100	3.25	12			\$ 2,270		
	700	50	3.25	6				\$ 1,140	
	700	50	3.50	6					\$ 1,140
<u>B Level</u>									
Showroom and Office	4,000	100	3.00	12	12,000				
	4,000	100	3.00	6		6,000			
	4,000	50	3.25	6			3,250		
	4,000	50	3.25	6				3,250	
	4,000	50	3.50	3					1,750
A Level - Storage	400	100	7.00	6				1,400	
	400	100	7.50	9					2,250
Total - Lower Level					\$14,100	\$ 8,100	\$ 5,520	\$ 5,790	\$ 5,140
<u>First Floor</u>									
112 East Main	454	100	5.20	8		\$ 1,570			
	454	100	5.20	12			\$ 2,360		
	454	100	5.20	4				\$ 780	
114 East Main	1,000	100	5.20	8		3,480			
	1,000	50	5.20	12			2,600		
	1,000	50	5.20	4				860	
Leaf & Ladle	3,500	100	9.00	7	18,370				
	3,500	100	9.50	3		8,310			
	3,500	100	10.50	3				9,190	
	3,500	100	11.30	3					\$ 9,890
North Entry	2,000	100	9.00	9	13,500				
Total - First Floor					\$31,870	\$13,360	\$ 4,960	\$10,830	\$ 9,890

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EXHIBIT 25

Schedule of Vacancies by Floor and by Lease Terms for
the Period of April 30, 1980 Through April 29, 1985

	Space Sq. Ft. ²	% Vacant	Annual Rental Rate Per Sq. Ft.	# of Months Vacant	Projection Period				
					4/30/80- 4/29/81	4/30/81- 4/29/82	4/30/82- 4/29/83	4/30/83- 4/29/84	4/30/84- 4/29/85
<u>Second Floor</u> ³									
201	150	100	6.50	12	\$ 900				
	150	100	6.50	12		\$ 900			
	150	100	7.00	12			\$ 1,050		
	150	100	7.00	12				\$ 1,050	
	150	100	7.60	12					\$ 1,140
202	600	100	6.70	6	2,010				
	600	50	7.20	12		2,160			
	600	50	7.20	12			2,160		
	600	50	7.80	6				1,170	
	600	50	7.80	3					580
203-4	543	100	6.20	12	3,370				
	543	50	6.70	12		1,820			
	543	50	6.70	12			1,820		
	543	50	6.70	9				1,360	
205-6	506	100	7.00	6	1,770				
	506	50	7.50	12		1,900			
	506	50	7.50	12			1,900		
	506	50	8.15	9				1,550	
	506	50	8.15	6					1,030
209-10	451	100	6.25	6	1,410				
	451	50	6.75	12		1,520			
	451	50	6.75	12			1,520		
	451	50	7.30	9				1,230	
215	415	100	6.75	12	2,800				
	415	100	7.30	6		1,510			
	415	100	7.30	3			760		
218-19	816	100	8.00	8				4,370	
	816	100	8.20	12					6,690
220-21	1,400	100	6.25	6	4,370				
	1,400	50	6.75	12		4,720			
	1,400	50	6.75	6			2,360		
	1,400	50	7.30	6				2,560	
Total - Second Floor					\$16,630	\$14,530	\$11,570	\$13,290	\$ 9,440

EXHIBIT 25 -- Continued

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Schedule of Vacancies by Floor and by Lease Terms for
the Period of April 30, 1980 Through April 29, 1985

	Space Sq. Ft. ²	% Vacant	Annual Rental Rate Per Sq. Ft.	# of Months Vacant	Projection Period				
					4/30/80- 4/29/81	4/30/81- 4/29/82	4/30/82- 4/29/83	4/30/83- 4/29/84	4/30/84- 4/29/85
<u>Third Floor³</u>									
301	150	100	5.75	12	\$ 860				
	150	100	5.75	12		\$ 860			
	150	100	6.20	12			\$ 930		
	150	100	6.20	12				\$ 930	\$ 1,000
	150	100	6.70	12					
302-3	1,179	100	5.75	6	3,390				
	1,179	50	6.20	12		3,650			
	1,179	50	6.20	12			3,650		
	1,179	50	6.70	6				3,950	
304	230	100	6.70	6	770				
	230	100	7.20	12		1,660			900
	230	100	7.80	6					
305-8	942	100	6.70	6	3,150				
	942	50	7.20	12		3,390			
	942	50	7.20	12			3,390		
	942	50	7.80	3					1,830
310-11	456	100	6.70	6	1,530				
	456	50	7.20	12		1,640			
	456	50	7.20	12			1,640		
312	234	100	5.75	12	1,340				
	234	100	6.20	12		1,450			
	234	100	6.20	12			1,450		
	234	100	6.70	12				1,570	
	234	100	6.70	12					1,570
315	731	100	6.70	4	1,610				
320-24	1,363	100	7.00	12	9,540				
	1,363	100	7.60	6		5,150			
Total - Third Floor					\$22,190	\$17,800	\$11,060	\$ 6,450	\$ 5,300

EXHIBIT 25 -- Continued

Schedule of Vacancies by Floor and by Lease Terms for
the Period of April 30, 1980 Through April 29, 1985

	Space Sq. Ft. ²	% Vacant	Annual Rental Rate Per Sq. Ft.	# of Months Vacant	Projection Period					
					4/30/80- 4/29/81	4/30/81- 4/29/82	4/30/82- 4/29/83	4/30/83- 4/29/84	4/30/84- 4/29/85	
<u>Fourth Floor</u>										
401	150	100	6.40	12	\$ 960					
	150	100	6.40	12		\$ 960				
	150	100	6.90	12			\$ 1,040			
	150	100	6.90	12				\$ 1,040		
	150	100	7.45	12					\$ 1,120	
412	202	100	6.40	12	1,290					
	202	100	6.40	12		1,290				
	202	100	6.90	12			1,400			
	202	100	6.90	12				1,400		
	202	100	7.40	12					1,500	
416-19	1,370	100	6.00	6	4,110					
	1,370	50	6.50	12		4,450				
	1,370	50	6.50	12			4,450			
	1,370	50	7.00	12				4,800		
	1,370	50	7.00	6					2,400	
420-20a	560	100	6.70	6	1,880					
	560	50	6.70	12		1,870				
	560	50	7.20	9			1,520			
Total - Fourth Floor					\$ 8,240	\$ 8,570	\$ 8,410	\$ 7,240	\$ 5,020	
<u>Fifth Floor</u>										
502	842	100	7.50	12	\$ 6,310					
	842	50	8.00	12		\$ 3,410				
	842	50	8.00	12			\$ 3,410			
	842	50	8.75	6				\$ 3,410		
520	555	100	7.70	6			2,130			
	555	50	7.80	12				2,160		
	555	50	8.90	9					\$ 1,850	
Total - Fifth Floor					\$ 6,310	\$ 3,410	\$ 5,540	\$ 5,570	\$ 1,850	

EXHIBIT 25 -- Continued

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Schedule of Vacancies by Floor and by Lease Terms for
the Period of April 30, 1980 Through April 29, 1985

	Space Sq. Ft. ²	% Vacant	Annual Rental Rate Per Sq. Ft.	# of Months Vacant	Projection Period				
					4/30/80- 4/29/81	4/30/81- 4/29/82	4/30/82- 4/29/83	4/30/83- 4/29/84	4/30/84- 4/29/85
<u>Sixth Floor</u>									
601	150	100	6.70	12	\$ 1,000				
	150	100	6.70	12		\$ 1,000			
	150	100	7.20	9			\$ 810		
602-4	1,473	100	6.00	6	4,420				
	1,473	50	6.50	12		4,770			
	1,473	50	6.50	12			4,770		
	1,473	50	7.00	9				\$ 3,870	
	1,473	50	7.00	6					\$ 2,580
605	204	100	6.40	12	1,300				
	204	100	6.40	12		1,300			
	204	100	6.90	12			1,410		
	204	100	6.90	9				1,060	
617	250	100	7.75	4	640				
620-24	1,262	100	6.70	12	8,450				
	1,262	100	7.20	6		4,540			
	1,262	100	7.20	6			4,540		
	1,262	50	7.80	9				3,690	
Total - Sixth Floor					\$15,810	\$11,610	\$11,530	\$ 8,620	\$ 2,580
<u>Seventh Floor</u>									
No Vacancies Projected									
<u>Eighth Floor</u>									
801	150	100	7.00	10	\$ 880				
	150	100	7.00	12		\$ 1,050			
	150	100	7.50	6			\$ 560		
Total - Eighth Floor					\$ 880	\$ 1,050	\$ 560	0	0

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EXHIBIT 25 -- Continued

Schedule of Vacancies by Floor and by Lease Terms for
the Period of April 30, 1980 Through April 29, 1985

	Space Sq. Ft. ²	% Vacant	Annual Rental Rate Per Sq. Ft.	# of Months Vacant	Projection Period				
					4/30/80- 4/29/81	4/30/81- 4/29/82	4/30/82- 4/29/83	4/30/83- 4/29/84	4/30/84- 4/29/85
<u>Ninth Floor</u>									
909-10	700	100	6.50	6		\$ 2,280			
	700	100	7.00	6			\$ 2,440		
922-23	355	100	7.00	12			2,500		
	355	100	7.60	6				\$ 1,350	
Total - Ninth Floor					0	\$ 2,280	\$ 4,940	\$ 1,350	0
<u>Tenth Floor</u>									
1009-10	455	100	6.50	12	\$ 2,950				
	455	100	7.00	12		\$ 3,190			
	455	100	7.00	9			\$ 2,390		
1014	229	100	6.25	12	1,430				
	229	100	6.25	12		1,430			
	229	100	6.70	6				770	
1019-20	680	100	6.70	1	380				
Total - Tenth Floor					\$ 4,760	\$ 4,620	\$ 2,390	\$ 770	0
TENNEY BUILDING TOTALS ⁴					\$120,790	\$85,330	\$66,480	\$59,910	\$39,220

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EXHIBIT 25 -- Continued

Notes to Schedule of Vacancies by Floor and by Lease Terms
For the Period of April 30, 1980 Through April 29, 1985

- ¹The lower level space has a continued record of vacancy; it is assumed that until the space is made more marketable by remodeling, rents will not keep pace with the market. Uses other than a showroom for the 4000 sq. ft. will need to be explored; subdividing the larger space for office space and/or storage space are possibilities.
- ²It is assumed that the smaller office spaces from 200-500 square feet will experience less overall vacancy than the larger spaces. There appears to be a trend toward several small independent businessmen sharing a common secretarial staff; some of the larger vacant suites could be remodeled for this type of use.
- ³The second and third floors have the greatest amount of vacancy due to the exodus of State tenants. By the end of June, 1980, the State's move alone will cause 44% of the second floor vacancies; the third floor will experience a vacancy rate of 39.5% due to loss of State tenants; the State related vacancy rates on the fourth and sixth floors will be 29% and 21% respectively. A most probable buyer will have to anticipate a large capital investment in 1980 to remodel and refurbish the Building to make it competitive in the Class B office market that already has a large supply of space available on and near the Square.
- ⁴Vacancies are assumed to gradually decrease between 1981 and 1983; a most probable buyer will institute a vigorous marketing program which will involve research of space needs in the area and remodeling which will be targeted to those needs.

Schedule of Projected Revenues and Expenses From
April 30, 1980 Through April 29, 1985

<u>Revenues:</u>	<u>4/30/80- 4/29/81</u>	<u>4/30/81- 4/29/82</u>	<u>4/30/82- 4/29/83</u>	<u>4/30/83- 4/29/84</u>	<u>4/30/84- 4/29/85</u>
Gross Income	\$493,960	\$522,120	\$537,260	\$565,460	\$586,210
Less: Vacancies	<u>(120,790) (24.5%)</u>	<u>(85,330) (16.3%)</u>	<u>(66,480) (12.4%)</u>	<u>(59,910) (10.6%)</u>	<u>(39,220) (6.7%)</u>
Effective Gross	373,170	436,790	470,780	505,550	546,990
Parking Rentals	<u>12,960</u>	<u>12,960</u>	<u>12,960</u>	<u>14,000</u>	<u>14,000</u>
 Total Revenues	 \$386,130	 \$449,750	 \$483,740	 \$519,550	 \$560,990
 <u>Expenses:</u> ¹					
Accounting & Legal	4,200	4,640	5,120	5,650	6,240
Building Security ²	21,840	24,100	26,620	29,390	32,440
Insurance	7,000	7,730	8,530	9,420	10,400
Maintenance ³	28,850	31,850	35,160	38,820	42,860
Wage & Salaries	60,000	66,240	73,130	80,730	89,130
Payroll Taxes	11,500	12,700	14,020	15,470	17,080
Repairs	14,880	16,430	18,130	20,020	22,100
Telephone ⁴	1,600	1,770	1,950	2,150	2,380
Utilities ⁴	90,600	101,470	107,560	114,380	122,020
Office Expenses ⁵	7,040	7,520	8,250	8,840	9,690
Management ⁶	22,390	26,320	27,540	30,280	32,570
Concourse Special Assessment	<u>2,360</u>	<u>2,410</u>	<u>2,630</u>	<u>2,550</u>	<u>2,480</u>
 Total Operating Expenses Before R.E. Taxes ⁷	 <u>(\$272,260)</u>	 <u>(\$303,180)</u>	 <u>(\$328,640)</u>	 <u>(\$357,700)</u>	 <u>(\$389,390)</u>
 Net Operating Income Before R.E. Taxes	 \$113,870	 \$146,570	 \$155,100	 \$161,850	 \$171,600
 Real Estate Taxes ⁸	 <u>(26,680)</u>	 <u>(28,000)</u>	 <u>(29,400)</u>	 <u>(30,880)</u>	 <u>(32,420)</u>
 Net Operating Income	 \$ 87,190	 \$118,570	 \$125,700	 \$130,970	 \$139,180

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EXHIBIT 27

Notes to Schedule of Projected Revenues and Expenses
From April 30, 1980 Through April 29, 1985

¹Expenses

In general, expenses are projected to increase according to the average annual change of 10.4% in the All Item Consumer Price Index over the past five years. (See amended Exhibit 27).

²Building Security

Security personnel is hired from 10 P.M. to 6 A.M. on weekdays with 24 hour coverage on the weekends. The building is open to the public from 6 A.M. to 6 P.M. each weekday. The continuing problems created by the presence of bars and adult entertainment places across the street make this security protection mandatory.

³Maintenance

This account includes an elevator maintenance contract at \$9,060 a year.

⁴Utilities

At present the Tenney Building consumes approximately 55,000 to 70,000 gallons of No. 2 fuel oil per year depending upon the weather. The cost of fuel has increased as follows:

January 12, 1979	.43/gallon
October 1, 1979	.77/gallon
February 1, 1980	.95/gallon

In thirteen months the cost has risen 121%. Though the Tenney Building is converting to natural gas on its primary boiler, the cost of natural gas is also volatile. Over the past five years natural gas has had an average annual increase of 17.6% for the commercial time-of-use consumer, according to Milton Spiros, Madison Gas & Electric Co.

The installation of combination storm windows throughout the building should help to conserve fuel costs. To stabilize utility costs it is assumed management will place energy cost escalators in renewed leases; therefore in the pro forma income statement utility costs are escalated at 12 percent annually with 50 percent of the increase passed through to the tenant after year 2.

⁵Office expenses include rental of space in the Tenney Building for management operations.

⁶Management costs are computed as 6% of effective gross office revenue with 4% allowed for management and 2% for leasing commissions for space turnover.

Notes to Schedule of Projected Revenues and Expenses
From April 30, 1980 Through April 29, 1985

7 Total operating expenses are calculated before including real estate taxes for ease in using the MRCAP discounted cash flow program.

8 Real estate taxes are calculated as 5.4% of gross revenues in the first year and increased at 5% per annum thereafter. These calculations are based on the following fact and assumptions:

1. The assessed value as of 1/1/80 is \$1,200,000.
2. The mill rate is assumed to increase slightly (approximately 1%) after several years of decrease.
3. Taxes will continue to increase due to inflated city budgets and decreasing state aids.

4. Conversion of Net Income to Present Value

The MRCAP program from the National EDUCARE library of programs, previously described, is used to convert net income to a present value after taxes as of April 30, 1980, for the Tenney Building at the end of a five-year holding period.

C. Assumptions Used in MRCAP

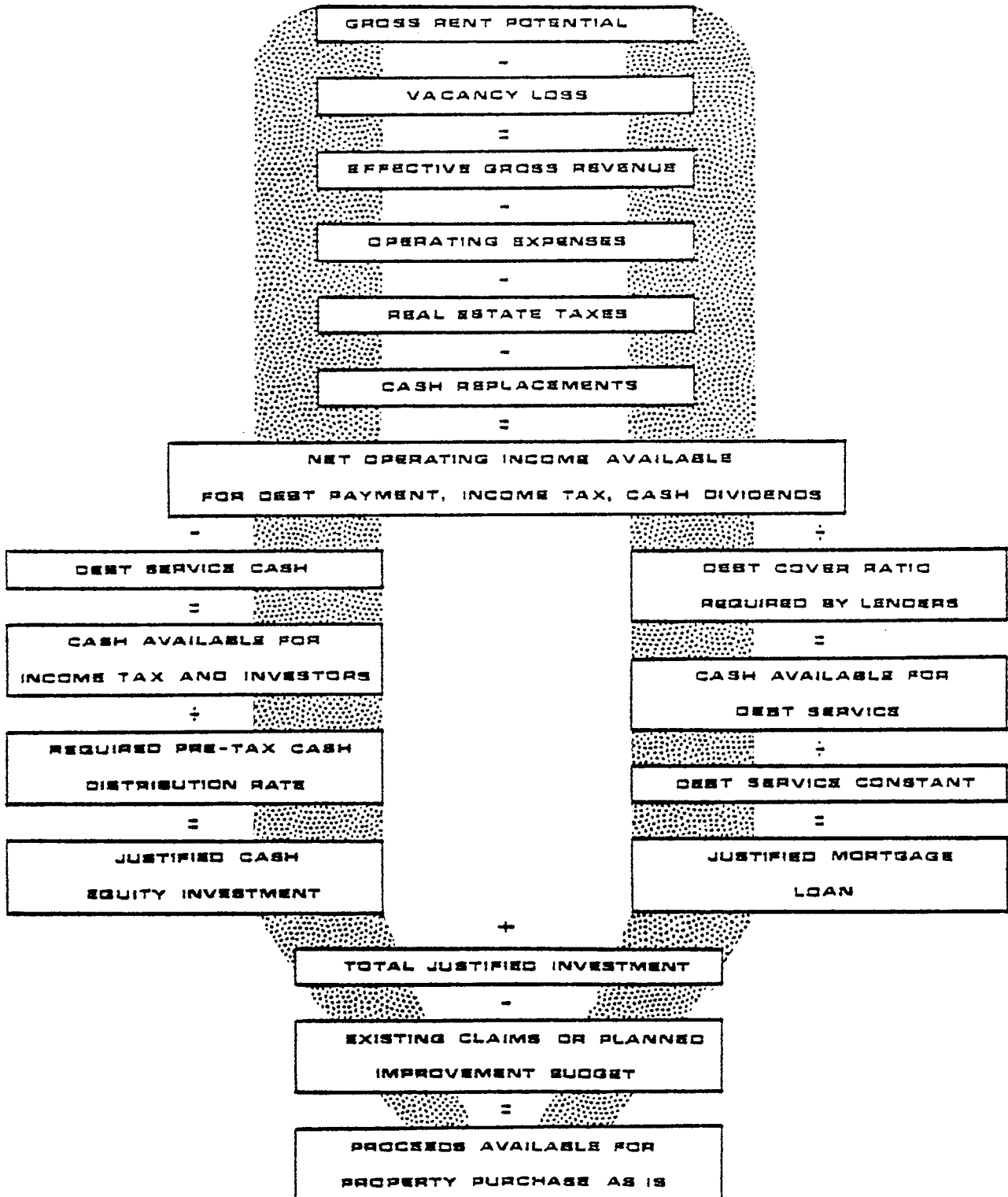
The MRCAP discounted cash flow program can solve for a justified project value by specifying the ratio of net income to debt service acceptable to an institutional mortgage lender. Given the interest rate and term available as of April 30, 1980, the program will solve for the justified amount of mortgage and for justified cash equity, assuming typical before-tax cash-on-cash investor requirements for office buildings, with potential for inflation sensitive rents. Exhibit 28 is a simplified flow chart depicting the steps in solving for the justified project budget.

On April 30, 1980, prudent lenders will require a minimum debt cover ratio of 1.3 and equity investors expect no less than 6 percent cash-on-cash.

1. Inputs into MRCAP Program

- a. Debt cover ratio = 1.3
- b. Before tax cash-on-cash requirements = 6%
- c. Project holding period = 5 years

REVENUE JUSTIFIED CAPITAL BUDGET
DEBT COVER RATIO APPROACH



- d. Real estate taxes = historical pattern suggests real estate taxes at 5.4 percent of first year's gross with an annual inflation factor of 5% (see assumptions discussed below)
- e. Discount rate = 13% (present value factor used to discount cash flow)
- f. Reinvestment rate = 6% after tax rate applied to after tax cash flow
- g. Resale price = 10 times net operating income in year of sale
- h. Resale cost rate = 4%
- i. Working capital reserves from equity to cover one month's expenses = \$30,000
- j. Investor marginal income tax rate = 50%
- k. Land = \$340,000, as of most recent appraisal for IRS
- l. Buildings = 60% of total improvement value
- m. Mechanicals and site improvements = 40% of total improvement value
- n. Elevators = remaining book value of \$73,000
- o. Improvements for Energy Conservation = a total of \$54,000 which includes \$43,000 for storm windows and \$11,000 for natural gas conversion unit.
- p. Tenant Improvements = \$50,000 for carpeting and partitions as needed to upgrade vacant office space
- q. Investment Credit Dummy = to allow for tax benefit of investment credit in first year for capital improvement for energy conservation
- r. Mortgage = principal amount determined by debt cover ratio; interest rate a minimum of 12% with a 20-year term, paid monthly, on the first mortgage and 13% interest and an 8-year term for the second mortgage

2. Real Estate Tax Assumptions

Real estate taxes are a function of assessed value (or fair market value when assessed value is 100 percent of market value) and the net mill rate; therefore, real estate taxes are estimated as a function of gross rental income. During the past two years, real estate taxes have been between 5 percent and 6 percent of the Building's potential gross rental income. As a result of tests of several values between 5 percent and 6 percent, it is determined that 5.4 percent of gross rental revenues best represents the historical pattern of the Building's real estate taxes. MRCAP is programmed to use 5.4 percent of the first year's gross rental income to compute the first year's real estate taxes and then provides for a growth factor of 5 percent to increase the taxes each year thereafter.

D. Analysis of Test Results

Four runs of the MRCAP program were done using different assumptions about the amount of real estate taxes that would be paid on the subject property. Taxes and net mill rates for the past three years on the subject property have been:

<u>Year</u>	<u>1977</u>	<u>1978</u>	<u>1979</u>
<u>Real Estate Taxes</u>	\$33,118.75	\$29,951.95	\$25,340.93
<u>Net Mill Rate</u>	.026495	.024153	.022036

Real estate taxes estimated at various percentages of the first year's projected gross and inflated 5 percent a year gave these results in the MRCAP runs:

Percentage of First
Year's Gross Rental
Revenue

Real Estate Taxes

	<u>1980</u>	<u>1981</u>	<u>1982</u>	<u>1983</u>	<u>1984</u>
5.0	\$24,698	\$25,933	\$27,230	\$28,591	\$30,021
5.4	\$26,674	\$28,008	\$29,408	\$30,878	\$32,422
5.8	\$28,650	\$30,082	\$31,586	\$33,166	\$34,824
6.0	\$29,638	\$31,119	\$32,675	\$34,309	\$36,025

The real estate taxes estimated at 5.4 percent of the first year's gross rent best approximates the shift from a decreasing to an increasing net mill rate that can now be expected due to an anticipated decrease in state aids to cities. Rising costs of local government can be expected to be borne by the local taxpayer.

The input and output for the MRCAP program using real estate taxes estimated at 5.4 percent of gross rental revenue are found in Exhibit 29.

If taxes are a conservative 5.4 percent of gross rental revenue, MRCAP substantiates the fair market value of \$1,150,000 estimated by the market comparison approach to value.

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EXHIBIT 29

MRCAP INPUT AND OUTPUT--
JUSTIFIED CAPITAL BUDGET WITH
REAL ESTATE TAXES AT 5.4% OF
FIRST YEAR'S GROSS RENT

MRCAP 09:49CST 12/20/80

ENTER INPUT FILE NAME?TENNEY

THE PROGRAM MRCAP IS THE PROPERTY OF
MICHAEL L. ROBBINS
C/O REAL ESTATE DYNAMICS INC.
4701 WINNEQUAH RD.
MONONA, WISC.

USER NO. 36

(608)-221-1120

NO REPRESENTATION IS MADE THAT THE ASSUMPTIONS OR
COMPUTATIONAL FORMAT USED IN THIS PROJECTION WILL
BE ACCEPTABLE TO TAXING AUTHORITIES.

*\$10.00 LIB CHG APPLIED

R E P O R T S E C T I O N N U M B E R 1 PAGE 1
=====

* GROSS RENT	\$ 554378.	* RATE OF GROWTH OF GROSS RENT	0.0432
* EXPENSES	\$ 330234.	* RATE OF GROWTH OF EXPENSES	0.0936
* R E TAXES	\$ 29478.	* RATE OF GROWTH OF R E TAXES	0.0500
INCOME TAX RATE	0.5000	PROJECT VALUE GROWTH OF	2.0000
* VACANCY RATE	0.1375	WORKING CAPITAL LOAN RATE	0.1400
EQUITY DISCOUNT	0.1300	EXTRAORDINARY EXPENSES	\$ 0.
RESALE COST	0.0400	REINVESTMENT RATE	0.0600
UKG CAPITAL RS	\$ 30000.	CAPITAL RESER INTEREST RATE	0.
INITIAL COST	\$ 1091502.	INITIAL EQUITY REQUIRED	\$ 486009.

ALL (*) VALUES ARE AVERAGE AMOUNTS FOR HOLDING PERIOD. OF 5 YRS.

INITIAL COST DERIVED THROUGH BACKDOOR TYPE 3 USING 2 MORTGAGES

EXHIBIT 29 -- Continued

PRO FORMA
 INVESTMENT ANALYSIS OF
 BUILDING
 FOR

REPORT SECTION NUMBER 2

PAGE 1

=====

COMPONENT SUMMARY

TITLE	PCT. DEPR	BEGIN USE	USEFUL LIFE	DEPR METHOD	COST	SCH
LAND	0.	1	25.	0	\$ 340000.	0
BUILDING	0.80	1	29.	2	\$ 358221.	0
HVAC	0.90	1	9.	2	\$ 225481.	0
ELEVATORS	0.90	1	4.	2	\$ 73000.	0
ENERGY CONSERVATION	0.90	1	5.	2	\$ 54000.	0
TENANT IMPROVEMENTS	0.90	1	10.	4	\$ 50000.	0
INVESTMENT CREDIT DU	1.00	1	1.	2	\$ 10800.	0

MORTGAGE SUMMARY

TITLE	INTR RATE	BEGIN YR.	END YR.	TERM	ORIG BALC	PCT VALUE
FIRST MORTGAGE	0.1200	1	20	20	\$ 531493.	0.487
SECOND MORTGAGE	0.1300	1	9	8	\$ 104000.	0.095

P R O F O R M A
 INVESTMENT ANALYSIS OF
 BUILDING
 FOR

REPORT SECTION NUMBER 3

PAGE 1

CASH FLOW ANALYSIS

	1980	1981	1982	1983	1984
1 GROSS INCOME	506920.	555080.	550220.	572460.	600210.
2 LESS VACANCY	120790.	85330.	66480.	54910.	69320.
3 LESS REAL ESTATE TAXES	26674.	28008.	29408.	30678.	32422.
4 LESS EXPENSES	272260.	303180.	328640.	357700.	389390.
5 NET INCOME	87196.	118562.	125692.	130972.	139178.
6 LESS DEPRECIATION	76323.	64398.	63442.	62629.	45513.
7 LESS INTEREST	76472.	74515.	72298.	69785.	66938.
8 TAXABLE INCOME	-63599.	-20351.	-10048.	-1443.	26726.
9 PLUS DEPRECIATION	76323.	64398.	63442.	62629.	45513.
10 LESS PRINCIPAL PAYMENTS	14730.	16687.	18904.	21417.	24263.
11 CASH THROW-OFF	-4006.	27361.	34490.	39770.	47976.
12 LESS TAXES	0.	0.	0.	0.	13363.
13 LESS RESERVES	0.	0.	0.	0.	0.
14 CASH FROM OPERATIONS	0.	27361.	34490.	39770.	34613.
15 WORKING CAPITAL LOAN	0.	0.	0.	0.	0.
16 DISTRIBUTABLE CASH AFR TAX	0.	27361.	34490.	39770.	34613.
17 TAX SAVING ON OTHER INCOME	32799.	10175.	5024.	721.	0.
18 SPENDABLE CASH AFTER TAX	32799.	37536.	39514.	40491.	34613.

EXHIBIT 29 -- Continued

MARKET VALUE & REVERSION
=====

CASH FLOW ANALYSIS

=====	1980	1981	1982	1983	1984
19 END OF YEAR MARKET VALUE	871962.	1185625.	1256921.	1309717.	1391778.
20 LESS RESALE COST	34679.	47425.	50277.	52389.	55671.
21 LESS LOAN BALANCES	620764.	604077.	585173.	563750.	539493.
22 PLUS CUM. CASH RESERVES	25994.	25994.	25994.	25994.	25994.
23 BEFORE TAX NET WORTH	242314.	560117.	647460.	719500.	822608.
24 CAPITAL GAIN (IF SOLD)	-181096.	182544.	313511.	426719.	551596.
25 CAPITAL GAINS TAX	-36219.	36509.	62702.	85344.	110319.
26 MINIMUM PREF. TAX	0.	0.	0.	0.	0.
27 INCOME TAX ON EXCESS DEP.	1500.	2438.	2897.	2950.	2657.
28 TOTAL TAX ON SALE	-16610.	38946.	65599.	88294.	112977.
29 AFTER TAX NET WORTH	258924.	521171.	581867.	631273.	709632.

BEFORE TAX RATIO ANALYSIS
=====

CASH FLOW ANALYSIS

=====	1980	1981	1982	1983	1984
30 RETURN ON NET WORTH B/4 TAX	-0.5014	1.4245	0.2175	0.1728	0.2099
31 CHANGE IN NET WORTH B/4 TAX	-243696.	317803.	87349.	72100.	103042.
32 ORIG EQUITY CASH RTNB/4 TAX	-0.0082	0.0563	0.0710	0.0618	0.0987
33 ORIG EQUITY PAYBACK B/4 TAX	0.0000	0.0563	0.1273	0.2091	0.2803
34 B/4 TAX PRESENT VALUE	846386.	1092030.	1126006.	1142995.	1174189.

AFTER TAX RATIO ANALYSIS
=====

CASH FLOW ANALYSIS

=====	1980	1981	1982	1983	1984
35 RETURN ON NET WORTH AFR TAX	-0.3998	1.1578	0.1923	0.1545	0.1790
36 CHANGE IN NET WORTH AFR TAX	-227086.	262248.	60696.	49405.	78359.
37 ORIG EQUITY CASH RTNAFR TAX	0.0675	0.0772	0.0813	0.0833	0.0712
38 ORIG EQUITY PAYBACK AFR TAX	0.0675	0.1447	0.2260	0.3293	0.3806
39 AFTER TAX PRESENT VALUE	893655.	1102039.	1124564.	1133367.	<u>1150092.</u>

CASH FLOW ANALYSIS

=====	1980	1981	1982	1983	1984
40 NET INCOME-MARKET VALUE RTO	0.1000	0.1000	0.1000	0.1000	0.1000
41 LENDER BONUS INTEREST RATE	0.0000	0.0000	0.0000	0.0000	0.0000
42 DEFAULT RATIO	0.7896	0.7894	0.8165	0.8260	0.8547

EXHIBIT 29 -- Continued

INPUT FILE

09:48CST 12/20/80

110 1. BUILDING. DAVIS
 120 10.1980.0.1.1.0.5.74000
 130 20.3.2.1.3.06.2.2
 140 40.493960.522120.537260.565460.586210
 150 50.12960.12960.12960.14000.14000
 160 60.120790.85330.66480.59910.39220
 170 70.054.05.*
 180 80.272260.303180.328640.357700.389390
 190 100.13.50.00
 200 101.0.10.2
 210 102.14.1.04.0
 220 103.0.30000.0.0
 230 200.1.1LAND
 240 201.1.340000.0.0
 250 202.1.1.25.0
 260 200.2.BUILDING
 270 201.2.60.80.2
 280 202.2.1.29.0
 290 200.3.HVAC
 300 201.3.40.90.2
 310 202.3.1.9.0
 320 200.4.ELEVATORS
 330 201.4.73000.90.2
 340 202.4.1.4.0
 350 200.5.ENERGY CONSERVATION
 360 201.5.54000.90.2
 370 202.5.1.5.0
 380 200.6.TENANT IMPROVEMENTS
 390 201.6.50000.90.4
 400 202.6.1.10.0
 410 200.7.INVESTMENT CREDIT DUMMY
 420 201.7.10800.1.0.2
 430 202.7.1.1.0
 440 300.1.FIRST MORTGAGE
 450 301.1.1.0.12.0.20
 460 302.1.12.1.20.0
 470 303.1.0.0.0.0
 480 300.2.SECOND MORTGAGE
 490 301.2.104000.13.0.8
 500 302.2.12.1.8.0
 510 303.2.0.0.0.0
 520 400.9
 530 403.99.1.2.3.4.5
 540 999.99

IV. Aside from the problem of defining and allocating income and reversion to the real estate interest, income property appraisal is at C. with the problem of cash equivalency adjustments for both comparable sales and the subject property. Many of the issues on how to appraise properties with economic development loans, state-subsidized housing loans, or seller financed property relate to when and how cash equivalency rules should be applied.

A. Fair market value seems to call for cash to the seller (Exhibit 3) but then provides an exception where market practice may be different. The Institute textbook says,

"Unusual financing or other factors that might result in a price deviation from market value are also excluded. However, if the availability of other than conventional financing (such as FHA or VA loan terms) is sufficiently extensive to constitute a market within which the property being appraised is expected to sell, the typical purchaser may be expected to take advantage of this available financing, and the market value of the property reflects the probable sale price in this market. In market valuation assignments the appraiser first identifies the market in which the property being appraised will be exposed and sold. The market value of the property is then identified within parameters that reflect conditions in this market." Source: The Appraisal of Real Estate, Seventh Edition.

B. In addition to market characteristics, we need to know the purpose of the appraisal before determining where their fair market value based on fee simple title or most probable price or going concern value is appropriate.

1. For example, the assessor is required by law to look at fee simple title; he does not recognize contract rents when they are below market rent nor can he look at premium rents and going concern values over and above market or economic rents. Cash equivalency is a must.

2. However, in a Section 8 loan from a state housing authority, it is typical to take an assignment of the general partnership position which can be exercised by the Housing Authority in the event of default on the mortgage terms or the related property management agreement. Control of the property can pass through subsequent assignment without disturbing the tax position or the special non-market interest rate of the deal. Moreover, the rights transferred include existing reserve funds. Therefore, fair market value is not relevant relative to the security of the loan. The investor purchases a fee simple title encumbered by transfers of owner prerogatives to the government in exchange for tax privileges and minimum income guarantees for 20-40 years. That is the question of most probable price or going concern value.

Exhibit 30

MC CLOUD B. HODGES, JR.
REAL ESTATE INVESTMENT, VALUATION AND COUNSELING
410 PINE STREET, SUITE 203
VIENNA, VIRGINIA 22180 703 - 281-5668

October 9, 1980

MEMORANDUM FOR several interested RE appraisers/counselors,
trial attorneys and academicians

Enclosed is an expanded and revised list of OARs and assessment/sales ratios which are self explanatory. This list is not a pure (random) sample by statistical rules. On one hand it is much larger than a sample need be, as it covers nearly 70% of all known property sales for the areas described, in the price range above about one-half million dollars, excluding MF apartment properties sold for condo conversion. On the other hand, it is possible that the 30% of investors-purchasers who, thus far, have not cooperated in furnishing data for this survey, may have shown slightly lower average OARs and A/S ratios.

This study, consuming several hundred man-hours in visits to offices of investors and inspections of their properties, was initiated more than two years ago primarily to obtain market data for rebutting several ad valorem tax valuations of properties owned by my clients. But it is now evident, from the specific results of the study and from its sheer coverage, that it ought to serve as the basis for a new educational manuscript advocating modern methods of valuing investment classed property. The "OAR" capitalization method, regardless of how the OAR is derived or constructed, is quite crude, often erroneous, and therefore useless as applied to higher priced property valuations. It was made even more useless during the last year in which many institutional sources of long term, level payment mortgage loans have withdrawn or have changed their lending practices in order to share in part of the inflation-produced cash flow through additional interest and/or future capital gain.

The second enclosure, a revised edition of "Effects of Financing on Price and Value", should explain the main reasons for the variances in OARs shown in the first enclosure: financing and tax shelter. The other reasons for OAR variances are the buyers' anticipated future changes in net income and resale/exchange values. Some properties are expected to produce large profits, or their only profits, in the distant future, while others will be nominally profitable only in the short range. This reduces the "NOI" either as a first year or a "stablized" figure to a position of invalidity in the valuation appraisal practice.

Enclosures

MCCLOUD B. HODGES, JR.
 REAL ESTATE INVESTMENT, VALUATION AND COUNSELING
 410 PINE STREET, SUITE 203
 VIENNA, VIRGINIA 22180 703 - 281-5668

Sample of investment-classed property resales in the Virginia and Maryland suburbs of Washington, D. C., showing the wide variations in the overall capitalization rate (OAR) and in the assessment/sale price ratio. For any property which was not sold for cash above new, market-rate mortgage financing, the price shown is the cash-equivalent price, being the sum of the equity cash and the balances of the mortgage loans after discounting the loans to their estimated cash liquidable values at dates of property sales.

The OAR is based upon the cash-equivalent sales price and the net operating income (NOI) produced in the first year following the date of sale. If a full year had not passed by the date of any datum sale analysis, the NOI is that which was budgeted by the new owners. The assessment/sale price ratio is based upon 100% market value assessment and the cash equivalent sales price. Supporting data for all property sales are contained in a separate, confidential listing with corresponding identification (ID) numbers.

<u>ID</u>	<u>Year of Sale</u>	<u>Kind of Property and Location</u>	<u>Cash Equiv. Price</u>	<u>OAR</u>	<u>Assmt/Sale</u>
100	1977	Garden apts., Fairfax Co.	440,000	.1298	118%
105	1980	Office Bldg., Fairfax Co.	467,074	.0856	118%
107	1978	Elevator apts., Montgomery Co.	474,389	.0942	148%
110	1978	Elevator Apts., Arlington Co.	559,800	.0857	71%
113	1978	Office Bldg., Montgomery Co.	585,126	.1324	133%
115	1977	Garden apts., Fairfax Co.	589,000	.1091	94%
120	1980	Office Bldg., Fairfax Co.	590,255	.0860	158%
125	1980	Office Bldg., Fairfax Co.	638,975	.1291	229%
130	1976	Garden Apts., Alexandria City	730,058	.1232	77%
132	1978	Office Bldg., Montgomery Co.	746,833	.0818	97%
135	1978	Garden Apts., Fairfax Co.	802,900	.1396	104%
140	1980	Garden Apts., Fairfax Co.	836,857	.0874	96%
141	1977	Garden Apts, Prince Georges Co.	850,000	.1012	87%
142	1978	Office Bld., Montgomery Co.	950,000	.0759	89%
143	1978	Elevator Apts., Prince Georges Co	994,808	.1151	101%
144	1978	Office Bldg., Montgomery Co.	1,010,865	.0868	59%
145	1980	Office Bldg., Fairfax Co.	1,120,209	.0957	112%
147	1979	Garden Apts., Prince Georges Co.	1,159,172	.1267	102%
150	1977	Office Bldg., Fairfax Co.	1,245,200	.1124	106%
155	1976	Garden Apts., Arlington Co.	1,395,000	.1019	103%

<u>ID</u>	<u>Year of Sale</u>	<u>Kind of Property and Location</u>	<u>Cash Equiv. Price</u>	<u>OAR</u>	<u>Assmt/Sale</u>
157	1977	Shopping Cntr., Montgomery Co.	1,461,500	.0879	98%
160	1976	Garden Apts., Alexandria City	1,577,300	.1065	108%
162	1980	Garden Apts., Ann Arundel Co.	1,638,000	.1416	90%
163	1979	Garden Apts., Prince Georges Co.	1,716,505	.1290	101%
164	1979	Garden Apts., Prince Georges Co.	1,732,107	.1827	144%
166	1978	Office Bldg., Arlington Co.	1,751,835	.0645	90%
168	1976	Garden Apts., Fairfax Co.	1,879,250	.1248	123%
170	1976	Garden Apts., Fairfax Co.	1,960,835	.1140	114%
175	1975	Elevator Apts., Fairfax Co.	1,984,500	.1321	156%
180	1978	Elevator Apts., Falls Church	2,000,000	.0821	91%
184*	1977	Garden Apts., Montgomery Co.	2,113,500	.1192	115%
185	1980	Shopping Center, Fairfax Co.	2,144,706	.1081	125%
190	1975	Elevator Apts., Alexandria City	2,153,606	.0831	137%
195	1978	Garden Apts., Fairfax Co.	2,324,000	.1224	106%
200	1975	Garden Apts., Fairfax Co.	2,375,000	.0950	115%
205	1977	Elevator Apts., Arlington Co.	2,400,000	.0975	66%
210	1980	Office Bldg., Fairfax Co.	2,510,492	.1290	133%
225	1978	Garden Apts., Fairfax Co.	2,569,500	.1068	85%
300	1975	Elevator Apts., Alexandria City	2,558,669	.1234	93%
301**	1979	Garden Apts., Prince Georges Co.	2,960,244	N/A	131%
303	1975	Garden Apts., Alexandria City	2,789,190	.0775	122%
304	1978	Garden Apts., Prince Georges Co.	3,090,639	Neg.	95%
305	1979	Office Bldg., Montgomery Co.	3,100,000	.1221	78%
306	1976	Garden Apts., Fairfax Co.	3,117,300	.1056	165%
307	1977	Garden Apts., Prince Georges Co.	3,125,000	.1070	102%
310	1979	Garden Apts., Alexandria City	3,214,928	.1110	110%
315	1980	Shopping Center, Fairfax Co.	3,765,341	.1093	132%
317*	1977	Garden Apts., Prince Georges Co.	4,000,000	.0810	86%
318	1978	Garden Apts., Prince Georges Co.	4,100,000	.1439	97%
319	1979	Garden Apts., Prince Georges Co.	4,128,173	.0962	98%
320	1975	Garden Apts., Fairfax Co.	4,190,700	.1359	155%
323	1977	Elevator Apts., Montgomery Co.	4,796,255	.0790	154%

* Financed under FHA 223(f) rehabilitation and refinancing program.

** Nominal price shown. No information available on terms of sale or NOI in first year of ownership.

<u>ID</u>	<u>Year of Sale</u>	<u>Kind of Property and Location</u>	<u>Cash Equiv. Price</u>	<u>OAR</u>	<u>Assmt/Sale</u>
325	1980	Garden Apts., Fairfax Co.	4,871,282	.1316	124%
328*	1978	Garden Apts., Prince Georges Co	5,426,138	.0921	116%
330	1980	Office Bldg Complex, Fairfax Co	5,529,031	.1071	110%
335	1979	Garden Apts., Alexandria City	6,296,800	.1345	113%
340	1980	Office Bldg., Fairfax Co	6,593,267	.1121	154%
344	1979	Garden Apts., Prince Georges Co	6,726,848	.1457	88%
345	1976	Garden Apts., Fairfax Co.	6,735,450	.1161	102%
352	1979	Elevator Apts., Montgomery Co.	8,189,554	Neg.	208%
354	1979	Office Building, Montgomery Co	8,850,000	.0862	120%
355	1979	Office Bldg., Arlington Co.	8,857,450	.0593	128%
360	1978	Office Bldg., Montgomery Co.	10,729,000	.1025	80%
365	1976	Elevator Apts., Fairfax Co.	12,819,124	.0936	99%
375	1978	Office Bldg., Fairfax Co.	14,957,334	.0881	89%
385	1979	Elev. & Gdn. Apts., Prince Geo.	18,866,955	.0674	72%

* Financed under FHA 223(f) rehabilitation and refinancing program.

EFFECT OF FINANCING ON PRICE AND VALUE

WHAT CAN A 4-PERSON PARTNERSHIP PAY FOR A 10-YR. OLD, GOOD QUALITY APARTMENT COMPLEX UNDER 3 DIFFERENT SETS OF FINANCING TERMS ?

FACTORS CONSTANT IN ALL 3 ANALYSES:

- NET INCOME BEFORE R.E. TAXES STARTS AT \$350,000 AND RISES ON A 4% SLOPE IN ACTUAL INFLATION \$.
- R.E. TAX RATE = .0121; ASSESSED VALUE = SALE PRICE.
- DEPRECIABLE ASSETS = 85% OF PRICE, 25 YR. LIFE, 125% S/L D.B.
- NO MAJOR CAPITAL REPLACEMENTS IN NEXT TEN YEARS.
- RESALE PRICE 10 YEARS LATER = \$3,662,000, CASH-TO-SELLERS.
- OWNERS WILL REMAIN IN 50% FED. & 5.75% STATE INCOME TAX BRACKET DURING ALL 10 YEARS OF OWNERSHIP.
- OWNERS WANT 18% EQUITY YIELD (I.R.R.) AFTER INCOME TAX.
- 1978 TAX ACT GOVERNS INCOME, GAIN & ADD-ON TAXES.

VARIABLE FACTOR: FINANCING

1ST MTGE	\$1,479,786 Asmd. @ 7½%, 17 More Yrs.	New \$1,850,000 @ 13%, 30 Yr. Amort., Ballooning 10 Yrs.	None
2ND MTGE	\$1,500,000 DPMM @ 6% Int. Only, 10 Yrs.	None	
PRICE/VALUE	\$ 3 537 073	\$ 2 527 098	\$ 1 435 046
EQUITY CASH	557 287	677 098	1 435 046
AFTER-TAX CASH FLOW IN YEAR			
1	\$ 85 460	\$ 88 738	\$ 189 003
2	86 244	92 103	193 988
3	87 085	95 555	199 054
4	87 960	99 081	204 196
5	88 849	102 664	209 411
6	89 730	106 289	214 695
7	93 655	112 136	221 295
8	97 373	117 879	227 890
9	100 857	123 503	234 488
10	912 938	1297 106	2905 060
"O.A.R."	.0869	.1264	.2318

"Overall Rate" = Year 1 Net Income After R.E. Taxes ÷ Total Sale Price/Value

10/7/80

3. Going concern value may be more relevant to an economic development loan. The public purpose of the loan subsidy is to create employment, improved physical environment, and the seeds of an economic base appropriate to redevelopment. In appraising the property for loan purposes the cash equivalency of fee simple title is not relevant if eventual delinquency on the loan gives the lender several options other than foreclosure. For example:
 - a. assignment of business ownership as collateral permits transfer and sale of the going concern to better management.
 - b. it could permit a change of use within constraints of the economic development program as a workout.
 - c. it could look to additional forms of subsidy, such as applied to Section 8 rehab money as a deep subsidy applied to rescue of a delinquent moderate 236 subsidy program.
 - d. Public purposes may create a monopoly for the facility to be appraised which provides a market price superior to fee simple title where it is not directly encumbered by long-term public priorities and commitments.
- C. If the appraisal is for loan security, then the issue is whether similar nonmarket credit terms would be available to the next buyer. VA loans are assignable; economic development loans may be transferable with a change in management; subsidized rental housing loans may be undisturbed by default because of the assignability of control via transfer of partnership interests.
1. The appraiser does not discount a purchase price of a home purchased with a shared appreciation mortgage. That is contingent interest for the lender.
 2. If a builder of condominiums buys down the loan of his customer, what are those points really worth? It depends on how long the buyer owns the property and is really an oblique form of a shared appreciation mortgage, is it not? Contingent interest for the borrower as well as the lender.
 3. Appraisers have generally overlooked cash equivalency arguments relative to the seller paying the points to buy down the loan for the buyer in VA loans. Similarly, it should be disregarded on financing through prior builders' commitments. Do you discount project unit values because he bought a FNMA commitment or hedged in the GNMA certificates market? After all, these costs are also included in the price and may be included in the resale price.
- D. What is a point really worth? Refer to Exhibit 30A.

WHAT IS A POINT REALLY WORTH?

Daniel J. O'Connell

Many real estate professionals compile lists of personal rules of thumb. Ideally these rules of thumb serve to reduce effort and raise productivity in daily decision making—with minimal sacrifice in accuracy and quality.

One rule-of-thumb that seems to have made a lasting impression is that the payment of one loan point¹ should equate to an 1/4 percent reduction in the loan interest rate. For example, a borrower choosing between a 12-3/4 percent loan with 2 points from ABC Mortgage Company and a 13 percent loan without points from the XYZ Mortgage Company would be indifferent as to the choice.² According to the rule-of-thumb, the two-point charge supposedly equates to the 1/4 percent (1/4 percent per point) difference in interest rates. However, that may not be a valid rule, as can be seen when comparing the points and no-points alternatives.

A purchaser buys a house to be financed with a \$100,000, 30-year loan. Financing is available from ABC Mortgage at 12-3/4 percent plus 2 points (\$2,000), and is also available from XYZ Mortgage at 13 percent with no points. This is illustrated in Table 1.

Assume the borrower plans to hold the property for a period of only two years at which point the balance of the

loan will be paid. The difference in payments between the two loans is \$468.00 for the two-year period, favoring the lower interest rate loan:

2-year payments @ 13%	\$26,548.80
2-year payments @ 12-3/4%	- 26,080.80
Payment savings with 12-3/4% loan	\$ 468.00

The difference in remaining balances upon the loan pay-off must also be taken into account. Because the 12-3/4 percent loan will amortize faster, it will have a remaining balance that is \$34.71 lower than the 13 percent loan at the end of the two years. Adding this balance to the \$468.00 in reduced payments results in a savings of \$502.71 over the two-year life of the loan:

Payment savings with 12-3/4% loan	\$468.00
Additional loan reduction	- 34.71
Total savings with 12-3/4% loan	\$502.71

The borrower, if choosing the 12-3/4 percent loan, saves \$502.71 in payments and additional amortization over the 13 percent loan, but has paid \$2,000 to do so. Obviously, the two-point fee does not always equate to the corresponding 1/4

Table 1	ABC Mortgage Co.	XYZ Mortgage Co.
Loan	\$100,000	\$100,000
Interest rate	12-3/4%	13%
Monthly payments	\$1,086.70	\$1,106.20
Annual payments	\$13,040.40	\$13,274.40
Points	2	0
\$ Point charge	\$2,000	0

¹As used here, a point is defined as an additional, up-front charge made by a lender and paid by a borrower, that enables a loan to be made at a lower interest rate. A point is computed as 1% of the loan amount. More than one point may be charged, with

each point creating a corresponding decrease in the interest rate.

²Assuming the borrower has the available funds to pay the points.

Table 3

Discounted, after-tax payment savings with 12 $\frac{3}{4}$ % loan

	1	2	3	4	5
Year	Payment Difference	Tax Savings On 13% Loan	Annual After-Tax Payment Savings	Column 3 Discounted @ 8%	Cumulative Payment Savings
1	\$234.00	\$92.74	\$141.26	\$130.80	\$ 130.80
2	234.00	93.26	140.74	120.66	251.46
3	234.00	93.82	140.18	111.28	362.74
4	234.00	94.41	139.59	102.60	465.34
5	234.00	95.02	138.98	94.59	559.93
6	234.00	95.56	138.44	87.24	647.17
7	234.00	96.31	137.69	80.34	727.51
8	234.00	96.95	137.05	74.04	801.55
9	234.00	97.62	136.38	68.22	869.77
10	234.00	98.25	135.75	62.88	932.65
15	234.00	100.49	133.51	57.26	1,180.99
20	234.00	97.34	136.66	54.27	1,350.33
25	234.00	77.38	156.62	22.87	1,475.26
30	234.00	12.91	221.09	21.97	1,584.75

Column 1 is the annual difference in payments between the two loans with the advantage to the 12 $\frac{3}{4}$ % loan.

Column 2 is the annual savings in taxes attributable to the 13% loan due to additional interest payments.

Column 3 is the combined effects of the first two columns: Column 1 minus Column 2 = Column 3.

Column 4 is Column 3 discounted to the present at 8% per annum.

Column 5 is the cumulative total of Column 4.

Table 4

Discounted, after-tax pay-off and combined savings with 12 $\frac{3}{4}$ % loan

	1	2	3	4
Year	Pay-Off Difference	Column 1 Discounted @ 8%	Cumulative Payment Savings (Table 3, Col. 5)	Combined Savings
1	\$ 16.65	\$ 15.42	\$ 130.80	\$ 146.22
2	34.71	29.76	251.46	281.22
3	54.29	43.10	362.74	405.84
4	75.44	55.45	465.34	520.79
5	98.26	66.87	559.93	626.80
6	122.80	77.38	647.17	724.55
7	149.09	86.99	727.51	814.50
8	177.13	95.70	801.55	897.25
9	206.96	103.59	869.77	973.30
10	238.51	110.48	932.65	1,043.13
11	271.70	116.53	990.61	1,107.14
12	306.38	121.67	1,044.06	1,165.73
13	342.37	125.89	1,093.37	1,219.26
14	379.38	129.16	1,138.90	1,268.06
15	416.98	131.45	1,180.99	1,312.44
20	569.40	126.45	1,350.33	1,476.78
25	601.55	87.84	1,475.26	1,563.10
30	0	0	1,584.75	1,584.75

Figure A

Present value of borrower's after-tax savings with up-front point deduction (TABLE 4)

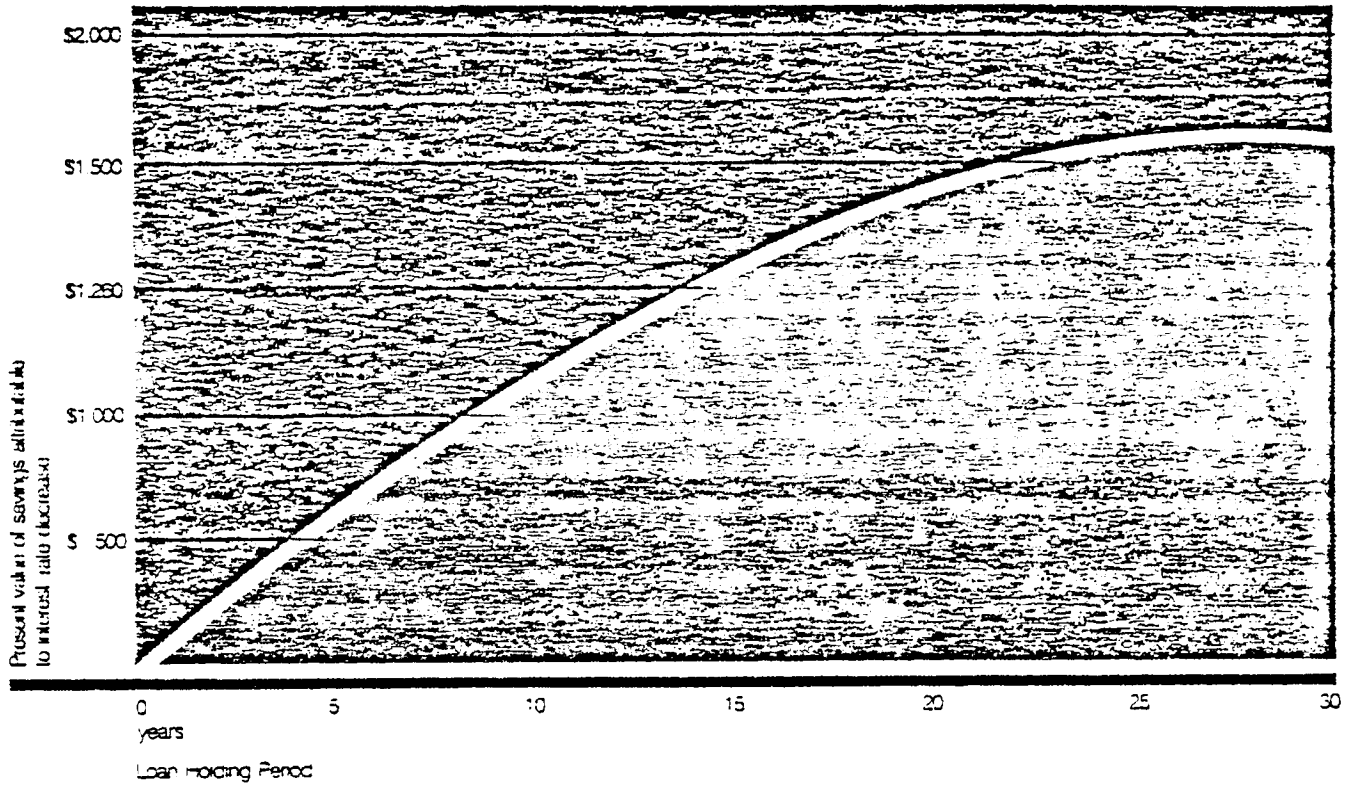
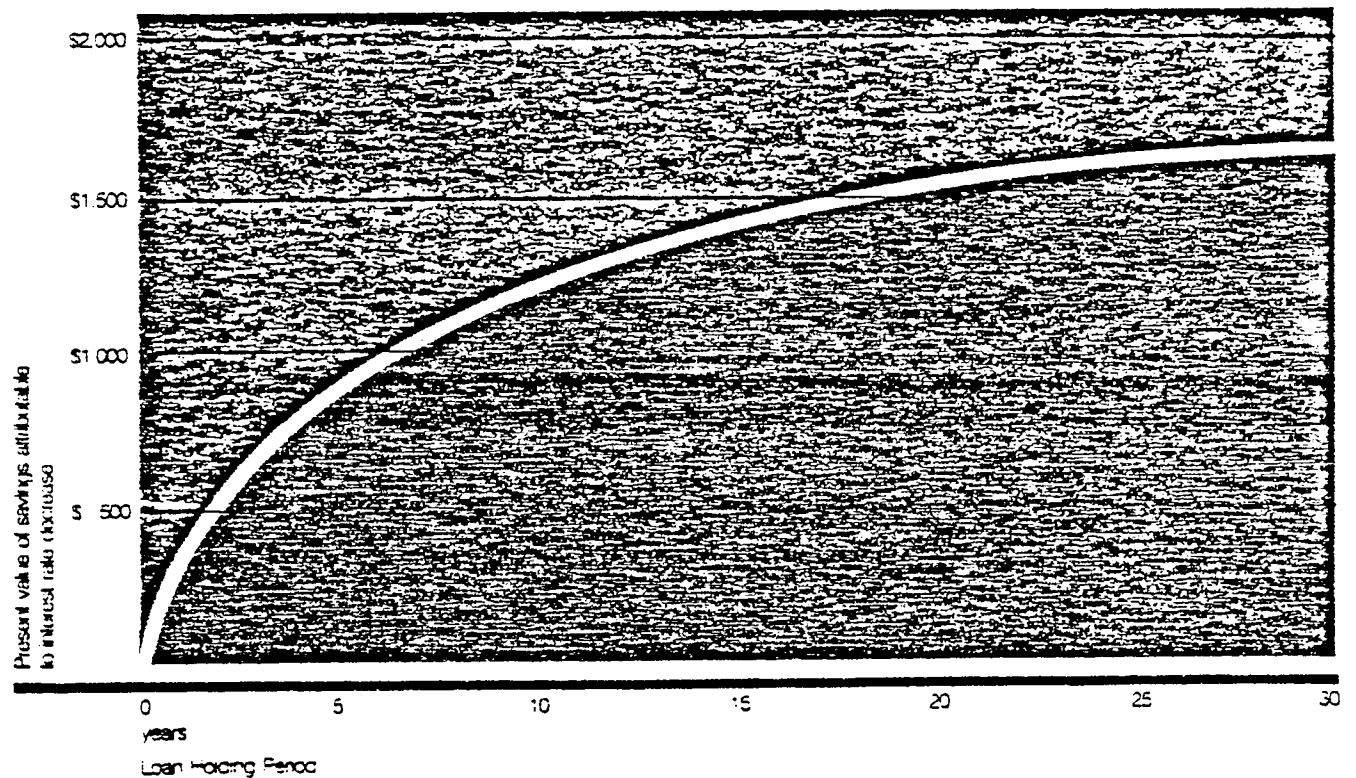


Figure B

Present value of borrower's after-tax savings with point charge added to basis



Example Problem: Cash Equivalent Price - Existing Mortgage plus
Purchase Money Mortgage

Given the following information, determine the cash equivalent price of the transaction:

Sale Price	\$1,000,000
Existing Mortgage (assumed)	Balance \$682,052 Mo. Pmt. \$6,039.20 Contract rate 8.5% Expired Term 6 years Remaining Term 19 years
Purchase Money Mortgage	\$200,000 @ 10% Amortization over 20 years, balloon in 10 years
Current Financing	14.5%, 20 year amortization with 10 year balloon

- What is the equity investment?
- What is the balance outstanding on the existing (assumed) mortgage in 10 years?
- What is the payment on the PMM?
What is the balance outstanding EOY 10?
- What is the cash equivalent price of the transaction?

Suggested Solution - II
Existing Mortgage plus PMM

A.	\$117,948
B.	\$454,781
C.	\$ 1,930 \$146,049
D.	Equity \$117,948
	Assumed Existing Mortgage
	PW \$6,039.20, 120 mos. @ 14.5%
	PW \$454,781, EOY 10 @ 14.5%
	Purchase Money Mortgage
	PW \$1,930, 120 mos. @ 14.5%
	PW \$146,049, EOY 10 @ 14.5%
	<u>\$ 34,558</u>
	Total (Cash Equivalent Price) \$763,581

* Courtesy of Byrl Boyce

IX. PROBLEM (CASH EQUIVALENCY)*

*Courtesy of A. Robert Parente, SREA, MAI.

An income producing property (special purpose) was resold by the Midland National Bank on a "workout." The terms of the sale were as follows:

Sale Price:	\$1,178,808, no cash by purchaser, i.e., 100% debt financing
Terms of Financing:	First year - interest only at a rate of 4-1/2% and payable monthly
	Second year - interest only at a rate of 6% and payable monthly
	For the next 23 years - principal and interest at 8-1/2%, payable monthly

The property (a 12,000 sq. ft., 3-year old restaurant building) was purchased on November 10, 1977 for \$1,178,808. Typical terms of financing at that time (11/77) were 9-3/4% interest for 25 years on a 75% loan-to-value ratio. It is estimated that equity required a 12-15% return.

Questions:

- A. What are the monthly interest costs in years 1 and 2?
- B. What is the constant on the amortized portion of the mortgage?
- C. What is the monthly payment on the mortgage?
- D. What is the unadjusted sales price per square foot for use in the DSC approach?
- E. What is the cash equivalent price assuming 100% financing were typical in the market?
- F. What is the cash equivalent price assuming an equity yield requirement of 12% 15%?
- G. What is the adjusted sales price per square foot under each of the conditions set forth above?

Suggested Solution - IX
 Problem (Cash Equivalency)

A. Year 1: \$4,420.53
 Year 2: \$5,894.04

B. $f = .09913$

C. \$9,737.97

D. $\$1,178,808 \div 12,000 = \$98.23/\text{sq. ft.}$

E. PW i Costs Year 1 @ 9-3/4% = \$ 50,347.92
 PW i Costs Year 2 @ 9-3/4% = 60,918.28
 PW Amortization payments
 Years 3-25 @ 9-3/4% = 881,198.63

Cash Equivalent Price
 (100% Financing) = \$992,464.83*

*\$186,343.17 less than face value of note

$\$992,464.83 \div 12,000 = \$82.71/\text{sq. ft.}$

F. Discount Rates given $Y = 12\%$, $Y = 15\%$, $m = 75\%$ $i = 9.75\%$

$Y = 12\%$	$Y = 15\%$
Mortgage $.75 \times .0975 = .073125$	$.75 \times .0975 = .073125$
Equity $.25 \times .12 = \underline{.03}$	$.25 \times .15 = \underline{.0375}$
Discount Rate (r) = .103125	Discount rate (r) = .110625

	PWCF @ 11.0625%
PWCF @ 10.3125%	
Year 1 \$ 50,198.33	\$ 49,999.88
Year 2 60,399.42	59,715.07
Years 3-25 <u>835,796.73</u>	<u>780,188.86</u>
\$946,394.48**	\$889,903.81***

\$232,413.52 below face *\$288,904.19 below face

G. $\$946,394.48 \div 12,000 = \$78.87/\text{sq. ft.}$

$\$889,903.81 \div 12,000 = \$74.16/\text{sq. ft.}$

* Courtesy of Byrl Boyce

EXHIBIT 33

CASH EQUIVALENCY EXAMPLE

NAKOMA HEIGHTS
 168 APARTMENT UNITS
 SOLD NOVEMBER 1, 1979
 NOMINAL SALES PRICE \$3,450,000

A. One appraisal reviewed recently contained the following summary analysis. It is used as it probably parallels the Madison Assessor's Office perception of the transaction:

<u>Date</u>	<u>Price</u>	<u>Gross</u>	<u>Net</u>	<u>GIM</u>	<u>Income Expense</u>	<u>S.P. Unit</u>	<u>OAR</u>
7/79	\$3,450,000	\$449,249	\$196,548	7.68	56.3	\$20,536	5.7

B. Cash Equivalency - Monthly payment differential

If 25% down with 75% L/V at 10.55 for 25 years

Down	862,000
Mortgage	<u>\$2,588,000</u>
	\$3,450,000

Monthly payment \$24,528; Annual payment \$294,335

1979 - 4/80 Conv. Mortgage \$294,335
 L.C. (9.25) 272,875
 \$ 21,460/12 = \$1,788 (A)

4/80 - 4/81

\$2,950,000			Conv. Mortgage	\$294,335
<u>250,000</u>				<u>249,750</u>
\$2,700,000	x	.0925	=	\$ 44,585/12 = \$3,715 (B)

4/81

\$2,700,000				\$294,335
<u>250,000</u>				<u>226,625</u>
\$2,450,000	x	.0125	=	\$ 67,710/12 = \$5,643 (C)

NET PRESENT VALUE UNDER
L.C. FINANCING AND BALLOON PAYOUT
ACCORDING TO CONTRACT ON 12/31/85

	<u>1979</u>	<u>1980</u>	<u>1981</u>	<u>1982 - 84</u> 4 years
Down Payment	\$500,000	\$250,000	\$250,000	
	<u>3,576</u> (2A)	5,364 (3A)	11,145 (3B)	\$ 67,710 (12C)
	\$503,576	<u>33,435</u> (9B)	<u>50,787</u> (9C)	
		\$288,799	\$311,932	
				Balance <u>2,450,000</u>
				\$2,517,710

NET PRESENT VALUE CONVENTIONAL LOAN

	<u>1979</u>		
Down Payment	\$862,000	--	Balance <u>2,404,022</u>

Cash year 1	\$503,576	\$288,799	\$311,932	
		<u>.884666</u>	<u>.796455</u>	
Cash year 2	255,491	\$255,491		
Cash year 3	248,440		248,440	
Cash year 4	48,551			\$67,710
Cash year 5	43,710			67,710
Cash year 6	39,351			67,710
Cash year 7	<u>\$1,317,332</u>			
	\$2,456,451			\$2,517.710
		Total Cash Equivalency (Versus \$3,450,000 nominal selling price)		

INCOME PREPOTED (Contract)	GROSS INCOME	\$499,249
	NET INCOME	<u>196,548</u>

MARKET RENT LEVELS

At least gross	\$450,000
Less 40% expense	<u>180,000</u>
NOI	\$270,000

$$\text{OAR} = \frac{270,000}{2,456,451} = .109915$$

$$\text{SP/Unit} = \frac{2,456,451}{168} = 14,622$$

1. Most probable price always requires a statement as to the financial terms which are a condition of effective demand at that price. Fair market value definition is sufficiently ambiguous to require a statement of financial terms as a qualification on conclusion.
 2. In practice you ignore points paid by the seller in a VA loan. To predict the most probable price, why not ignore points paid by the seller for a conventional loan? For loan security the lender is interested in the most probable price at which it will sell or whether the spread between probable price and fair market value will be covered by private mortgage insurance. In the latter case the appraiser could provide both numbers if asked.
 3. Only the assessor is locked into cash equivalent fair market value!
- E. The mechanics of cash equivalency values come into play where income properties are sold subject to non-market financing or for purposes other than income investment, such as syndication or condominium conversion. Professors Byrl Boyce and William Kinnard have prepared an excellent half-day presentation on cash equivalencies. The cases in Exhibits 31 and 32 are from their seminar and are suggestive of the mechanics of cash equivalency due to non-market financing.
- V. The fair market value appraisal for tax assessment of subsidized, rental housing is a very frustrating experience for both the assessor and the ownership position. None of the components of value are what they seem to be.
- A. It should be noted that 221 d3 and d4 and 236 projects involve subsidy of the interest rate only, while Section 8 recognize the damage done by inflation to cost to construct and operating expenses, so that it subsidizes the total project.
1. Section 8 was intended to subsidize conventionally financed apartments within a larger project, thus avoiding a ghetto of subsidized projects and permitting the depth of subsidy to vary; government would pay the difference between fair market rents and 25% of eligible tenants income.
 2. The legislation included instructions that the subsidy would cover full taxes and utilities, presuming taxes would be similar to non-subsidized development pegged at prevailing market rents. It was an operating subsidy program with no specific relationship to financing.
 3. The 1974 legislation did say that if the Section 8 contract was used as collateral to obtain financing, HUD had the right to approve financing and refinancing.
 4. Three factors precluded the original concept - rising interest rates in the conventional market, the evolution of HUD prerogatives for auditing, management, and tenant selection or eviction, and finally the operating procedures of state housing finance agencies and GNMA tandem plans which provide virtually all of the financing.



Wisconsin Housing Finance Authority

I. GENERAL INFORMATION			
1. Development Name: <u>Woodview Park</u>	<u>Real</u>	4. <input checked="" type="checkbox"/> Feasibility <input type="checkbox"/> Firm	
2. Development Sponsor: <u>Munz Investment Estate, Inc.</u>			
3. Development Location: <u>Tyrell Ave. & Geneva St.</u> (Street) <u>Delavan, Walworth</u> (City) (County)		5. Type of Mortgagor: <input checked="" type="checkbox"/> L.D. <input type="checkbox"/> N.P.	
6. <input checked="" type="checkbox"/> New Construction <input type="checkbox"/> Rehabilitation	7. Permanent Mtg. Interest Rate <u>7.5%</u>	3. Construction Financing: <input checked="" type="checkbox"/> WHFA <input type="checkbox"/> Conventional	
9. Type of Development	No. of Units	No. of Stories	
<input checked="" type="checkbox"/> Low Rise (1-3 stories)	<u>84</u> Apt. Units <u>6</u> T.H. Units <u> </u> Duplex Units <u> </u> S.P. Units	<u>E - 3</u> Story <u>F - 2</u> Story	
<input type="checkbox"/> Mid Rise (4-6 stories)	<u> </u> No. of Units	<u> </u>	
<input type="checkbox"/> High Rise (7 stories and over)	<u> </u> No. of Units	<u> </u>	
10. Accessory Buildings: (No. and type)	<u>None</u>		
11. Total Number of Buildings:	<u>Three</u>		
12. Total Number of Units:	<u>90</u>	(Family <u>22</u> ; Elderly <u>68</u> ; Handicap <u> </u>)	
13. Total Number of Units:	<u>90</u>	Revenue; <u> </u> Non-Revenue	
14. Density:	<u>20</u> Units Per Acre		
15. Building Information:	Structural System <u>Wood frame w/ exterior & interior masonry</u> Exterior Finish <u>Masonry</u> / Bearing Walls Floor System <u>Wood</u>		
16. Gross Floor Area (Including Basement and Common Areas)	<u>85,600</u> Sq. Ft.		
17. Net Rentable Floor Area:	<u>53,396</u> Sq. Ft.		
18. Number of Parking Spaces: <u>34 Elderly</u> <u>44 Family</u>	19. Parking Ratio: <u>1/.87</u>		

II. AMENITIES		III. SERVICES	
<input checked="" type="checkbox"/> Range (Gas Electric)		Included in Rent	
<input checked="" type="checkbox"/> Refrigerator		Yes	No
<input checked="" type="checkbox"/> Air Conditioning (Sleeve Only)		Heat	
<input type="checkbox"/> Air Conditioning (Sleeve Unit)		Gas/Hot Water.....	<input checked="" type="checkbox"/> ()
<input type="checkbox"/> Central Air Conditioning		Gas/Forced Air.....	<input checked="" type="checkbox"/> 3Bdr. ()
<input checked="" type="checkbox"/> Kitchen Exhaust Fan		Electric.....	() ()
<input checked="" type="checkbox"/> Central Laundry Facilities		Hot Water	
<input checked="" type="checkbox"/> Unit Laundry Facilities		Gas.....	<input checked="" type="checkbox"/> ()
<input checked="" type="checkbox"/> Disposal		Electric.....	() ()
<input type="checkbox"/> Dishwasher		Unit Electric.....	<input checked="" type="checkbox"/> ()
<input checked="" type="checkbox"/> Carpet		(Lights, Cooking, etc.)	
<input checked="" type="checkbox"/> Drapes		Water.....	<input checked="" type="checkbox"/> ()
<input checked="" type="checkbox"/> Shades		Other Fuel (Specify).....	
<input checked="" type="checkbox"/> Rods		() ()
<input checked="" type="checkbox"/> Common Area Furnishings		() ()
<input checked="" type="checkbox"/> Tot Lot		() ()
<input checked="" type="checkbox"/> Other (Specify)		() ()
_____		_____	_____
_____		_____	_____
_____		_____	_____

IV. RENT SCHEDULE

No. of Units	Type	Bdrms	Size by Sq. Ft.		FMR	Contract Rent	Utility Allowance
			Net	Gross			
67	E -L.R.	1	500	546	\$271	\$258.10	\$14G, \$4E
1	E -L.R.	2	800	860	\$348	\$278.84	\$20G, \$8E
16	W- L.R.	2	820	875	\$293	\$278.84	\$20G, \$8E
6	T.H.	3	996	1080	\$381	\$372.21	\$35G, \$12E

Gross Annual Contract Rent - - - - - \$ 291,194
 Gross Annual Contract Rent & Utility Allowance - - - - - \$ 314,762

V. EQUITY CALCULATION

1. Total Replacement Cost - - - \$ 2,212,267
2. Mortgage Amount- - - - - \$ 1,991,040
3. BSPRA - - - - - \$ 192,737
4. BSPRA & Mtg. Amount - - - - \$ 2,183,777
5. Equity Cash (Line 1 - - - - \$ 28,490
 minus Line 4)

VI. INCOME COMPUTATION

1. Gross Annual Income
 (Contract Rent) - - - - - \$ 314,762
2. Vacancy (5%) - - - - - \$ 15,738
3. Effective Gross Income - - - \$ 299,024
4. Debt Service (7 1/2 %) - - - \$ 157,229
5. MIFA Service Fee (4 %) - - - \$ 9,955
6. Total Operating
 Expenses & Taxes - - - - - \$ 118,568
7. Return on Equity- - - - - \$ 13,274

VII. SETTLEMENT REQUIREMENTS - INITIAL CLOSING

- | | |
|---|--|
| <ol style="list-style-type: none"> 1. <u>Cash</u>
 Equity Cash - - - - - \$ _____ Construction Adjustments- - \$ _____ Off-Site- - - - - \$ _____ Completion Assurance- - - - \$ _____ Total Cash Requirement - - - \$ _____ | <ol style="list-style-type: none"> 2. <u>Letter of Credit</u>
 Construction Adjustments- - \$ _____ Off-Site- - - - - \$ _____ Completion Assurance- - - - \$ _____ Total Letter of Credit
 Requirement - - - - - \$ _____ 3. <u>Total Cash & Letter of
 Credit Requirement</u> - - - - \$ _____ 4. <u>Bonds</u>
 Completion Assurance- - - - \$ _____ Off-Site- - - - - \$ _____ |
|---|--|

VIII. RECONCILIATION

1. ACC Authorization - - - - - \$ _____
2. Tenant Payments - - - - - \$ _____
3. Expected HUD Contributions- - - - \$ _____
4. Total Revenue - - - - - \$ _____
5. Total Expenses- - - - - \$ _____

IX. REPLACEMENT COST AND MORTGAGE

A. CONSTRUCTION CONTRACT		Per Unit	Total
1. STRUCTURES:			
1a. Apartments	- - - - -	\$ 15,162	\$ 1,273,600
1b. Townhouses	- - - - -	\$ 23,000	\$ 138,000
1c. Duplexes	- - - - -	\$	\$
1d. Single Family	- - - - -	\$	\$
1e. Other Buildings	- - - - -	\$	\$
1f. TOTAL STRUCTURES	- - - - -	\$ 15,684	\$ 1,411,600
2. LAND IMPROVEMENTS:			
2a. Usual (landscaping paving, etc)	- - - - -	\$ 1,433	\$ 129,000
2b. Unusual	- - - - -	\$	\$
2c. TOTAL LAND IMPROVEMENTS	- - - - -	\$ 1,433	\$ 129,000
3. GENERAL REQUIREMENTS (___ %)	- - - - -		\$ 35,550
4. GENERAL OVERHEAD (___ %)	- - - - -		\$ 28,935
5. BOND PREMIUM/LETTER OF CREDIT FEE	- - - - -		\$ 16,123
6. OTHER	- - - - -		\$ 55,260
			Tyrell Ave. Improvements-Eng. Est. \$70 ⁵ 75000 ÷ 122 D.U.'s = \$614 per D.U. X 90 =
7. TOTAL CONSTRUCTION CONTRACT	- - - - -		\$ 1,676,468
7a. Per Unit Construction Contract	- - - - -	\$ 13,627	
8. ARCHITECTURAL FEES			
8a. Design (___ %)	- - - - -	\$	46,000
8b. Supervision (___ %)	- - - - -	\$	14,000
8c. TOTAL ARCHITECTURAL FEES	- - - - -		\$ 60,000
8d. Per Unit Architectural Fees	- - - - -	\$ 666.67	
9. TOTAL CONSTRUCTION CONTRACT & ARCHITECTURAL FEES	- - - - -		\$ 1,736,468
			8 mo. @ 8% for 3 Bdrms.
10. CONSTRUCTION INTEREST (10 mo. @ 8 %) for 1 & 2 Bdrms.	- - - - -	\$	65,139
11. CONSTRUCTION TAXES	- - - - -	\$	13,875
12. CONSTRUCTION INSURANCE	- - - - -	\$	3,020
13. TITLE & RECORDING	- - - - -	\$	2,366
14. WHFA PROCESSING FEE (2.5 %)	- - - - -	\$	49,776
15. LOAN LOSS RESERVE (2.5%)	- - - - -	\$	49,776
16. LEGAL (\$ 4950) & COST CERTIFICATION (\$ 2,000)	- - - - -	\$	6,950
17. TOTAL CARRYING CHARGES & FINANCING FEES	- - - - -		\$ 190,902
17a. Per Unit Carrying Chgs. & Fin. Fees	- - - - -	\$ 2,121	
18. TOTAL (Lines 9 - 17)	- - - - -		\$1,927,370
19. BSPRA	- - - - -		\$ 192,737
20. LAND	- - - - -		\$ 92,150
21. TOTAL REPLACEMENT COST (Lines 18 + 19 + 20)	- - - - -		\$2,212,267
21a. Per Unit Replacement Cost	- - - - -	\$ 24,581	
22. MORTGAGE (90 %)	- - - - -		\$1,991,040
22a. Per Unit Mortgage	- - - - -	\$ 22,123	

X. OPERATING EXPENSES			
	Est. assessed value	Mkt. Per Unit	Sub-Total
1. REAL ESTATE TAXES:			
	E \$17,000	x 68 x 67% =	\$774,520
	Z Br \$19,000	x 16 x 67% =	\$203,680
1a. Est. Assessed Val. 67	U Br \$26,000	x 6 x 67% =	\$104,520
		X \$1,082,720	
	\$ 33.37 per \$1000		\$ 26,672
1b. Per Unit R.E. Taxes			\$ 408
2. SERVICE ACCOUNTS:			
2a. Fuel (Htg. & Dom. Hot Water)	\$ 198.40		\$ 17,856
2b. Electric	\$ 63.47		\$ 5,712
2c. Water - Sewer	\$ 45.07		\$ 4,056
2d. Garbage & Trash Removal	\$ 27.00		\$ 2,430
2e. Other - Advertising	\$ 3.00		\$ 270
2f. TOTAL SERVICE ACCOUNTS			\$ 30,324
2g. Per Unit Service Accounts			\$ 336.94
3. INSURANCE			\$ 4,062
4. AUDIT			\$ 1,080
5. LEGAL			\$ 540
6. MANAGEMENT:			
6a. Fees			
6b. Central			-\$ 6,756
6c. On-Site			-\$ 9,192
6d. Administrative			-\$
6e. TOTAL MANAGEMENT			\$ 15,948
6f. Per Unit Management			\$ 177.20
7. MAINTENANCE:			
7a. Caretaker Salary			-\$ 6,480
7b. Other Salaries			-\$
7c. Contract Services			-\$ 4,998
7d. Supplies			-\$ 2,700
7e. Other - Repair Services			-\$ 7,170
7f. TOTAL MAINTENANCE			\$ 21,348
7g. Per Unit Maintenance			-\$ 237.20
8. REPLACEMENT RESERVE			\$ 8,594
9. TOTAL OPERATING EXPENSES (Lines 1a + 2f + 3 + 4 + 5 + 6e + 7f + 8)			\$ 118,568
10. DEBT SERVICE			\$ 167,183
10a. Per Unit Debt Service			\$ 1,857.59
11. RETURN ON EQUITY			\$ 13,274
12. TOTAL OPERATING EXPENSES, DEBT SERVICE & RETURN ON EQUITY (Lines 9 + 10 + 11)			\$ 299,025



WISCONSIN HOUSING FINANCE AUTHORITY

Page 1 of 1

Date: 5/12/77
 Contractor: Mung Woodmen
 Project No.: 214
 Name of Project: Woodwin Park
 Location: Delavan Wis

This form represents the Contractor's and/or Mortgagee's firm costs and services as a basis for disbursing dollar amounts when advances are requested.

NO	TRADE ITEM	COST	TRADE DESCRIPTION	
2	Excavating & Backfill	47439		
3	Concrete	95657		
4	Masonry	147125		
5	Metals	10639		
6	Rough Carpentry	147682		
6	Rough Carpentry Labor	94292		
6	Finish Carpentry	23157		
6	Finish Carpentry Labor	40094		
7	Waterproofing	5007		
7	Insulation	25400		
7	Roofing	20032		
7	Sheet Metal	16175		
8	Doors	47500		
8	Windows	13263		
8	Glass	12282		
9	Lath & Plaster	---		
9	Drywall	93050		
9	Tile Work	7250		
9	Acoustical	4100		
9	Wood Flooring	---		
9	Resilient Flooring	4025		
9	Painting & Decorating	17625		
10	Specialities	5999		
11	Special Equipment	6563		
11	Cabinets	32157		
11	Appliances	49900		
12	Blinds & Shades, Artwork	9325		
12	Carpets	45600		
13	Special Construction	---		
14	Elevators	24911		
15	Plumbing & Hot Water	122000		
15	Heat & Ventilation	125073		
15	Air Conditioning	1000		
16	Electrical	149777		
	Accessory Structures	4000		
	TOTAL STRUCTURE(S)	1428627		
2	Earth Work	11250		
2	Site Utilities	16406		
2	Roads & Walks	30720		
2	Site Improvements	4000		
2	Lawns & Planting	24964		
2	Unusual Site Condition	55260		
	TOTAL LAND IMPRVTS.	157600		
	TOT. STRUCT. & LAND IMPRVTS.	1586227		
1	GENERAL REQUIREMENTS	35500		
2	SUBTOTAL (Lines 41 and 42)	161673		
2	BUILDER'S OVERHEAD	28935		
2	BUILDER'S PROFIT	---		
2	SUBTOTAL (Lines 43 thru 45)	164568		
2	OTHER FEES	---		
2	NON(1) PREMIUM	16123		
	TOTAL FOR ALL IMPROVEMENTS	1668786		
	TOTAL FOR ALL IMPROVEMENTS LESS LINE 52	---		

Mortgagee: Mung Woodmen By: _____ Date: 5/12/77
 Contractor: Mung Investment By: _____ Date: 5/12/77

IFA _____ Date _____

- B. Fair market rent (FMR) has nothing to do with rents from the marketplace for the specific units in question. Instead, they are established by HUD at a level which is expected to justify construction costs in a particular locale; if the FMR's don't work, deviations as high as 10% upward are permitted, but they are indexed to HUD estimates of cost to construct rather than community norms.
- C. Using the FMR's for the unit mix of a proposed project, the developer works through the 2013 form (See WHFA, Exhibit 34) backwards to arrive at a capital budget available for hard construction costs; he typically buys his land at a value not to exceed 90% of the HUD acceptable unit cost of land. The 2013 budget is then a tentative maximum but actual project costs are audited and any savings are used to adjust the maximum mortgage commitment. The 2013 does not recognize points paid for the permanent loan or overruns on cost, but the audit doesn't recognize rents collected prior to the audit certification date. With adroit phasing these costs may be offset with revenues during a period when most operating costs are funded as indirect costs of construction.
- D. The cost approach to value is distorted by HUD's specifications, lengthy procedures, hidden profit centers in fixed allowances for design, supervision, bonding, overhead, etc. Space allocations within the project may reflect social purposes such as meeting rooms, medical centers, craft shops, and infirmary. Moreover most projects are multiple site, multiple buildings, mixed units where perhaps the FMR on elderly will subsidize inadequate FMR's on family units.
- E. Comparative operating budgets for 100-unit one bedroom project is provided in Exhibit 35.
- F. The market comparison approach is inoperative because of constraints on resale inherent in the mortgage and management contracts, the tax trap of accelerated depreciation, the loss of depreciation benefits to the second owner, the emphasis on profit centers for construction rather than management, the rent controls following construction, and the fact that conversion to a conventional market rent structure in the early years would mean rents below the government level with interest rates higher than government level, thus forcing a resale price at a capital loss to the sellers.
- G. In short, it will be almost impossible to find or simulate a sale at fee simple title. Rather a transfer would come with all the liens and contractual obligations because the owners are not the controlling powers; HUD and the finance authorities are. Owners may change but the contractual pyramid will remain in place.
1. The Legislature recognized higher costs and higher risks could not be funded up front by direct subsidy so what has emerged is a series of mandatory management and operational reform and a series of initial and delayed profit centers, augmented by favorable tax rules, and automatically guaranteed.

2. Three groups of restrictions are the 1974 Act, complimentary administrative rules, and financing restrictions.
 3. Section 8 developments are built to conform to the regulatory mold rather than market or merchandising feasibility. Size 10-15% less, finishes are utilitarian, secondary locations, etc. for inferior products.
 4. The inferior product may cost more because of mandatory union wages, mandatory bonding and escrows, and non-competitive bidding to the degree that FMR's permit capital cost inflation. These costs can only be amortized by maintaining Section 8 agreements or conversion to tenant ownership. HUD is not encouraging the latter and there is no financing available that would place the tenants as owners at the same level of occupancy costs.
- H. As a practical matter revenue could be subsidy payments plus actual payments from the tenants. But the subsidy payment includes a payment for the right to set rents, tenant eligibility standards and cash dividends to the investor - in short, a defeasible partial transfer of the fee to the public. Is that parallel to a lease or an easement in gross to the public?
1. As a practical matter the assessor can use the annual audited financial statement of the Section 8 project.
 2. Gross rent equals $1/5$ the ACC contract amount plus actual receipts from tenants.
 3. Operating expenses should be used for the actual operations because they are different for subsidized projects (See Exhibit 36).

COMPARATIVE OPERATING BUDGETS FOR 100 ONE-BEDROOM UNITS

			Conventional			
Section 8			High Range		Low Range	
Rent	342,000	285/U	276,000	230/mo	240,000	200/mo
Management	15,800	158/yr	16,200	162/yr	12,000	120/yr
Maintenance	20,300	203/yr	18,000	180/yr	10,000	100/yr
Services/ Heat	27,000	270/yr	24,000	240/yr	22,000	220/yr
Insurance	6,850	68/yr	6,000	60/yr	4,000	40/yr
Audit/Legal	900	9/yr				-0-
Replacement Reserve	9,200	92/yr				-0-
Equity Return	14,000	140/yr	-0-	-0-		
Taxes*	51,600		42,960		37,200	
Mortgage	2,150,000		1,532,567		1,405,125	
Debt Service	184,834		168,840		154,800	
Total Replacement Cost	2,391,000		1,803,020		1,653,088	
*Based Upon Unadjusted Total Costs						

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Exhibit 36

Assessment Valuation of Section 8
Using Income Approach

Gross Receipts = \$142,000 Collected from tenants
 190,000 Collected from ACC contract for
 five years totalling \$950,000

Net Revenue \$332,000

Vacancy deduction - none ACC pays up to 60 days of vacancy and
 tenants pay only when occupying unit

Management fee \$ 15,800

Maintenance 20,300

Services/heat* 27,000

Insurance 6,850

Audit-legal 900

Replacement reserve 9,200

Net operating exp \$80,050

Net operating income
 B/4 real estate taxes \$251,950 or \$252,000
 $\$252,000 / .1374264 = 1,833,344$ or 1,830,000
 Capitalization rate = .126384 (25 year 12% mortgage)

$(.126384 \times .85) + (.15 \times .05) + (.75 \times .03 \text{ mill rate})$

 .1074264 .0075 .02225 =

Cap rate .1374264

*Be sure gross receipts include utility allowance; in some cases
 the tenant contribution is less than the utility bill.

** Local tax equalization rate

85% loan ratio x \$1,830,000 x 126384 = 196,590
 $\frac{\$252,000}{196,600} = 1.28$ debt cover ratio

V1. Until now, cash equivalent prices have made adjustment for differences in fixed mortgage constants and predictable mortgage balances due at some future point in time. However, today we are faced with variable rate mortgages and a subsector of those called mortgage participation loans.

- A. Variable rate mortgages should offer the appraiser little problem; indeed, it should help in that tricky allocation problem in terms of the source of value. Adjusting a sale price subject to an existing favorable mortgage is simply attributing value to the intangible element of finance rather than the productive asset of real estate.
1. To the degree that the variable rate mortgage removes the commodity speculation in money from the benefits of ownership, the more likely the price represents the value of the real estate rather than real estate plus an option on cheap money.
 2. The form of the variable rate mortgage may cause cash throwoff to vary or net reversion on sale to vary. Hence, the necessity of doing a spread sheet if the appraiser has reason to believe rates will be adjusted upward or downward within the foreseeable future. In the absence of a rate notification or in the presence of a maximum rate limit, the appraiser does not have to speculate (capital budgeting theory would hold that the cap rates should be loaded for the third moment of the maximum interest variance to reflect the risk of alternative financial outcomes, but I doubt if appraisers are ready for that).
 3. Lenders may modify debt cover ratios or mortgage investment guides like default points or loan-per-unit.
- B. Various forms of equity participation represent contingent interest payments to the lender. The appraiser has no alternative but to do a spread sheet forecast year by year for five or ten years of the proforma income and resale possibilities of the property. Participation takes on a variety of forms:
1. Participation in gross rent, generally above a floor of normalized gross. (May reduce value for mortgage loan-to-ratio value purposes).
 2. Participation in effective gross rent (set at a minimum level so that excessive vacancy penalizes the borrower; may exclude certain rental units or percentage rents or rents for services not funded by mortgage, i.e., a defined base effective rent).
 3. Percentage of net operating income (certain expenses allowed in full while other discretionary expenses and vacancy allowance may be defined in amount or percentage of effective gross). Sometimes found on land leases and reduces net income available for debt service if land lease is unsubordinated.

4. Percentage of cash throwoff, after debt service and with defined priorities and allowable debt limits. Other restrictions may include mandatory reserves to be set aside before participation.
 5. One of the above plus participation in refinancing surplus, net resale proceeds, or other capital transactions subject to a floor permitting recapture of equity capital and a ceiling for good fortune.
- C. Some forms of equity participation are more subtle, such as the convertible mortgage which takes several forms:
1. A community shopping center costing \$6 million to build and with a million in runaway construction interests can be sold for \$7.3 million for \$800-850,000 net operating income in the first five years. Lender provides \$7.3 million for 11% interest only ten-year mortgage; in addition, he receives 50% of cash throwoff and whatever percentage of ownership is needed in the tenth year to provide overall 18% return.
 2. An office building in San Francisco received 100% financing for construction and eight year balloon. In addition, the developer-borrower becomes a general partner with two limited partners, the land owner and the lender, each receiving some percentage of tax shelter, cash dividends, refinancing surplus or resale value and perhaps retaining first right of refusal as well.
 3. In each case, the mortgage loan represents fee simple title while the interests above that represent entitlements to tax shelter, nonvested future interests, managements and contracting fees and marketing skills.

Howard Johnson -
 Schedule of Projected Income and Expenses
 For the Years Commencing May 1, 1974-78

Period	1974-75	1975-76	1976-77	1977-78	1978-79
Occupancy (163 rooms)	68%	70%	71%	72%	73%
Revenue:					
Available Rooms	59,463	59,400	59,400	59,400	59,400
Occupied Rooms	40,463	41,580	42,174	42,768	43,362
Rate Average ¹	18.89	19.00	19.50	20.00	20.50
Room Revenue	764,450	790,020	822,390	855,360	888,920
Public Room Rental ²	7,116	7,200	7,200	7,200	7,200
Restaurant Rental ³	31,500	31,500	31,500	31,500	31,500
Telephone ⁴	(14,345)	(14,795)	(15,375)	(15,960)	(16,560)
Other Income ⁵	6,113	6,165	6,405	6,650	6,900
Room Service Commissions ⁶	1,635	1,850	1,920	1,995	2,070
Total Revenue	796,468	821,940	854,040	886,745	920,030
Operating Expenses:					
Payroll ⁷	166,180	164,390	170,808	177,349	184,006
Housekeeping ⁸	33,160	33,700	34,200	34,700	35,200
Adm. & Gen. ⁹	83,150	85,890	89,250	92,665	96,145
Adv. & Promotion ¹⁰	82,250	82,735	84,704	86,352	88,030
Utilities ¹¹	66,500	76,030	79,000	82,025	85,100
Repairs & Maintenance ¹²	16,550	13,500	13,500	13,500	13,500
Total Operating Expenses	447,790	455,245	471,432	486,591	501,981
House Profit	348,678	365,695	382,578	400,154	418,049
Misc. Interest Income	720	720	720	720	720
Gross Profit	349,398	366,415	383,298	400,874	418,769
Less: Insurance	10,314	9,926	9,926	9,926	9,926
Land Rental ¹³	7,680	7,680	7,680	7,680	7,680
Income to Furnishing ¹⁴	64,000	64,000	64,000	64,000	64,000
Income before RE Taxes and Debt Service to Land and Buildings	267,404	284,809	301,692	319,268	337,163

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Howard Johnson
 Randall, Inc.

Notes to Exhibit 4-6

1. Rate Average:

- The average room rate for the year ending April 30, 1975 was \$18.89. This was a \$.19 increase over the room rate for the period ending April 30, 1974, or about 1%. The increase was due in large part to standardizing room discounts for major clients and for functions requiring a large number of rooms.

2. Public Rooms:

- For the year ending April 30, 1975 the total dollar volume was \$7,116. In comparison, for the year ending December 31, 1974, the total volume was \$6,854. Public room rental was not found to be related to the level of occupancy or total revenues, thus it is assumed to be fairly fixed in character.

3. Restaurant Rental:

- The restaurant is leased to Howard Johnson's for a minimum rent of \$31,500, plus 5% of the amount of gross receipts which exceeds 20 times the minimum rental.

4. Telephone:

- Telephone revenues have averaged 3.4% of room revenues, compared with an industry average of 3.6% (Lodging Industry, by Laventhal, Krekstein, Horwath, and Horwath).
- Annual equipment lease payment is \$12,764.40.
- Net losses have average 1.8% of revenues. With increased occupancy, losses should not exceed 1.5%, comparable to national averages in Laventhal, Krekstein, Horwath and Horwath.

5. Other Income:

- Includes valet and laundry, vending sales, sundry sales, and 10% commission on banquet food sales. Vending has averaged 1/2 of 1% of total revenues. The remainder accounts for 1/4 of 1% of total revenues.

6. Room Service Commissions:

- 2% commission on restaurant bills and room service charged through motel plus 20¢/room service ticket, thus variable with occupancy.

7. Payroll:

- Actual and target results are 20% of total revenues.

8. Housekeeping:

- Averages have ranged from \$33,157 (December 31, 1974 closing) to \$33,775 (April 30, 1975 closing), or 4.06% to 4.27% of total revenues. Dollar amounts are fairly constant within a narrower range of occupancies.
- Includes commissions to travel agencies.

9. Administrative and General:

- For the year ending December 31, 1974 the total amount was approximately \$82,750, or 10.45% of revenues. The totals are comprised of expenditures the majority of which are variable in nature.
- Includes a 3% fee for management services.

10. Advertising and Promotion:

Schedule

	<u>1975-76</u>
Outdoor Sign	
Sign Co.	\$1625.50/mo.
Advertising Co.	31.50/mo.
Less: Howard Johnson's share	(275.00/mo.)
Total	\$1377/month X 12 = \$16,524
Promotions	1,500
Publications	7,200
Franchise Fee (5% of gross room receipts plus public room rentals)	39,537
Manager Expense and Promotion	3,475
Miscellaneous Advertising	2,500
Reservation Charge to Howard Johnson	<u>12,000</u>
Total	<u>\$82,736</u>

11. Utilities:

- The total is comprised of four elements: electric bulbs, electric current, fuel, and water. The total for the year ending December 31, 1974 was \$64,274 or 8.12% of total revenues.
- Interim rate increases by Gas and Electric commenced in June 1975. Electric increased 17.7% while fuel (gas) increased 7.33%. At present, additional proposed increases are being evaluated by the Public Service Commission which would become effective in 1976. Electric increases are proposed to be an additional 14.9% while gas is to increase 4.9%. Beyond 1976, increases are expected to be between 5% and 10% per year for both forms of energy.
- Utilities are not expected to exceed 9.23% of total revenues without a corresponding increase in room rates. Increases in utilities are expected to occur faster than any corresponding increase in room rates, thus it should be some time before the utility expense ratio will stabilize at approximately 9%.
- Year to date totals indicate the projections for 1975-76 are consistent with the above assumptions concerning the room revenue increase lag.

12. Repairs and Maintenance:

- Contracts
 - Plabocki Sign Repair Contract \$1,060
 - Westinghouse Elevator Contract 3,336
 - Pellitteri Wast Removal 738
- Actual for year ending December 31, 1974 was approximately \$16,550.
- For the year 1975-76, the year to date totals indicate a decrease in expenditure. Such expenditures should remain fairly constant over the next five years.

13. Land Rent:

Monthly rental charges	\$1000
Less: Recovery from leased property	<u>(360)</u>
Net land cost per month	640

14. Furnishings and Other Assets:

Furnishings and Equipment	
Furnishings and Equipment	\$251,120
Carpeting	60,490
Two Autos	9,480
Signs	9,967
Leasehold Improvements	<u>5,778</u>
Total per Audit	336,835

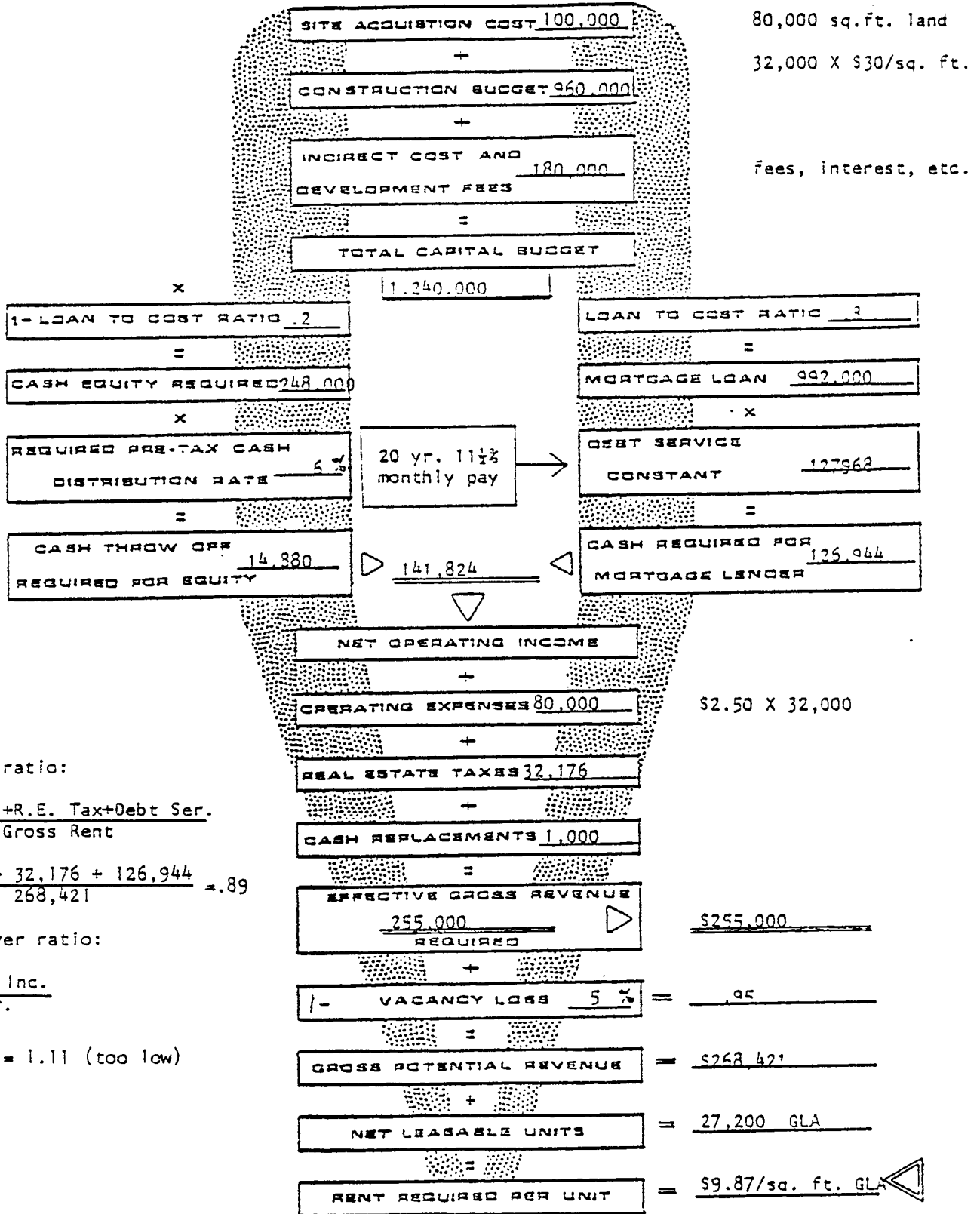
Factors Attributed to Furnishings

Rate of Return	9.0%
Recapture	10.0%
Personal Property Tax	4.5%

Income Equivalent of Recapture and Return to Equity

$$336,835 + 336,835(9\% \times 10 \text{ years}) = 639,987$$
$$639,987 + 10 = 63,999 \text{ or } \underline{\underline{64,000}}$$

EXHIBIT 1 LOAN TO COST RATIO APPROACH



Default ratio:

$\frac{\text{Op. Exp. + R.E. Tax + Debt Ser.}}{\text{Gross Rent}}$

$$\frac{80,000 + 32,176 + 126,944}{268,421} = .89$$

Debt cover ratio:

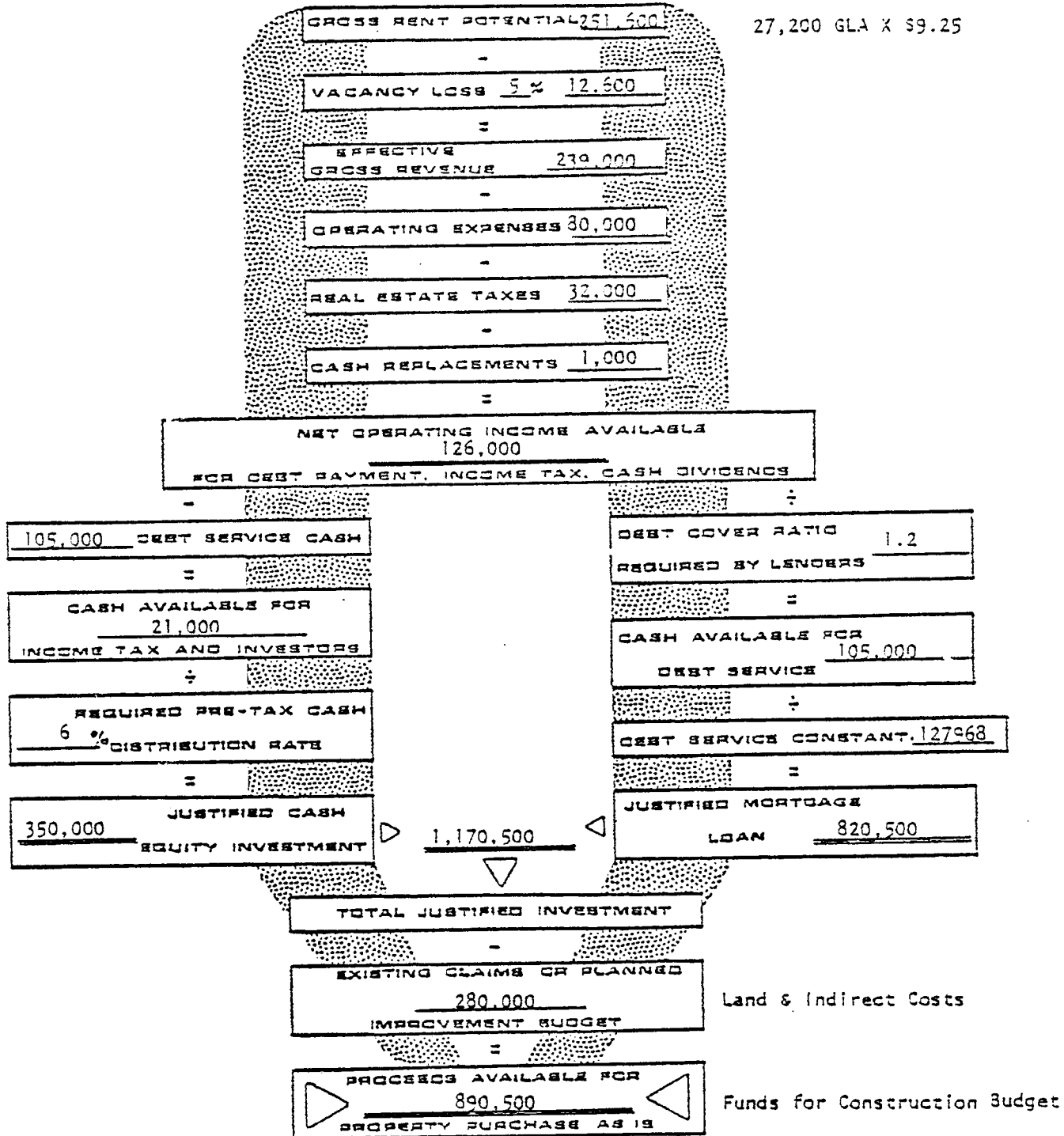
$\frac{\text{Net Op. Inc.}}{\text{Debt Ser.}}$

$$\frac{141,824}{126,944} = 1.11 \text{ (too low)}$$

LENDER'S POINT OF VIEW

EXHIBIT 2

DEBT COVER RATIO APPROACH

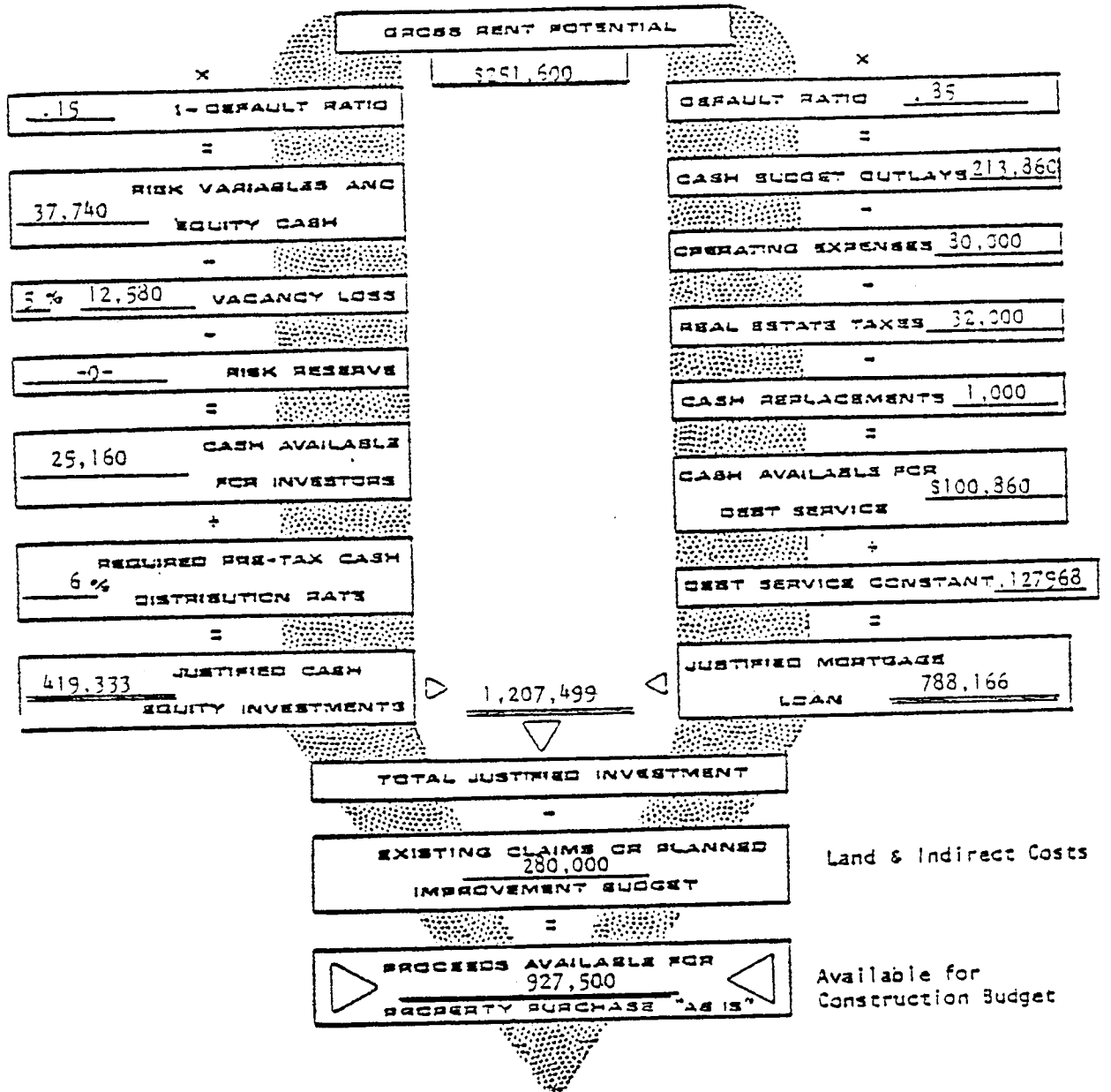


$\frac{890,500}{32,000} = \$27.80/\text{sq. ft. justified building budget}$

DEVELOPER'S POINT OF VIEW

EXHIBIT 3

DEFAULT RATIO APPROACH



\$37/sq. ft. of gross area for justified bldg. budget

Northwest Center for Professional Education

13555 Bel-Red Road, Suite 207, C96870
Bellevue, Washington 98009

PROGRAM EVALUATION

We appreciate your participation in this program. Your feedback is important. Your critical comments help us evaluate the effectiveness of the topic material and its presentation, and guide in the development of new programs for you and your professional peers. Thanks for your help.

Contemporary Appraising of
Program Title Income Properties Location (city) #8256

Please tell us your primary objective in attending this program. _____

How well was this objective achieved through your participation in the program?

Well achieved _____ Mostly achieved _____ Moderately _____ Not _____

Please rate the program elements by circling the appropriate numbers below:

	EXCELLENT		GOOD		AVERAGE		FAIR		POOR	
The course in general	10	9	8	7	6	5	4	3	2	1
The instructor (s)	10	9	8	7	6	5	4	3	2	1
Relevance of information	10	9	8	7	6	5	4	3	2	1
Handout materials	10	9	8	7	6	5	4	3	2	1
Quality of facility	10	9	8	7	6	5	4	3	2	1
Program Management	10	9	8	7	6	5	4	3	2	1

What's the best feature of the program? _____

What did you like least about the program? _____

What changes should we make in the program? _____

Your general comments about the program: _____

May we publish your remarks? Yes _____ No _____

Name _____ Firm _____

(optional)

(over please)

In the following category lists, please circle the identifying numbers which apply to you.

YOUR PROFESSION

- | | |
|--------------------------------------|-----------------------------|
| 1 - Attorney | 8 - Real Estate Appraiser |
| 2 - Accountant | 9 - Builder/Developer |
| 3 - Tax preparer or Consultant | 10 - Real Estate Investor |
| 4 - Mortgage lender or banker | 11 - Architect/Engineer |
| 5 - Real Estate Broker/Assoc. Broker | 12,- Other (Please specify) |
| 6 - Real Estate Salesperson | _____ |
| 7 - Life Insurance Agent | _____ |

YOUR PROFESSIONAL MEMBERSHIPS

- 1 - (Your state)Association of Realtors
- 2 - Multiple Listing Service (s)
- 3 - An Exchange Club
- 4 - A Homebuilders' Association
- 5 - Other memberships or affiliations _____

YOUR PROFESSIONAL READING (Subscribe to, or read?)

- 1 - Real Estate Review
 - 2 - Creative Real Estate
 - 3 - Real Estate Today
 - 4 - Other professional or trade publications? _____
-

THE PROPERTY YOU DEAL WITH

- | | |
|--------------------------|----------------------------|
| 1 - Residential | 5 - Recreational |
| 2 - Commercial/Retail | 6 - Farm/Ranch |
| 3 - Industrial | 7 - Other (Please specify) |
| 4 - Income or Investment | _____ |

Are there other topics, programs or speakers you'd like?

Thanks for your help,

Norm Swent

Norm Swent

Executive Director

CONTEMPORARY ISSUES AND METHODS FOR
APPRAISING COMMERCIAL PROPERTIES

Presented by

Professor James A. Graaskamp, Ph.D., CRE, SREA
University of Wisconsin, School of Business

INTRODUCTION

I. INTRODUCTION TO CONTEMPORARY ISSUES

Appraisal of real estate income properties is a critical social function with high ethical requirements because it is a pivotal benchmark for decisions involving social equity, validation of financial institution assets for regulatory purposes, governance of private contracts, and benchmarking of the effectiveness of asset manager.

- A. Appraisal is a specialty in the rapidly evolving information business. Appraisers systematically collect information, organize and analyze the data, and reach decisions about value while communicating essential information to a client. This is similar to the work of:
 - 1. Accountants
 - 2. Insurance managers
 - 3. Security and investment counselors
 - 4. Lawyers
- B. Unlike accountants and others, appraisers receive little help from their professional organizations in the form of position papers which define appropriate methods for a particular question.
 - 1. Accounting has the Financial Accounting Standards Board (FASB) that continually modifies generally accepted accounting principles to fit new problems such as mergers, current values of fixed assets, accounting for real estate operations, etc.
 - 2. Securities people have the Midwest Securities Association.
 - 3. The insurance education program is controlled by two independent organizations, the American College of Life Underwriters and the American College of Property and Casualty Underwriters.

4. Appraisers have no such independent fixed point. Even the Eighth Edition of the Institute textbook disclaims any responsibility for being a standard. The flyleaf of the Eighth Edition says:

"FOR EDUCATION PURPOSES ONLY
The opinions and statements set forth herein are those of the individual members of the Institute's editorial staff and do not necessarily reflect the viewpoint of the American Institute of Real Estate Appraisers or its individual members."

- C. As a result, the appraisal process is evolving into one of the following:
 1. The art of disinformation as in military intelligence where the appraiser is implicitly part of a conspiracy with his client to provide documents that satisfy regulators, provide cover against future charges of negligence, or provide bargaining points for income tax, real estate tax, divorce settlements, partnership dissolution, and other negotiations.
 2. The discipline of rigid format and language for purposes of standardization at the expense of relevance and as an alternative to qualifications of the appraiser's judgment as opposed to form filling ability.
 3. A counseling assignment wherein the appraiser must select and match the basic elements of the appraisal assignment to the requirements of the decision for which the appraisal is sought as a benchmark.
- D. Distinguishing carefully between advocacy and suitability, the ethical and professional appraiser must counsel his client on the basics to establish a fit between the appraisal and the issue for which it is required as a benchmark, including, but not limited to:
 1. Definition of real estate interests to be appraised

2. Definition of highest and best use
3. Definition of market value
4. Definition of what constitutes market comparison
5. Definition of accounting rules for the income approach
6. Definition of the economic context assumed
7. Definition of buyer and seller perspectives
8. Definition of rules for anticipating future benefits
9. Definition of who is considered an independent observer

CONTEMPORARY ISSUES AND METHODS FOR
APPRAISING COMMERCIAL PROPERTIES
(Continued)

II. BASIC PREMISES OF CONTEMPORARY APPRAISAL

The basic premises of the contemporary approach stem from the fundamental belief that pricing is a behavioral science, that analysis should be inductive rather than deductive wherever possible, and that appraised values are intended to serve as a benchmark for some decision process.

- A. A price is a social transaction and the behavior of the parties and configuration of the transaction reflects a consensus at some point in time between external market forces sufficiently strong to impose on the outcome and internal forces on the supply side sufficiently strong to pursue their own self-perceived interests. (See Exhibit 1.)

Notice that the above does not presume:

1. Both demand and supply forces to have alternatives of equal indifference.
 2. Negotiation abilities of equal force, or
 3. Cash maximization as their sole criteria - all of which characterize the traditional approach.
- B. The contemporary view sees appraisal as a limited and fictional case of feasibility analysis which, in turn, is a limited case in problem solving which, in turn, is part of a larger planning framework.
- C. Appraisal as a fictional feasibility study is a model of a decision process and, therefore, like all models is constrained by the following elements:
1. What is the nature of the question?
 2. What quantity and quality of data may be available?

3. What theory or hypothesis may edit and focus the available data as a tentative answer to the question?
 4. What techniques and data management can be used reliably by the analysts?
 5. What techniques and data management have credibility with the ultimate decision maker hiring the analyst?
 6. What techniques and data management are cost effective in terms of the dollar consequences of the decision?
- D. Functions of appraisal differ dramatically and lead to multiple definitions of value.
1. Validation (mortgage loans)
 2. Benchmarking performance (pension funds)
 3. Confrontation (legal cases)
 4. Counseling (investment decisions)

CONTEMPORARY ISSUES AND METHODS FOR
APPRAISING COMMERCIAL PROPERTIES
(Continued)

III. THE PROCESS OF CONTEMPORARY APPRAISAL

In that light, the sequence of steps required of the contemporary appraisal process referred to by Wisconsin students as RATGRAM is as follows:

- A. What is the issue for which the appraisal is sought as a benchmark?
 1. Problem perceived redefined to the problem as understood
 2. Statutory or financial
 3. Perspective in time, viewpoint, and continuum as going concern
- B. What are the attributes of the property and the potential for productive alternative courses of action for future use?
 1. Responsibility for engineering, marketing, or legal/political assumptions
 2. What special enhancements or encumbrances are to be valued as additional sticks in the bundle of rights to be appraised
 3. Opportunities for monopoly in space, place, or time
- C. Given the basic alternatives, what is the most probable use matrix relevant to the appraisal purpose?
 1. English Royal Institute of Chartered Surveyors (RICS) distinguish between existing use and all possible uses
 2. With or without zoning change
 3. With or without possible assemblage value
 4. With or without administrative rule recognition

5. With or without opportunity cost doctrine
- D. Given the most probable use, who is the most probable buyer in terms of class, motivation profile, or market position? (See Exhibit 3.)
 - E. Given the most probable use and most probable buyer assumptions, there are three approaches to predicting most probable price:
 1. Inference from past transactions involving properties of similar potential and buyers of similar motivation.
 2. Failing adequate transaction data, it is then acceptable to simulate the pricing methods of the most probable buyer.
 3. Failing to find either similar properties or articulate buyers, the appraiser is then permitted to use normative methods which indicate what might happen if buyer and seller were as smart as the appraiser.
 - F. With an initial estimate of value, it may then be modified for external conditions unique to the parties, the place, or the time.
 - G. The adjusted value must then be tested to demonstrate that results at that price would be consistent with the minimum goals of all major parties to the transaction.
 - H. Since the appraiser is predicting price under conditions of uncertainty and many different market terms, the appraisal conclusion must be expressed as a central tendency within a transaction zone which is qualified by financial terms and/or critical assumptions about unknowable facts.
 1. Although the Institute uses fair market value and most probable price interchangeably, that is a travesty on the work of modern theorists and a deliberate attempt to confuse or negate the implied criticism of traditional ways by contemporary analysis. (See Exhibits 1 and 2.)

2. Contemporary theory recognizes explicitly the errors in forecasting, the role of financial terms, and the reality of bargaining position.
 - I. These general precepts are then expanded into an appraisal report outline of the general type included in Exhibit 4.
 - J. We believe it is important that every appraisal first report fair market value strictly defined as cash to the seller for the real estate interest as a standard point of departure and that value enhancements and encumbrances then be reported in reference to that base number. Most probable price will only be the same as fair market value where the most probable buyer behaves as though he were the most prudent man buying only returns attributable to land and building.

EXHIBIT 1

CONTEMPORARY DEFINITION OF MOST PROBABLE PRICE

"Most Probable Selling Price", as defined by Professor Richard U. Ratcliff:

The most probable selling price is that selling price which is most likely to emerge from a transaction involving the subject property if it were exposed for sale in the current market for a reasonable time at terms of sale which are currently predominant for properties of the subject type. [1]

[1] Unpublished quotation, Richard U. Ratcliff speaking on his book Valuation for Real Estate Decisions, Santa Cruz, CA, Democratic Press, 1972.

EXHIBIT 3

SAMPLE PROFILES OF MOST PROBABLE USE AND BUYER

The most probable use of the subject property would be as a shell for conversion to three small retail units on the first floor, four townhouses in the three-story structure, and two 700 square feet office modules with skylights in the second-story structure.

A review of sales on the Square and along the State Street Mall reveals that the buyers of these properties have been either a local businessman who was seeking a new location for his business or a professional real estate investor who was willing and able to execute extensive renovation and re-leasing. Those comparables that were bought by businessmen primarily for their own use were small and narrow; the larger buildings, similar in size to the subject property or larger, were purchased by professional developers who already had other commitments in the downtown area. The old Leath Furniture building, which was purchased by amateur businessmen for use as a restaurant, is again available for rent because the new owners discovered that their intended use was not compatible with building codes. Three of the seven comparables were partially occupied by the new owner; five were financed by the seller with a 10 percent to 15 percent down payment and a land contract at 8 percent; six were sold for significantly less than May 1, 1976, assessed valuation; and in six of them, the first floor was subdivided into retail rental units with about 20 feet of frontage each.

Therefore, the most probable buyer will be a professional real estate developer who expects to remodel and redirect marketing of the subject property. The most probable buyer expects generous land contract terms and resale, before or after conversion, to a small group of participating equity investors. The professional investor will negotiate only after the owner has had the property on the market for a protracted period of time and is willing to sell it well below assessed valuation.

EXHIBIT 4

CONTEMPORARY REAL ESTATE APPRAISAL REPORT OUTLINE

Letter of Transmittal

1. Brief statement of appraisal issue
2. Definition of value applied
3. Value conclusion (qualified by financing, terms of sale, and range of probable transaction zone as appropriate)
4. Sensitivity of conclusion to critical assumptions
5. Property observations or recommendations
6. Incorporation by reference of limiting assumptions and conditions

Table of Contents

List of Exhibits

Digest of Facts, Assumptions, and Conclusions

1. Property type
2. Property location
3. Property ownership
4. Determinant physical attributes
5. Controlling legal-political attributes
6. Pivotal linkage attributes
7. Marketable dynamic attributes
8. Most probable use conclusion
9. Most probable buyer profile assumed
10. Initial probable price prediction and central tendency
11. Adjustment of preliminary value estimate for external factors or market position of parties
12. Testing of corrected probable price for consistency with most probable buyer objectives
13. Final value conclusion and range of error estimate as appropriate

I. Appraisal Problem Assignment

- A. Statement of issue or circumstances for which appraisal is intended to serve as a decision benchmark and date of valuation
- B. Special problems implicit in property type or issue that affect appraisal methodology and definition of value

EXHIBIT 4 (continued)

- C. Special assumptions or instructions that are provided by others
 - D. Definition of value, which is the objective of appraisal analysis and disciplines appraisal process
 - 1. Selected definition and source
 - 2. Implicit conditions of the definition
 - 3. Assumptions required by relevant legal rulings
 - E. Definition of legal interests to be appraised
 - 1. Legal description and source
 - 2. Permits, political approvals, and other public use entitlements
 - 3. Fixtures or personalty to be included with sale
 - 4. Specific assets or liabilities excluded as inconsistent with issue or premise of appraisal
- II. Property Analysis to Determine Alternative Uses
- A. Site Analysis
 - 1. Physical (static) site attributes (size, shape, geology, slope, soil hydrology, etc.)
 - 2. Special site improvements (wells, bulkheads, irrigation systems, parking surfaces with unique salvage or re-use characteristics, etc.)
 - 3. Legal-political attributes (applicable federal, state and local zoning, covenants, easements, special assessments, or other land use codes and ordinances, etc.)
 - 4. Linkages of site (key relationships to networks, populations, or activity centers that might generate need for subject property)
 - 5. Dynamic attributes of site (perceptual responses of people to site in terms of anxiety, visibility, prestige, aesthetics, etc.)
 - 6. Environmental attributes of site as related to off-site systems or impact areas.
 - B. Improvement Analysis
 - 1. Physical (static) attributes of improvements, cataloged by type, construction, layout, condition, structural flaws, etc.
 - 2. Mechanical attributes (brief statement of heating, ventilating, air conditioning, electrical, plumbing, and fire or safety systems in terms of limitations on use or efficiency)

EXHIBIT 4 (continued)

3. In short, it is useful to subdivide improvements into subsystems:
 - a. Foundation system
 - b. Structural system
 - c. Vertical circulation
 - d. Horizontal circulation
 - e. Floor system
 - f. Ceiling system
 - g. Roof system
 - h. Internal wall system
 - i. External wall system
 - j. HVAC system
 - k. Communications system
 - l. Traffic separation system
 - m. Security system
 - n. Life safety system
 - o. Waste removal system
 4. Special structural linkages to off-site elements (tunnels, bridges, adjoining structures, etc.)
 5. Legal-political constraints on use of existing improvements (federal, state and local building codes, fire codes, conditional use procedures, neighborhood associations, and inspection liens of record for violations).
 6. Dynamic attributes of existing improvements (impressions created by type, bulk, texture, previous uses, past history, or functional efficiency)
 7. Current uses and tenancies of improvements, if any
 8. Environmental impact attributes of improvements on environs
- C. Identification of Alternative Use Scenarios for Subject Property
1. Marketing existing uses of property as is
 2. Renovation of existing property and marketing improved space
 3. Redirection of existing property to alternative tenancies and uses
 4. Replacement of existing improvements or program with new uses

EXHIBIT 4 (continued)

III. Selection of Most Probable Use

A. Comparative Analysis of Alternative Uses

1. Testing and ranking alternative use strategies for legal-political compatibility
2. Testing alternative use scenarios for fit to physical property attributes within reasonable cost to cure
3. Selection of scenarios that justify market research

B. Analysis of Effective Demand for Selected Uses

1. Search for rents and income potentials of scenario space-time products
2. Screen and rank market targets
3. Apply income-justified residual investment approach to rank economic power of alternative market scenarios
4. Evaluate marginal revenue, marginal investment risk trade-offs

C. Summary Matrix for Selection of Most Probable Use Scenario

1. Physical fit
2. Legal-political risk
3. Strength of market demand
4. Adequacy of available financing
5. Revenue and cost assumptions risk

IV. Prediction of Price for Subject Property

A. Specification of Most Probable Buyer Type Implied by Most Probable Use

1. Criteria motivations of alternative buyer types
2. Selection of most probable buyer type as basis for prediction
3. Specification of essential site, improvement, financial, or key decision criteria of principal alternative buyer types

EXHIBIT 4 (continued)

- B. Explanation of Appraisal Methodology for Prediction of Probable Purchase Price
1. Preferred method: to infer buyer behavior from actual market transaction and market data available from sales by comparable buyers of acceptable alternative properties
 2. In the absence of adequate market sales data, the alternative method selected for simulation of probable buyer decision process
 3. If market influence of simulation is impossible, select normative model such as investment value, or cost to replace
- C. Search for Comparable Market Sales Transactions
1. Unit of comparison
 2. Method of comparison
 4. Investigation of sale transaction circumstances
 5. Evaluation for comparability
 6. Definition of predominant terms of sale
 7. Source of comparative adjustments
- D. Determination of Suitability of Existing Market Data for Inference of Value for Subject Property
1. Where data is adequate, selection of market comparison method to estimate value
 2. Where data is lacking or misleading, selection of method leads to simulation in E or normative methods in F
- E. Simulation of Probable Buyer Decision Process if Market Comparison Approach is Inconclusive or Impossible
1. Source and explanation of simulation model
 2. Schedules of simulation assumptions
 3. Range of alternative simulation value predictions (sensitivity analysis)
- (OR) F. Selection of Normative Model of Buyer Behavior
1. Investment model
 2. Cost-to-replace model
 3. Nonquantitative decision models
- G. Computation of Most Probable Price and Standard Error of Prediction

EXHIBIT 4 (continued)

- H. Correction of Preliminary Value Estimate for External Factors
 - 1. Identification of conditions relative to date of appraisal not present in market comparison assumptions
 - 2. Specification of political contingencies that might upset normal appraisal assumptions of substitution
 - 3. Identification of any violation of conditions in the definition of value by the appraisal methodology
 - 4. Indication of adjustment necessary to preliminary probable price estimate or
 - 5. Explicit statement that no adjustment is necessary

- I. Test of Most Probable Price or Value Conclusion by Means of:
 - 1. Comparison to values derived from selected alternative appraisal methodology
 - 2. Demonstration of achievement of objectives of most probable buyer minimum selection criteria
 - 3. Measurement of fit of financial cash requirements to market rents, lender ratios, or other relevant constraints
 - 4. Comparison to decision criteria appropriate to issue (financial ratios required by mortgage lender, comparative assessments of similar property for the tax appeal board, rates of return in alternative investments, construction prices for similar property, or whatever demonstrates consistency with statement of the issue)

- V. Appraisal Conclusion and Limiting Conditions
 - A. Definition of Value and Value Conclusion of the Report
 - B. Certification of Independent Appraisal Judgment
 - C. Statement of Limiting Conditions that Establish:
 - 1. Contributions of other professionals on which report relies
 - 2. Facts and forecasting under conditions of uncertainty
 - 3. Critical assumptions provided by the appraiser
 - 4. Assumptions provided by the client
 - 5. Controls on use of appraisal imposed by the appraiser

EXHIBIT 4 (continued)

Appendices

Maps, data sets, only if referred to in the text. These data collections would slow down the reader if included as an exhibit and are secondary to the argument in the body of the report.

CONTEMPORARY ISSUES AND METHODS FOR
APPRAISING COMMERCIAL PROPERTIES
(Continued)

IV. THREE BASIC METHODS OF APPRAISAL

Dilmore has the most basic philosophical view of the three approaches to value while Ratcliff has the most operational sense of researching and forecasting value.

A. Dilmore refers to the three approaches as order, chance, and beauty

1. Assuming order, there is a universe in which the parts fit and we shave away the chaotic mass of information until we find the critical pattern. Like the test for color blindness, the appraiser is looking for the pattern of red dots in a field of random dots of various colors which appear to be scattered.
2. Chance acknowledges the possibility that in the closed system there may be possibilities which were not considered or that there may be an error. No respectable scientist is afraid of the word "error". In appraisal, imprecision is built into the process of choosing data subjectively before we attempt to treat it objectively.
3. Beauty simply recognizes intuition and elegance in our forecasting model may be legitimate reasons for its use. Intuitive reactions, qualitative judgments, or gut feelings are a form of aesthetics in the decision process.

B. Ratcliff concludes that most appraisals are concerned with prediction of a future event, a transaction price. Since an appraisal method is a forecasting tool, forecasting is best done with inference from selected past experience. Failing that, the best method is simulation of the real estate market process.

1. Given reliable information on past market behavior, the preferred method of appraisal is to process the data, statistically if possible, to derive a prediction of future price behavior under given conditions and with means for estimating the reliability of the prediction.
 2. Statistical prediction if possible.
 3. Set theory for definition of a data set at the least.
- C. Should market data be unavailable or inconclusive, the appraiser is forced to resort to the second method of appraisal, namely the construction of a real estate investment or decision model of factors which reflect his understanding of how buyers and sellers might behave.
1. The income approach and the cost approach are submodels of how an investor is supposed to behave.
 2. After-tax investment models are another submodel of market behavior, but while these may measure demand from the buyer's viewpoint, it may not measure the minimum price expected by the seller who also has a tax model to consider. In using the second approach, the appraiser must be very careful to indicate price on the supply side representing minimum expectations (Vs) of the seller.
- D. Should there be no sales and no way to verify how buyers would review the specific property (utility case - rate base or kilowatt production?), then the appraiser falls back to normative methods.
1. Normative means what the buyer would do if he were as smart as the appraiser and motivated only by a desire to maximize wealth.
 2. The traditional income approach or the cost approach are normative models unless it can be proven buyers behave accordingly.

3. After-tax cash flow models are normative models until it can be shown that buyers and sellers use cash flow to value property.
- E. Highest and best use or most probable use in order to identify most probable user and buyer, requires analysis and explicit recognition of possible uses which are:
1. Legal/political acceptability
 2. Physical/technical feasibility
 3. Effective demand and marketability
 4. Financial viability
 5. Community compatibility
- (See Exhibits 5, 6, and 7.)
- F. Most probable use presumes economic feasibility while many projects today require only financial solvency due to special enhancements or encumbrances which modify the operating characteristics of the property. These are not inherent in fee simple title but require expansion of the definitions of legal interests to be acquired; the appraiser may require legal support for presuming the transferability of these enhancements or a cost for elimination for an encumbrance.
1. Enhancements include special entitlements under land use control laws, subsidized financing program, financial reserves which travel with the title and the assumable financing, and all manner of profit centers provided by operating agreements which may be assignable under certain review procedures.
 2. Encumbrances such as licenses, easements, and leases may be removed depending on relative positions of buyer and seller which are not within the American rule that fee simple title is the sum of the parts.

3. Economic surplus for the user is not adjusted for economic costs to external parties unless the political system can find methods to internalize these opportunity costs as anticipated in the definition of best use in Exhibit 5.
4. Fair market value may take the premise that existing leases will run out their term while most probable price may reflect a probability of renegotiation between landlord and tenant for mutual benefit or background information which makes it impossible for the status quo to persist.
 - a. Check Dunn and Bradstreet on the tenants
 - b. Analyze reported sales volume relative to breakeven point
 - c. Analyze opportunity cost of the status quo

COFFEE BREAK

EXHIBIT 5

DEFINITION OF HIGHEST AND BEST USE

That reasonable and probable use that will support the highest present value, as defined, as of the effective date of the appraisal.

Alternatively, that use, from among reasonably probable and legal alternative uses, found to be physically possible, appropriately supported, financially feasible, and which results in highest land value.

The definition immediately above applies specifically to the highest and best use of land. It is to be recognized that in cases where a site has existing improvements on it, the highest and best use may very well be determined to be different from the existing use. The existing use will continue, however, unless and until land value in its highest and best use exceeds the total value of the property in its existing use. See Interim Use.

Implied within these definitions is recognition of the contribution of that specific use to community environment or to community development goals in addition to wealth maximization of individual property owners. Also implied is that the determination of highest and best use results from the appraiser's judgment and analytical skill, i.e., that the use determined from analysis represents an opinion, not a fact to be found. In appraisal practice, the concept of highest and best use represents the premise upon which value is based. In the context of most probable selling price (market value) another appropriate term to reflect highest and best use would be most probable use. In the context of investment value an alternative term would be most profitable use.

Source: Byrl N. Boyce, Real Estate Appraisal Terminology, Revised Edition, AIREA, SREA, Ballinger, Cambridge, Mass., 1981, p. 107-108.

FEASIBILITY OF ALTERNATIVE USES

	<u>Scenario 1</u>	<u>Scenario 2</u>	<u>Scenario 3</u>	<u>Scenario 4</u>	<u>Scenario 5</u>	<u>Scenario 6</u>
<u>Feasibility Factor</u>	<u>Return to Former Use</u>	<u>Purchase by Welfare Agency</u>	<u>Conversion to Class B/C Office</u>	<u>Conversion to Apartments with Office on 1st Floor</u>	<u>Conversion to Apartments with Existing Bar</u>	<u>Demolition and Sale of Site</u>
Market Demand Risks	Demand very elastic relative to price unless room rates subsidized by welfare agencies	Welfare agencies lack capital resources to purchase and remodel facilities, given the absence of government funding	Office market becoming more price sensitive; would not accept neighborhood and lack of parking unless rents were lower than necessary to support remodeling	Strong demand for spacious two bedroom units in CBD area	Though there is a strong demand for affordable downtown housing, consumer survey shows tenant reluctance to live above noisy/potentially malodorous bar-restaurant	Soft market for vacant sites which cannot be assembled into larger plot-tage; parking revenues from 20 spaces inadequate to carry clearance costs
Legal/Political Acceptability	Inconsistent with long term City goals for Olin Place	Mixed acceptability as interim use as housing for transient sales by some groups; favored by welfare advocates and disfavored by local residents	Neighborhood resistance to increased demand for street parking	Preferred use, given need for downtown housing and political statements by alderpersons for reduction of bar business in residential neighborhoods	Preferred use for housing is compromised by existing bar management agreement	Inconsistent with constituency favoring landmark designation
Technical Construction Problems and Capital Cost Risks	Failure to repair within one year may have jeopardized grandfathered non-conforming building conditions. Otherwise this use has lowest construction risks of Scenarios 1 through 5	Capital costs of renovation to state standards excessive for short term use	Variance needed for parking requirement of 1 stall per 300 SF to 1 stall per 2,500 SF of office space	Spacious apartments with views provide favorable rent/cost per SF ratio--housing code creates more remodeling risk than commercial code	Apartment mix cheapened by retaining existing bar operation--smaller units require more plumbing and bring less favorable rent/cost per SF ratio	None
Relative Investment Power Based Upon Revenue Generation Potential	\$192,765	\$120,380	\$80,331	\$103,220	(\$10,513)	\$13,778
Special Income Tax Advantages or Public Subsidies Available	None	None	Rehabilitation tax credit of 20% for older commercial building conversion plus possible industrial bond financing	Possible historic landmark status for 25% rehabilitation tax credit plus tax incremental financing (TIF) assistance	Possible historic landmark status for 25% rehabilitation tax credit. TIF less likely because increase in tax is smaller	None
Real Estate Tax Consequences to City	Modest increase in assessed value	Loss of \$194,300 tax base with tax-exempt agency as owner	Real estate tax base would be multiplied approximately 3 times the present assessment	Real estate tax base would be multiplied approximately 3 1/2 times the present assessment	Real estate tax base would be multiplied approximately 2 1/2 times the present assessment	Loss of approximately \$140,000 of tax base

EXHIBIT 6

EXHIBIT 7

**DEMONSTRATION OF SELECTION OF BEST USE SCENARIO FOR
VACANT OFFICE TOWER REQUIRING
COMPLETE MECHANICAL RENOVATION**

B. Alternative Uses for Private Square

A combination of the physical characteristics of the property and the general demand characteristics of the Hilldale area suggest the following alternative scenarios for use of the subject property (Appendix D):

Scenario #1: The building would be remodeled into multi-tenant office space of class A on floors 4 to 14 and class B on floors 1 to 3.

Scenario #2: The building would be modified into residential apartments on floors 4 to 14 and class B office space on floors 1 to 3.

Scenario #3: The building would be modified into residential condominiums on floors 4 to 14 and class B office space on floors 1 to 3.

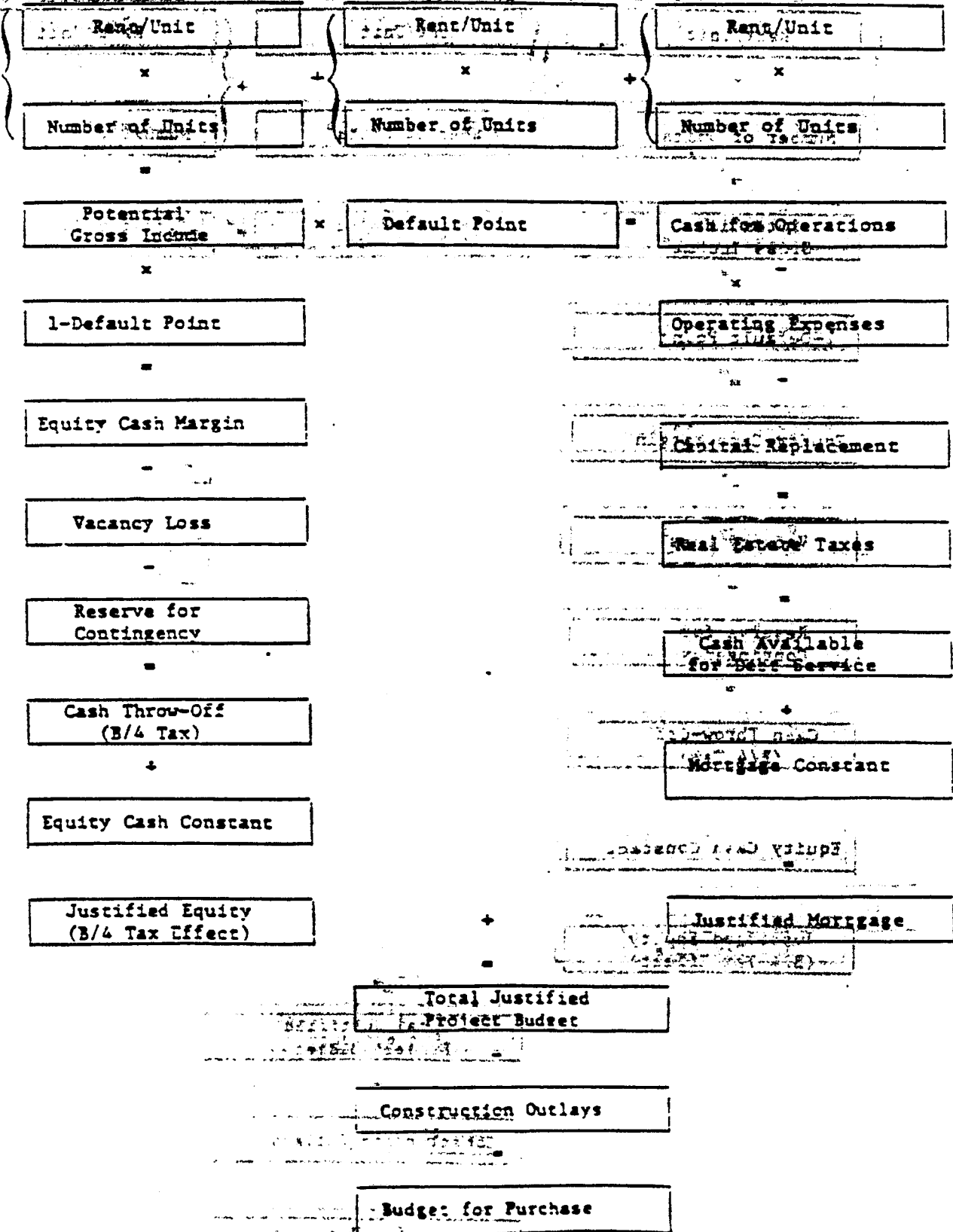
Scenario #4: The building would be modified into a hotel facility with hotel rooms on floors 4 to 14, a restaurant on floor 3, and seminar and office space on the remainder.

C. Economic Ranking of Alternatives

The alternative uses that might be plausible for the subject property can first be ranked in terms of the general budget parameters inherent in revenues and expenses for each. The best financial alternatives must then be screened for effective demand, political acceptability, and risk. In order to reveal the general range of justified investment on the existing property, the appraiser developed a logic of converting rents to justified investment by determining a market rent for each use and assuming an acceptable cash breakeven point¹ for financial planning and budgeting. This process capitalizes funds available for debt service or cash dividends into amounts of justified investment. This residual approach can be misleading if there are small errors in the cash-flow forecast, but if estimating bias is consistent when applied to the alternative uses, it does rank the alternatives in terms of their ability to pay for the subject property as is. The logic of this process is provided in Exhibit 15; the cost assumptions and calculations are provided in Appendix D.

¹ The ratio of cash expenses, real estate taxes, and debt service to potential gross income.

BASIC LOGIC FOR RANKING ALTERNATIVE PROGRAM SCENARIOS BY JUSTIFIED PROJECT PURCHASE BUDGET



A summary of these calculations from the Appendix are provided in Exhibit 16. A preliminary ranking based on a cash-justified investment (Line 3, Exhibit 16), without regard to future reversion value, demonstrates that Scenario 1 is the preferable use of the structure as is.

D. Ranking of Alternatives

In terms of estimating risks, Scenario 1 offers more certainty in regard to construction budget because multi-tenant office use is more similar to the previous use. Less extensive remodeling plans imply that fewer problems will arise. In Scenarios 2, 3, and 4, all new plumbing facilities and windows are required for floors 4 to 14. The same improvements simply need refurbishing if the building remains office use. In addition, the market for a high-rise residential or hotel facility is largely untested in the Hilldale area, but office use has been expanding. A change from office use of Pyare Square carries business risks that are difficult to ascertain, and the costs incurred in those risks could be great.

E. Political Compatibility of Alternatives

According to the village administrator of Shorewood Hills, all four of the scenarios would be politically acceptable because the village wants to see improvement of the building. However, Scenarios 2, 3, and 4 require a zoning change that must be approved by the village—an effort that is likely to be more time-consuming than futile.

Although condominiums are a relatively new idea to Shorewood Hills, the community boasts of being a residential suburb, and so a well-conceived plan should pass the board. A hotel use, however, is questionable and would be subject to serious scrutiny because demand is not evident. Office use appears to be most probable in light of the fact that costs are lower, zoning is proper, and demand is evident.

F. Conclusions

Since the estimated residual justified purchase prices of Scenarios 1 and 3 are fairly close, the choice in determining the most probable fitting use relates to the higher costs of converting to residential coupled with the risks involved in tapping an untested market. A prudent investor would seek to stabilize his income by choosing the less speculative scenario. A review of the summary feasibility data in Exhibit 17 supports the conclusion that the most probable use of the subject property in the opinion of the appraiser is Scenario 1.

The most probable use of the subject property would be renovation to a multi-tenant office building.

EXHIBIT 16

SUMMARY OF BUDGETS FOR ALTERNATIVE USE SCENARIOS

Budget Item	Scenario #1	Scenario #2	Scenario #3	Scenario #4
1. Cost to construct	(2,509,975)	(2,414,225)	(2,668,140)	(2,569,600)
2. Justified investment for property as is	2,897,566	1,409,513	2,868,983	(4,662,172)
3. Total justified investment in subject property as is	387,591	(1,004,712)	200,843	(7,231,772)

EXHIBIT 7 (Continued)

EXHIBIT 17

SUMMARY MATRIX OF FEASIBILITY OF ALTERNATIVE USES

Feasibility Factor	Scenario #1	Scenario #2	Scenario #3	Scenario #4
Justified Investment in subject	387,600	Negative	200,843	Negative
Remodeling Risks	Moderate	Significant	Significant	Serious
Effective Market demands	Positive	Positive	Questionable	Soft
Political acceptability	Strong	Strong	Strong	Mixed
Financial Risk	Depends on marketing ability in projecting new image for the building	Depends on desire to live in a high-rise	Depends on desire to own a home in a high-rise	Financial risk is great-- Hilldale is not a major office center nor a stop for travellers.

EXHIBIT 7 (Continued)

CONTEMPORARY ISSUES AND METHODS FOR
APPRAISING COMMERCIAL PROPERTIES
(Continued)

11. DECISION THEORY AND IMPROVED METHODS FOR THE
MARKET COMPARISON APPROACH

There are a number of basic books on decision theory which the appraiser should read to better understand alternative appraisal models available in the age of the micro computer. One such book is The Complete Problem Solver, by John R. Hayes, Franklin Institute Press, Philadelphia, PA, 1981. It is useful to look at the problem of market comparison approaches to value as a decision model in the complex world where a limited number of facts have to be focused on the problem.

- A. Hayes described four general types of decisions which require different decision procedures.
 1. Decisions under certainty
 2. Decisions under risk
 3. Decisions under uncertainty
 4. Decisions under conflict
- B. Many appraisal decision systems are modeled under the methods in Exhibit 8. (Page 157)
- C. Hayes distinguishes between risk where we can calculate probability, such as gambling, or uncertainty where there is an element of chance which can't be calculated. Decisions under conflict are like moves in chess or strategy where the outcome must anticipate countermoves by other players in the game. Appraisal pricing decisions are either decisions under certainty or decisions under conflict. Between sharp distinctions for risk and uncertainty, there is a broad area in which we operate under judgmental probability.
- D. A guide for the bewildered decisionmaker can be found by answering the following questions relative to the decision tree in Exhibit 9.

1. Is this a decision under certainty?
 2. Does it involve costly search?
 3. Is this a decision under conflict?
 4. Can you estimate the relevant probabilities with reasonable accuracy?
 5. Does the decision involve catastrophic outcomes?
- E. Appraisal decision theory for economic behavior fits the theory of "bounded rationality" which describes economic decision processes today. A short definition of bounded rationality is included in Exhibit 10.
- F. Market inference is the preferred method of valuation if we can discover a pricing pattern in the random dots of properties and transactions. The search for pattern must also be consistent with appraisal protocol.
1. Valuation directly from a regression formula violates appraisal protocol if the appraiser has not inspected all of the comparables used, because the subject property is compared to a hypothetical mean property from the set of observations, and because the appraiser is not directly responsible for the selection or weights given the attributes selected as the basis of comparison. Moreover, the amount of data points were limited relative to the number of variables which were thought to be relevant so that the risk characteristic of statistical variance were also suspect.
 2. Market comparison is set theory using a limited number of subjectively selected properties in a relatively objective comparison on a few factors thought to be highly correlated to prices paid. An additive weighting system is one method for managing the information integration for a market comparison.

- G. One influential method is to develop a pricing algorithm which provides an estimated price for each comparable and then presumes the same algorithm can be applied to the subject property. The steps involved are as follows:
1. Adjust prices for terms of sale and time on comparable properties. Comparable properties would be those bought for renovation, or for the owners own use, etc. You may choose to abstract out land values where size or locational quality is significantly different.
 2. Selecting a proper unit of comparison
 3. Developing a hierarchy of significant attributes thought to affect price and scoring each property on a point system
 4. Developing a weighting system to rank the relative importance of ordinal attribute scores on a cardinal scale
 5. Developing a price per weighted point per unit of comparison
 6. Testing the price weighting formula for best estimate of the sales price of actual comparables in order to minimize dispersion and variance between actual price and price estimated by formula
 7. Application of a price per point formula to the subject property to estimate range of alternative prices
 8. Adjustment of predicted price for unique externalities such as land, financing, or non-transferable license
- H. Search for an appropriate unit of comparison as a single variable in a linear regression by trying three or four unit concepts, such as: (See Exhibit 11.)
1. Gross building area
 2. Net leasable area

3. Cubage
 4. Two times the first floor area plus gross building area
 5. Barrels of cranberries rather than acres of cranberries
 6. Number of bedrooms rather than square feet
- I. Arrive at a price per unit as the first step in establishing a price algorithm
- J. Identify property attributes which distinguish subject properties qualitatively from one another and develop a simple scoring system
1. 5-3-1 is one method, but scores may become multipliers and lead distortion
 2. Dilmore prefers:

<u>Rating</u>	<u>Points</u>
Excellent	26
Good	20
Average	15
Fair	13
Poor	10
- K. See selection of examples in Exhibits 11 through 24.
- L. The market comparison approach presumes that the appraiser can match sales price to the real estate interest required and the productivity anticipated by the buyer and the seller or that differences in each transaction can be factored out.
1. Litigation always involves kid stuff arguments involving gross rent multipliers where rents include or exclude utilities, furnishings, and window air conditioners.
 2. In recent years cash equivalency adjustments for seller financing have further distorted the growth or adjusted sales price.

3. More subtle are the sales prices which are engineered by accountants and lawyers to shift asset values among asset classifications for land, structure, inventory, control of management contracts, accounting periods for related parties for tax purposes, public accounting figures, or balance sheet diplomacy.
 4. The public is further confused by engineered sales prices to support syndication prospecti of \$90 million on a single office building which was also appraised for \$35 million in the same month for taxes.
 5. Market comparable sales are suspect when one party names the price if the other names the terms; the appraiser has adapted his style so that the customer names the value and the appraiser gets to define the real estate interests appraised and the limiting conditions which control the relevancy and reality of his report.
 6. Discounted cash flows defined by proper accounting become a more sensitive and more realistic appraisal tool than the market comparison method.
- M. The traditional normalized net operating income divided by the cap rate should be recognized as a market comparison approach of the income multiplier family. There are imaginary "cap rates" out there, the reciprocals of price earnings ratios, which benchmark prices, but should not be confused with a true income approach.
1. Appraisers must be careful not to confuse thumbnail benchmarks for valuation procedures and never confuse market multipliers with contemporary income simulation methods.
 2. There is a danger that appraisers use street talk and conventional wisdom as a market determined rate as in "Phoenix is a 9 percent cap rate town, or "Indianapolis has a net income multiplier of 9-1/2." These are applied without sensitivity to differences among properties or sensitivity to present values.

EXHIBIT 8

DECISION MAKING METHODS
UNDER CERTAINTY

Method	Type	Use this method:	Cost of computation required	Number of alternatives examined
Dominance	optimizing	for preliminary screening of alternatives	low	all
Lexicography	optimizing	when attributes are very different in weight	very low	all
Additive Weighting	optimizing	when it is important to find the best alternative	high	all
Effectiveness Index	optimizing	when it is <i>very</i> important to get best alternative	very high	all
Satisficing	non-optimizing	when the cost of examining the whole set of alternatives is very high	very low	some

Source: John R. Hayes, The Complete Problem Solver, 1981, The Franklin Institute Press, Philadelphia, PA, p. 157.

EXHIBIT 9

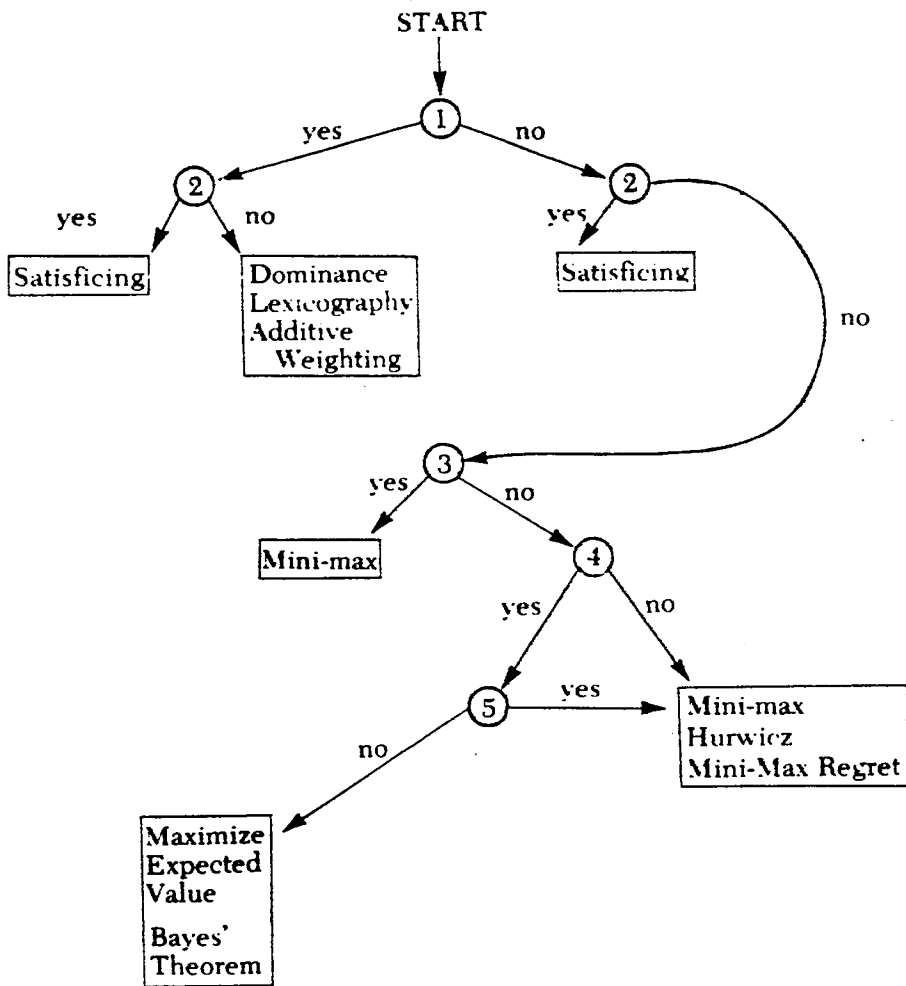


Figure 2. A Decision Tree for Choosing a Decision Procedure

Source: John R. Hayes, The Complete Problem Solver, 1981,
The Franklin Institute Press, Philadelphia, PA, p. 180.

EXHIBIT 11
CORRELATION COEFFICIENTS AND R² OF SALES PRICE

Space Unit	Correlation	R ²
First floor frontage (frc)	0.745	55.5%
Lot area	0.908	82.4
First floor (1st fl)	0.790	62.4
First floor + Upper floors (upp fl)	0.933	87.0
1st fl + .05 (upp fl)	0.919	84.5
2(1st fl) + upp fl	0.919	84.5
(1st fl) x (frc)	0.784	61.5
[1st fl + 0.5 (upp fl)] x (frc)	0.864	74.6
[2(1st fl) + upp fl] x (frc)	0.864	74.6
(1st fl + upp fl) x (frc)	0.874	76.4

RATGRAM STYLE

WOOLWORTH BUILDING
 SCALE FOR SCORING COMPARABLES ON
 IMPORTANT INVESTOR CONSIDERATIONS FOR
 OFFICE - RETAIL SPACE IN MADISON
 C-4 ZONING

LOCATION
 10%

5 = High visibility
 3 = Corner visibility limited
 1 = Inside lot

EXPANSION POTENTIAL
 30%

5 = Potential for significant
 increases of floor space
 3 = Flexible layouts due to
 bay spacing and elevator
 position
 1 = Inflexibility of layout due
 to old bearing walls and
 elevator shafts

CONDITION AT
 TIME OF PURCHASE
 25%

5 = Fully renovated and leased
 3 = Long-term retail leases in
 place. Serviceable as retail
 in tired space.
 1 = Vacant and in need of total
 rehabilitation. Short-term
 lease or large vacancy in
 need of total rehabilitation.

ELEVATORS AT
 TIME OF PURCHASE
 20%

5 = Two passenger and freight
 3 = Two passenger
 1 = One passenger

FENESTRATION ON UPPER LEVEL
 15%

5 = Large windows facing
 the Square
 3 = Limited window area
 1 = No windows

WOOLWORTH BUILDING
 WEIGHTED MATRIX FOR COMPARABLE PROPERTIES
 SCORE/WEIGHTED SCORE

ATTRIBUTE	WEIGHT	COMPARABLE NO. 1 30 N. CARROLL WOLFF KUBLY	COMPARABLE NO. 2 14 W. HIFFLIN	COMPARABLE NO. 3 5 & 7 E. HIFFLIN CENTRE SEVEN	COMPARABLE NO. 4 50 E. HIFFLIN EMPORIUM	COMPARABLE NO. 5 2 W. HIFFLIN WOOLWORTH	SUBJECT
LOCATION	10%	3/0.30	1/0.10	1/0.10	3/0.30	5/0.50	5/0.50
EXPANSION POTENTIAL AT TIME OF SALE	30%	3/0.90	1/0.30	1/0.30	5/1.50	3/0.90	3/0.90
CONDITION AT TIME OF SALE	25%	1/0.25	5/1.25	1/0.25	3/0.75	3/0.75	1/0.25
ELEVATORS IN PLACE	20%	5/1.00	3/0.60	1/0.20	3/0.60	1/0.20	1/0.20
FENESTRATION ON UPPER FLOORS	15%	1/0.15	5/0.75	5/0.75	1/0.15	3/0.45	3/0.45
TOTAL WEIGHTED SCORE	100%	2.60	3.00	1.60	3.30	2.80	2.30
ADJUSTED SELLING PRICE (1)		\$625,000	\$750,000	\$240,000	\$850,000	\$662,500	
DATE OF SALE		7/17/80	2/27/84	12/31/77	4/30/78	7/31/78	
GROSS BUILDING AREA (GBA)		41,000 SF	40,000 SF	26,000 SF	42,500 SF	39,000 SF	39,000 SF
ADJUSTED PRICE/GBA		\$15.24	\$18.75	\$ 9.23	\$20.00	\$16.99	
ADJUSTED PRICE/GBA/ WEIGHTED POINT SCORE		\$5.86	\$6.25	\$5.77	\$6.06	\$6.08	

(1) See Appendix _ for assumptions and calculations to determine adjusted selling price.

EXHIBIT 13
RATGRAM STYLE

Attributes = 5

Attribute Names, Prelim. Weights
LOCATION 20
EXPANSION POTENTIAL 20
CONDITION AT TIME OF SALE 20
ELEVATORS IN PLACE 20
PENESTRATION ON UPPER FLOORS 20

of Observations = 5

Observ. # 1 WOLFF-KUBLY-30 N. CARROLL Price 19.36
 LOCATION 3
 EXPANSION POTENTIAL 3
 CONDITION AT TIME OF SALE 1
 ELEVATORS IN PLACE 5
 PENESTRATION ON UPPER FLOORS 1

Observ. # 2 14th S. HIFFLIN Price 18.75
 LOCATION 1
 EXPANSION POTENTIAL 1
 CONDITION AT TIME OF SALE 5
 ELEVATORS IN PLACE 3
 PENESTRATION ON UPPER FLOORS 5

Observ. # 3 CENTRE SEVEN-S & 7 N. PINCKNEY Price 9.23
 LOCATION 1
 EXPANSION POTENTIAL 1
 CONDITION AT TIME OF SALE 1
 ELEVATORS IN PLACE 1
 PENESTRATION ON UPPER FLOORS 5

Observ. # 4 EMPORIUM-50 E. HIFFLIN Price 20
 LOCATION 3
 EXPANSION POTENTIAL 5
 CONDITION AT TIME OF SALE 3
 ELEVATORS IN PLACE 3
 PENESTRATION ON UPPER FLOORS 1

Observ. # 5 WOOLWORTH-2 W. HIFFLIN Price 16.99
 LOCATION 5
 EXPANSION POTENTIAL 3
 CONDITION AT TIME OF SALE 3
 ELEVATORS IN PLACE 1
 PENESTRATION ON UPPER FLOORS 3

The Matrix:

20	20	20	20	20
10	10	10	10	10
15	15	15	15	15
25	25	25	25	25
30	30	30	30	30

Median = 5.861538
 Mean = 5.913963
 Standard Deviation = .5837666

Weights:
 LOCATION = 20
 EXPANSION POTENTIAL = 20
 CONDITION AT TIME OF SAL = 20
 ELEVATORS IN PLACE = 20
 PENESTRATION ON UPPER FL = 20

Final Results:
 Number of Combinations = 3125
 Number of Combinations Adding to 100X = 381

Median = 6.060606
 Mean = 6.00175
 Standard Deviation = .1893679

Weights:
 LOCATION = 10
 EXPANSION POTENTIAL = 30
 CONDITION AT TIME OF SAL = 25
 ELEVATORS IN PLACE = 20
 PENESTRATION ON UPPER FL = 15

WOOLWORTH - RATGRAM STYLE
2nd RUN

Attributes = 5

Attribute Names, Prelim. Weights

- LOCATION 20
- EXPANSION POTENTIAL 20
- CONDITION AT TIME OF SALE 20
- ELEVATORS IN PLACE 20
- PENESTRATION ON UPPER FLOORS 20

of Observations = 5

Observ. # 1 WOLFF-KUEBLY-30 N. CARROLL Price 15.26

- LOCATION 3
- EXPANSION POTENTIAL 3
- CONDITION AT TIME OF SALE 1
- ELEVATORS IN PLACE 5
- PENESTRATION ON UPPER FLOORS 1

Observ. # 2 14 W. MIFFLIN Price 18.75

- LOCATION 1
- EXPANSION POTENTIAL 1
- CONDITION AT TIME OF SALE 5
- ELEVATORS IN PLACE 3
- PENESTRATION ON UPPER FLOORS 5

Observ. # 3 CENTRE SEVEN-5 & 7 N. PINKNEY Price 9.23

- LOCATION 1
- EXPANSION POTENTIAL :
- CONDITION AT TIME OF SALE 1
- ELEVATORS IN PLACE :
- PENESTRATION ON UPPER FLOORS 5

Observ. # 4 EMPORIUM-50 E. MIFFLIN Price 20

- LOCATION 3
- EXPANSION POTENTIAL 5
- CONDITION AT TIME OF SALE 3
- ELEVATORS IN PLACE 3
- PENESTRATION ON UPPER FLOORS 1

Observ. # 5 WOOLWORTH-2 W. MIFFLIN Price 16.99

- LOCATION 5
- EXPANSION POTENTIAL 3
- CONDITION AT TIME OF SALE 3
- ELEVATORS IN PLACE 1
- PENESTRATION ON UPPER FLOORS 3

The Matrix:

10	30	25	20	15
0	20	15	10	5
5	25	20	15	10
15	35	30	25	20
20	40	35	30	25

Median = 6.060606
 Mean = 6.00175
 Standard Deviation = .1893479

Weights:

- LOCATION = 10
- EXPANSION POTENTIAL = 30
- CONDITION AT TIME OF SAL = 25
- ELEVATORS IN PLACE = 20
- PENESTRATION ON UPPER PL = 15

Final Results:

Number of Combinations = 3125
 Number of Combinations Adding to 100% = 381

Median = 6.060606
 Mean = 6.00175
 Standard Deviation = .1893479

Weights:

- LOCATION = 10
- EXPANSION POTENTIAL = 30
- CONDITION AT TIME OF SAL = 25
- ELEVATORS IN PLACE = 20
- PENESTRATION ON UPPER PL = 15

EXHIBIT 15

WOOLWORTH - RATGRAM STYLE

CALCULATION OF MOST PROBABLE PRICE USING
MEAN PRICE PER POINT EQUATION METHOD

COMPARABLE PROPERTY	SELLING PRICE PER SF OF GBA	POINT SCORE	PRICE PER SF OF GBA/ TOTAL WEIGHTED SCORE (x)
1	\$15.24	2.60	\$5.86
2	18.75	3.00	6.25
3	9.23	1.60	5.77
4	20.00	3.30	6.06
5	16.99	2.80	<u>6.08</u>
TOTAL			<u>\$30.02</u>

Total of Price Per SF of GBA = \$30.02
Total Weighted Score

Mean Value (\bar{x}) = 30.02/5 = \$6.00

Standard Deviation = $\sqrt{\frac{\sum (x-\bar{x})^2}{n-1}}$ = \$0.19 where:

x	\bar{x}	$(x-\bar{x})$	$(x-\bar{x})^2$	n	n-1
\$5.86	\$6.00	= -\$0.14	0.0196	5	4
6.25	6.00	= 0.25	0.0625		
5.77	6.00	= - 0.23	0.0529		
6.06	6.00	= 0.06	0.0036		
6.08	6.00	= 0.08	<u>0.0064</u>		
			0.1450		

$$\sqrt{\frac{0.1450}{4}} = \sqrt{0.03625} = 0.190394 \text{ or } \$0.19$$

EXHIBIT 15 (Continued)

Value Range of Price/Point Score: $\$6.00 \pm \0.19

Since GBA of subject is 39,000 square feet and total weighted point score of subject is 2.3, then:

High
Estimate: $\$6.19 \times 2.3 \times 39,000 \text{ SF} = \$555,243 \text{ or } \$560,000$
($\$14.23/\text{SF}$)

Central
Tendency: $\$6.00 \times 2.3 \times 39,000 \text{ SF} = \$538,200 \text{ or } \$540,000$
($\$13.80/\text{SF}$)

Low
Estimate: $\$5.81 \times 2.3 \times 39,000 \text{ SF} = \$521,159 \text{ or } \$520,000$
($\$13.36/\text{SF}$)

JUSTIFICATION OF COMPARABLE PRICE FORMULA FOR
 WOOLWORTH BUILDING
 BY MEANS OF ANALYSIS OF VARIANCE OF ACTUAL SALE PRICE VS. PREDICTED PRICE
 OF COMPARABLES USING MEAN PRICE PER POINT EQUATION METHOD

NO.	COMPARABLE PROPERTY	WEIGHTED POINT SCORE	MEAN PRICE PER POINT SCORE	PREDICTED PRICE/ SF GBA	ACTUAL PRICE/ SF GBA	VARIANCE	\$ OF VARIANCE TO ACTUAL PRICE
1	WOLFF KUBLY 30 N. Carroll Street	2.60	66.00	\$15.60	\$15.24	\$ 0.36	2.41
2	14 W. Hifflin Street	3.00	6.00	18.00	18.75	- 0.75	4.0
3	CENTRE SEVEN 5 & 7 N. Pinckney Street	1.60	6.00	9.60	9.23	0.37	4.0
4	DIPORTUM 50 E. Hifflin Street	3.30	6.00	19.80	20.00	- 0.20	1.0
5	WOOLWORTH 2 W. Hifflin Street	2.80	6.00	16.80	16.99	- 0.19	1.1
NET VARIANCE						\$ - 0.41	

RATGUM STYLE

EXHIBIT 16

WOOLWORTH BUILDING
 SCALE FOR SCORING COMPARABLES ON
 IMPORTANT INVESTOR CONSIDERATIONS FOR
 OFFICE - RETAIL SPACE IN MADISON
 C-4 ZONING
 DILMORE STYLE

LOCATION
 15%

26 = High visibility
 15 = Corner visibility limited
 10 = Inside lot

EXPANSION POTENTIAL
 30%

26 = Potential for significant
 increases of floor space
 15 = Flexible layouts due to
 bay spacing and elevator
 position
 10 = Inflexibility of layout due
 to old bearing walls and
 elevator shafts

CONDITION AT
 TIME OF PURCHASE
 40%

26 = Fully renovated and leased
 15 = Long-term retail leases in
 place. Serviceable as retail
 in tired space.
 10 = Vacant and in need of total
 rehabilitation. Short-term
 lease or large vacancy in
 need of total rehabilitation.

ELEVATORS AT
 TIME OF PURCHASE
 15%

26 = Two passenger and freight
 15 = Two passenger
 10 = One passenger

WOOLWORTH BUILDING
 WEIGHTED MATRIX FOR COMPARABLE PROPERTIES
 SCORE/WEIGHTED SCORE
 DILMORE STYLE

ATTRIBUTE	WEIGHT	COMPARABLE NO. 1 30 N. CARROLL WOLFF KUBLY	COMPARABLE NO. 2 14 W. HIFFLIN	COMPARABLE NO. 3 5 & 7 E. HIFFLIN CENTRE SEVEN	COMPARABLE NO. 4 50 E. HIFFLIN EMPORIUM	COMPARABLE NO. 5 2 W. HIFFLIN WOOLWORTH	SUBJECT
LOCATION	15%	15/2.25	10/1.50	10/1.50	15/2.25	26/3.90	26/3.90
EXPANSION POTENTIAL AT TIME OF SALE	30%	15/4.50	10/3.00	10/3.00	26/7.80	15/4.50	15/4.50
CONDITION AT TIME OF SALE	40%	10/4.00	26/10.40	10/4.00	15/6.00	15/6.00	10/4.00
ELEVATORS IN PLACE	15%	26/3.90	15/2.25	10/1.50	15/2.25	10/1.50	10/1.50
TOTAL WEIGHTED SCORE	100%	14.65	17.15	10.00	18.30	15.90	13.90
ADJUSTED SELLING PRICE (1)		\$625,000	\$750,000	\$240,000	\$850,000	\$662,500	
DATE OF SALE		7/17/80	2/27/84	12/31/77	4/30/78	7/31/78	
GROSS BUILDING AREA (GBA)		41,000 SF	40,000 SF	26,000 SF	42,500 SF	39,000 SF	39,000 SF
ADJUSTED PRICE/GBA		\$15.24	\$18.75	\$ 9.23	\$20.00	\$16.99	
ADJUSTED PRICE/GBA • WEIGHTED POINT SCORE		\$1.04	\$1.09	\$0.92	\$1.09	\$1.07	

(1) See Appendix _ for assumptions and calculations to determine adjusted selling price.

WOOLWORTH - DILMORE STYLE
1st RUN

Attributes = 5

Attribute Names: Prelim. Weights

- LOCATION 20
- EXPANSION POTENTIAL 20
- CONDITION AT TIME OF SALE 20
- ELEVATORS IN PLACE 20
- FENESTRATION ON UPPER FLOORS 20

of Observations = 5

- Observ. # 1 WOLFF-KUBLY Price 15.26
 - LOCATION 15
 - EXPANSION POTENTIAL 15
 - CONDITION AT TIME OF SALE 10
 - ELEVATORS IN PLACE 26
 - FENESTRATION ON UPPER FLOORS 10
- Observ. # 2 14 W. MIFFLIN Price 18.75
 - LOCATION 10
 - EXPANSION POTENTIAL 10
 - CONDITION AT TIME OF SALE 26
 - ELEVATORS IN PLACE 15
 - FENESTRATION ON UPPER FLOORS 26
- Observ. # 3 CENTRE SEVEN Price 9.23
 - LOCATION 10
 - EXPANSION POTENTIAL 10
 - CONDITION AT TIME OF SALE 10
 - ELEVATORS IN PLACE 10
 - FENESTRATION ON UPPER FLOORS 26
- Observ. # 4 EMPORIUM Price 20
 - LOCATION 15
 - EXPANSION POTENTIAL 26
 - CONDITION AT TIME OF SALE 15
 - ELEVATORS IN PLACE 15
 - FENESTRATION ON UPPER FLOORS 10
- Observ. # 5 WOOLWORTH Price 16.99
 - LOCATION 26
 - EXPANSION POTENTIAL 15
 - CONDITION AT TIME OF SALE 15
 - ELEVATORS IN PLACE 10
 - FENESTRATION ON UPPER FLOORS 15

The Matrix:

20	20	20	20	20
10	10	10	10	10
15	15	15	15	15
25	25	25	25	25
30	30	30	30	30

Median = 1.048745
 Mean = 1.012559
 Standard Deviation = .1756356

Weights:

- LOCATION = 20
- EXPANSION POTENTIAL = 20
- CONDITION AT TIME OF SALE = 20
- ELEVATORS IN PLACE = 20
- FENESTRATION ON UPPER FL = 20

Final Results:

Number of Combinations = 3125
 Number of Combinations Adding to 100% = 381

Median = 1.068553
 Mean = 1.024281
 Standard Deviation = .1314307

Weights:

- LOCATION = 15
- EXPANSION POTENTIAL = 30
- CONDITION AT TIME OF SALE = 30
- ELEVATORS IN PLACE = 15
- FENESTRATION ON UPPER FL = 10

Attributes = 5

WOOLWORTH - DILMORE STYLE
2nd RUN

Attribute Names, Profile, Weights

- LOCATION 30
- EXPANSION POTENTIAL 20
- CONDITION AT TIME OF SALE 20
- ELEVATORS IN PLACE 20
- PENETRATION ON UPPER FLOORS 20

of Observations = 5

- Observ. # 1 : WOLFF-KLEBY Price 15.24
 LOCATION 15
 EXPANSION POTENTIAL 15
 CONDITION AT TIME OF SALE 10
 ELEVATORS IN PLACE 26
 PENETRATION ON UPPER FLOORS 10
- Observ. # 2 14 W. HIFFLIN Price 18.75
 LOCATION 10
 EXPANSION POTENTIAL 10
 CONDITION AT TIME OF SALE 26
 ELEVATORS IN PLACE 15
 PENETRATION ON UPPER FLOORS 26
- Observ. # 3 CENTRE SEVEN Price 9.23
 LOCATION 10
 EXPANSION POTENTIAL 10
 CONDITION AT TIME OF SALE 10
 ELEVATORS IN PLACE 10
 PENETRATION ON UPPER FLOORS 26
- Observ. # 4 EMPORIUM Price 20
 LOCATION 15
 EXPANSION POTENTIAL 26
 CONDITION AT TIME OF SALE 15
 ELEVATORS IN PLACE 15
 PENETRATION ON UPPER FLOORS 10
- Observ. # 5 WOOLWORTH Price 16.99
 LOCATION 26
 EXPANSION POTENTIAL 15
 CONDITION AT TIME OF SALE 15
 ELEVATORS IN PLACE 10
 PENETRATION ON UPPER FLOORS 15

The Matrix:

15	30	30	15	10
5	20	20	5	0
10	25	25	10	5
20	35	35	20	15
25	40	40	25	20

Median = 1.048553
 Mean = 1.024281
 Standard Deviation = .1314307

Weights:
 LOCATION = 15
 EXPANSION POTENTIAL = 30
 CONDITION AT TIME OF SALE = 30
 ELEVATORS IN PLACE = 15
 PENETRATION ON UPPER FL = 10

Final Results:
 Number of Combinations = 3125
 Number of Combinations Adding to 100% = 381

Median = 1.048553
 Mean = 1.043607
 Standard Deviation = 7.084803E-02

Weights:
 LOCATION = 15
 EXPANSION POTENTIAL = 30
 CONDITION AT TIME OF SALE = 40
 ELEVATORS IN PLACE = 15

EXHIBIT 20

WOOLWORTH BUILDING
 CALCULATION OF MOST PROBABLE PRICE USING
 MEAN PRICE PER POINT EQUATION METHOD
 DILMORE STYLE

COMPARABLE PROPERTY	SELLING PRICE PER SF OF GBA	POINT SCORE	PRICE PER SF OF GBA/ TOTAL WEIGHTED SCORE (x)
1	\$15.24	14.65	\$1.04
2	18.75	17.15	1.09
3	9.23	10.00	0.92
4	20.00	18.30	1.09
5	16.99	15.90	<u>1.07</u>
TOTAL			\$5.21

Total of Price Per SF of GBA = \$5.21
Total Weighted Score

Mean Value (\bar{x}) = \$5.21 + 5 = \$1.04

Standard Deviation of the Mean = $\sqrt{\frac{\sum (x-\bar{x})^2}{n-1}}$ = \$0.07 where:

x	\bar{x}	(x- \bar{x})	$\frac{(x-\bar{x})^2}{n-1}$	n	n-1
\$1.04	\$1.04	= \$0.00	0.0000	5	4
1.09	1.04	= 0.05	0.0025		
0.92	1.04	= - 0.12	0.0144		
1.09	1.04	= 0.05	0.0025		
1.07	1.04	= 0.03	<u>0.0009</u>		
			0.0203		

$$\sqrt{\frac{0.0203}{4}} = \sqrt{0.005075} = 0.071239 \text{ or } \$0.07$$

EXHIBIT 20 (Continued)

Value Range of Price/Point Score: \$1.04 ± \$0.07

Since GBA of subject is 39,000 square feet and total weighted point score of subject is 13.90, then:

High
 Estimate: \$1.11 x 13.90 x 39,000 SF = \$601,731 or \$600,000
 (\$15.43/SF)

Central
 Tendency: \$1.04 x 13.90 x 39,000 SF = \$563,784 or \$560,000
 (\$14.46/SF)

Low
 Estimate: \$0.97 x 13.90 x 39,000 SF = \$525,837 or \$530,000
 (\$13.48/SF)

COMPARISON OF WOOLWORTH DEMONSTRATION -
 RATGRAM STYLE
 AND WOOLWORTH - DILMORE STYLE

	RATGRAM STYLE	DILMORE STYLE	% VARIANCE RATGRAM TO DILMORE
Estimated Value			
Central Tendency	\$540,000	\$560,000	3.7%

JUSTIFICATION OF COMPARABLE PRICE FORMULA FOR
 WOOLWORTH BUILDING
 BY MEANS OF ANALYSIS OF VARIANCE OF ACTUAL SALE PRICE VS. PREDICTED PRICE
 OF COMPARABLES USING MEAN PRICE PER POINT EQUATION METHOD
 DILMORE STYLE

NO.	COMPARABLE PROPERTY	WEIGHTED POINT SCORE	MEAN PRICE PER POINT SCORE	PREDICTED PRICE/ SF GBA	ACTUAL PRICE/ SF GBA	VARIANCE	% OF VARIANCE TO ACTUAL PRICE
1	WOLFF KUBLY 30 N. Carroll Street	14.65	\$1.04	\$15.24	\$15.24	\$ 0.00	0.0%
2	14 W. Mifflin Street	17.15	1.04	17.84	18.75	- 0.91	4.9
3	CENTRE SEVEN 5 & 7 N. Pinalney Street	10.00	1.04	10.40	9.23	1.17	12.7
4	EMPORIUM 50 E. Mifflin Street	18.30	1.04	19.03	20.00	- 0.97	4.9
5	WOOLWORTH 2 W. Mifflin Street	15.90	1.04	16.54	16.99	- 0.45	2.6
					NET VARIANCE	\$ - 1.16	

EXHIBIT 21

EXHIBIT 22

SCALE FOR SCORING COMPARABLE SALE ATTRIBUTES

Location 15%	5 = Corner lot with high visibility on major traffic artery 3 = Inside lot with low visibility on major traffic artery 1 = Inside lot with low visibility on secondary street
Investor Perception of Neighborhood Image 15%	5 = Strong identification with Square (within 1 block) or established commercial or residential area 3 = Neutral investor attitude 1 = General identification with deteriorated neighborhood
Structural Condition of Improvements 25%	5 = Fire-resistant construction, well maintained, operational, marketable 3 = Ordinary mill construction (brick bearing walls-wood beams), poorly maintained, needs mechanical work 1 = Boarded up and/or partially damaged or vandalized
Reuse Potential 30%	5 = Dominant commercial/retail reuse potential with anticipation of Landmark designation with 1981 tax laws applied 4 = Dominant commercial/retail reuse potential with anticipation of Landmark designation prior to 1981 tax law 3 = Residential reuse potential with 1981 tax laws applied 2 = Residential reuse potential prior to 1981 tax law 1 = Warehouse 0 = Improvements demolished leaving land only

EXHIBIT 22 (Continued)

Bargaining Position
of Seller
15%

- 5 = Income adequate to carry property or seller with strong asset position
- 3 = Little or no steady income but seller not known to be under financial pressures
- 1 = Building owner known to have financial pressures or multiple liens on property

WEIGHTED MATRIX FOR COMPARABLE PROPERTIES

FEATURE	WEIGHT	Rating/Weighted Rating							
		#1 Frautschi 215-219 King	#2 Sutherland Elec. 323 E. Wilson	#3 Fess Hotel 123 E. Doty	#4 Miller Horne 714 Williamson	#5 Miller Horne 722 Williamson	#6 Atrium 25 W. Finckney	#7 Old Sorority 10 Langdon	Cardinal Hotel SUBJECT
Location	15%	3/ .45	5/ .75	5/ .75	3/ .45	3/ .45	1/ .15	3/ .45	5/ .75
Investor Perception of Neighborhood Image	15%	3/ .45	3/ .45	5/ .75	1/ .15	1/ .15	5/ .75	5/ .75	1/ .15
Structural Condition of Improvements at Time of Sale	25%	3/ .75	5/1.25	1/ .25	5/1.25	5/1.25	3/ .75	1/ .25	1/ .25
Reuse Potential	30%	4/1.2	1/ .30	4/1.2	2/ .60	4/1.2	4/1.2	4/1.2	5/1.5
Bargaining Position of Seller	15%	<u>5/ .75</u>	<u>3/ .45</u>	<u>1/ .15</u>	<u>3/ .45</u>	<u>1/ .15</u>	<u>1/ .15</u>	<u>1/ .15</u>	<u>3/ .45</u>
Total Point Score		3.6	3.2	3.1	2.9	3.2	3.0	2.8	3.1

	#1 Frantschi 215-219 King	#2 Sutherland Elec. 323 E. Wilson	#3 Fess Hotel 123 E. Doty	#4 Miller Horne 714 Williamson	#5 Miller Horne 722 Williamson	#6 Atrium 25 W. Finckney	#7 Old Sorority 10 Langdon
Nominal Sale Price	\$320,000	\$165,000	\$120,000	\$148,000	\$300,000	\$150,000	\$91,000
Date of Sale	November 1978	July 1979	January 1975	January 1979	November 1981	April 1977	July 1981
Terms of Sale	Land contract \$50,000 - down 270,000 - 2 yrs 10% Year 1 6% Year 2	Cash to seller	Land contract	Land contract \$23,000 down 125,000 @ 9 3/4% - 5 years	Land contract	\$100,000 cash 50,000 seller 2nd subordinated to construction loan	Cash to seller
Adjustment for:							
Terms of Sale	Discount 10%	No adjustment	5% Finder's fee for \$320,000 construction loan	Reduce to \$140,000	Discount 20% for creative financing	Discount 2nd-20%	None
Time of Sale (5%/year from 1/1/79 on)	Appreciate 17.5%	Appreciate 15%	Appreciate 17.5%	Appreciate 17.5%	Appreciate 2.5%	Appreciate 17.5%	Appreciate 5%
Adjusted Price for Terms and Time	\$338,400	\$189,750	\$121,500	\$164,500	\$246,000	\$164,500	\$95,550
Land Area	21,728 SF	8,221 SF	8,712 SF	8,712 SF	17,424 SF	8,712 SF	6,720 SF
Adjustment for Land Area Differences @ \$5.00/SF	(\$108,640)	(\$41,105)	(\$43,560)	(\$43,560)	(\$87,120)	(\$43,560)	(\$33,600)
Adjusted Price less Allowance for Land Value	\$229,760	\$148,645	\$77,940	\$120,940	\$158,880	\$120,940	\$61,950
Gross Building Area (GBA) (Square Feet)	21,000 SF	17,790 SF	9,330 SF	28,000 SF	30,000 SF	16,060 SF	10,500 SF
Adjusted Price per Square Foot of GBA	\$10.94/SF of GBA	\$8.36/SF of GBA	\$8.35/SF of GBA	\$4.32/SF of GBA	\$5.30/SF of GBA	\$7.53/SF of GBA	\$5.90/SF of GBA
Total Point Score	3.6	3.2	3.1	2.9	3.2	3.0	2.8
Price per Square Foot/Point Score	\$3.04	\$2.61	\$2.69	\$1.49	\$1.66	\$2.51	\$2.11

EXHIBIT 22 (Continued)

EXHIBIT 22 (Continued)

CALCULATION OF MOST PROBABLE PRICE USING
MEAN PRICE PER POINT EQUATION METHOD

Comparable Property	Adjusted Selling Price per SF of GBA	Weighted Point Score	$\frac{\text{Price per SF}}{\text{Weighted Point Score}}$ (x)
1	\$10.94	3.6	\$3.04
2	8.36	3.2	2.61
3	8.35	3.1	2.69
4	4.32	2.9	1.49
5	5.30	3.2	1.66
6	7.53	3.0	2.51
7	5.90	2.8	<u>2.11</u>
TOTAL			\$16.11

Central Tendency = $\frac{\sum x}{n} = \frac{16.11}{7} = 2.30$

Dispersion = $\sqrt{\frac{\sum (x-\bar{x})^2}{(n-1)}} = \sqrt{\frac{1.9417}{6}} = .569$

where:

x	\bar{x}	$(x-\bar{x})$	$(x-\bar{x})^2$	n	n-1
3.04	2.30	= .74	.5476	7	6
2.61	2.30	= .31	.0961		
2.69	2.30	= .39	.1521		
1.49	2.30	= .81	.6561		
1.66	2.30	= .64	.4096		
2.51	2.30	= .21	.0441		
2.11	2.30	= .19	.0361		
$\sum (x-\bar{x})^2$			= 1.9417		

EXHIBIT 22 (Continued)

Value range: $x \pm \text{dispersion} = 2.30 \pm .57$

Gross Weighted
Building x Point x (Central Tendency \pm Dispersion) =
Area Score

17,900 SF x 3.1 x (2.30 \pm .57) =

High Estimate of \$159,256 or \$160,000

Central Tendency of \$127,627 or \$130,000

Low Estimate of \$95,998 or \$100,000

All value estimates are rounded

EXHIBIT 23

COMPUTER OUTPUT OF DILMORE QUANTITATIVE
POINT WEIGHTING PROGRAM
AND
COMPUTERIZATION OF
ALL OF THE MARKET COMPARISON
CALCULATIONS

EXHIBIT 23 (Continued)

**** GOODWILL 3 ****

* Attributes = 5

Attribute Names, Prelim. Weights ← Preliminary weights selected by the appraisers

GROSS BUILDING AREA (GBA) 20

LOCATION 20

RATIO OF LAND TO GBA 20

EFFICIENCY OF BUILDING DESIGN FOR STORAGE AND DISTRIBUTION 20

QUALITY OF HVAC SYSTEM 20

* of Observations = 6 ← Comparable sales with score for each comparable

- Observ. # 1 1115 O'NEILL ST Price 14.46

GROSS BUILDING AREA (GBA) 5

LOCATION 1

RATIO OF LAND TO GBA 3

EFFICIENCY OF BUILDING DESIGN FOR STORAGE AND DISTRIBUTION 3

QUALITY OF HVAC SYSTEM 5
- Observ. # 2 2810 BRYANT ST Price 10.73

GROSS BUILDING AREA (GBA) 3

LOCATION 3

RATIO OF LAND TO GBA 1

EFFICIENCY OF BUILDING DESIGN FOR STORAGE AND DISTRIBUTION 1

QUALITY OF HVAC SYSTEM 3
- Observ. # 3 901 WATSON AVE Price 10.81

GROSS BUILDING AREA (GBA) 1

LOCATION 5

RATIO OF LAND TO GBA 1

EFFICIENCY OF BUILDING DESIGN FOR STORAGE AND DISTRIBUTION 1

QUALITY OF HVAC SYSTEM 3
- Observ. # 4 4401 COTTAGE GROVE RD Price 15.21

GROSS BUILDING AREA (GBA) 3

LOCATION 5

RATIO OF LAND TO GBA 5

EFFICIENCY OF BUILDING DESIGN FOR STORAGE AND DISTRIBUTION 5

QUALITY OF HVAC SYSTEM 1
- Observ. # 5 4610-22 FERMITE RD Price 17.4

GROSS BUILDING AREA (GBA) 5

LOCATION 3

RATIO OF LAND TO GBA 3

EFFICIENCY OF BUILDING DESIGN FOR STORAGE AND DISTRIBUTION 5

QUALITY OF HVAC SYSTEM 5
- Observ. # 6 3103 WATFORD WAY Price 14.94

GROSS BUILDING AREA (GBA) 5

LOCATION 5

RATIO OF LAND TO GBA 1

EFFICIENCY OF BUILDING DESIGN FOR STORAGE AND DISTRIBUTION 3

QUALITY OF HVAC SYSTEM 1

The Matrix: ← Test matrix to select optimal combination of weights

20	20	20	20	20
10	10	10	10	10
15	15	15	15	15
25	25	25	25	25
30	30	30	30	30

EXHIBIT 23 (Continued)

Median = 4.565106 ← Initial results using
 Mean = 4.528223 appraiser's weights
 Standard Deviation = .441591

Weights: ← Appraiser's initial weights
 GROSS BUILDING AREA (GBA) = 20
 LOCATION = 20
 RATIO OF LAND TO GBA = 20
 EFFICIENCY OF BUILDING D = 20
 QUALITY OF HVAC SYSTEM = 20

Final Results: ← Iterations to
 Number of Combinations = 3125 select optimal
 Number of Combinations Adding to 100% = 381 weight

Median = 4.153846 ← Final results using
 Mean = 4.175902 optimal weights
 Standard Deviation = 5.067353E-02

Weights: ← Optimal weights
 GROSS BUILDING AREA (GBA) = 30
 LOCATION = 30
 RATIO OF LAND TO GBA = 10
 EFFICIENCY OF BUILDING D = 10
 QUALITY OF HVAC SYSTEM = 20

Program Choices Are:

1. Enter/edit/display/file input data
2. Analyze quality point ratings
3. Display output to screen
4. Print output to printer
5. Select options
6. Quit

Enter your choice: ? 1

Load/edit file options Current disk file: None

1. Create new data file
2. Load existing disk file for editing
3. Display current data
4. Edit current data
5. Save current data to disk file
6. Clear (erase) all current data
7. Quit load/edit options, return to main program

Enter selection number:

Enter selection number: 1

Enter new data

Enter heading for output: INDUSTRIAL WAREHOUSE

Enter number of attributes: ? 5

Enter name for attribute: 1 ? GROSS BUILDING AREA (GBA)

Preliminary weight: 1 ? 20

Enter name for attribute: 2 ? LOCATION

Preliminary weight: 2 ? 20

Enter name for attribute: 3 ? RATIO OF LAND TO GBA

Preliminary weight: 3 ? 20

Enter name for attribute: 4 ? EFFICIENCY OF BUILDING DESIGN -

Preliminary weight: 4 ? 20

Enter name for attribute: 5 ? QUALITY OF HVAC SYSTEM

Weight for QUALITY OF HVAC SYSTEM is 20, so that total of weights is 100.

EXHIBIT 23 (Continued)

Enter number of observations? 6
 Do you want to <1> Enter a unit price or
 <2> Enter a total price & size
 Enter your choice? 1

Observation number 1 :
 Enter name 1 ? 1115 O'NEILL ST.
 Enter price 1 ? 14.46

Score for GROSS BUILDING AREA (GBA)? 5
 Score for LOCATION? 1
 Score for RATIO OF LAND TO GBA? 3
 Score for EFFICIENCY OF BUILDING DESIGN? 3
 Score for QUALITY OF HVAC SYSTEM? 5

Observation number 2 :
 Enter name 2 ? 2810 BRYANT ST.
 Enter price 2 ? 10.73

Score for GROSS BUILDING AREA (GBA)? 3
 Score for LOCATION? 3
 Score for RATIO OF LAND TO GBA? 1
 Score for EFFICIENCY OF BUILDING DESIGN? 1
 Score for QUALITY OF HVAC SYSTEM? 3

Observation number 3 :
 Enter name 3 ?

Score for QUALITY OF HVAC SYSTEM? 3

Observation number 3 :
 Enter name 3 ? 910 WATSON AVE.
 Enter price 3 ? 10.81

Score for GROSS BUILDING AREA (GBA)? 1
 Score for LOCATION? 5
 Score for RATIO OF LAND TO GBA? 1
 Score for EFFICIENCY OF BUILDING DESIGN? 1
 Score for QUALITY OF HVAC SYSTEM? 3

Observation number 4 :
 Enter name 4 ? 4401 COTTAGE GROVE RD.
 Enter price 4 ? 15.21

Score for GROSS BUILDING AREA (GBA)? 3
 Score for LOCATION? 5
 Score for RATIO OF LAND TO GBA? 5
 Score for EFFICIENCY OF BUILDING DESIGN? 5
 Score for QUALITY OF HVAC SYSTEM? 1

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EXHIBIT 23 (Continued)

Observation number 5 :
Enter name 5 ?

Score for QUALITY OF HVAC SYSTEM? 1

1	Observation number 5 :
2	Enter name 5 ? 4610-22 FEMRITE RD.
3	Enter price 5 ? 17.40
4	Score for GROSS BUILDING AREA (GBA)? 5
5	Score for LOCATION? 3
6	Score for RATIO OF LAND TO GBA? 3
7	Score for EFFICIENCY OF BUILDING DESIGN? 5
8	Score for QUALITY OF HVAC SYSTEM? 5

9	Observation number 6 :
10	Enter name 6 ? 3103 WATFORD WAY
11	Enter price 6 ? 14.94
12	Score for GROSS BUILDING AREA (GBA)? 5
13	Score for LOCATION? 5
14	Score for RATIO OF LAND TO GBA? 1
15	Score for EFFICIENCY OF BUILDING DESIGN? 3
16	Score for QUALITY OF HVAC SYSTEM? 1

Enter subject property name:? INDUSTRIAL WAREHOUSE

Enter the name of the designated unit of comparison
(acre, square foot, etc.) ? SQUARE FOOT

Enter number of units of comparison for subject
(acres, square feet, etc.) ? 30195

Enter attribute scores for subject property

GROSS BUILDING AREA (GBA)	? 3
LOCATION	? 3
RATIO OF LAND TO GBA	? 1
EFFICIENCY OF BUILDING DESIGN?	? 1
QUALITY OF HVAC SYSTEM	? 5

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EXHIBIT 23 (Continued)

Load/edit file options Current disk file: None

1. Create new data file
2. Load existing disk file for editing
3. Display current data
4. Edit current data
5. Save current data to disk file
6. Clear (erase) all current data
7. Quit load/edit options; return to main program

Enter selection number: 5

Enter name for data file: SAMPLE

Load/edit file options Current disk file: SAMPLE

1. Create new data file
2. Load existing disk file for editing
3. Display current data
4. Edit current data
5. Save current data to disk file
6. Clear (erase) all current data
7. Quit load/edit options; return to main program

Enter selection number: 3

Project title: INDUSTRIAL WAREHOUSE

Unit prices Search interval = 5

	GROSS	LOCAT	RATIO	EFFIC	QUALI	Price
Prel. wts.	20	20	20	20	20	-
1115 O'NEIL	5	1	3	3	5	\$14.46
2810 BRYANT	3	3	1	1	3	\$10.73
910 WATSON	1	5	1	1	3	\$10.81
4401 COTTAG	3	5	5	5	1	\$15.21
4610-22 FEM	5	3	3	5	5	\$17.40
3103 WATFOR	5	5	1	3	1	\$14.94
INDUSTRIAL	3	3	1	1	5	-

Press any key to continue

EXHIBIT 23 (Continued)

```

-----
[ QP                               Version 2.1
-----
-- Program Choices Are:
    1. Enter/edit/display/file input data
    2. Analyze quality point ratings
    3. Display output to screen
    4. Print output to printer
    5. Select options
    6. Quit
-- Enter your choice: ? 2
-----

```

Pass # 1 Combination # 6

Standard deviation = .4693161 Mean = 4.497911

Status	GROSS	LOCAT	RATIO	EFFIC	QUALI	S.D.	Mean
Prelim. Wts.	20	20	20	20	0	.461591	4.528223

EXHIBIT 23 (Continued)

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QP

Version 2.1

Program Choices Are:

1. Enter/edit/display/file input data
2. Analyze quality point ratings
3. Display output to screen
4. Print output to printer
5. Select options
6. Quit

Enter your choice: ? 3

Display Output to Screen

Select output to be displayed:

1. Weighted matrix for properties
2. Value range determination: mean price per point method
3. Value range per unit of dispersion
4. Transaction zone: mean price per point method
5. Transaction zone: linear regression method
6. Mean price per point method: predicted vs. actual price for comparables
7. Linear regression method: predicted vs. actual price for comparables
8. Input data
9. Computation matrix

<Return> to quit

Enter your choice: 1

EXHIBIT 23 (Continued)

Feature/ Attribute	Weighted Matrix					Wtd. score
	GROSS	BU	LOCATION	RATIO OF	EFFICIEN	
Initial weights	20	20	20	20	0	100
Final weights	30	30	10	10	20	100
1115 O'NEILL S	5/ 1.50	1/ 0.30	3/ 0.30	3/ 0.30	5/ 1.00	3.40
2810 BRYANT ST	3/ 0.90	3/ 0.90	1/ 0.10	1/ 0.10	3/ 0.60	2.60
910 WATSON AVE	1/ 0.30	5/ 1.50	1/ 0.10	1/ 0.10	3/ 0.60	2.60
4401 COTTAGE G	3/ 0.90	5/ 1.50	5/ 0.50	5/ 0.50	1/ 0.20	3.60
4610-22 FEMRIT	5/ 1.50	3/ 0.90	3/ 0.30	5/ 0.50	5/ 1.00	4.20
3103 WATFORD W	5/ 1.50	5/ 1.50	1/ 0.10	3/ 0.30	1/ 0.20	3.60
INDUSTRIAL WAR	3/ 0.90	3/ 0.90	1/ 0.10	1/ 0.10	5/ 1.00	3.00

Press any key to continue

EXHIBIT 23 (Continued)

Display Output to Screen

Select output to be displayed:

- 1. Weighted matrix for properties
- 2. Value range determination: mean price per point method
- 3. Value range per unit of dispersion
- 4. Transaction zone: mean price per point method
- 5. Transaction zone: linear regression method
- 6. Mean price per point method: predicted vs. actual price for comparables
- 7. Linear regression method: predicted vs. actual price for comparables
- 8. Input data
- 9. Computation matrix

<Return> to quit

Enter your choice: 2 (and 3)

Value Range Determination: Mean Price Per Point Method

Mean price per point: \$4.18
 Dispersion About the Mean: \$0.05
 Coefficient of Dispersion: 0.0121

Value Range Per Unit of Dispersion

	Subject Point Score		Mean (+/- One Standard Deviation)		Price Per Unit
Low Estimate	3.00	X	\$4.13	=	\$12.38
Central Tendency	3.00	X	\$4.18	=	\$12.53
High Estimate	3.00	X	\$4.23	=	\$12.68

Press any key to continue

EXHIBIT 23 (Continued)

Display Output to Screen

Select output to be displayed:

- 1. Weighted matrix for properties
- 2. Value range determination: mean price per point method
- 3. Value range per unit of dispersion
- 4. Transaction zone: mean price per point method
- 5. Transaction zone: linear regression method
- 6. Mean price-per point method: predicted vs. actual price for comparables
- 7. Linear regression method: predicted vs. actual price for comparables
- 8. Input data
- 9. Computation matrix

<Return> to quit

Enter your choice: 4

(and 5)

Transaction Zone: Mean Price Per Point Method

Number of units in subject property: 30195

Low Estimate	\$373,679	or	\$374,000
Central Tendency	\$378,274	or	\$378,000
High Estimate	\$382,869	or	\$383,000

Transaction Zone: Linear Regression Method

a = -7.505322E-02 Standard Error of the Forecast = .2056632
 b = 4.200016

Prediction equation: price =

$$30195 \text{ units} \times [-7.505322E-02 + (4.200016 \text{ +/- } .2056632) \times 3]$$

Low Estimate	\$359,562	or	\$360,000
Central Tendency	\$378,192	or	\$378,000
High Estimate	\$396,822	or	\$397,000

Press any key to continue

EXHIBIT 23 (Continued)

Display Output to Screen

Select output to be displayed:

1. Weighted matrix for properties
2. Value range determination: mean price per point method
3. Value range per unit of dispersion
4. Transaction zone: mean price per point method
5. Transaction zone: linear regression method
6. Mean price per point method: predicted vs. actual price for comparables
7. Linear regression method: predicted vs. actual price for comparables
8. Input data
9. Computation matrix

<Return> to quit

Enter your choice: 6

Mean Price Per Point Method: Predicted vs. Actual Price for Comparables

	Predicted Price	Actual price	Error
1115 O'NEILL ST.	\$14.20	\$14.46	-\$0.26
2810 BRYANT ST.	\$10.86	\$10.73	\$0.13
910 WATSON AVE.	\$10.86	\$10.81	\$0.05
4401 COTTAGE GROVE	\$15.03	\$15.21	-\$0.18
4610-22 FEMRITE RD	\$17.54	\$17.40	\$0.14
3103 WATFORD WAY	\$15.03	\$14.94	\$0.09

Press any key to continue

EXHIBIT 23 (Continued)

Display Output to Screen

Select output to be displayed:

- 1. Weighted matrix for properties
- 2. Value range determination: mean price per point method
- 3. Value range per unit of dispersion
- 4. Transaction zone: mean price per point method
- 5. Transaction zone: linear regression method
- 6. Mean price per point method: predicted vs. actual price for comparables
- 7. Linear regression method: predicted vs. actual price for comparables
- 8. Input data
- 9. Computation matrix

<Return> to quit

Enter your choice: 7

Linear Regression Method: Predicted vs. Actual Price for Comparables

	Predicted Price	Actual price	Error
1115 O'NEILL ST.	\$14.20	\$14.46	-\$0.26
2810 BRYANT ST.	\$10.84	\$10.73	\$0.11
910 WATSON AVE.	\$10.84	\$10.81	\$0.03
4401 COTTAGE GROVE	\$15.05	\$15.21	-\$0.16
4610-22 FEMRITE RD	\$17.57	\$17.40	-\$0.17
3103 WATFORD WAY	\$15.05	\$14.94	\$0.11

Press any key to continue

EXHIBIT 23 (Continued)

Display Output to Screen

Select output to be displayed:

1. Weighted matrix for properties
2. Value range determination: mean price per point method
3. Value range per unit of dispersion
4. Transaction zone: mean price per point method
5. Transaction zone: linear regression method
6. Mean price per point method: predicted vs. actual price for comparables
7. Linear regression method: predicted vs. actual price for comparables
8. Input data
9. Computation matrix

<Return> to quit

Enter your choice: 8

Project title: INDUSTRIAL WAREHOUSE

Unit prices Search interval = 5

	GROSS	LOCAT	RATIO	EFFIC	QUALI	Price
Prél. wts.	30	30	10	10	20	-
1115 O'NEIL	5	1	3	3	5	\$14.46
2810 BRYANT	3	3	1	1	3	\$10.73
910 WATSON	1	5	1	1	3	\$10.81
4401 COTTAG	3	5	5	5	1	\$15.21
4610-22 FEM	5	3	3	5	5	\$17.40
3103 WATFOR	5	5	1	3	1	\$14.94
INDUSTRIAL	3	3	1	1	5	-

Press any key to continue

EXHIBIT 23 (Continued)

Display Output to Screen

Select output to be displayed:

1. Weighted matrix for properties
2. Value range determination: mean price per point method
3. Value range per unit of dispersion
4. Transaction zone: mean price per point method
5. Transaction zone: linear regression method
6. Mean price per point method: predicted vs. actual price for comparables
7. ~~Linear regression method: predicted vs. actual price for comparables~~
8. Input data
9. Computation matrix

<Return> to quit

Enter your choice: 9

Computation Matrix

20	20	20	20	0
10	10	10	10	10
15	15	15	15	15
25	25	25	25	25
30	30	30	30	30

Press any key to continue

EXHIBIT 23 (Continued)

 Display Output to Screen

Select output to be displayed:

1. Weighted matrix for properties
2. Value range determination: mean price per point method
3. Value range per unit of dispersion
4. Transaction zone: mean price per point method
5. Transaction zone: linear regression method
6. Mean price per point method: predicted vs. actual price for comparables
7. Linear regression method: predicted vs. actual price for comparables
8. Input data
9. Computation matrix

<Return> to quit

Enter your choice: 10

----- Iterations -----

		GROSS	LOCAT	RATIO	EFFIC	QUALI	S.D.	Mean
Prelim	Wts.	20	20	20	20	20	.441591	4.528223
Pass #	1	30	30	10	10	20	5.067353E-02	4.175902
Pass #	2	30	30	10	10	20	5.067353E-02	4.175902

 Press any key to continue

EXHIBIT 23 (Continued)

QP

Version 2.1

Program Choices Are:

1. ~~Enter/edit/display/file input data~~
2. Analyze quality point ratings
3. Display output to screen
4. Print output to printer
5. Select options
6. Quit

Enter your choice: ? 5

Special options

Enter your selection:

1. Change search interval

<Return> for no changes
Enter your choice: ? 5

EXHIBIT 24

EXCERPTED FROM APPRAISAL OF INDUSTRIAL SITE

C. Adjustments for Differences to Relate the
Comparables to the Subject Property

To estimate the fair market value of the subject property, based upon the sale prices of the comparables, adjustments are made to account for the differences in the price sensitive attributes of the comparables and the subject property. The comparable properties and the subject property are scored according to the scale detailed in Exhibit 9.

The subject site, which contains 2.5 acres, receives a score of 3 because it is an average sized lot. Since it does not command a more highly visible corner location, a score of 1 is given.

Linkages are extremely sensitive to price. Sites located in major retail areas command higher prices than do warehouses and light manufacturing sites. No retail uses are in sight of the subject so a score of 1 is given. International Lane, a traffic collector, feeds into Packers Avenue, a major arterial, so the subject receives a score of 3. A bus line on Packers Avenue is within two to three blocks of the subject to yield a score of 3. Electricity, telephone, and natural gas lines are available in the general area, but there are no curbs, gutters,

EXHIBIT 24 (Continued)

EXHIBIT 9 (Continued)

SCALE FOR SCORING COMPARABLE SALES
BASED UPON PRICE SENSITIVE ATTRIBUTES

PHYSICAL ATTRIBUTES = 35%

Size 20%	5 = Less than 1 acre 3 = 1 to 4 acres 1 = Greater than 4 acres
Corner Location 15%	5 = Yes 3 = Next to corner on a major road 1 = No

LINKAGES = 50%

Proximity to Major Retail Area 20%	5 = Near a shopping center 3 = Near strip retail area 1 = No retail uses in sight
Access to Major Highways 15%	5 = On a major boulevard or highway 3 = On a traffic collector 1 = On a side street
Availability of Madison Metro 5%	5 = On a bus line 3 = Within 2-3 blocks of bus line 1 = None
Availability of Utilities 10%	5 = Water, sewer, gas, curb, and gutter 3 = Water, sewer, gas 1 = None

EXHIBIT 24(Continued)

EXHIBIT 9 (Continued)

DYNAMIC ATTRIBUTES = 15%

Positive Public Recognition of Street/Location 5%	5 = High visibility or recognition of location 3 = Average 1 = Relatively unknown
--	--

Perceived Adverse Influences 5%	5 = None 3 = Noise/Odor/Visual Problems 1 = Physically threatening
---------------------------------------	--

Immediate View from Property Frontage 5%	5 = Well-landscaped office, shops, and residential 3 = Office/warehouses well-screened and partially landscaped 1 = Assortment of office/warehouse uses with inadequate screening and/or poorly maintained or vacant
---	---

or sidewalks. A score of 3 is given the subject for the availability of utilities.

Dynamic attributes, (the public's perceptions of the property's attributes) contribute to value. Since International Lane is a well-known location with positive public recognition, the subject is given a score of 5. Since the noise from planes landing and taking off could be disruptive, the subject receives a 3. The view from the subject is marred by old barracks converted to offices and warehouse buildings that would no longer meet the more stringent architectural controls now in existence in Truax Air Park West, so the subject receives a score of 1.

Each comparable is scored in a similar manner; the weighted point score matrix which details the calculation of a total point score for both the comparable and the subject is found in Exhibit 10.

The price per square foot for each comparable is divided by its point score and the results are also found in Exhibit 10.

The mean point score per square foot is applied to the point score of the subject to indicate a central tendency value of \$111,000, or \$1.01 per square foot. These calculations are detailed in Exhibit 11.

The range of estimates yields a high of \$123,500, or \$1.13 per square foot and a low of \$98,000, or \$0.90 per square foot.

EXHIBIT 9 (Continued)

WEIGHTED POINT SCORE MATRIX FOR COMPARABLE SALES
BASED UPON PRICE SENSITIVE ATTRIBUTES

ATTRIBUTE	WEIGHT	#1 1905 ABERG AVENUE	#2 1801 COMMERCIAL AVENUE
<u>Physical Attributes</u>		[1]	
Size of Site	20%	3/ .60	1/ .20
Corner Location	15%	1/ .15	1/ .15
<u>Linkages</u>			
Proximity to Retail	20%	3/ .60	1/ .20
Access to Major Roads	15%	5/ .75	3/ .45
Availability of City Bus	5%	3/ .25	5/ .25
Availability of Utilities	10%	5/ .50	5/ .50
<u>Dynamic Attributes</u>			
Public Recognition	5%	5/ .25	3/ .15
Perceived Adverse Factors	5%	3/ .15	5/ .25
View from Site	<u>5%</u> 100%	<u>1/ .05</u>	<u>1/ .05</u>
TOTAL POINT SCORE		3.30	2.20

Sale Price		\$80,000	\$181,150
Date of Sale		8/82	10/80
Land Area (SF)		53,426 (1.23 A)	175,547 (4.03 A)
Price per Square Foot		\$1.50	\$1.03
Total Point Score		3.30	2.20
Price per SF/Point Score		\$0.45	\$0.47

[1] Explanation of weighted score: point score/score x weight

EXHIBIT 9 (Continued)

ATTRIBUTE	WEIGHT	#3 3520 PACKERS AVENUE	#4 814 ATLAS AVENUE (Backs on to Cottage Grove Rd.)	#5 LOT 1, BLK. 7, MADISON INDUSTRIAL SUB., #1	#6 2447 ADVANCE (a.k.a. 4701 Pflaum Road)	#7 LOT 6, BLK. 3, MADISON INDUSTRIAL SUB., #1
<u>Physical Attributes</u>		[1]				
Size of Site	20%	5/1.00	3/ .60	3/ .60	3/ .60	5/1.00
Corner Location	15%	5/ .75	1/ .15	1/ .15	5/ .75	1/ .15
<u>Linkages</u>						
Proximity to Retail	20%	3/ .60	3/ .60	1/ .20	1/ .20	1/ .20
Access to Major Roads	15%	3/ .45	5/ .75	1/ .15	3/ .45	1/ .15
Availability of City Bus	5%	5/ .25	5/ .25	1/ .05	1/ .05	1/ .05
Availability of Utilities	10%	5/ .50	5/ .50	5/ .50	5/ .50	5/ .50
<u>Dynamic Attributes</u>						
Public Recognition	5%	1/ .05	3/ .15	1/ .05	5/ .25	1/ .05
Perceived Adverse Factors	5%	3/ .15	5/ .25	5/ .25	5/ .25	5/ .25
View from Site	<u>5%</u> 100%	<u>1/ .05</u>	<u>3/ .15</u>	<u>3/ .15</u>	<u>3/ .15</u>	<u>3/ .15</u>
TOTAL POINT SCORE		3.80	3.40	2.10	3.20	2.50
<u>Sale Price</u>		\$30,000	\$125,000	\$70,000	\$60,000	\$20,900
<u>Date of Sale</u>		2/79	6/83	9/82	9/82	9/82
<u>Land Area (SF)</u>		21,747 (0.50)	80,613 (1.85 A)	73,109 (1.68 A)	45,472 (1.04 A)	22,997 (0.53 A)
<u>Price per Square Foot</u>		\$1.55 [2]	\$1.55	\$0.96	\$1.32	\$0.91
<u>Total Point Score</u>		3.80	3.40	2.10	3.20	2.50
<u>Price per SF/Point Score</u>		\$0.41	\$0.46	\$0.46	\$0.41	\$0.36

[1] Explanation of weighted score: point score/score x weight
 [2] This older sale is adjusted upward 12 percent for time. (1.12 x \$1.38 = \$1.55)

EXHIBIT 24(Continued)

EXHIBIT 9 (Continued)

ATTRIBUTE	WEIGHT	#8 LOT 2, BLK. 6. MADISON INDUSTRIAL SUB., #1	#9 4484 ROBERTSON ROAD MADISON IND. SUB., #1	SUBJECT LOT 2, CSM 928
<u>Physical Attributes</u>		[1]		
Size of Site	20%	5/1.00	3/ .60	3/ .60
Corner Location	15%	1/ .15	1/ .15	1/ .15
<u>Linkages</u>				
Proximity to Retail	20%	1/ .20	1/ .20	1/ .20
Access to Major Roads	15%	1/ .15	1/ .15	3/ .45
Availability of City Bus	5%	1/ .05	1/ .05	3/ .15
Availability of Utilities	10%	5/ .50	5/ .50	3/ .30
<u>Dynamic Attributes</u>				
Public Recognition	5%	1/ .05	1/ .05	5/ .25
Perceived Adverse Factors	5%	5/ .25	5/ .25	3/ .15
View from Site	<u>5%</u>	<u>3/ .15</u>	<u>3/ .15</u>	<u>1/ .05</u>
	100%	2.50	2.10	2.30
<hr/>				
Sale Price		\$32,000	\$98,600	N/A
Date of Sale		2/82	1/82	N/A
Land Area (SF)		24,975 (0.57)	98,600 (2.26 A)	109,493 (2.51 A)
Price per Square Foot		\$1.28	\$1.00	N/A
Total Point Score		2.50	2.10	2.30
Price per SF/Point Score		\$0.51	\$0.48	N/A

[1] Explanation of weighted score: point score/score x weight

EXHIBIT 24 (Continued)

EXHIBIT 24 (Continued)

EXHIBIT 9 (Continued)

CALCULATION OF MOST PROBABLE PRICE USING
MEAN PRICE PER POINT EQUATION METHOD

Comparable Property	Adjusted Selling Price per SF	Weighted Point Score	<u>Price per SF</u> Weighted Point Score
1	\$1.50	3.30	\$0.45
2	1.03	2.20	0.47
3	1.55	3.80	0.41
4	1.55	3.40	0.46
5	0.96	2.10	0.46
6	1.32	3.20	0.41
7	0.91	2.50	0.36
8	1.28	2.50	0.51
9	1.00	2.10	<u>0.48</u>
		TOTAL	\$4.01

$$\text{Central Tendency [1]} = \frac{\sum x}{n} = \frac{4.01}{9} = .44$$

$$\text{Dispersion} = \sqrt{\frac{\sum (x-x)^2}{(n-1)}} = \sqrt{\frac{.0168}{8}} = .05$$

$$[1] \quad x = \text{Sum of } \frac{\text{Price per SF}}{\text{Weighted Point Score}}$$

n = Number of Observations

$$\bar{x} = \text{Average } \frac{\text{Price per SF}}{\text{Weighted Point Score}}$$

EXHIBIT 24 (Continued)

EXHIBIT 9 (Continued)

where:

\bar{x}	$\bar{\bar{x}}$	$\angle(x-\bar{x})\angle$	$(x-\bar{x})^2$	\bar{n}	$n-1$
.42	.44	.02	.0004	9	8
.47	.44	.03	.0009		
.41	.44	.03	.0009		
.46	.44	.02	.0004		
.46	.44	.02	.0004		
.41	.44	.03	.0009		
.36	.44	.08	.0064		
.51	.44	.07	.0049		
.48	.44	.04	.0016		

$$\sum(x - \bar{x})^2 = .0168$$

Value range for subject property:

$$\bar{x} \pm \text{dispersion} = \$0.44 \pm .05$$

Square Footage of Subject x Weighted Point Score x (Central Tendency \pm Dispersion) =

$$109,493 \times 2.30 \times (\$0.44 \pm .05) =$$

High Estimate of \$123,500 or \$1.13 per square foot

Central Tendency of \$111,000 or \$1.01 per square foot

Low Estimate of \$98,000 or \$0.90 per square foot

As a check on the appropriateness of the appraiser's selection and weighting of price sensitive factors, the point scores calculated for each comparable is multiplied by the mean price per square foot per point score to predict or estimate the actual selling price of each comparable. The results are as follows:

<u>COMPARABLE NUMBER</u>	<u>WEIGHTED POINT SCORE</u>	<u>ESTIMATED PRICE/SF</u>	<u>ACTUAL PRICE/SF</u>	<u>RESIDUAL ERROR</u>
1	3.30	1.45	1.50	-.05
2	2.20	0.96	1.03	-.07
3	3.80	1.67	1.55 (adj.)	+.12
4	3.40	1.50	1.55	-.05
5	2.10	0.92	0.96	-.04
6	3.20	1.41	1.32	+.09
7	2.50	1.10	0.91	+.19
8	2.50	1.10	1.28	-.18
9	2.10	0.92	1.00	<u>+.08</u>
NET RESIDUAL ERRORS				+.09

There appears to be a tight fit between the estimated and the actual price; so it can be concluded that the selection and weighing of the price sensitive factors successfully reflected buyer behavior.

EXHIBIT 24 (Continued)

The market comparable approach is sensitive to the appraiser's ability to predict buyer perceptions in a changing market. The weighted point scores are an attempt to capture these perceptions. Consequently, this calculated value is only the initial step in determining the final price estimate. This initial transaction zone must be adjusted in light of certain external factors such as the buyer's alternative option to lease surrounding land from Dane County instead of buying in fee which, in turn, will be affected by the current cost of financing land purchases, the income tax consequences of buy versus lease decision, and the effect of the Consumer Price Index (CPI) escalator upon rental rates for leased land. Other external factors include the effect of the Truax Air Park covenants upon the quality of future development in the area, and the future expansion of the Dane County Regional Airport.

CONTEMPORARY ISSUES AND METHODS FOR
APPRAISING COMMERCIAL PROPERTIES
(Continued)

III. THE INCOME APPROACH OR INVESTMENT SIMULATION APPROACH
APPLIED TO LARGE INCOME PROPERTY

The basic concept of the income approach is that the property value is the present value of an income stream to the investor plus the present value of the reversion to the investor. That simple truism requires very disciplined, systematic, but internally consistent logic to carry off.

- A. First there is the problem of defining the perspective of the buyer or buyer presumed by the issue for which the appraisal is required as a benchmark. This perspective will determine what revenues and expenses must be considered.
- B. There is the problem of defining the source, amount, and timing of receipt in terms of accounting theory (cash or accrual) and in terms of business practice (receivables versus collections).
- C. There is the problem of defining expenses attributable to the real estate as opposed to the occupancy as perceived by the most probable buyer.
- D. Selection of a forecast period also determines necessary charges to operations for tenant improvement, leasing commissions, reserve for replacement and refurbishment, and other soft capital items to be amortized over nominal periods of time.
- E. Then there is the problem of defining the most probable capital structure for buyer financing of the property assuming cash to the seller and/or assuming some seller financing.
- F. There is the problem of selecting a conversion process with which to define a net reversion assumed for some future point in time in an uncertain future.

- G. There is the problem of recognizing entitlements or submerged profit centers which can be controlled through purchase of real estate because real estate traditionally does not carefully delineate net income from real estate, personalty, intangible assets, captive consumers, or managment.
- H. Given the complexities of the above, how do buyers convert cash flows, reversions, peripheral profit centers, and portfolio effects to a purchase price.

CONTEMPORARY ISSUES AND METHODS FOR
APPRAISING COMMERCIAL PROPERTIES
(Continued)

IV. CONTEMPORARY APPRAISAL AND
ACCOUNTING THEORY

Fundamental issues which will lead to standardization of perspective by the FASB, the American Appraisal organizations, and the European Common Market in which RICS played a major role.

- A. Unwitting deviation from derivation of the income approach which:
 - 1. Originally intended to measure economic surplus of an asset in terms of normalized net income projected over a mathematical line for the life of an asset;
 - 2. Investment band theory shifted value to the sum of present value claims on the income, specifically liability valuation.
 - 3. Equity valuation in the securities markets recognize claims from income were prioritized by risk and critical path of service provided. Earnings were irregular, related to investor tax status, and manipulated by marketing monopoly or operating control.

- B. This evolution from economic surplus to claims on liabilities to going concern values has produced incredible confusion and opportunity for valuation disinformation because appraisers don't know any accounting.
 - 1. Economic productivity requires accrual accounting
 - 2. Financial productivity requires cash accounting
 - 3. Going concern valuation requires profit center segregation and venture capital discounting based on source and application

CONTEMPORARY ISSUES AND METHODS FOR
APPRAISING COMMERCIAL PROPERTIES
(Continued)

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- B. This evolution from economic surplus to claims on liabilities to going concern values has produced incredible confusion and opportunity for valuation disinformation because appraisers don't know any accounting.
1. Economic productivity requires accrual accounting
 2. Financial productivity requires cash accounting
 3. Going concern valuation requires profit center segregation and venture capital discounting based on source and application

- C. Some computer systems for property management already have the feature of converting from accrual to cash accounting and several studies are underway to define accounting conventions for appraisers.
1. Exhibit 25 contains generalized theory for converting accrual accounting to cash accounting
 2. Exhibit 26 contains an analysis of the feasibility of a small city office rehab project
 3. Exhibit 27 contains the format for an income property pro forma on a cash accounting basis
 4. Exhibit 28 contains an example of discounted cash flow without a computer
- D. Accounting theory also distinguishes value by a variety of perspectives in order to fit the function of the accounting task to measure the appropriate economic aspect:
1. Exit value assuming completion of normal business cycle in an orderly fashion (benchmarking).
 2. Exit value assuming abrupt liquidation (construction loan validation).
 3. Replacement value with asset of current technology.
 4. Reproduction value of asset at original state of technology.
 5. Market value in an organized market for tangible goods.
 6. Current value in an organized market for tangible goods.
 7. Discounted value of future receipts at interest factor.
 8. Value of asset not yet charged to consumption or production.

- E. Discounted cash flow must also anticipate that the collectibility of CPI adjustments and pass-throughs as well as deferred rent concessions must be examined. The shorter the lease term and the lower the tenant investment in improvements, the less probability there is of collection.
1. The appraiser must not only read the leases, but determine the degree to which management has collected future adjustments as a measure of effective rents rather than contract rents.
 2. However, the appraiser is not expected to be an auditor and his statement of limiting conditions should contain a clause indicating the presumption of the appraisal, i.e., that payments due the landlord have in fact been collected, does not represent a conclusion based on an audit of past operations.
 3. Tenant improvements which will benefit the property after the lease has expired or greatly in excess of allowances in the original contract represent a form of rent guaranty which might be identified by the appraiser when making an assumption about the collectibility of all forms of reimbursements.
 4. The appraiser should also note if property management is releasing under terms which convert old escalators to monthly reimburseables or CAM items which are collectible monthly on an anticipated average basis to be adjusted at the end of each fiscal year, significantly altering cash flows and the certainty of collection in the future.

- F. The increasing use of CAM payments and the broadening scope of costs included introduce another problem in analyzing real estate receipts. Property managers generally include a 10 to 15 percent surcharge on actual outlays for the work of collecting and accounting for CAM; CAM contains a profit center for management. The appraiser must determine if that profit center belongs to the building owner to offset the general management fee or has been considered as part of the compensation formula to the management function. In the latter case, it is clearly not real estate revenue to be capitalized into the value of the property.
1. Management compensation formulas have become more complex so that simple appraisal accounting for a percentage of effective gross plus a leasing commission can be very misleading.
 2. Formulas generally involve different leasing commissions for renewals versus replacement of tenants, construction supervision fees for renovations, tenant improvements, etc., as well as reimbursement for advertising, after-hours servicing, or negotiation of casualty losses.
 3. Construction supervision, tenant relations, as well as actual refurbishment expenses suggest how much is being invested in the future of the building, like R & D in a manufacturing corporation.
- G. Fair market value presumes definition of economic rent attributable to the real estate as opposed to intangible assets or personal property.
1. Is income attributable to entitlements that go with fee simple title to the land and are point specific or to transportable permits?
 - a. For example--does liquor license go with the building? Is permit to build or maintain a dam assignable? Does right to management fee and brokerage fee go with general partnership or property?
 2. Is the real estate income from retailing of space or from wholesaling of space?

- a. Parking ramp lease versus parking space by the hour, observation deck versus ticket, condominium conversion fee versus apartment project investment.
 3. Is the income for extraordinary services or intangible assets rather than customary?
 - a. Maid service versus janitorial, shopping center premium for proximity or for joint merchandising and risk management.
 4. Ancillary to, rather than integral with the project.
 - a. Can services be acquired off premises such as janitorial or utilities?
 5. IRS classification as 1250 property (real) or 1231 property (personalty) and Section 453, 453A and B, or Section 38 (tangible) or Section 45 (intangible).
 6. Is income attributable to governmental agencies in exchange for contractual entitlements of control or use to the public interest for the term of the contract?
- H. Defining expenses attributable to the real estate is particularly difficult where you have a current occupancy/owner, such as a home office for a bank or insurance company. There are many distortions in the general ledger due to:
1. Superadequacy of maintenance.
 2. Corporate accounting to shift or conceal division profits
 3. Confusion of busines security with building operations
 4. Deliberate concealment of corporate pet projects as building expense
 5. Artificial corporate accounting charges for space or corporate services

- I. Careful accounting distinctions are the critical differences in valuing property for real estate taxes, or liquidating value for a lender, or going concern value for a limited partnership or unit value of a comingled fund.
 1. Choice of the accounting format is also related to selection of the number of periods on a forecast. The assessor can accept short-term forecasts since there is opportunity for periodic review; the mortgage lender needs a longer term forecast to anticipate cyclical contractions of cash flow threatening the mortgage payment.
 2. However, what time frame is appropriate for valuing assets in a comingled fund? Large, unrecognized assets and negative cash flows have their payoff over the average lease term or longer; how should the valuation formula recognize these intangible assets?
- J. Selection of a forecast period as five or ten years or more reflects purpose and sensitivity to value to long term assumptions and the curve of compound interest. Ten-year convention seems to be growing although a single lease rollover period is sufficient to strain the forecasting talents of most appraisers.
- K. The decision by the Institute to require definition of fair market value with all cash to the seller before reporting a value attached to special financing provided by the seller is critical in providing the hope of its standard against which all manner of structuring can be related.
 1. Financing is not the only entitlement which enhances value beyond fair market value. There may be favorable leases, tax abatements, monopolies, and all manner of regulatory entitlements which are not included in fee simple title, but travel with the real estate. The increment attributable to these should generally be flagged as well.

2. Fee simple encumbered by leases is generally identified, but what about fee simple encumbered by special district rules, title flaws, or regulatory controls like those of the FERC?
- L. Submerged profit centers are becoming much more significant due to management loads on CAM, back-end loads on finite financing agreements, and penalties for prepaid financing, cancelled contracts, windfall real estate tax returns, or sale of services and equipment leasing to the tenants. As control of property shifts to asset managers, so does control of the captive consumers within the building and the customer lists of potential tenant relocation in the future go to the benefit of the asset manager at the expense of the building owner.
- M. Problem of defining or forecasting a reversion:
1. Pricing real estate for utilitarian purpose, to buy access to service sales, or speculate in long term demand/supply commodity relationships or long term commodity/money ratios.
 2. Can the appraiser prove presence of necessary conditions for appreciation and amount of depreciation?
 - a. Rising net income
 - b. Falling interest rates
 - c. Falling investor expectations
 3. When is appreciation speculative, non-vested, and excluded from fair market value?
- N. The most common reversion process is to estimate net income for the year after the year of sale--year six in a five-year forecast, or year eleven in a ten-year forecast.
1. This income is then capitalized at some rate, either a market rate at the time of the forecast or a more conservative rate to reflect aging of the property and the anticipation that it would be sold when the possibility of further increases in net income had declined significantly.

2. The critical question is how dependent is value on the change in retail price? Dilmore indicates there are seven sources of cash return which might each be discounted separately to represent the risk inherent in realizing the expected flow. These elements are:
 - a. Return of original equity investment
 - b. Value of cash flows at first year level
 - c. Growth (decline) of cash flow stream
 - d. Tax shelter of subject's cash flow
 - e. Tax shelter of external income
 - f. Growth of equity from amortization
 - g. Growth of equity from value appreciation
3. See "Component Capitalization" by Gene Dilmore in Real Estate Issues, Spring-Summer 1985.
4. Perhaps the most important paragraph at the end of the Dilmore article, with reference to a simple future price or Monte Carlo resale price estimate is:

"Whether the appraiser considers this as an independent value indication from the income approach, or as a testing of the probable price indicated by analysis of the market data, is a matter of individual choice. In either case, a report section on externalities should follow these calculations giving consideration to the external factors (money markets, investor moods, political contingencies, local phenomena altering market expectations, etc.) which can push the indicated price in either direction."

5. Probability models are not likely to be accepted soon for three practical limitations--appraisers have limited knowledge of statistics, decision-makers prefer their subjective intuitions, and thoroughness may not be cost effective in terms of decisions to buy, sell, or lend.
6. There is a sensitivity algorithm called the Cady-Westby model which can directly compute changes in net present value or IRR or the break-even ratio which can occur for each one percent variance in key variables. It works quickly on a PC; it is based on response theory, but the algorithm represents high security information for nuclear power plant management. It will allow appraisers to avoid probability modeling just a set theory by-passes the problems with degrees of freedom in a limited data base.

EXHIBIT 27

PRO FORMA INCOME PROPERTY FORMAT

(Cash Accounting Basis)

- I. Expected Receipt
 - Base rent (Monthly)
 - Index to base rent (Annual adjustment to monthly base)
 - Percentage rent (Quarterly estimate with fifth quarter adjustment)
 - Amortized tenant improvements (Monthly, fixed)
 - CAM (Monthly average with 14th month adjustment)
 - Reimburseables (Annual pass through)
 - Escalators with stop (Annual review)
 - Interest on reserves (Quarterly sweep)
 - Government transfer payments (Negotiated and deferred)
 - Total receipts
- II. Loss of Potential Receipts
 - Vacancy losses
 - Rent collection losses
 - Reimbursement collection losses
 - Receivables
 - Concessions
 - Total reduction in expected receipts
- III. Actual Revenues for Operations
- IV. Gross Outlays for Operations
 - CAM items
 - Reimburseables
 - Escalator items
 - Owner costs
 - Refurbishment
 - Renewal tenant improvements
 - Renewal lease commissions
 - Total operating outlays
- V. Total Cash from Operations
- VI. Capital Charges
 - Interest payments
 - Principal payments
 - Capital improvements
- VII. Net Cash from Operations before Taxes
 - + Transfers from cash reserves from previous period
 - + Net increases in loan balances outstanding
- VIII. Cash Available for Distribution and/or Taxes
 - Less distribution and taxes
 - = Net addition to cash reserves in following period

EXAMPLE OF DISCOUNTED CASH FLOW
WITH 100% EQUITY FINANCING

YEAR	ANNUAL NET OPERATING INCOME (NOI)	DISCOUNT FACTOR AT 17%	PRESENT VALUE OF EQUITY
Last 6 Months of 1982	\$189,758	0.924500	\$175,431
1983	364,022	0.790171	287,640
1984	410,013	0.675360	276,906
1985	457,118	0.577230	263,862
1986	454,429	0.493359	224,197
1987	579,334	0.421674	244,290
1988	574,943	0.360405	207,212
1989	591,365	0.308039	182,163
1990	624,054	0.263281	164,302
1991	659,043	0.225026	148,302
First 6 Months of 1992	323,726	0.208037	67,347
	RESALE PRICE		
1992	4,839,000	0.208037	1,007,000
	PRESENT VALUE OF EQUITY		\$3,248,652
	TOTAL VALUE WITH 100% EQUITY		\$3,248,652
		ROUNDED	\$3,200,000

EXAMPLE OF DISCOUNTED CASH FLOW
WITH 100% EQUITY FINANCING

YEAR	ANNUAL NET OPERATING INCOME (NOI)	DISCOUNT FACTOR AT 17%	PRESENT VALUE OF EQUITY
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First 6 Months of 1992	323,726	0.208037	67,347
	RESALE PRICE		
1992	4,839,000	0.208037	1,007,000
	PRESENT VALUE OF EQUITY		\$3,248,652
	TOTAL VALUE WITH 100% EQUITY		\$3,248,652
		ROUNDED	\$3,200,000

EXHIBIT 28 (Continued)

EXAMPLE OF DISCOUNTED CASH
FLOW WITH CONVENTIONAL FINANCING

YEAR	ANNUAL NET OPERATING INCOME (NOI)	ANNUAL DEBT SERVICE BASED ON DEBT COVER RATIO (DCR) OF 1.3 [1]	NOI LESS DEBT SERVICE EQUALS CASH THROW-OFF (CTO)	DISCOUNT FACTOR AT 17%	PRESENT VALUE OF EQUITY
Last 6 Months of 1982	\$189,758	140,000	\$49,750	0.924500	\$46,000
1983	364,022	280,000	84,000	0.790171	66,400
1984	410,013	280,000	130,000	0.675360	87,800
1985	457,118	280,000	177,100	0.577230	102,200
1986	454,429	280,000	174,400	0.493359	86,000
1987	579,334	280,000	299,300	0.421674	126,200
1988	574,943	280,000	295,000	0.360405	106,300
1989	591,365	280,000	311,400	0.308039	96,000
1990	624,054	280,000	344,100	0.263281	90,600
1991	659,043	280,000	379,000	0.225026	85,300
First 6 Months of 1992	323,726	140,000	183,700	0.208037	38,200
1992	RESALE PRICE 4,839,000	RESALE PRICE LESS MORTGAGE BALANCE [2] 3,042,000		0.208037	632,800
	PRESENT VALUE OF EQUITY				\$1,563,800
	ORIGINAL MORTGAGE BALANCE				2,001,753
	TOTAL VALUE WITH CONVENTIONAL FINANCING				\$3,565,553
				ROUNDED	\$3,600,000

[1] Based on first full year NOI

[2] Maximum mortgage which NOI can carry, assuming a DCR of 1.3, interest at 13.5 percent for a 25 year term with monthly payments, is \$2,001,753. At the end of a ten year holding period the balance due is \$1,797,196 or rounded \$1,797,000.

EXHIBIT 28 (Continued)

EXAMPLE OF DISCOUNTED CASH
FLOW WITH SELLER FINANCING

YEAR	ANNUAL NET OPERATING INCOME (NOI)	ANNUAL DEBT SERVICE BASED ON DEBT COVER RATIO (DCR) OF 1.1 [1]	NOI LESS DEBT SERVICE EQUALS CASH THROW-OFF (CTO)	DISCOUNT FACTOR AT 17%	PRESENT VALUE OF EQUITY
Last 6 Months of 1982	\$189,758	\$165,450	\$24,300	0.924500	\$22,500
1983	364,022	330,900	33,100	0.790171	26,200
1984	410,013	330,900	79,100	0.675360	53,400
1985	457,118	330,900	126,200	0.577230	72,900
1986	454,429	330,900	123,500	0.493359	60,900
1987	579,334	330,900	248,400	0.421674	104,800
1988	574,943	330,900	244,000	0.360405	88,000
1989	591,365	330,900	260,500	0.308039	80,200
1990	624,054	330,900	293,100	0.263281	77,200
1991	659,043	330,900	328,100	0.225026	73,800
First 6 Months of 1992	323,726	165,450	158,300	0.208037	33,000
	RESALE PRICE	RESALE PRICE LESS MORTGAGE BALANCE [2]			
1992	4,839,000	2,602,000		0.208037	541,300
					1,234,200
					2,528,995
					<u>\$3,763,195</u>
					=====
				ROUNDED	<u>\$3,800,000</u>
					=====

[1] Based on first full year NOI

[2] Maximum mortgage which NOI can carry, assuming a DCR of 1.1, interest at 12.5 percent amortized over 25 years with monthly payments, is \$2,528,995. At the end of a ten year holding period the balance due is \$2,237,023 or \$2,237,000, rounded.

EXHIBIT 28 (Continued)

EXAMPLE OF DISCOUNTED CASH
FLOW WITH SELLER FINANCING

YEAR	ANNUAL NET OPERATING INCOME (NOI)	ANNUAL DEBT SERVICE BASED ON DEBT COVER RATIO (DCR) OF 1.1 [1]	NOI LESS DEBT SERVICE EQUALS CASH THROW-OFF (CTO)	DISCOUNT FACTOR AT 17%	PRESENT VALUE OF EQUITY
Last 6 Months of 1982	\$189,758	\$165,450	\$24,300	0.924500	\$22,500
1983	364,022	330,900	33,100	0.790171	26,200
1984	410,013	330,900	79,100	0.675360	53,400
1985	457,118	330,900	126,200	0.577230	72,900
1986	454,429	330,900	123,500	0.493359	60,900
1987	579,334	330,900	248,400	0.421674	104,800
1988	574,943	330,900	244,000	0.360405	88,000
1989	591,365	330,900	260,500	0.308039	80,200
1990	624,054	330,900	293,100	0.263281	77,200
1991	659,043	330,900	328,100	0.225026	73,800
First 6 Months of 1992	323,726	165,450	158,300	0.208037	33,000
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1992	4,839,000	2,602,000		0.208037	541,300
					1,234,200
					2,528,995
					<u>\$3,763,195</u>
					=====
				ROUNDED	<u>\$3,800,000</u>
					=====

[1] Based on first full year NOI

[2] Maximum mortgage which NOI can carry, assuming a DCR of 1.1, interest at 12.5 percent amortized over 25 years with monthly payments, is \$2,528,995. At the end of a ten year holding period the balance due is \$2,237,023 or \$2,237,000, rounded.

CONTEMPORARY ISSUES AND METHODS FOR
APPRAISING COMMERCIAL PROPERTIES
(Continued)

VIII. CONTEMPORARY MODELS FOR CONVERSION OF
CASH FLOWS TO VALUE ESTIMATES

The new income approach for large income properties has become a hybrid of a CPA format and appraisal models for converting cash flows to value estimates.

- A. Several computer software packages make it possible to detail and project large numbers of leases so that total project revenue is supported by a series of schedules as indicated by Exhibit 29. When using a discounted cash flow model, it is imperative to stay as close to cash accounting as possible.
- B. All forms of reimbursement must reflect time lags, and collection losses and renewals should be charged for concessions on past due proposals. Appraisers would be well advised to introduce a limiting condition to the effect that:

"Pro forma budgets and assumptions about actual collection of reimbursable expenses and supplemental rent are not based upon an actual audit of property operations and reflect only a business plan which could be accomplished through effective management."
- C. Operating expenses for appraisers were traditionally divided between fixed variable and reserve for replacement. Today operating expenses should be organized by groups which reflect method of, or degree of, reimbursement by tenants.
 1. Revenue projections can be prepared by a CPA or a property management firm with the computer systems to handle complex allocations, timing, and changeovers in leasing format. The appraiser explicitly recognized source and can allocate liability for same to the CPA or CPM who prepared the estimate.

2. Building owners or investment bankers may provide the computerized lease data base for the appraiser as a point of departure.
 3. The critical functions of the appraiser will be to estimate:
 - a. Rate of increase or decrease in operating expenses during the forecast period;
 - b. Estimate the tenant turnover and resulting loss of income from vacancy, concession, and relocation costs;
 - c. Estimate the rate and degree of application and collection of rental increases; and
 - d. Estimate concessions required to keep existing tenants, including special tenant improvements and refurbishing.
 4. Some clients are beginning to prescribe the specific assumptions for indexing rents and the ratio of tenant turnover and tenant renewal; again, these assumptions become significant limiting conditions on the appraisal report or the subject for extensive footnote discussion.
 5. CAM expenses are prorated on space occupied rather than usable area, so be careful where you apply flat vacancy allowances. Parking may be fully leased even if the building has substantial vacancies; at the same time, hotel room rates and office rents may conceal parking charges which are reallocated to the parking concession, so that the appraiser may unwittingly double-count.
- D. Many projects today are the beneficiaries of income generating reserves required of revenue bond issues, HODAG and UDAG grants, or municipal subsidy arrangements such as tax incremental financing. This income is part of the property value for mortgage loan purposes, but must be excluded for real estate tax purposes. The income from these reserves is generally available on a quarterly basis and the amount depends upon the reinvestment rate and allowable arbitrage at the times these reserves were created.

1. Reserves tied to the finances must be deducted from sales price on FNA or IRB financed deals, solely subject to the mortgage, or prices can be seriously overstated.
 2. R-41b specifically permits recognition of supplementary income from services regularly offered to tenants, such as the elderly.
 3. See Exhibits 31 and 32.
 4. Elderly housing pro forma.
- E. It is not necessary today to always use a mortgage equity approach. The conversion of net cash to present values may take several basic patterns.
1. Simple discounting of annual net cash by a project discount rate assuming no financing and reasonably stable re-sale price as shown in Exhibit 30 done for a pension fund.
 2. A simple mortgage equity approach using a five-year forecast and a debt cover ratio and other loan parameters based on natural averages of the American Council of Life Underwriters, Schedule M (see Exhibit 33).
 3. A basic mortgage package presuming responsible underwriting plus the sale value of appreciable base and tax credits to a professional buyer for syndication. For example: syndicators might pay 35 percent of depreciable base plus 80 percent of first-year tax investment credit; more conservative syndicators might pay exactly one-half of the tax value of equity.
 4. Custom crafted finance packages with variable rates, credit enhancements, interest rate caps, and participations become investment value situations which must be compared to fair market value so that the increment to value through the modification of the financial stand is revealed.

- F. As a result of all of the above, the appraisal process is subdivided into those firms which knowingly or unwittingly exploit the lack of accounting precedent to generate high values in the fine art of commercial disinformation. On the other hand, a fully-professional firm will integrate professional specialties into a clinic shop which contains a CPA, a mechanical engineer, a physical planner, an information processor, and an appraiser. The fastest growing segment of appraisal is the business consulting firm opening an appraisal subsidiary. Arthur Andersen went from almost "0" to \$16,000,000 last year, probably in third place behind the old-style firms of American Appraisal at \$66,000,000 and Marshall and Stevens at \$26,000,000. It is estimated that 20 percent of their volume is spent in marketing.

PAGES 121 TO 150 ARE MISSING

SEE:

JAMES A. GRAASKAMP COLLECTION OF TEACHING MATERIALS
V. INDUSTRY SEMINARS AND SPEECHES - SHORT TERM

- A. Appraisal Organizations
 - d. "Contemporary Issues and Methods for Appraising Commercial Properties", sponsored by AIREA Arizona Chapter 41, October 9, 1985.

**A RETIREMENT LIVING CENTER
 SCHEDULE OF PROJECTED REVENUES FROM
 JANUARY 1, 1985, THROUGH DECEMBER 31, 1994 (1)**

		ESTIMATED GROWTH RATES FROM 1987-1994 (2)									
		1985	1986	1987	1988	1989	1990	1991	1992	1993	1994
EFFECTIVE GROSS APARTMENT/SERVICE REVENUE (3)											
81 - 1 BR Apartment Units	5%	0	239501	221640	337092	353947	371644	390226	409737	430224	451735
60 - 2 BR Apartment Units	6%	0	266976	309093	327639	347297	368135	390223	413636	438454	464762
8 - 2 BR Deluxe Apartment Units	7%	0	47680	50719	54270	58069	62133	66483	71136	76116	81444
Service/Amenity Package - 149 Residents (3) (1st Occupant)	6%	0	435204	543639	576253	610828	647477	686326	727506	771156	817425
Service/Amenity Package - 37 Residents (2nd Occupant)	6%	0	68772	85907	91661	96525	102318	108455	114963	121861	129172
SUBTOTAL: EFFECTIVE GROSS APARTMENT/ SERVICE REVENUE		0	1058333	1310394	1386314	1466689	1551706	1641713	1736978	1837811	1944539
EFFECTIVE GROSS PARKING REVENUE (4)											
48 Attached Garages	5%	0	19114	21480	22954	23682	24666	25109	27415	28786	30225
60 Ancillary Attached Garages	5%	0	9360	14364	15082	15836	16628	17460	18333	19249	20212
SUBTOTAL: EFFECTIVE GROSS PARKING REVENUE		0	28474	35844	37636	39518	41494	42569	45747	48035	50438
LAUNDRY - EFFECTIVE GROSS REVENUE (5)											
5%	0	1712	2118	2224	2335	2452	2575	2703	2838	2980	2980
OTHER - EFFECTIVE GROSS REVENUE (5)											
7%	0	16892	21300	22791	24306	26093	27929	29874	31965	34203	34203
SUBTOTAL: EFFECTIVE GROSS REVENUE-RENT/ PARKING, LAUNDRY & OTHER SOURCES		0	1105411	1369656	1448965	1532904	1621745	1715776	1815303	1920649	2032158
INTEREST INCOME (6)											
Security Deposit @ 9%	0%	0	7599	8954	8954	8954	8954	8954	8954	8954	8954
Debt Service Reserve Fund @ 11.5%	0%	64400	64400	64400	64400	64400	64400	64400	64400	64400	64400
SUBTOTAL: INTEREST INCOME		64400	71999	73354	73354	73354	73354	73354	73354	73354	73354
TOTAL EFFECTIVE GROSS REVENUE (7)		64400	1177409	1443010	1522320	1606259	1695099	1789130	1888657	1994004	2105512

FOOTNOTES TO EXHIBIT 31 (Continued)

A RETIREMENT LIVING CENTER
 SCHEDULE OF PROJECTED REVENUES FROM JANUARY 1, 1985,
 THROUGH DECEMBER 31, 1994

[1] Detailed calculations of projected potential and effective gross revenue are found in Appendix C. The potential gross revenue and vacancy loss from each revenue source for each year are shown.

[2] Vacancy Loss: Although completion of ~~the project~~ is targeted for the late fall of 1985, for purposes of this appraisal it is assumed that operations begin on January 1, 1986, and all pre-leased units are occupied at that time. Based upon occupancy/vacancy projections detailed in Exhibit III-6 the 81 one-bedroom units will have an average vacancy loss of 23 percent in 1986 and apartment rents will remain at the same level as in 1984-85. The average vacancy thereafter will be stable at 1.7 percent per year for tenant turnover.

The 60 two-bedroom units will have an average vacancy loss of 10 percent in 1986 and will then be stabilized at 1.7 annually for tenant turnover.

The eight deluxe two-bedroom units have a waiting list 1-1/4 years before the project is scheduled to open. Vacancy will be 0 percent in 1986 and will average 1 percent thereafter to account for the time needed to redecorate as tenancy changes.

Inflation Rate: Landmark Research, Inc.'s 1984 apartment rental survey in ~~Seattle~~ and in ~~Seattle~~ indicates a varying pattern of rental increases from February 1984 to November 1984. The City of ~~Seattle~~ Department of Planning and Development previously referenced study also indicates a steady increase in rents for one- and two-bedroom units. The data given for efficiencies and three-bedroom units were discovered to contain some distortions, but the one- and two-bedroom information appears to be consistent with the 1982 data and Landmark's information. Landmark's rental study and the City of ~~Seattle~~ comparative rent data for 1982 and 1984 are found in Appendix B of this appraisal.

FOOTNOTES TO EXHIBIT 31 (Continued)

Based upon historic market rent increases in _____ and _____, comparative rents of other retirement centers in _____ and _____ on file in Landmark's office, changes in the consumer price index, and demand factors for unit types, the following inflation factors are projected for _____ :

For one-bedroom units, the rental revenue is expected to increase annually from 1987 at 5 percent after the initial rent-up period.

The two-bedroom units will have a greater demand in the early years of the project; the market survey results and the pre-leasing unit mix confirm this consumer preference. The appraiser estimates that the two-bedroom monthly service charge at \$675 per month was initially understated when compared with other _____ and _____ retirement center fees; because of the strong demand for two-bedroom units and the initial understatement of the total monthly service charge, the rent portion is expected to increase 3 percent in 1986 and is projected to increase at 6 percent annually thereafter.

The demand is high for the larger two-bedroom, 1.75 bath unit and therefore the rent is expected to increase 5 percent in 1986 and 7 percent per year thereafter, a rate which includes both a high demand and an inflationary factor.

- [3] The monthly service package, as detailed in Exhibit III-8, is projected to increase at 6 percent per year. As residents learn to live in and fully utilize the varied spaces and services available in a well-managed retirement living center, the value of this package will increase in intrinsic value to each resident. The revenue from the service package varies with occupancy; in 1986 occupancy is estimated to be 83.5 percent and in 1987 and thereafter, occupancy is expected to average 98.4 percent overall.
- [4] In 1986 the 48 attached garage stalls located on the south end of wings A and B are projected to experience a vacancy loss of 7.5 percent and an average of 1 percent thereafter. The rent is expected to increase by 2-1/2 percent in 1986 and at 5 percent thereafter.

FOOTNOTES TO EXHIBIT 31 (Continued)

The 60 ancillary enclosed garage stalls, expected to have a longer rent-up period, are projected to have a vacancy loss of 35 percent in 1986 and thereafter the vacancy loss is projected to be 5 percent annually. Rents will remain flat through 1986 and will then increase at the rate of 5 percent per year.

- [5] Laundry revenue will vary with occupancy at 83.5 percent in 1986 and 98.4 percent in 1987 and thereafter. Laundry revenue will increase 2-1/2 percent in 1986 from the 1985 lease amount and thereafter the annual increase is estimated to be 5 percent per year. This percentage increase in laundry revenue anticipates greater use of the washer/dryer beyond the allowance limit as well as the effect of inflation.

Other income from the coffee shop, beauty shop, guest rooms, and other sources will vary with occupancy. In 1986 allowances for vacancy is 16.5 percent, and in 1987 and thereafter, vacancy loss is projected to be no more than 1.6 percent. The gross potential revenue from these sources is projected to remain at the 1985 base amount until 1987 when the residents will have gradually adapted to living in a retirement center and will make fuller use of these facilities and services. In 1987 and thereafter, revenue from other sources will increase at the rate of 7 percent per year.

- [6] The interest earned on security deposits varies with occupancy; in 1986 only 83.5 percent of the potential security deposits were earning interest, but from 1987 on, interest was earned on 98.4 percent of the potential security deposits. Interest at 9 percent is expected to remain stable.

Interest earned on the Debt Service Reserve Fund does not vary with occupancy and the interest rate is projected to be stable at 11.5 percent.

- [7] The total effective gross income for years 1985 through 1994 is entered into the discounted cash flow program MRCAP as fixed income net of vacancy losses. See Exhibit IV-10.

~~██████████~~
A RETIREMENT LIVING CENTER
SCHEDULE OF PROJECTED REVENUES AND EXPENSES FROM
JANUARY 1, 1985, THROUGH DECEMBER 31, 1994 [1]

		1985	1986	1987	1988	1989	1990	1991	1992	1993	1994
TOTAL EFFECTIVE GROSS REVENUE [1]		64400	1177409	1442010	1522320	1606250	1695099	1789130	1880657	1974004	2105512
EXPENSES		1985	1986	1987	1988	1989	1990	1991	1992	1993	1994
	Base Amount First Year of Operation										
MANAGEMENT FEE [2]	30 effective gross before interest revenue	0	55270	68483	72440	76445	81087	85789	90765	96032	101600
FOOD SERVICE CONTRACT [3]	264771	0	221000	272500	287200	301602	316402	332518	349142	366599	384929
ADMINISTRATIVE [4]											
Personnel	75670	0	82101	78190	82100	86205	90515	95041	99793	104783	110022
Legal/Audit	10700	0	10700	11235	11800	12390	13010	13660	14343	15060	15813
Supplies, Dues & Advertising	5875	0	4900	6070	6300	6699	7034	7396	7755	8143	8550
SUBTOTAL: ADMINISTRATIVE	92253	0	78791	95495	100200	105294	110550	116007	121891	127906	134385
UTILITIES [5]											
Electricity	28700	0	24000	29370	30500	31720	32989	34308	35681	37108	38592
Water & Sewer	10700	0	8950	11050	11600	12180	12789	13428	14100	14805	15545
Gas	7600	0	6350	8000	7560	8089	8655	9261	9910	10603	11346
Telephone Service	12000	0	10020	12500	13270	14066	14910	15805	16753	17758	18824
SUBTOTAL: UTILITIES	59000	0	49320	60920	62930	66055	69343	72803	76443	80274	84307

EXHIBIT 32

MAINTENANCE (6)

Personnel-Building Services	42430	0	35430	44260	46910	49725	52708	55871	59223	62776	66543
Grounds Care	4725	0	3950	4880	5130	5387	5656	5939	6234	6547	6875
Rubbish Removal	2650	0	2200	2740	2870	3014	3164	3322	3489	3663	3846
Janitorial Supplies & Services	5985	0	5000	6180	6490	6815	7155	7513	7889	8283	8697
Vehicle Usage & Maintenance	3600	0	3000	3720	3910	4106	4311	4526	4753	4990	5240
Building Repairs & Maintenance	9035	0	7550	9430	9990	10589	11225	11898	12612	13369	14171
Elevator Maintenance Contract	7000	0	7000	7350	7718	8103	8509	8934	9381	9850	10342
Parking Lot Repair	200	0	200	200	1700	1802	1910	2025	2146	2275	2411
Decorating	5250	0	5250	5850	6140	6447	6769	7108	7463	7836	8228
Exterminating	850	0	710	880	920	966	1014	1065	1118	1174	1233
Laundry Expense	300	0	260	320	330	347	364	382	401	421	442
SUBTOTAL: MAINTENANCE	82025	0	70550	85810	92108	97299	102785	108583	114710	121185	128028
ALL RISK INSURANCE (7)	14700	0	14700	18440	18208	17918	17861	18754	19691	20676	21710
OPERATING EXPENSES BEFORE R.E. TAXES		0	489721	599708	631206	663905	698317	734531	772642	812752	854966
REAL ESTATE TAX (8)	13300	11650	13300	150500	174100	182805	191945	201543	211620	222201	233311
TOTAL OPERATING EXPENSES		11650	503021	750208	805306	846710	890262	936073	984262	1034952	1088277
NET OPERATING INCOME (before reserves, debt service, and income taxes)		52750	674388	692802	717014	759549	804837	853057	904395	959052	1017235

EXHIBIT 32 (Continued)

FOOTNOTES TO EXHIBIT

SCHEDULE OF PROJECTED REVENUES AND EXPENSES FROM
JANUARY 1, 1985, THROUGH DECEMBER 1, 1994

- [1] Total effective gross revenue is taken from Exhibit IV-8 which details each revenue component.

The operating expenses used for this project are based upon estimates made by [REDACTED] and checked for reasonableness against actual expenses experienced by other property managers in [REDACTED] or from service suppliers. The annual inflation factor of 5 percent used to forecast most of the expenses is based upon the following pattern of changes in the Consumer Price Index and upon the premise that current Federal deficits will cause the inflation rate to accelerate gradually from recent lows.

1980	-	10.8%	
1981	-	8.1%	
1982	-	3.5%	
1983	-	3.5%	
1984	-	4.0%	(Annualized)

- [2] The management fee is 5 percent of the effective gross revenue before interest revenue.

- [3] The expense for the food service contract assumes that all residents will utilize the seven-day meal plan which entitles each resident to one full dinner/supper each day of the week. The monthly service charge also includes the charge for the seven-day meal plan. The rate of increase in food service has been relatively stable in the past few years. according to [REDACTED], President of [REDACTED] in [REDACTED], from whom the quote of \$3.90 per meal per day was obtained.

forecasts future price increases to be less than 5 percent per year, including increases both for food products and for labor. Food service charges are assumed to vary with occupancy. Full occupancy of 149 residents plus 37 second occupants will result in an initial food service cost of \$264,771 (186 residents x 365 days x \$3.90), but in 1986, at 83.5 percent occupancy, the expense is \$221,090. In 1987 and thereafter, occupancy is assumed to remain stable at 98.4 percent with expenses increasing annually at 5 percent.

FOOTNOTES TO EXHIBIT

(Continued)

[4] Administrative personnel include an administrator, a resident service coordinator, a secretary-bookkeeper, receptionists, and other part-time administrative assistants. Added to the estimated base salary cost of \$63,065 is 20 percent for fringe benefits for a total base of \$75,678. Salaries are estimated to increase at 5 percent annually and staff size will vary with occupancy. Legal and audit costs are fixed and are inflated at 5 percent per year. Supplies, dues, and advertising costs vary with occupancy and are inflated annually at 5 percent.

[5] The Electric Power Company in has experienced a 2 percent rate decrease in 1984 and less than a 1 percent decrease has been requested for 1985. A surplus of electricity generating capacity in Wisconsin will keep electricity costs stabilized for the near future. Costs are assumed to increase at a generous 4 percent per year.

Natural gas increases in September/October of 1984 were approximately 3 percent. Both pipeline and utility operators expect the commodity charge for natural gas to be flat in the future with only inflationary increases anticipated, according to a spokesman for Natural Gas Co. An inflation factor of 5 percent is assumed for both gas and sewer and water. Local telephone service will be included in the monthly service charge for each apartment. The basic quote of \$12,000 from the telephone company for all telephone service is expected to inflate at 6 percent per year, higher than the anticipated inflation rate, because of the uncertainty of the telephone company's pricing policy.

[6] The personnel for building services include a full-time building service coordinator, a part-time general maintenance person and housekeepers to clean common areas and to provide monthly cleaning services for each apartment. The estimated salaries of \$35,360 plus 20 percent for fringe benefits total \$42,432. Salary increases for this type of work, more likely to be influenced by labor unions, are estimated to increase 6 percent annually.

Many of the maintenance services such as landscaping, rubbish removal, exterminating, and elevator maintenance are expected to be performed by contract. Parking lot repair and decorating expenses (the apartment portion of the total expenses) are expected to be minimal in the first two years of operation. An annual inflation factor of 5 percent is used to forecast expense increases for all maintenance categories except for labor. All maintenance expenses, except for the elevator contract, vary with occupancy or the age of the project.

FOOTNOTES TO EXHIBIT

(Continued)

[7] An all-risk insurance policy is a fixed expense and the premium is estimated to increase at 5 percent annually. Insurance coverage during construction is included in the construction budget.

[8] Real estate assessments are made as of the first of January of each year based upon the value in place on that day. Taxes, based on January first assessments, are due and payable in the following year, or an annual, semi-annual, or quarterly basis. Land value in 1984 is estimated to be \$462,000, or \$3,100 per unit. The 1983 net mill rate for property located in County was 0.02232 based upon assessments at 95.94 percent of full market value. At full market value the mill rate would be 0.02232/0.9594, or 0.02326. In 1984 the assessments are at 88.47 percent of full market value and the mill rate has not yet been determined. Using the 1983 mill rate of 0.02232/0.8847 equals a 1984 mill rate of 0.02523. Average mill rate increases over the past four years range from 2.5 percent to 4.4 percent for and Counties. However, forecasting real estate tax increases, an annual increase of 5 percent is used because State and Federal governments are continually withdrawing their tax funds from local tax districts.

For 1984 real estate taxes, payable in 1985, a land value of \$462,000 times a mill rate of 0.02523 yields taxes of \$11,650. As of January 1, 1985, the contractor estimates \$40,000 of site improvements will be added to the site. Therefore \$462,000 plus \$40,000, or \$502,000 times 0.02649 (0.02523 x 1.05) is \$13,300 for 1985 real estate taxes due in 1986. As of January 1, 1986, the project is expected to be 90 percent complete. Market value for real estate tax purposes of \$40,000 per unit includes \$3,100 per unit for land. Therefore, an improvement value of \$5,900,400, which is 90 percent complete, plus land, taxed at 0.02781 (0.02649 x 1.05) yields real estate taxes of \$150,500, payable in 1987. The completed project as of January 1, 1987, would be taxed at \$174,100 based upon the previously stated assumptions and would increase at 5 percent per year thereafter.

Table M

**Commitments of \$100,000 and Over on Multifamily and Nonresidential Mortgages
Made by 20 Life Insurance Companies**

Loan Size Class Within Major Property Type, Second Quarter, 1984

Major Property Type Loan Size	No. of Loans	Amount Committed (\$000)	Loan Amount (\$000)	Interest Rate (by %)	Interest Rate (by \$)	Loan/ Value	Averages			Maturity (Years/Months)
							Capitaliza- tion Rate	Debt Coverage	Percent Constant	
APARTMENT - CONVENTIONAL	22	147,578	6,708	12.94X	12.92X	68.9X	10.2X	1.12	13.3X	9/10
Less than \$1 million	1	923	923	^	^	^	^	^	^	^
\$1 million - \$3,999(000)	1	1,950	1,950	^	^	^	^	^	^	^
\$4 million - \$7,999(000)	11	72,005	5,539	12.78	12.82	70.8	10.3	1.12	13.3	10/4
\$8 million - \$14,999(000)	6	56,700	9,450	13.12	13.13	69.0	9.9	1.14	13.3	8/6
\$15 million and over	1	16,000	16,000	^	^	^	^	^	^	^
COMMERCIAL RETAIL	34	578,040	17,001	12.91	12.74	65.8	10.5	1.30	13.2	10/11
Less than \$1 million	1	900	900	^	^	^	^	^	^	^
\$1 million - \$3,999(000)	6	14,750	2,458	12.79	12.70	63.4	11.1	1.64	13.2	10/8
\$4 million - \$7,999(000)	10	53,765	5,376	13.06	13.01	64.8	10.7	1.26	13.4	8/11
\$8 million - \$14,999(000)	5	55,125	11,025	13.15	13.13	67.8	10.3	1.13	13.3	8/7
\$15 million and over	12	453,500	37,792	12.75	12.66	66.4	9.9	1.25	12.9	14/1
OFFICE BUILDING	153	2,039,996	13,333	12.94	13.01	69.7	10.5	1.25	13.1	10/9
Less than \$1 million	6	4,185	698	13.59	13.67	60.4	11.9	1.14	14.0	6/8
\$1 million - \$3,999(000)	43	106,296	2,472	13.07	13.03	70.7	10.9	1.19	13.2	8/7
\$4 million - \$7,999(000)	43	242,231	5,633	13.08	13.06	69.2	10.4	1.39	13.2	9/6
\$8 million - \$14,999(000)	24	256,054	10,669	12.38	12.38	71.3	10.4	1.18	12.6	13/9
\$15 million and over	37	1,431,230	38,682	12.94	13.11	69.6	9.9	1.20	13.2	13/5
COMMERCIAL SERVICE	21	104,692	4,985	13.19	13.26	64.4	10.8	1.41	13.6	9/0
Less than \$1 million	1	710	710	^	^	^	^	^	^	^
\$1 million - \$3,999(000)	11	24,027	2,184	13.25	13.22	68.9	11.4	1.23	13.6	9/7
\$4 million - \$7,999(000)	5	25,725	5,145	12.88	13.00	53.4	9.4	1.59	13.7	9/7
\$8 million - \$14,999(000)	2	17,000	8,500	^	^	^	^	^	^	^
\$15 million and over	2	37,230	18,615	^	^	^	^	^	^	^

^Data not shown for a limited number of loans.

(cont'd)

Second Quarter, 1984 (Cont'd)

Table M - page 2

Major Property Type Loan Size	No. of Loans	Amount Committed (\$000)	Averages							
			Loan Amount (\$000)	Interest Rate (by %)	Interest Rate (by %)	Loan/ Value	Capitaliza- tion Rate	Debt Coverage	Percent Constant	Maturity (Years/Months)
INSTITUTIONAL AND RECREATIONAL	1	5,000	5,000	%	%	%	%	*	%	*
INDUSTRIAL	40	240,163	6,004	12.00	12.49	71.4	10.6	1.15	13.1	4/5
Less than \$1 million	3	2,420	807	14.04	13.97	61.8	10.9	1.33	14.0	3/8
\$1 million - \$3,999(000)	18	30,912	2,162	13.01	12.94	72.4	11.0	1.18	13.2	6/8
\$4 million - \$7,999(000)	13	75,283	5,791	12.00	12.81	72.8	10.2	1.09	12.8	5/0
\$8 million - \$14,999(000)	2	23,559	11,700	"	"	"	"	"	"	"
\$15 million and over	4	99,989	24,997	11.00	11.96	72.4	9.9	1.03	13.1	10/0
HOTEL AND MOTEL	11	101,732	9,240	13.34	13.30	48.7	11.0	1.05	13.8	8/9
\$1 million - \$3,999(000)	2	4,000	2,000	"	"	"	"	"	"	"
\$4 million - \$7,999(000)	5	27,982	3,396	13.37	13.39	44.2	11.4	1.34	14.7	11/4
\$8 million - \$14,999(000)	1	8,000	8,000	"	"	"	"	"	"	"
\$15 million and over	3	61,750	20,343	13.33	13.20	34.1	9.9	1.71	13.3	6/8
MULTIPLE PROPERTY COMPLEX (ATL \$15 million and over)	3	120,000	42,647	13.00	13.00	60.9	10.0	1.31	13.3	10/0
TOTAL	285	3,345,201	11,730	12.97	12.93	60.1	10.5	1.27	13.2	9/10

*Data not shown for a limited number of loans.

Note: Averages for capitalization rate, debt coverage ratio and percent constant may represent a fewer number of loans than the total for the specified category. Averages for interest rate are based on 273 loans. These include seven accrual loans with a mean accrual rate of 13.50% and a dollar-weighted average accrual rate of 13.67%. Nonrefundable fees were reported in connection with 31% of the total number and 42% of the amount committed. The comparable shares by property type ran 60% and 81% for apartments, 24% and 20% for commercial retail, 29% and 53% for office buildings, 24% and 24% for commercial services, 35% and 28% for industrial, and 9% and 17% for hotels and motels.

EXHIBIT 34

VALTEST
Discounted Cash Flow Model
(Renamed ATCF in Real Estate Planning Program)

4. Test for Investment Yield at Estimated
Market Value Assuming Cash to the Seller

A computerized discounted before and after tax cash flow program, VALTEST, is used to test the reasonableness of the appraised value. Input assumptions used are shown in Exhibit IV-4 and are taken from the Schedule of Revenues and Expenses (Exhibit IV-2) and from the MRCAP program output (Appendix C) which solved for the justified mortgage, assuming a debt cover ratio of 1.4 based upon the first year NOI of \$126,498. The net resale price is assumed to be \$1,130,000 based upon a net income multiplier of 6.5 applied to the NOI in the tenth year of the holding period, and cash resale costs of 4 percent.

The resulting modified internal rate of return of 15.6 percent before taxes and 14.2 percent after taxes represents a minimum threshold for equity investors. The Air Cargo Facility is fully priced at \$1,000,000 assuming cash to the seller and financed at a 13.25 percent interest rate and a 25-year term. (See Exhibit IV-4 for VALTEST output.)

EXHIBIT IV-4

INPUT ASSUMPTIONS

1. ENTER PROJECT NAME ? AIR CARGO FACILITY
2. ENTER PROJECTION PERIOD ? 10
3. DO YOU WANT TO ENTER EFFECTIVE GROSS REVENUE INSTEAD OF NOI? N
 - N.O.I. YEAR 1? 126498
 - N.O.I. YEAR 2? 131770
 - N.O.I. YEAR 3? 136943
 - N.O.I. YEAR 4? 142327
 - N.O.I. YEAR 5? 148691
 - N.O.I. YEAR 6? 154521
 - N.O.I. YEAR 7? 160588
 - N.O.I. YEAR 8? 167710
 - N.O.I. YEAR 9? 174280
 - N.O.I. YEAR 10? 181113
4. ACQUISITION COST: ? 1000000
5. DO YOU WANT TO USE STANDARD FINANCING? Y OR N?Y
 - MTG. RATIO OR AMOUNT, INT., TERM, NO PAY/YR ? 656633, .1325, 25, 12
6. ENTER RATIO OF IMP #1/TOTAL VALUE, LIFE OF IMP #1? 1, 18
 - IS THERE A SECOND IMPROVEMENT? Y OR N? N
7. DEPRECIATION METHOD, IMPROVEMENT #1 ? 1
 - IS PROPERTY SUBSIDIZED HOUSING ? Y OR N ?N
 - IS PROPERTY RESIDENTIAL? Y OR N? N
8. IS OWNER A TAXABLE CORPORATION? Y OR N ?N
 - THE MAXIMUM FEDERAL INDIVIDUAL ORDINARY RATE COULD BE:
 - 70% (PRE-1981 LAW)
 - 50% (1981 LAW, EFFECTIVE 1982)
 - (PLUS STATE RATE)
- ENTER:
 - 1) EFFECTIVE ORDINARY RATE 2) EFFECTIVE ORDINARY RATE (YEAR OF SALE)
 - ? .4, .4
9. RESALE PRICE (NET OF SALE COSTS) ? 1130000
10. IS THERE LENDER PARTICIPATION ?N
11. ENTER OWNER'S AFTER TAX REINVESTMENT RATE (Z)? 9
12. ENTER OWNER'S AFTER TAX OPPORTUNITY COST OF EQUITY FUNDS (Z)? 9

EXHIBIT IV-4 (Continued)

AFTER TAX CASH FLOW PROJECTION
AIR CARGO FACILITY
DATE 1/1/85

DATA SUMMARY

ACQUISTN COST: \$1,000,000.	MTG. AMT.: \$656,633.
NOI 1ST YR: \$126,498.	MTG. INT.: 13.25%
ORG. EQUITY: \$343,367.	MTG. TERM: 25. YRS
LTD 1ST YEAR: \$36,143.	DEBT SERVICE 1ST YEAR: \$90,355.
	MTG. CONST.: .137604
IMP. #1 VALUE: \$1,000,000.	IMP. #1 LIFE: 18.
INC. TX RATE: 40%	
SALE YR RATE: 40%	OWNER: INDIVIDUAL

DEPRECIATION IMPROVEMENT #1 : STRAIGHT LINE
NON-RESIDENTIAL PROPERTY
LENDER PARTICIPATION: CASH THROW-OFF: NONE REVERSION: NONE

NO REPRESENTATION IS MADE THAT THE ASSUMPTIONS BY LANDMARK RESEARCH, INC ARE PROPER OR THAT THE CURRENT TAX ESTIMATES USED IN THIS PROJECTION WILL BE ACCEPTABLE TO TAXING AUTHORITIES. NO ESTIMATE HAS BEEN MADE OF MINIMUM PREFERENCE TAX. CAPITAL LOSSES IN THE YEAR OF SALE ARE TREATED AS ORDINARY LOSSES (SECTION 1231 PROPERTY) AND ARE CREDITED AGAINST TAXES PAID AT THE ORDINARY RATE AT THE TIME OF SALE.
FOR THE PURPOSE OF THE MODIFIED INTERNAL RATE OF RETURN (M.I.R.R.) CALCULATION, NEGATIVE CASH IN ANY ONE PERIOD IS TREATED AS A CONTRIBUTION FROM EQUITY IN THAT PERIOD.

YEAR	NOI	MTG INT & LENDERS %	TAX DEP	TAXABLE INCOME	INCOME TAX	AFTER TAX CASH FLOW
1.	126498.	86793.	55556.	-15851.	-6341.	42484.
2.	131770.	86291.	55556.	-10077.	-4032.	45447.
3.	136943.	85718.	55556.	-4332.	-1734.	48322.
4.	142327.	85065.	55556.	1706.	682.	51290.
5.	148691.	84320.	55556.	8815.	3526.	54810.
6.	154521.	83470.	55556.	15495.	6198.	57968.
7.	160598.	82500.	55556.	22532.	9013.	61220.
8.	167710.	81394.	55556.	30761.	12304.	65051.
9.	174280.	80132.	55556.	38593.	15437.	68488.
10.	181113.	78692.	55556.	46866.	18746.	72012.
	\$1524441.	\$834375.	\$555556.	\$134508.	\$53799.	\$567089.

EXHIBIT 34 (Continued)

EXHIBIT IV-4 (Continued)

RESALE PRICE: \$1,130,000.
 LESS MORTGAGE BALANCE: \$587,454.
 PROCEEDS BEFORE TAXES: \$542,546.
 LESS LENDER'S %: \$0.
 NET SALES PROCEEDS
 BEFORE TAXES: \$542,546.
 =====

1ST YR B4 TAX EQ DIV: 10.5260%
 AVG DEBT COVER RATIO: 1.6872

RESALE PRICE: \$1,130,000.
 LESS LENDER'S %: \$0.
 NET RESALE PRICE: \$1,130,000.
 LESS BASIS: \$444,444.
 TOTAL GAIN: \$685,556.
 EXCESS DEPRECIATION: \$0.
 EXCESS DEP. FORGIVEN: \$0.
 CAPITAL GAIN: \$685,556.
 ORDINARY GAIN: \$0.
 =====

TAX ON ORDINARY GAIN: \$0.
 TAX ON CAPITAL GAIN: \$109,689.
 PLUS MORTGAGE BAL: \$587,454.
 TOTAL DEDUCTIONS FROM
 NET RESALE PRICE: \$697,143.
 =====

NET SALES PROCEEDS
 AFTER TAX: \$432,857.
 =====

IF PURCHASED AS ABOVE, HELD 10 YEARS & SOLD FOR \$1,130,000.
THE MODIFIED I.R.R. BEFORE TAXES IS 15.2639% AND AFTER TAXES IS 13.8784%.
 ASSUMING AN AFTER TAX REINVESTMENT RATE OF 9%, AND OPPORTUNITY COST OF 9%

EXHIBIT 34 (Continued)

EXHIBIT IV-4 (Continued)

EQUITY ANALYSIS
AIR CARGO FACILITY

BEFORE TAX EQUITY DIVIDEND

YR	NOI	YR END EQUITY	AMOUNT	CASH RETURN	
				ORG EQ	CUR EQ
1.	\$126,498.	\$346,930.	\$36,143.	.1053	.1042
2.	131,770.	350,994.	41,415.	.1206	.1180
3.	136,943.	355,631.	46,588.	.1357	.1310
4.	142,327.	360,921.	51,972.	.1514	.1440
5.	148,691.	366,956.	58,336.	.1699	.1590
6.	154,521.	373,842.	64,166.	.1869	.1716
7.	160,588.	381,697.	70,233.	.2045	.1840
8.	167,710.	390,658.	77,355.	.2253	.1980
9.	174,280.	400,882.	83,925.	.2444	.2094
10.	181,113.	412,546.	90,758.	.2643	.2200

ORIGINAL EQUITY: \$ 343367

MORTGAGE ANALYSIS
AIR CARGO FACILITY

YEAR	NOI	MORT INT.	MORT AMORT	DEBT SERV	DCR	MTG. BAL.
1.	126498.	86793.	3563.	90355.	1.400	653070.
2.	131770.	86291.	4064.	90355.	1.458	649006.
3.	136943.	85718.	4637.	90355.	1.516	644369.
4.	142327.	85065.	5290.	90355.	1.575	639079.
5.	148691.	84320.	6035.	90355.	1.646	633044.
6.	154521.	83470.	6885.	90355.	1.710	626158.
7.	160588.	82500.	7855.	90355.	1.777	618303.
8.	167710.	81394.	8961.	90355.	1.856	609342.
9.	174280.	80132.	10224.	90355.	1.929	599118.
10.	181113.	78692.	11664.	90355.	2.004	587454.
AVG	\$152,444.				1.687	

EXHIBIT IV-4 (Continued)

DEPRECIATION SCHEDULE
 AIR CARGO FACILITY
 IMPROVEMENT # 1
 STRAIGHT LINE
 NON-RESIDENTIAL

YEAR	TAX DEP.	S.L. DEP.	EXCESS DEP	BALANCE
1.	55555.6	55555.6	.0	944444.4
2.	55555.6	55555.6	.0	888888.9
3.	55555.6	55555.6	.0	833333.3
4.	55555.6	55555.6	.0	777777.8
5.	55555.6	55555.6	.0	722222.2
6.	55555.6	55555.6	.0	666666.6
7.	55555.6	55555.6	.0	611111.1
8.	55555.6	55555.6	.0	555555.5
9.	55555.6	55555.6	.0	500000.0
10.	55555.6	55555.6	.0	444444.4
=====				
TOTAL	555555.6	555555.6	.0	

DISTRIBUTION OF CASH THROW-OFF
 AIR CARGO FACILITY

YEAR	CASH THROW-OFF TOTAL	CASH THROW-OFF TO EQUITY	CASH BONUS TO LENDER
1.	36143.	36143.	0.
2.	41415.	41415.	0.
3.	46588.	46588.	0.
4.	51972.	51972.	0.
5.	58336.	58336.	0.
6.	64166.	64166.	0.
7.	70233.	70233.	0.
8.	77355.	77355.	0.
9.	83925.	83925.	0.
10.	90758.	90758.	0.

	620888.	620888.	0.

RESALE PRICE: \$1,130,000.
 LESS MORTGAGE BALANCE: \$587,454.
 PROCEEDS BEFORE TAXES: \$542,546.
 LESS LENDER'S %: \$0.
 NET SALES PROCEEDS
 BEFORE TAXES: \$542,546.
 =====

CASH THROW-OFF = 0% REVERSION = 0%

Copy



James A. Graaskamp, Ph.D., S.R.E.A., C.R.E.

Jean B. Davis, M.S.

May 13, 1985

Norman P. Swent, Executive Director
Northwest Center for Professional Education
13555 Bel-Red Road
C-96870
Bellevue, WA 98009

Dear Paul:

Here are the two one-day course outlines I promised. Let me know if there is more detail required.

Please send a note confirming the various dates for the fall-winter road show as I seem to have misplaced your note.

Best regards,

A handwritten signature consisting of several overlapping lines, appearing to be the name "James A. Graaskamp".

JAMES A. GRAASKAMP

NORTHWEST CENTER FOR PROFESSIONAL EDUCATION

One Day Seminar

CONTEMPORARY ISSUES AND METHODS FOR APPRAISING COMMERCIAL PROPERTIES

- 8:30 - 10:00 Defining the appraisal problem with the client, his attorney, and the accountant
- A. The issue for which the appraisal is required as a benchmark
 - B. The exact "sticks" in the bundle of rights to be appraised
 - C. The perspective in time, viewpoint, and going concern assumption controlling the appraisal
 - D. The definition of value to be applied
 - E. Responsibility for engineering, marketing, or legal/political data and assumptions
 - F. Special enhancements or encumbrances to be valued as components
 - G. Specification as to methods, data sources, and controls on use through letter of engagement

Coffee Break

- 10:15 - 12:00 Decision theory and improved methods for the market comparison approach
- A. The three approaches in the contemporary method
 - B. Market inference by means of proxy patterns
 - C. Why regression pricing is discredited
 - D. Developing a pricing algorithm for comparable properties
 - E. Selecting the proper unit of comparison
 - F. The price per point per unit of comparison
 - G. Developing a point system for significant attributes of comparison
 - H. Developing a weighting system for the attribute scores
 - I. Testing the price weighting system for best estimate of the comparables by hand or by computer
 - J. Variations on the theme by Dilmore

LUNCH

- 1:00 - 3:00 Professionalizing the income approach or investment simulation approach
- A. Recognizing the significance for allocating income to real estate, personalty, intangible assets or management, depending upon the issue for which the appraisal is sought as a benchmark

- B. Perspective and accounting: cash or accrual, normalized or simulated
- C. Revenue classification and projection
- D. Operating expense classification and projection
- E. Income from operations vs. cash for distribution
- F. Projecting increases, leakages, and concessions
- G. Formatting the pro forma real estate operating statement
- H. Financial footnotes in lieu of a narrative report

Coke Break

3:00 - 5:00

Case examples of defining the issue, the method, and the accounting relevant to litigation

- A. Real estate tax appeal for subsidized houses
- B. Credit enhanced elderly housing with HODAG and income from providing support services
- C. Right-of-way for a power transmission line
- D. Partnership values in dissolution

5:00 - 5:30

Professional status for the appraisers in litigation matters

- A. The vested interest of the attorney
- B. Counseling vs. advocacy
- C. Compensation relative to value of service

Northwest Center for Professional Education

Just sp.

13555 Bel-Red Road, C-96870, Bellevue, Washington 98009 • (206) 746-4173

June 19, 1985

Dr. James A. Graaskamp
Pyare Square Building
4610 University Ave.
Room 118
Madison, WI 53705

Dear Jim:

As I'm sure you probably know by now, as a result of your discussion with Clem, we have decided to keep the New York City dates, September 26 and 27, for your program.

As you indicated, this fits your schedule the best, coupled with your personal objectives, so we will go ahead and market the program accordingly.

We look forward to a successful series of seminars.

Sincerely,



Norman P. Swent
Executive Director

NPS/tk

PENSION FUND
REAL ESTATE VALUATION ISSUES

Presented by

Professor James A. Graaskamp
School of Business
University of Wisconsin

September 27, 1985

PENSION FUND
REAL ESTATE VALUATION ISSUES

Presented by

Professor James A. Graaskamp
School of Business
University of Wisconsin

November 10-13, 1985

NORTHWEST CENTER FOR PROFESSIONAL EDUCATION

One Day Seminar

REAL ESTATE VALUATION ISSUES FOR PENSION FUND REAL ESTATE

8:30 - 10:00

The case for greater standardization of appraisal/
accounting reporting for asset valuation and performance
measurement

- A. Appraisal process must respond to issues for which appraisal is required as a benchmark
 - 1. Adequacy of pension funding
 - 2. Entry/exit unit values of co-mingled shares in real estate pools
 - 3. Performance of asset managers
- B. Traditional presumptions of appraisal standardization
 - 1. Appraisal format imposed by professional societies in the U.S.
 - 2. Appraisal format imposed in the Common Market
 - 3. Appraisal format under development for imposition by American intermediary banking institutions, i.e. FHLB, FDIC, and FNMA
 - 4. Guidelines for pension managers by NCREIF
- C. Proposed research process of actual appraisal practices of pension real estate managers and methodology
 - 1. Formal pension policy, if any
 - 2. Selection and control of appraisals for asset measurement
 - 3. Pattern of practice revealed in actual paired appraisals
 - 4. Procedure and controls on internal appraisal values by asset managers between anniversary appraisals
- D. Preliminary findings of study financed by PREA interpreted by Graaskamp and Gibson are basis for following discussion

Coffee Break

10:15 - 12:00

Suggested requirements for developing consistent appraisal quality and performance by appraisers

- A. Basic components of standardization process
 - 1. Standards promulgated by industry association
 - 2. Written policy statement by pension fund sponsor

3. Written appraisal method statement to implement #2 by asset manager
4. Letter of engagement to the appraiser
5. Explicit methodology and terminology from appraisal association
- B. Standards promulgated by industry association
 1. FASB and MAIs
 2. Consistency with NCREIF guidelines
 3. Objectives of ERISA
 4. Total fee income and substantial economic ties constituting conflict of interest
 5. A vacuum of appraisal standards or white paper methods
- C. Valuation controls imposed by pension sponsor
 1. Frequency, quality, and independence
 2. Parameters for projection and simulation
 3. Responsibility for structural and mechanical engineering integrity
 - ~~4. Permissible level of aggregate simulation~~
 - ~~5. Segregated accounts vs. open co-mingled accounts~~
 - ~~6. Accounting issues in the aggregate~~
 - ~~7. Is the absence of specification relying on comprehensive interpretation of fiduciary responsibility?~~
- D. Some suggested formats

LUNCH

1:00 - 2:30

Basic problems in appraiser execution of the market approach to values

- A. Failure to establish the best unit of comparison between properties
- B. Failure to report terms of sale or quantitative adjustments for cash equivalency
- C. Failure to establish rules for selection and quantification of accounting patterns
- D. Failure to explain adjustments for differences
- E. Failure to report addresses and transaction details of comparables
- F. Other findings

Coke Break

2:45 - 3:45

The perceived need for a standardized accounting format, accounting rules, and assumptions

- A. Inconsistency of discounted cash flow concepts and appraisal pro forma accounting
- B. Establishing formats for revenue schedules, expense schedules, and working capital commitments to amortizable assets such as tenant improvements, lease renewal commissions, and financing charges
- C. Providing the appraiser with receipt and expenditure models pre-build by accountants for market review by appraisers--an ethical issue?

1. Independence vs. integration of accounting-
budgeting and appraisal forecasting
 2. Selecting value benchmarks relevant to
solvency, resale, and comparative
performance of asset manager
 3. Accounting vs. appraisal relative to
replcation, validation, and representativeness
of economic results
- D. Alternative methods of income property valuation
control revealed by PREA study

3:45 - 4:30

Philosophies and practices of asset managers relative to
internal appraisal procedures

- A. Alternative internal procedures and controls
- B. Justification of quarterly adjustments to
independent appraisals
- C. Integration of capital expenditures during
interim period with independent appraisers
- D. Reallocation of values relative to leasehold
value and investment value due to passage of
time and perceived changes in discount rates
- E. Should quarterly sequence of appraised value
changes and source of change be indicated for
each property for fund investors?

4:30 - 5:00

Alternatives to more disciplined appraisal practices
that would be easier to implement and more cost effective

- A. Valuation reserves reflecting potential
appraisal bias to the high side, which are
deducted from asset value
 1. Effect is to provide a bid and asked unit
price
 2. Effect recognizes that investors who are
exiting see less favorable risk/payoff
matrix than those who are remaining or
investing
- B. Dollar-averaging of commitments to invest or
disinvest over six quarters so that two
independent appraisals of total portfolio could
have occurred
- C. Prohibiting quarterly internal adjustments
to value with the exception that capital
expenditures would be carried as a separate
account to the next valuation date of each
property

PENSION FUND
REAL ESTATE VALUATION ISSUES

Presented by

Professor James A. Graaskamp, Ph.D., CRE, SREA
University of Wisconsin, School of Business

INTRODUCTION

- I. Appraisal is a specialty in the rapidly evolving information business in a society where a majority of the people are involved in information processing. Appraisers systematically collect information, organize, analyze, and interpret the data, reach decisions and communicate essential information to a client.
 - A. Real estate appraisal is a pivotal benchmark for decisions involving social equity (eminent domain and real estate taxes), validation of value for regulatory purposes (loans and pension security), benchmarking of asset management performance (pensions and fixed assets on balance sheets), and counseling for allocation of land uses and cost effective capital allocation. Ethical issues pervade the process.
 - B. Information processing by appraisers is similar to the work of accountants, lawyers, investment counselors, and insurance people. Unlike accountants and others, appraisers receive little help from their professional organizations in the form of position papers which define appropriate methods for a particular question.
 1. Financial Accounting Standards Board (FASB) continually modifies generally accepted accounting principles to fit new problems such as mergers, current values of fixed assets, accounting for real estate operations, etc.
 2. The Lawyers' Ethics Committee has placed responsibility for "misleading" appraisals in tax work and eminent domain on the attorneys. The IRS can blacklist appraisers whose values exceed 150 percent of ultimate courtroom settlements.
 3. Securities people have the SEC, Midwest Securities Associations, and various licensing agencies.

4. Appraisers have no such independent source or consensus. Even the eighth edition of the American Institute of Real Estate Appraiser's (AIREA) textbook, The Appraisal of Real Estate, disclaims any responsibility for being a standard.
- C. In the absence of professional standards, appraisal clients have taken responsibility for initiating true reforms or exploiting nominal format disinformation.
1. In the 1930s, reform of the residential mortgage markets led to development of the three approaches and creation of the Institute in order to define a standard of malfeasance and self-policing organization to control malpractice. The hope was that a very systematic format would provide a standard for evaluating performance.
 2. The volatility of real estate values due to inflation and the legal risks and costs of enforcement made it difficult to operationalize professional enforcement for 25,000 appraisers. However, pension fund real estate may involve only 250 appraisal firms or appraisers.
 3. Systematic formats once taught to everyone dealing with appraisal without stringent review leads to the potential for disinformation.
 4. Disinformation is military intelligence language for providing information which appears to be correct in form and terminology so that the reader rationalizes to the wrong conclusion.
 5. Disinformation through an appraisal format is a conspiracy of cooperation between the appraiser and his client to satisfy regulators, provide cover against second guessing on transactions which go awry, or rationalize common objectives to make a mortgage loan, negotiate real estate taxes, negotiate divorce settlements, etc.
- D. The opportunity for disinformation has been enhanced by low cost minicomputers which encourage standard formats for word processing and use of large data banks of unknown quality.
1. Sophisticated formats and boilerplate prose in industrial volume tend to conceal the validity of assumptions driving the process.
 2. Data banks lead to unknowing or deliberate misuses of statistics. Ultimately, the Home Loan Bank had to disallow single family home appraisals

using Ellwood because of the subtle potential for distortion of the appraisal process.

3. The ethics of data analysis, manipulation, and communication is overwhelming the professional societies and the costs of abuse are falling on public institutions such as FSLDIC and ERISA, rather than the appraiser or his client.
- E. The appraisal process was therefore unprepared to deal with real estate investment and fiduciary account where values had to be determined monthly, quarterly, or annually.
1. Real estate is a long-term investment which does not lend itself to constant measurement of value perceived, actual or by inference, from a market of fungible goods.
 2. The cost of proper valuation as well as the time to conduct the appraisal make any result untimely and less than cost-effective.
 3. The cost of cheap appraisal is a loss of sensitivity to the value fluctuations necessary to validate asset values, measure performance of the asset, or monitor the skills of the asset manager.
- F. Quality control of the appraisal process for pension fund assets will require a broad set of administrative efforts by associations of pension sponsors, asset managers, and appraisal organizations to overcome the general distrust of appraisal created by its use for disinformation in other areas and to accomplish its goals in facilitating efficient use of real estate capital.
1. Pressure must be taken off the cost-effectiveness of the appraisal process by reducing the frequency, but increasing the quality of independent appraisal by changing existing administrative policies.
 2. An association of pension sponsors and ERISA must establish the standards for selection and performance of appraisers since appraisal organizations are not well-equipped to deal with narrow specialities within a generic profession.
 3. Appraisal clients and appraisal organizations specifically concerned with pension real estate

will have to create their own appraisal methodology to meet objectives in a proactive format.

G. To that end, it will be useful to review various efforts to interface appraisal theory, methodology, and institutional regulatory objectives, in general, as well as in reference to pensions, in particular.

II. The general conceptual framework of the appraisal process has been expanding at a rate which would keep pace with information processing tendencies of our society. Valuation theories range from the mysticism of Dilmore to the pragmatism of Ratcliff to the deductive idealistic logic of traditional approaches.

A. In the information game there are three approaches to valuation methodology, according to Dilmore.

1. ORDER assumes under everything is a universe in which the parts fit, information has a shape. Remember the test for color blindness, as random dots in random colors until suddenly you see the red dots only as a letter or number. As appraisers, we look for the red dots. We try to organize data objectively which has been subjectively collected and perhaps naive.
2. CHANCE acknowledges the possibility of alternative outcomes in our little closed system. Imprecision is inherent to behavioral science. No respectable scientist is afraid of the work error or variance. We know in part and see but through a glass darkly. We may be able to predict without always understanding cause and effect because of unknown cross-correlations.
3. BEAUTY can be a legitimate basis for constructing a hypothesis--elegance is the ultimate intuitive choice, judgement, or gut response. Models may be elegant and not fully understood, but useful and sometimes dangerous like Ellwood, regression, and cost.

B. Each of the above may have application to the pension process to the effect that current value can be stabilized with standardized methods stressing investigation to expose the exception; chance must be an appropriate way of measuring present value of uncertain futures, and elegance may lead to development of portfolio models based on the entire portfolio of leases by industry rather than individual buildings per se or some other concept.

- C. Ratcliff restated contemporary real estate appraisal theory into an inductive, pragmatic process to be further considered today.
1. The issue for which the appraisal is sought as a benchmark would define value, the assets to be included in the appraisal, and the necessary cost effectiveness of the process. For Ratcliff, it was an inductive process which moved from description of the property to identification of alternative uses.
 2. Alternative uses could be evaluated to identify the most probable use, which in turn would identify the most probable buyer type.
 3. The appraisal problem was to forecast the price at which the most probable buyer and seller would make a deal under a specific set of decision rules or conditions.
- D. For Ratcliff, the best way to forecast how a specific buyer-type would behave in the future was to observe how they had behaved in the past in similar circumstances. Ratcliff advocated a specific hierarchy of approaches to valuation, once again a trinity, (1) INFERENCE FROM A SET OF MARKET TRANSACTIONS, (2) BUYER SIMULATION, or (3) NORMATIVE METHODS OF DEDUCTIVE LOGIC.
1. MARKET INFERENCE from a set of market transactions required actual transactions involving properties with similar productivity potential as the subject property to be appraised and buyers presumed to have similar motivation to the most probable buyer identified from the scenario of alternative uses. Depending on the number of available data points, inference could involve statistics, set theory, or simple bracketing.
 2. BUYER SIMULATION of the buyer calculus may be required in the absence of definitive sales. Simulation can range from conventional benchmarks like price per barrel of cranberry production or licensed nursing home beds to discounted cash flow models using probability techniques.
 3. NORMATIVE methods are the deductive logic of economists and appraisers reflecting what the market should do if it were as smart as the appraiser. Deductive approaches like the cost approach are the least likely to be predictive of market behavior, and therefore inappropriate for predicting most probable price, but logically

compatible with the artificial concept of fair market value.

- E. The traditional approaches at a simple, idealistic logic and economic rational is based on the principle of substitution--specifically that buyers and sellers had alternative of nearly equal acceptability, or sentiment, not to mention access to cash capital and freedom from irritation and duress.
1. MARKET COMPARISON methods are preferred, but the appraisal profession has found it difficult to develop objective methods for neutralizing differences and selecting properties objectively.
 2. The INCOME APPROACH is schizophrenic as to whether it is measuring economic productivity, the sum of liability, or the change in spendable cash for ownership through control of property rights.
 3. The COST APPROACH has moved from unethical according to the National Association of Realtors (NAR) in 1925, to pivotal in 1935, to embarrassing in 1985 since no one is sure if fiduciary responsibility requires a cost approach to avoid a sin of omission in the event of unforeseen disputes about value.
- F. However, none of these methodologies as logic systems structure the behavioral process required of the appraiser and his client. The client assumes that the task is defined when you ask for an appraisal and the appraiser assumes the client understands the rationale and appropriate application of fair market value or probable price. Both are more concerned with form than the substance of careful recognition of the problem for which the appraisal will serve as a benchmark. The problem suggests:
1. Objective appraisal
 - a. Validate purchase price as appropriate.
 - b. Identify change in price over time, if any.
 - c. Independent inspection of property and review of property management effectiveness.
 - d. Liquidating value of asset currently.
 - e. Future value of present assets.
 - f. Historical return on investment or future return on investment, real or nominal.
 2. Definition of value to be sought
 - a. Alternative definitions of value and related assumptions.

- b. Which definition of value is to be applied to which problem?
- c. Market value vs. probable price. (Exhibit 1)

3. Definition of assets to be valued

- a. Property rights to be appraised.
- b. Accounting rules to defining assets, collectively (going concern) or individually (liquidating).

4. Definition of methods to be used

- a. What constitutes comparative market data?
- b. What constitutes objective market comparisons?
- c. What constitutes an income approach to value?
- d. Relevance of the cost approach to appraisal and appraisal adjustments.
- e. Which appraisal methods are appropriate to which appraisal functions?

5. Definition of elements income approach

- a. Cash or accrual accounting.
- b. Going concern value or value attributed to land and buildings.
- c. Accounting rules for income.
- d. Forecasting rules for changing income and expenses.
- e. Estimating rules for changing income and expenses.
- f. Provision for resale cost.
- g. Conformity with historical pattern and leases in place for project.

6. Definition of appraiser/client relationship

- a. Who was considered an independent observer?
- b. Frequency of appraisal.
- c. Who was the arbiter of methods for integrating information into cohesive standardized formats suitable for measuring comparative performance?

III. Ironically, quality control of the appraisal process is in the hands of the customers for appraisal services, specifically those who stand to lose by permitting current conditions to continue. Historically, reform of the appraisal process has always been in the control of the customer who invests or guarantees real estate capital.

A. Historical origins of the three approaches

1. The cost approach and the life insurance industry.
 2. The income approach and academia and the FHA.
 3. The market approach and the National Association of Realtors.
- B. Standardized reporting requirements of the American Institute of Real Estate Appraisers begin with Canon 5 of their Code of Ethics and is provided in Exhibit 2.
1. The Institute has never issued white papers on specific appraisal problems to standardize professional response to changing issues of common interest.
 2. The Institute doubts if it is cost-effective to develop special standards for those who do pension work if only 150-200 of its 6,000 members have substantial business responsibility.
 3. Recently the Institute has tried to issue white papers as guidelines, and a sample of such an effort is provided in Exhibit 3.
- C. More recent efforts at quality control include:
1. The Home Loan Bank redirecting appraisal attention to R-41-b. (Exhibit 4).
 2. FNMA and FHLBMC and requirements for appraising multi-family development.
 3. Residential form appraisals for FNMA, VA, FHA, and FHLBMC.
- D. The Royal Institute of Chartered Surveyors and the European Common Market Accountants have been developing a standardized language and procedure for the valuation of and reporting balance sheet assets. (See Exhibits 5, 6, 7, 8.)
- E. Requirements for developing consistent appraisal performance standards for pension programs requires a six-step process:
1. Development of a written policy statement by pension fund trustees relative to reporting of real estate asset values by money managers responsible for real estate.
 2. A written appraisal standard followed by a specific real estate fund manager's report covering both minimum standards shared with an association of managers and unique features

believed to provide better communication to fund trustees of important underlying facts and assumptions inherent in the appraisals.

3. A standard letter of engagement when contracting for appraisal services implementing the written policies of sponsor and money manager.
 4. A standard procedure for in-house appraisal reviews in the interim between independent outside appraisal reviews, including tolerance for variance before reporting changed values.
 5. Auditing and monitoring of appraisal reports by specially trained, CPA reviewers as part of the accounting audit process.
 6. Spot checking of appraisal procedures and a review process for disapproval of appraisal firms found to be likely of misinformation or misapplication of technique by ERISA.
- F. An early effort at appraisal control was a Letter of Engagement used at First Asset Realty Advisors (FARA) together with knowledgeable efforts to select the best local assessors. (See Exhibit 9).
1. The best appraisers are difficult to pick by reputation as the big names delegate their work to apprentices.
 2. Some appraisers admit to being intimidated and avoiding the assignment or charging extra for the assignment, anticipating that FARA will be more demanding.
 3. On balance, we are getting better appraisals than most of the funds we have seen in our research at a higher average cost.
- G. The FARA letter was followed by an effort by the National Council of Real Estate Investment Fiduciaries (NCREIF) to develop guidelines and the result of that effort currently is shown by Draft #2 in Exhibit 10.
1. NCREIF Committee dominated by Prudential accounting firm.
 2. It concluded that standardization was not possible without review of a broad range of appraisals throughout various sectors of the industry.
 3. Many of the NCREIF Committee felt that empirical investigation of the appraisal practices might

discourage the utilitarian use of real estate in a pension portfolio and opposed independent study.

H. Appraisal standards are ultimately the responsibility of those funding the pension program and directing the money manager, rather than any failure by the appraisal profession. The profession has always done what it is paid to do and if its tasks were not fully defined, that is because it served the purposes of the customer who was ambiguous. The pension sponsors must determine what they are willing to pay for relevant appraisal value in terms of:

1. Frequency, quality, and independence.
2. Parameters for market comparison or inference.
3. Responsibility for structural and mechanical engineering integrity.
4. Accounting issues for income projection and discounting.
5. Relevance of cost approach.
6. Comprehensive interpretation of fiduciary responsibilities and relationship to appraiser.

EXHIBIT 1

DEFINITION OF MARKET VALUE
AND
MOST PROBABLE PRICE

CURRENT OFFICIAL DEFINITION OF FAIR MARKET VALUE

The most probable price in cash, terms equivalent to cash, or in other precisely revealed terms, for which the appraised property will sell in a competitive market under all conditions requisite to fair sale, with the buyer and seller each acting prudently, knowledgeably, and for self-interest, and assuming that neither is under undue duress.

Fundamental assumptions and conditions presumed in this definition are

1. Buyer and seller are motivated by self-interest.
2. Buyer and seller are well informed and are acting prudently.
3. The property is exposed for a reasonable time on the open market.
4. Payment is made in cash, its equivalent, or in specified financing terms generally available for the property type in its locale on the effective appraisal date.
5. The effect, if any, on the amount of market value of atypical financing, services, or fees shall be clearly and precisely revealed in the appraisal report. [1]

[1] American Institute of Real Estate Appraisers, The Appraisal of Real Estate, Eighth Edition, Chicago, IL, 1983, p. 33.

CONTEMPORARY DEFINITION OF MOST PROBABLE PRICE

"Most Probable Selling Price", as defined by Professor Richard U. Ratcliff:

The most probable selling price is that selling price which is most likely to emerge from a transaction involving the subject property if it were exposed for sale in the current market for a reasonable time at terms of sale which are currently predominant for properties of the subject type. [1]

[1] Unpublished quotation, Richard U. Ratcliff speaking on his book Valuation for Real Estate Decisions, Santa Cruz, CA, Democratic Press, 1972.

EXHIBIT 2

REPORTING REQUIREMENTS OF THE
AMERICAN INSTITUTE OF REAL ESTATE APPRAISERS

4

Reporting Requirements of the American Institute of Real Estate Appraisers

Canon 5 of AIREA Regulation 10 (Code of Professional Ethics and Standards of Professional Conduct) establishes the minimum requirements for both written and oral appraisal reports prepared by members and candidates of the Institute. The explanatory comments for Canon 5 state:

The Institute requires its Members, in arriving at an analysis, conclusion or opinion concerning real estate, to employ all of the recognized appraisal methods and techniques that will materially contribute to a proper evaluation of such real estate or to a solution of the real estate problem under consideration. As a corollary to this rule, the Institute also requires that the appraisal process contain a clear statement of all of the assumptions made, together with a reasonably complete summary of the work done in arriving at each analysis, conclusion or opinion concerning real estate contained in the report. . . . A Member of the Institute must preserve his or her supporting data relating to a written appraisal report.

There are a number of specific reporting rules; some are obligatory and others are recommendations that should be followed unless there are substantial reasons, disclosed in the report, for not doing so.

PROPERTY DESCRIPTION

A clear and reasonably complete description of the property may include the street address, legal description, ownership, building name, and any other information that will assist in identifying the property. The identification may be part of the larger property description section of the report or a separate one- or two-sentence capsule included in the introduction to the report.

Property Identification

A complete address may suffice for a conforming residential property. For other properties an address should be included if one is available; if there have been recent changes in the street names or numbering schemes, both the present and prior addresses should be included. If the property is a vacant lot, the property address might be "the lot lying between or adjacent to" a property with an assigned street address. If only a part of the

address is the subject of the report, or if the report covers a project identified by the address plus adjacent excess land, the address portion of the property identification should make this clear. For example:

1250 Sleepy Hollow Lane
Centerland, California 92660

1250 Sleepy Hollow Lane
(previously known as 940 Tallow Street)
Centerland, California 92660

The 50' by 120' lot situated between
1050 and 1056 Main Street
Centerland, California 92660

456 Main Street
Centerland, California 92660
except for the rear 75 feet of
that address facing on the alley

320 Main Street
Centerland, California 92660
plus the rear 75 feet of
318 Main Street

Legal Description

A legal description of the property, if available, should be included. A reasonably short description can be included in the body of the report; a lengthy legal description may be placed in the addenda. If the description is at all complex, it is advisable to provide the source of the description—e.g., deed, title policy, assessor's records, or record of survey. If a legal description is not available, the report should say so and a clear map identifying the property should be included in the report. For example:

Lot 23 of Tract 4630 per map recorded in Page 23 of Book 4215 on July 15, 1957, in the Official Records of Simon County.

Exhibit B in the Addenda of this report contains a metes and bounds legal description as it appeared on the Grant Deed transferring ownership of the subject property to the Cowly Corporation on July 15, 1978.

As of the date of this appraisal, a legal description conforming to the portion of the Smith Ranch that is the subject of this appraisal had not been prepared. The subject property is outlined in red on the map labeled "Plat of Land" on page 23 of this report. It is assumed that a legal description that is adequate for the transfer of real property and that conforms to the property delineated on this map will be prepared.

Ownership data assist in the clear identification of property. For example:

The subject property consists of that 42.5 acres of vacant unimproved land which was acquired by Mr. Frank L. Smith on December 30, 1979, by Grant Deed recorded in Page 1521, Book 43762 of Deeds, in the Collins County Courthouse.

Even if there is a six-page detailed description of the property elsewhere in the report, the property identification and description portion is enhanced by a concise description of the property, such as:

The subject property is a six-year-old, three-story office building containing 24,320 square feet of gross building area. It is located on a 52,320-square foot parcel of land with 126 feet of frontage on Main Street.

STATEMENT OF FACTS, CONDITIONS, AND ASSUMPTIONS

It is good business practice for the appraiser and the client to agree in advance on the assumptions and limiting conditions that will apply to the report. Many appraisers include a copy of assumptions and limiting conditions with the appraisal proposal or contract. This portion of the report sets forth not only general assumptions and conditions that would apply to every report, but also any specific assumptions that apply to the particular appraisal.

Some assumptions and limiting conditions make a report a limited appraisal report; in such cases, there are additional requirements, which will be discussed and illustrated later in this chapter.

STATEMENTS RELATIVE TO NEIGHBORHOOD DECLINE

All written appraisal reports concerning residential real estate that state that a neighborhood is undergoing decline or is about to undergo decline must contain the specific facts or reasoning from which the opinion or conclusion of neighborhood decline is drawn.

DATE OF VALUE

The date of value is usually included in the letter of transmittal, in the introductory section of the report, and in the concluding valuation statement. This date is not to be confused with the date the transmittal letter was prepared, the date the assignment was started, or the date of inspection. Any or all of these dates may be the same as the date of value, but they usually are not. The only mandatory date is the date of value, but good business practice dictates that other significant dates also be identified, e.g., the transmittal date (the date the completed report is transmitted to the client), the date of inspection, the date of verification, and the date of photographs.

REASONING THAT SUPPORTS THE VALUATION

Unless the appraisal report is a limited report—one that does not show all of the appraiser's reasoning—and has been properly qualified as such, the reader must be able to follow the appraiser's thought processes from the data presented to the conclusions formed. A "limited report" must comply with the special requirements of a limited report (see pp. 27-28).

SPECIAL DISCLOSURES

Fractional Interests

All appraisal reports that involve a valuation of a fractional interest, i.e., less than the whole fee simple estate, must clearly state that the value reported relates only to a fractional interest in the real estate involved, and that the value of this fractional interest plus

the value of all other fractional interests may or may not equal the value of the entire fee simple estate. Typically, this is included in the statement of assumptions and limiting conditions. A common example is a report of a leasehold interest appraisal. The qualifying statement is required to demonstrate to the reader that the sum of the lessor's and lessee's interests is not necessarily equal to the fee simple estate.

Larger Parcel

All appraisal reports relating to the valuation of a geographic portion of a larger parcel or tract of real estate must clearly state that the value reported is for that portion only and should not be construed as applying with equal validity to other portions of the larger parcel or tract. In addition, it must be clear that the value reported for the portion plus the value of all other geographic portions may or may not equal the value of the entire parcel or tract. This statement typically appears in the assumptions and limiting conditions section of the report.

Personal Interest or Bias

All written appraisal reports must state that the appraiser has no present or contemplated future interest in the property appraised, and that the appraiser has no personal interest or bias with respect to the subject matter or the parties involved in the appraisal. If a statement of this nature cannot be made, the report must clearly and frankly disclose all such personal interest or bias.

PROFESSIONAL CONTRIBUTION OF OTHERS

Written appraisal reports are to acknowledge the professional contributions of others in arriving at the analyses, conclusions, or opinions concerning real estate contained in the appraisal report or state that no one other than the person or persons signing the report prepared the analyses, conclusions, and opinions therein.

If several professional appraisers work on a report, and all agree to and sign it, they include a statement similar to the following in their certificate:

No one other than the appraisers whose signatures appear below has prepared the analyses, conclusions, and opinions concerning real estate which are included in this report.

If the appraisers were assisted by a cost estimator who worked only on the cost portion of the report, they may use something similar to the following:

The assistance of John A. Doe, who prepared the cost estimate used in this report, is acknowledged. Except for Mr. Doe's assistance, no one other than the appraisers whose signatures appear below prepared the analyses, conclusions, and opinions concerning real estate which are included in this report.

If another appraiser, who asks not to be identified because of personal or policy considerations, was consulted and contributed substantially to the report, the statement might be:

The assistance and counsel of another appraiser not employed by this firm and who

requests that he not be identified is hereby acknowledged. Except for this appraiser's assistance, no one other than the undersigned prepared these analyses, conclusions, and opinions concerning real estate contained in this report.

Canon 5 does not require a member of the Institute to acknowledge assistance received in obtaining the data on which the appraisal report is based, assistance received in the physical preparation of the report (e.g., taking photographs; preparing charts, maps, or graphs; or typing or printing), or any other assistance that does not directly involve the exercise of judgment in arriving at the analyses, opinions, or conclusions concerning real estate.

The rule requiring acknowledgment of the professional contributions of others does not reduce the responsibility of those who sign a written appraisal report; in evaluating such reports, clients, mortgage lenders, and other users are entitled to rely on the signatures of all who sign. Therefore, although others may participate in the preparation of a written appraisal report, any member of the Institute who signs or cosigns a report must accept responsibility for the contents of the entire report.

PUBLIC DISCLOSURE

The recommended public disclosure statement of the Institute's Code of Ethics (Canon 7, Regulation 10) is:

Disclosure of the contents of this report is governed by the Bylaws and Regulations of the American Institute of Real Estate Appraisers of the National Association of Realtors. Neither all nor any part of the contents of this report (especially any conclusions as to value, the identity of the appraiser or any reference to the American Institute of Real Estate Appraisers or to the MAI or RM designation) shall be disseminated to the public through advertising media, public relations media, news media, sales media or any other public means of communication, without the prior written consent and approval of the author.

This statement is meant to preclude the potential misuse of the Institute's name and professional designations that can arise when a member's client elects to publicize the results of an appraisal report. Excessive or exploitative use of designations, sometimes out of appropriate context, does not serve the interests of the Institute, which its members should seek to protect. A client may be inclined to excerpt or quote portions of the report in promotional literature, and such practices are a potential source of great damage.

The language of a report can be misquoted, used out of context, or printed without reference to the assumptions or limiting conditions contained in the report, and may thus give a false impression of the report, the appraiser, or the profession. Although the specific use of a report is generally a matter of negotiation between the appraiser and the client, the Institute encourages its members to be aware of potential abuses and, whenever possible, to include appropriate contractual restrictions on a client's freedom to reproduce or republish an appraisal report.

CERTIFICATE

According to the Institute's Code of Ethics, all written reports must contain a certificate substantially in the following form:

I (we), the undersigned, do hereby certify that I (we) have (or have not) inspected the subject property and that to the best of my (our) knowledge and belief, the statements

of fact contained in this report, upon which the analyses, opinions, and conclusions expressed herein are based, are true and correct; also, this report sets forth all of the limiting conditions affecting the analyses, opinions, and conclusions contained in this report; also, this report has been made in conformity with and is subject to the requirements of the Code of Professional Ethics and Standards of Professional Conduct of the American Institute of Real Estate Appraisers of the National Association of Realtors.

The American Institute of Real Estate Appraisers conducts a voluntary program of continuing education for its designated members. MAIs and RMs who meet the minimum standards of this program are awarded periodic educational certification.

One of the following statements also must be included:

I am certified under this program through_____.

I was last certified under this program through_____.

I have not been certified under this program.

LIMITED APPRAISAL AND REPORT

A distinction is made between a limited appraisal, as defined by Canon 4 of Institute Regulation 10, and a limited report, as defined by Canon 5 of Regulation 10. In Canon 4 limitations on the scope of the appraisal process are treated; in Canon 5 limitations on the completeness of the report are addressed.

A limited appraisal could consist of an investigation and analysis that do not meet the requirements of established procedures of the Institute. For example, when a limited time schedule is required by the client, portions of the investigation and analysis may be curtailed or omitted. One of the approaches to value that would normally be included may be omitted, or certain reasonable assumptions may be made relative to highest and best use without the full investigation normally undertaken. However, before an appraiser can accept and perform such an assignment, three important requirements must be met.

1. Prior to accepting a limited assignment, the member must advise the client that the assignment calls for something less than the work required for a full and complete appraisal and that the appraisal report will be qualified to reflect the limited scope of the assignment.
2. The limited scope of the assignment must be sent forth in the appraisal report (and in any testimony concerning the appraisal) in a clear, precise manner.
3. The scope of the assignment must not be so limited that the results obtained are meaningless or could mislead the client or the public.

These requirements deal with a limitation on the scope of the appraisal process; Canon 5 deals with a limitation on the completeness of the report. It is quite possible that a complete investigation and analysis were undertaken but, by prior agreement, only the conclusions are set forth and the data and reasoning are retained in the appraiser's file. The result is what is typically referred to as a letter report (see Chapter 5).

Although part or all of the data and reasoning can be omitted, the following must be included: the certificate of appraisal, an adequate identification of the property, a date of value, the required limiting conditions referred to in the certificate of appraisal statement, acknowledgment of the contributions of others, and the statement of nonbias. To omit any of these items would make the report meaningless or misleading.

A limited report must meet the same three conditions listed above for a limited appraisal. There are also requirements for preparing an expanded appraisal report, which contains more than is required by Institute standards. In these cases, the same three rules apply.

The first condition of prior client advice is best met by an agreement in writing. This can be part of the proposal letter or can be contained in a specific instruction from the client or the attorney of the client.

THE EVALUATION REPORT

The preface to the Institute's Regulation 10 clearly states that it applies to both valuation and evaluation reports. The word *valuation* is used to refer to the estimate of the value of a particular parcel of real estate at a particular point in time. The word *evaluation* is used in the broader sense as an evaluation of the nature, quality, or utility of any parcel of real estate. Examples of evaluation reports include marketability studies, feasibility reports, land-use studies, investment decision analyses, and cost-benefit studies.

When the reporting rules of Canon 5 apply to valuation assignments only, the qualifying phrase "a valuation of a particular parcel or tract of real estate" is used. In all other instances, the reporting rules apply equally to evaluation and valuation reports as do the general considerations of good communication.

5

The Letter Report

In some instances, by prior agreement with the client, the appraiser will submit the results of an appraisal in letter form. As described in the preceding chapter, this type of report generally sets forth only the conclusions of the appraiser's investigations and analyses. Although much of the data and reasoning is omitted from the letter, the following items must be included to make the report meaningful: the certificate, adequate identification of the property, the date of value, limiting conditions, acknowledgment of the contributions of others, and a statement of nonbias.

Example 5.1 offers a typical letter report, documenting the appraisal of a mobile home park.

EXAMPLE 5.1. Letter of Opinion

(Appraiser's Letterhead)

August 25, 1981

Mr. Harold S. Huntington
Trans-Atlantic Factors
2082 Murphy Drive, Suite 300
Irvine, California 92715

Re: Appraisal of 274-Space Mobile Home Park
3200 Fedlow Road
San Jose, California

Dear Mr. Huntington:

Upon your authorization, we have conducted the investigations and analyses necessary to form an opinion of the market value of the fee simple interest in the mobile home park located at 3200 Fedlow Road in the City of San Jose.

The opinions set forth in this letter are stated as of July 15, 1981.

The term "market value" is defined as:

The highest price on the date of valuation that would be agreed to by a seller, being willing to sell but under no particular or urgent necessity for so doing, nor obliged to sell, and a buyer, being ready, willing, and able to buy but under no particular necessity for so doing, each dealing with the other with full knowledge of all the uses and purposes for which the property is reasonably adaptable and available.

The analyses and opinions in this letter are subject to the following premises, assumptions, and limitations:

Per the request of the client, this appraisal is limited in that the only approach to value used is the income approach. Market data and reasoning supporting our analyses, conclusions, and opinions have been retained in our files.

Based upon these investigations and analyses, and upon our experience as real estate appraisers, we have reached the opinion that the subject, as of July 15, 1981, has a market value of:

THREE MILLION SIX HUNDRED THOUSAND DOLLARS
(\$3,600,000)

Mr. Lafferty certifies that, during the completion of the assignment, he has personally inspected the property that is the subject of this report. Ms. Sullivan has not inspected the property.

The undersigned hereby certify that, except as specifically noted:

1. We have no present or contemplated future interest in the real estate or personal interest with respect to the subject matter or the parties involved in this appraisal letter, and our employment in this matter is not in any manner contingent upon anything other than the delivery of this report.
2. To the best of our knowledge and belief, the statements of fact contained in this appraisal letter, upon which the analyses, opinions, and conclusions expressed herein are based, are true and correct.
3. This appraisal letter sets forth all of the limiting conditions (imposed by the terms of our assignment

continued

or by the undersigned) affecting the analyses, opinions, and conclusions contained in this report.

4. This appraisal letter has been made in conformity with, and is subject to, the requirements of the Code of Professional Ethics and Standards of Professional Conduct of the American Institute of Real Estate Appraisers of the National Association of Realtors.
5. We alone have prepared the analyses, opinions, and conclusions concerning real estate that are set forth in this appraisal letter.

Disclosure of the contents of this appraisal letter is governed by the Bylaws and Regulations of the American Institute of Real Estate Appraisers of the National Association of Realtors. In furtherance of the aims of the Institute to develop higher standards of professional performance by its members, the appraisers may be required to submit to authorized committees of said Institute copies of this report and any subsequent changes or modifications thereof.

Respectfully submitted,

Charles W. Lafferty
Ruth V. Sullivan, MAI

6

The Form Report

Many lending institutions and certain government agencies prefer a form report to a narrative report. This is particularly true for single-family residential appraisals. The form appraisal is preprinted with a combination of check-off boxes and blank lines for insertion of words or short comments.

The advantage of a form report is that the review appraiser knows exactly where to find all essential elements of the report and can do so quickly and efficiently. The disadvantage is that the appraisal problem is frequently not suited to the form. If special analyses or discussions are required, the form must be supplemented with attachments, which must be cross-referenced to specific sections of the form.

For Institute members and candidates, a form report must meet the reporting requirements of the Institute or otherwise qualify as a limited report under the conditions set forth in Canon 5 of Regulation 10.

A sample of a form report appears on the following pages.

EXAMPLE 6.1 FNMA-FHLMC Form Appraisal

RESIDENTIAL APPRAISAL REPORT File No

Borrower _____ **County** Cook **Map Reference** _____

Property Address 7540 Halesia **City** Parkside **State** IL **Zip Code** 60062

Legal Description _____

Sale Price \$ _____ **Date of Sale** _____ **Loan Term** _____ yrs **Property Rights Appraised** Fee Leasehold DeMinimus PUD

Actual Real Estate Taxes \$ _____ **1/yr Loan charges to be paid by seller \$** _____ **Other sales concessions** _____

Lender/Client Michael Haber/Fred Heiss **Address** _____

Occupant Mr. & Mrs. Avron **Appraiser** _____ **Instructions to Appraiser** _____

Location Urban Suburban Rural

Built Up Over 75% 25% to 75% Under 25%

Growth Rate Fully Dev Rapid Steady Slow

Property Values Increasing Stable Declining

Demand/Supply Shortage In Balance Over Supply

Marketing Time Under 3 Mos 4-6 Mos Over 6 Mos

Present Land Use 60% % 1 Family 2 % 4 Family 10 % Apts 10 % Condo _____ % Commercial

Change in Present Land Use Industrial 20 % Vacant _____ %

Predominant Occupancy Owner Tenant _____ % Vacant _____ %

Single Family Price Range \$ 80,000 to \$ 130,000 **Predominant Value** \$ 110,000

Single Family Age 1 yrs to 10 yrs **Predominant Age** 5-7 yrs

Comments: PHLMC/FNMA do not consider race or the racial composition of the neighborhood to be reliable appraisal factors. Comments including those factors, favorable or unfavorable, affecting marketability (e.g. public parks, schools, view, noise)

The subject is located near schools and church in a neighborhood consisting of well-maintained residences of similar quality and age.

Dimensions 70 ft. x 125 ft. (estimated) **Sq Ft** 8,750+ Corner Lot

Zoning classification Residential **Present improvements** do do not conform to zoning regulations

Highest and best use Present use Other (specify) _____

Elec Public Other (describe) _____ **OFF SITE IMPROVEMENTS** **Type** Level

Gas _____ **Street Access** Public Private **Site** Typical for neighborhood

Water _____ **Surface** asphalt **Shape** Rectangular

San Sewer _____ **Maintenance** Public Private **View** South-toward residential

Storm Sewer Curb/Gutter **Drainage** Appears adequate

Underground Elect & Tel Sidewalk Street Lights **Is the property located in a HUD identified Special Flood Hazard Area?** No Yes

Comments: Favorable or unfavorable including any apparent adverse easements, encroachments or other adverse conditions

No survey was furnished to the appraiser. All dimensions are approximate.

Improvements Existing Proposed Under Constr. **No Units** 1 **Type** (det, duplex, semi-det, etc.) Detached **Exterior Walls** By/Frame

Yrs. Age Actual 7 Effective 3 to 5 **No. Stories** 1+ **Roof Material** Asphalt shingle **Windows (Type)** Casement **Insulation** None Floor Ceiling Roof Wall

Foundation Poured concrete **Basement** 0 % Basement Floor Drain Finished Ceiling Outside Entrance Sump Pump Finished Walls Concrete Floor Finished Floor Evidence of Dampness Termites Settlement

Comments: Lower level includes laundry room, family room, den and full bath. There is a fireplace in the family room. Finish consists of carpeting and paneling.

Room List	Foyer	Living	Dining	Kitchen	Den	Family Rm	Rec Rm	Bedrooms	No. Baths	Laundry	Other
1st Level						1	1		1	1	
2nd Level	1	1	1	1				4	2		

Finished area above grade contains a total of 7 rooms, 4 bedrooms, 2 baths. Gross Living Area 1,798+ sq. ft. Basement Area 0 sq. ft.

Kitchen Equipment Refrigerator Range/Oven Disposal Dishwasher Fan/Hood Compactor Washer Dryer

HEAT Type FA **Fuel** Gas **Cond** Good **AIR COND** Central Other Adequate Inadequate

Floors Hardwood Carpet Over _____ _____

Walls Drywall Plaster _____

Trim/Finish Good Average Fair Poor

Bath Floor Ceramic _____

Bath Wainscot Ceramic _____

Special Features (including energy efficient items) _____

ATTIC Yes No Stairway Drop star Scuttle Floored

Finished (Describe) _____ Heated

CAR STORAGE Garage Built-in Attached Detached Car Por.

No. Cars 2+ Adequate Inadequate **Condition** Good

PROPERTY RATING

Quality of Construction (Materials & Finish) Good Avg Fair Poor

Condition of Improvements Good Avg Fair Poor

Room sizes and layout Good Avg Fair Poor

Chimney and Stove Good Avg Fair Poor

Insulation - adequacy Good Avg Fair Poor

Plumbing - adequacy and condition Good Avg Fair Poor

Electrical - adequacy and condition Good Avg Fair Poor

Kitchen Cabinet - adequacy and condition Good Avg Fair Poor

Compatibility to Neighborhood Good Avg Fair Poor

Overall Usability Good Avg Fair Poor

Appraisal and Marketability Good Avg Fair Poor

Yrs. Est. Remaining Economic Life 50 to 60 (explain less than 50 Yrs)

FIREPLACES, PATIOS, POOL, FENCES, etc. (describe)

Fireplace in family room; patio in rear.

COMMENTS: (including functional or physical inadequacies, repairs needed, modernization, etc.)

No inadequacies noted.

FHLMC Form 70 Rev. 7/78

ATTACH DESCRIPTIVE PHOTOGRAPHS OF SUBJECT PROPERTY AND STREET SCENE

FNMA Form 1004 Rev. 7/78

continued

VALUATION SECTION

Purpose of Appraisal is to estimate Market Value as defined in Certification & Statement of Limiting Conditions (FHLMC Form 438/FNMA Form 1004B). If submitted for FNMA, the appraiser must attach (1) sketch or map showing location of subject, street names, distance from nearest intersection, and any detrimental conditions and (2) exterior building sketch of improvements showing dimensions.

Measurements	No. Stories	Sq. Ft.	ESTIMATED REPRODUCTION COST - NEW - OF IMPROVEMENTS:
29' x 26' = 1 = 754			Dwelling 1,798+ Sq. Ft. @ \$ 35.00 = \$ 62,930
29' x 36' = 1 = 1,044			LL. Fin. 1,044+ Sq. Ft. @ \$ 22.75 = 23,751
			Extra Central air = 1,500
			Fireplace = 1,500
			Special Energy Efficient Items
			Porches, Patios, etc. = 1,000
			Garage/Car Port 750 Sq. Ft. @ \$ 9.75 = 7,313
			Site Improvements (driveway, landscaping, etc.) = 2,000
			Total Estimated Cost New = \$ 99,994
			Less Physical Depreciation \$ 10,000 = \$ 89,994
			Less Functional Depreciation = \$ 25,000
			Less Economic Depreciation = \$ 25,000
			ESTIMATED LAND VALUE (If leasehold, show only leasehold value) = \$ 25,000
			INDICATED VALUE BY COST APPROACH = \$114,994

Total Gross Living Area (List in Market Data Analysis below) 1,798+

Comment on functional and economic obsolescence: No obsolescence noted.

The undersigned has reviewed three recent sales of properties most similar and proximate to subject and has considered these in the market analysis. The description includes a dollar adjustment, reflecting market reaction to those items of significant variation between the subject and comparable properties. If a significant item in the comparable property is superior to, or more favorable than, the subject property, a minus (-) adjustment is made, thus reducing the indicated value of subject. If a significant item in the comparable is inferior to, or less favorable than, the subject property, a plus (+) adjustment is made, thus increasing the indicated value of the subject.

ITEM	Subject Property	COMPARABLE NO. 1	COMPARABLE NO. 2	COMPARABLE NO. 3
Address	7540 Halesia	7637 E. Palm Ct. Parkside, IL	15423 S. Primrose Parkside, IL	15124 Lilac Lane Parkside, IL
Proximity to Subj.		less than 1/2 mile	less than 1/2 mile	less than 1/2 mile
Sales Price		\$ 118,500	\$ 114,000	\$ 120,000
Price/Living Area		\$ 64.40	\$ 63.33	\$ 63.69
Date of Sale and Time Adjustment		8-80	4-81	5-81
Location	Good			
Site/View	70 x 125	irr.	irr.	irr.
Design and Appeal	Split level			
Quality of Constr.	Br/Fr Good			
Age	7	6	5	7
Condition	Good			
Living Area Room Count and Total	Total: 8-rms, 2-baths 7 4 2	Total: 8-rms, 2-baths 7 4 2	Total: 6-rms, 2-baths 6 3 2 +2000	Total: 8-rms, 2-baths 7 4 2
Gross Living Area	1,798+ Sq. Ft.	1,840 Sq. Ft.	1,800+ Sq. Ft.	1,884 Sq. Ft.
Lower Level	2 rooms finish		1 room 1 bath +2000	
Functional Utility	Good			
Air Conditioning	Central			
Garage/Car Port	2-car			
Porches, Patios, Pools, etc.	Patio			
Special Energy Efficient Items				
Other (e.g. fireplaces, kitchen equip., remodeling)	1-fireplace	None +1500		
Sales or Financing Concessions		Conventional	Conventional	Conventional
Net Adj. (Total)		\$ Plus, \$ Minus \$ 1,500	\$ Plus, \$ Minus \$ 4,000	\$ Plus, \$ Minus \$ -0-
Indicated Value of Subject		\$ 120,000	\$ 118,000	\$ 120,000

Comments on Market Data: All comps. are located in same neighborhood and are very similar. No time adjustment indicated. Financing concessions may affect the sale prices and are not reported.

INDICATED VALUE BY MARKET DATA APPROACH = \$ 120,000

INDICATED VALUE BY INCOME APPROACH (If applicable) Economic Market Rent \$ _____ Mo. x Gross Rent Multiplier _____ = \$ _____ R/A

This appraisal is made "as is" subject to the repairs, alterations, or conditions listed below completion per plans and specifications.

Comments and Conditions of Appraisal: See attached sheet

No survey furnished the appraiser; all dimensions are approximate.

Final Reconciliation: Market approach most indicative of buyer and seller reactions in marketplace.

Construction Warranty Yes No Name of Warranty Program _____ Warranty Coverage Expires _____

This appraisal is based upon the above requirements, the certification, contingent and limiting conditions, and Market Value definition that are stated in FHLMC Form 438 (Rev. 10/78)/FNMA Form 1004B (Rev. 10/78) filed with client _____ 19 _____ attached.

ESTIMATE THE MARKET VALUE, AS DEFINED, OF SUBJECT PROPERTY AS OF October 24 1981 to be \$ 120,000

Appraiser(s) _____ Review Appraiser (if applicable) Did Did Not Physically Inspect Property

continued

DEFINITION OF MARKET VALUE: The highest price in terms of money which a property will bring in a competitive and open market under all conditions requisite to a fair sale, the buyer and seller, each acting prudently, knowledgeably and assuming the price is not affected by undue stimulus. Implicit in this definition is the consummation of a sale as of a specified date and the passing of title from seller to buyer under conditions whereby: (1) buyer and seller are typically motivated; (2) both parties are well informed or well advised, and each acting in what he considers his own best interest; (3) a reasonable time is allowed for exposure in the open market; (4) payment is made in cash or its equivalent; (5) financing, if any, is on terms generally available in the community at the specified date and typical for the property type in its locale; (6) the price represents a normal consideration for the property sold unaffected by special financing amounts and/or terms, services, fees, costs, or credits incurred in the transaction. ("Real Estate Appraisal Terminology," published 1975.)

CERTIFICATION AND STATEMENT OF LIMITING CONDITIONS

CERTIFICATION: The Appraiser certifies and agrees that:

1. The Appraiser has no present or contemplated future interest in the property appraised; and neither the employment to make the appraisal, nor the compensation for it, is contingent upon the appraised value of the property.
2. The Appraiser has no personal interest in or bias with respect to the subject matter of the appraisal report or the participants to the sale. The "Estimate of Market Value" in the appraisal report is not based in whole or in part upon the race, color, or national origin of the prospective owners or occupants of the property appraised, or upon the race, color or national origin of the present owners or occupants of the properties in the vicinity of the property appraised.
3. The Appraiser has personally inspected the property, both inside and out, and has made an exterior inspection of all comparable sales listed in the report. To the best of the Appraiser's knowledge and belief, all statements and information in this report are true and correct, and the Appraiser has not knowingly withheld any significant information.
4. All contingent and limiting conditions are contained herein (imposed by the terms of the assignment or by the undersigned affecting the analyses, opinions, and conclusions contained in the report).
5. This appraisal report has been made in conformity with and is subject to the requirements of the Code of Professional Ethics and Standards of Professional Conduct of the appraisal organizations with which the Appraiser is affiliated.
6. All conclusions and opinions concerning the real estate that are set forth in the appraisal report were prepared by the Appraiser whose signature appears on the appraisal report, unless indicated as "Review Appraiser." No change of any item in the appraisal report shall be made by anyone other than the Appraiser, and the Appraiser shall have no responsibility for any such unauthorized change.

CONTINGENT AND LIMITING CONDITIONS: The certification of the Appraiser appearing in the appraisal report is subject to the following conditions and to such other specific and limiting conditions as are set forth by the Appraiser in the report.

1. The Appraiser assumes no responsibility for matters of a legal nature affecting the property appraised or the title thereto, nor does the Appraiser render any opinion as to the title, which is assumed to be good and marketable. The property is appraised as though under responsible ownership.
2. Any sketch in the report may show approximate dimensions and is included to assist the reader in visualizing the property. The Appraiser has made no survey of the property.
3. The Appraiser is not required to give testimony or appear in court because of having made the appraisal with reference to the property in question, unless arrangements have been previously made therefor.
4. Any distribution of the valuation in the report between land and improvements applies only under the existing program of utilization. The separate valuations for land and building must not be used in conjunction with any other appraisal and are invalid if so used.
5. The Appraiser assumes that there are no hidden or unapparent conditions of the property, subsoil, or structures, which would render it more or less valuable. The Appraiser assumes no responsibility for such conditions, or for engineering which might be required to discover such factors.
6. Information, estimates, and opinions furnished to the Appraiser, and contained in the report, were obtained from sources considered reliable and believed to be true and correct. However, no responsibility for accuracy of such items furnished the Appraiser can be assumed by the Appraiser.
7. Disclosure of the contents of the appraisal report is governed by the Bylaws and Regulations of the professional appraisal organizations with which the Appraiser is affiliated.
8. Neither all, nor any part of the content of the report, or copy thereof (including conclusions as to the property value, the identity of the Appraiser, professional designations, reference to any professional appraisal organizations, or the firm with which the Appraiser is connected), shall be used for any purposes by anyone but the client specified in the report, the borrower if appraisal fee paid by same, the mortgagee or its successors and assigns, mortgage insurers, consultants, professional appraisal organizations, any state or federally approved financial institution, any department, agency, or instrumentality of the United States or any state or the District of Columbia, without the previous written consent of the Appraiser, nor shall it be conveyed by anyone to the public through advertising, public relations, news, sales, or other media, without the written consent and approval of the Appraiser.
9. On all appraisals, subject to satisfactory completion, repairs, or alterations, the appraisal report and value conclusion are contingent upon completion of the improvements in a workmanlike manner.

Julie Miller
 Julie Miller, Appraiser

REVIEWED AND APPROVED BY:
James R. Webster
 James R. Webster, MAI

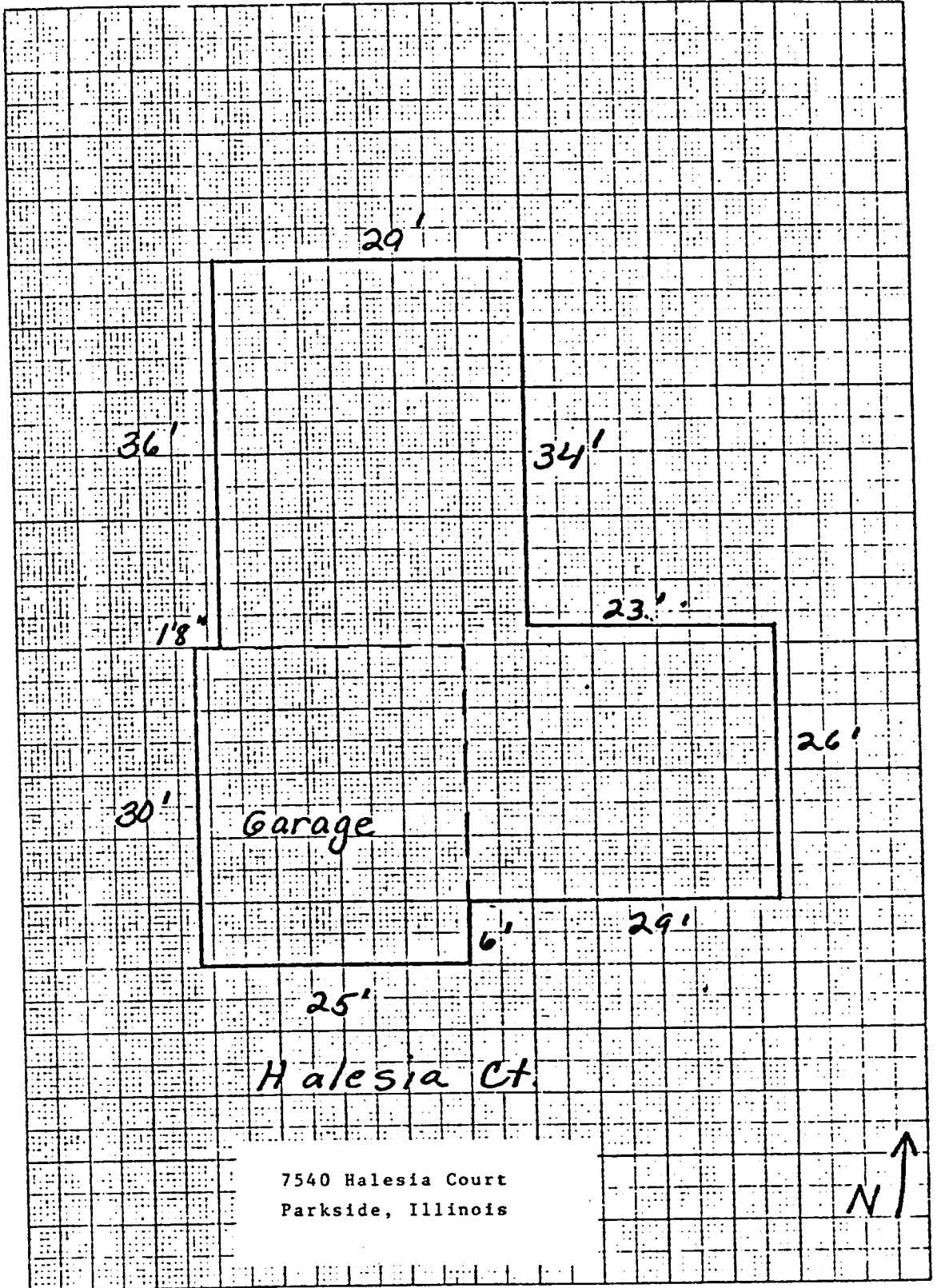
Date: October 24, 1981

PHLBC FORM 1000 REV. 10/79

FEMA FORM 1000 REV. 10/79

continued

PROPERTY MAP



7

The Narrative Report

In a narrative appraisal report, the appraiser is afforded the best opportunity to present data and reasoning that support the conclusions reached. As stressed earlier, good organization is essential.

LETTER OF TRANSMITTAL

Transmittal letters introduce the report and present it to the client. A good transmittal letter should be concise and in compliance with accepted standards of business correspondence. It is useful to begin the letter with a reference to the terms and circumstances of the authorization of the assignment. Important points that may be included in a transmittal letter are:

1. Date of the letter (not necessarily or usually the same as the date of value).
2. Client name and address; if it is a corporate client, a reference to the individual who will receive the report should be included. Include the person's title.
3. A reference that will identify the property by name or street address and possibly a file or purchase order reference.
4. Appropriate salutation.
5. Reference to the authorization that initiated the assignment.
6. Reference to the inspection, investigation, and analyses undertaken by the appraiser for the purpose of forming an opinion of value.
7. A concise statement of the value conclusion and the date of value.
8. An indication that the value conclusion is subject to certain assumptions and limiting conditions set forth in the body of the accompanying report.
9. A clear reference that the letter itself is not the appraisal but that it merely serves to transmit the appraisal report that follows.
10. The signatures of all appraisers who bear responsibility for the analyses and conclusions within the report.

Some appraisers choose to incorporate the certificate of value within the transmittal letter; others choose to include it within the body of the report. A typical transmittal letter is presented in Example 7.1.

EXAMPLE 7.1. Transmittal Letter

(Appraiser's Letterhead)

May 13, 1981

Our File No. 758.3

Your Reference No. 8046-C-52

Universal Investment Company
123 Main Street
Middletown, CA 99990

Attn: Mr. William D. Jones, President

Re: Appraisal Report
Office Building at 300 Broad Street
Middletown, California

Gentlemen:

In response to your authorization letter of March 1, 1981, we have conducted the required investigation, gathered the necessary data, and made certain analyses that have enabled us to form an opinion of the market value of the fee simple interest in the above-captioned subject property.

Based on the inspection of the property and the investigation and analyses undertaken, we have formed the opinion that, as of April 8, 1981, and subject to the assumptions and limiting conditions set forth on page 8 of this report, the subject has a market value of:

FOUR MILLION SEVEN HUNDRED FIFTY THOUSAND DOLLARS
\$4,750,000

The narrative appraisal report that follows sets forth the identification of the property, the assumptions and limiting conditions, pertinent facts about the area and the subject property, comparable data, the results of the investigations and analyses, and the reasoning leading to the conclusions set forth.

Respectfully submitted,

Jane A. Adams
John B. Roe, MAI

INTRODUCTION TO REPORT

The opening section of the report sets forth the purposes and objectives of the appraisal, an identification of the property and the property rights appraised, and a definition and explanation of important concepts fundamental to the report. Many appraisers list the assumptions and limiting conditions of the report in this section.

Purpose of Report or Objective of Appraisal

The purpose of the report is to communicate the data and reasoning leading to a conclusion. The purpose of the appraisal, or objective of the assignment, is usually to arrive at a supportable opinion. In a simple assignment, the appraiser may express both ideas in a brief paragraph such as:

The objective of this appraisal is to estimate the market value of the City National Bank Building as of April 5, 1981. The purpose of this report is to present the data and reasoning that the appraiser has used to form the opinion of value.

Other, more complex appraisal assignments require a more detailed statement of the appraisal problem as illustrated in Example 7.2.

Property Rights Valued

If the assignment concerns the appraisal of a fee simple estate interest, it may be sufficient to describe the property rights in the statement of purpose. A separate statement may be required for more complex fractional interests.

Identification of Property

The property should be clearly and unambiguously identified by as many different means as possible, including:

1. Legal description (if lengthy, it may be put in the addenda and referred to within the identification section of the report).
2. Street address, including any qualifiers if the parcel is more or less than that encompassed by the street number.
3. Assessor's parcel number if numbers tend to remain the same from year to year in the jurisdiction involved.
4. Reference to the nearest intersection (e.g., "the parcel with 100 feet of frontage on the north side of Main Street, located 360 feet west of the centerline of the intersection of Main Street and Baldwin Avenue").
5. Reference to any common name for the property, such as the "City National Bank Building."
6. Identification by property type, such as "the three-story, wood-frame office building at the southwest corner of Pierce and Franholm Avenues."
7. Reference to ownership and transfer such as "the 20-acre portion of the southwest quarter of Section 15, Range 10 N. Township 5 S, transferred to Frank Smith by deed recorded November 10, 1980, in Book 3516; Page 431 of Official Records."

EXAMPLE 7.2. Statement of Objective

The objective of this appraisal assignment is to undertake the investigations and analyses required to reach four supportable estimates for each of the following premises:

Premise A

Assuming the lawsuit to overturn the county's approval of Environmental Impact Report No. 568 is unsuccessful and the joint venture is permitted to proceed with development of the Moonrise Bay Hotel and commercial project described herein,

- A-1. Estimate the market value of the site "as is."
- A-2. Estimate the market value of the project, assuming completion in accord with the plans and specifications identified and described herein.
- A-3. Estimate the market value of the project, assuming completion in accord with the plans and specifications identified and described herein and also assuming completion of the leasing of the commercial space at market rent levels.
- A-4. Estimate the amount of time after completion of construction for the commercial space to be leased.
- A-5. Estimate the occupancy level and average daily rate for the hotel during its first full year of operation and estimate the time after completion for the hotel to achieve stabilized occupancy.

Premise B

Assuming the decision of the court is to sustain the Environment Alliances lawsuit to overturn Environmental Impact Report No. 568 on the basis of the arguments in their petition,

- B-1. Estimate the highest and best use of the subject site as is.
 - B-2. Estimate the market value of the subject site as is.
 - B-3. Estimate the highest and best use of the subject site as if joined with the adjacent 12.5-acre Coffin parcel described herein.
 - B-4. Estimate the market value of the subject site and the adjacent 12.5-acre Coffin site as if they were joined.
-

Ownership and Recent History

It is good practice to list current ownership and the date, price, and terms of acquisition. If there have been several transfers in recent years, it is also helpful to mention these. If the appraisal is of a parcel seriously encumbered by other rights created by easements or deed reservations, these must be clearly explained. Some corporations, lenders, and public agencies require a five- or ten-year property history as a part of their appraisal requirements. Salient facts can be enumerated as follows:

This appraisal is of the leasehold estate created by the ground lease executed December 31, 1947, between the Crafton Estate Company, as lessor, and the Loomis Company, as lessee. Through successive assignments of the leasehold interest, the leasehold estate is now vested in the name of Donbrow Realty Company, a California corporation. The lease and assignments of lease are reproduced as Exhibit D in the Addenda of this report. A synopsis and analyses of the lease begins on page 53 of this report.

Definitions of Significant Terms

Appraisal terms and legal concepts should be defined early in the report. In almost every instance, there should be a definition of *market value*, perhaps with a discussion of significant elements of the definition.

The appraiser should use the definition of market value appropriate to the particular assignment. In condemnation work, market value may be defined by statute or legal precedent in the jurisdiction involved. Assignments for lending institutions may require a definition imposed by one or more regulatory agencies. The appraiser may prefer to use the definition of market value in *Real Estate Appraisal Terminology*. Example 7.3 shows one way of presenting a definition of market value.

Other terms that may require definition include *highest and best use*, *market rent*, *market feasibility*, and, in condemnation work, *special benefits*, *severance damages*, *the part taken*, and *the larger parcel*. The authority or source of any definitions should be cited. Some appraisers incorporate the definitions in the "Assumptions and Limiting Conditions."

Assumptions and Limiting Conditions

Canon 5 of the Code of Professional Ethics and Standards of Professional Conduct of the American Institute of Real Estate Appraisers requires the appraiser to "clearly and unequivocally set forth all facts, assumptions and conditions upon which the appraisal is based." A variety of assumptions and limiting conditions might apply, depending on the appraisal. A list of those the appraiser may require appears in Example 7.4. Alternate wordings as used by different appraisers are given.

This section of the report may be called "Contingent and Limiting Conditions" or "Premises, Assumptions, and Limiting Conditions." Some appraisers prefer to place the entire section at the end of the report near the certificate of value. Others prefer to put specific conditions in the introductory section and general assumptions and limiting conditions at the end of the report. By placing all assumptions and limiting conditions early in the report, the reader is alerted to the premises underlying the data analysis and reasoning of the appraisal.

EXAMPLE 7.3. Market Value Definition and Implications

Market value is defined in *Real Estate Appraisal Terminology*¹ as:

"The most probable price in terms of money which a property should bring in competitive and open market under all conditions requisite to a fair sale, the buyer and seller, each acting prudently, knowledgeably, and assuming the price is not affected by undue stimulus.

"Implicit in this definition is the consummation of a sale as of a specified date and the passing of title from seller to buyer under conditions whereby:

- "1. buyer and seller are typically motivated.
- "2. both parties are well informed or well advised, and each acting in what they consider their own best interest.
- "3. a reasonable time is allowed for exposure in the open market.
- "4. payment is made in cash or its equivalent.
- "5. financing, if any, is on terms generally available in the community at the specified date and typical for the property type in its locale.
- "6. the price represents a normal consideration for the property sold unaffected by special financing amounts and/or terms, services, fees, costs, or credits incurred in the transaction."

An understanding of the most likely segment of the investment submarket capable of bidding on the property is essential. Appraisers study and adopt the motivations of the potential buyer group which will exert the greatest pressure on the price structure.

1. American Institute of Real Estate Appraisers and Society of Real Estate Appraisers, *Real Estate Appraisal Terminology*, revised edition, ed. Byrl N. Boyce (Cambridge, Mass.: Ballinger Publishing Company, 1981), pp. 160-161.

EXAMPLE 7.4. Assumptions and Limiting Conditions**GENERAL CONDITIONS**

1. That the term *fair market value*, as herein used, is defined as "the highest price on the date of valuation that would be agreed to by a seller, being willing to sell but under no particular or urgent necessity for so doing, nor obliged to sell, and a buyer, being ready, willing, and able to buy under no particular necessity for so doing, each dealing with the other with full knowledge of all the uses and purposes for which the property is reasonably adaptable and available" (Cal. Code of Civ. Proc., Title 7, Sec. 1263.320).
2. That the date of value to which the opinions expressed in this report apply is set forth in the letter of transmittal. The appraiser assumes no responsibility for economic or physical factors occurring at some later date which may affect the opinions herein stated.
3. That no opinion is intended to be expressed for legal matters or that would require specialized investigation or knowledge beyond that ordinarily employed by real estate appraisers, although such matters may be discussed in the report.
4. That no opinion as to title is rendered. Data on ownership and the legal description were obtained from sources generally considered reliable. Title is assumed to be marketable and free and clear of all liens and encumbrances, easements, and restrictions except those specifically discussed in the report. The property is appraised assuming it to be under responsible ownership and competent management and available for its highest and best use.
5. That no engineering survey has been made by the appraiser. Except as specifically stated, data relative to size and area were taken from sources considered reliable, and no encroachment of real property improvements is assumed to exist.
6. That maps, plats, and exhibits included herein are for illustration only, as an aid in visualizing matters discussed within the report. They should not be considered as surveys or relied upon for any other purpose.
7. That no opinion is expressed as to the value of subsurface oil, gas, or mineral rights and that the property is not subject to surface entry for the exploration or removal of such materials except as is expressly stated.

FOR COURT OR HEARING TESTIMONY

8. That testimony or attendance in court or at any other hearing is not required by reason of rendering this appraisal unless such arrangements are made a reasonable time in advance.
9. That, because the date of value used herein is the date of trial, the appraiser reserves the right to consider and evaluate additional data that become available between the date of this report and the date of trial and to make any adjustments to the value opinions that may be required.

FOR DISCLOSURE OF PROFESSIONAL ASSISTANCE

10. That, although the valuation contained in this report is the work product of the appraiser, specialized professional studies relating to the engineering cost estimate prepared by Frank L. Doe, Registered Land Engineer, have been relied on in formulating conclusions.

FOR DISCLOSURE OF PERSONAL INTEREST

11. That the appraiser acknowledges personal interest, limited to ownership of ten shares of stock in the American Telephone and Telegraph Company, in the subject of this appraisal, but concludes that such interest will not affect his professional judgment, and that he has made full disclosure of such interest to the client.

continued

FOR TITLE REPORT NONAVAILABILITY

12. That, because no title report was made available to the appraiser, she assumes no responsibility for such items of record not disclosed by her normal investigation.

FOR QUESTIONABLE SOIL OR GEOLOGIC CONDITIONS

13. That no detailed soil studies covering the subject property were available to the appraiser. Therefore, premises as to soil qualities employed in this report are not conclusive but have been considered consistent with information available to the appraiser.
14. That, since earthquakes are common in the area, no responsibility is assumed due to their possible effect on individual properties unless detailed geologic reports are made available.

FOR A LIMITED APPRAISAL

15. That, at the request of the client, the scope of this appraisal report has been limited to include the valuation of only the land and/or improvements that the appraiser considers to have been affected by the proposed taking and construction.
16. That, at the request of the client, the valuation herein reported relates to only a fractional interest in the real estate involved, and that the value of all other fractional interests may or may not equal the value of the entire fee simple estate considered as a whole. The fractional interest appraised relates to only the leasehold estate.

FOR IMPROVED PROPERTY

17. That the appraiser has personally inspected the subject property and finds no obvious evidence of structural deficiencies except as stated in this report; however, no responsibility for hidden defects or conformity to specific governmental requirements, such as fire, building and safety, earthquake, or occupancy codes, can be assumed without provision of specific professional or governmental inspections.
18. That, although no termite inspection report was available, the appraiser personally inspected the subject property and found no significant evidence of termite damage or infestation.
19. That no consideration has been given in this appraisal to personal property located on the premises, or to the cost of moving or relocating such personal property; only the real property has been considered.
20. That consideration has been given in this appraisal to certain items of equipment located on the property and itemized herein, which, in the opinion of legal counsel, are to be considered in the property valuation.
21. That rental areas herein discussed have been calculated in accord with standards developed by the American Standards Association as included in *Real Estate Appraisal Terminology*.
22. That income and expense data herein relied upon were provided by Realty Management Corporation but do not represent an audited return.

FOR PROPOSED CONSTRUCTION

23. That the plans and specifications furnished by the client and prepared by Franklin Jones, AIA, March 10, 1979, upon which this valuation is predicated, are assumed to show the intent of the builder, but the appraiser assumes no responsibility for their correctness or for undisclosed modifications. A copy of the plans and specifications is in the appraisal files.

continued

FOR AGRICULTURAL PROPERTY

24. That no consideration has been given in the appraisal to the value, if any, attributable to growing crops on any portion of the property appraised.
25. That the present owner will be allowed to harvest the current crop.

FOR PARTIAL TAKING

26. That this project will be constructed in the manner proposed as described briefly in this report and in detail in the condemnor's construction plans.
27. That during the proposed construction, existing access and utilities will remain usable by properties presently dependent upon them, or these will be rerouted without disruption in service during the proposed construction, after which they will be replaced to provide usage equal to or better than previously existed.

FOR PIPELINE CONSTRUCTION UNDER AN EASEMENT

28. That the top of the proposed pipeline will have sufficient cover to permit any legal use not specifically prohibited by the wording of the acquisition easement deeds. Copies of these deeds are included in this report.
29. That topsoil replaced after construction will be equal to or better than displaced topsoil.
30. That the excess subsoil will be removed from each parcel where it would adversely affect the parcel after construction.
31. That the construction area of all parcels will be cleared of debris after construction.
32. That the trench area of parcels not under agricultural use will be mounded to accommodate expected settlement after construction.
33. That no consideration is given to potential damage that may or may not arise from ultimate subsidence in the trench area.
34. That construction will be confined to the right-of-way as described in this report.
35. That the condemnor will pay for restoration of all items of permitted use that may be damaged by his entry to and/or over the easement area, regardless of when such items were installed unless such damage occurs from an entry necessary for the removal of items prohibited by the easement language.
36. That where the proposed pipeline crosses watercourses and/or storm water drainage ways, it shall be constructed at a sufficient depth and with sufficient erosion control so as not to interfere with natural water flow or to divert such water flow over adjacent lands.

FOR POSSIBLE UNLAWFUL CONDUCT

37. That the appraiser has become aware, through the media, that certain aspects of the subject property operations are being investigated by the Internal Revenue Service. The value opinion herein reported is based upon reliance on the legality of the subject property operation and resulting financial statements. However, the appraiser reserves the right to consider and evaluate data that become available as a result of the IRS investigation and to make any required adjustment to the value opinion.

FOR REVIEW WITHOUT INSPECTION

38. That the appraiser's sole role in this appraisal was that of review and approval and did not include personal inspection of the property appraised or the market data used.

Scope of Investigation

Some appraisers add a section in the introduction that details the scope of investigation undertaken. This may be presented in a generalized form or in detail. If included, it can be either a narrative or an outline. See Example 7.5.

EXAMPLE 7.5. Scope of Investigation

As part of this appraisal, the appraiser made a number of independent investigations and analyses. She relied on data retained in her office, which is updated regularly for use in all assignments. Listed below are the investigations undertaken and the major data sources.

AREA AND NEIGHBORHOOD ANALYSIS

Examined South Quincy Regional Planning Report for demographic data, land use policies and trends, growth forecasts, and employment data. Reviewed 1979 Planning Update and interviewed Ralph G. Calvin, assistant planning director, in 1980, to ascertain development patterns and trends for portion of Quincy lying west of Interstate 13. Interviewed the following industrial brokers active in the area: Margaret L. Raines of Industrial Realtors, Frank P. Major of Northlake Realtors, and Samuel P. Smith of Morris Industrial Brokers.

SITE DESCRIPTION AND ANALYSIS

Consulted Quincy Planning and Engineering Departments, Public Utility Company, and Suffex County Geologists Office. Reviewed American Title Report 40-31245 prepared January 5, 1980. Physically inspected site on October 1, 1980, walked perimeter of property, and photographed subject site, surrounding area, and street scenes.

IMPROVEMENT DESCRIPTION AND ANALYSIS

Reviewed plans and specifications prepared by Wilson and Wilson, AIA, and inspected similar building at 3150 Crosstown Lane by same architect and builder. Interviewed Judith G. Wilson on October 6, 1980.

MARKET DATA PROGRAM

Vacant and improved transfers were obtained by researching all transfers occurring between January 1, 1979, and October 15, 1980, which were industrially zoned and located west of Interstate 13 and within the Quincy Metropolitan Area. Copies of deeds and financing instruments were obtained from the courthouse and an attempt was made to contact buyers, sellers, or both to verify transaction data and ensure that the sales were at arms length. Details of the verified sales are included in the addenda as Exhibit E.

RENTAL DATA PROGRAM

The brokers listed in "Area and Neighborhood Analysis" above were questioned on the most recent industrial leases consummated in the subject's vicinity. They also provided data on expenses from three similar properties. The appraiser used recent lease data on other properties on file. Morris Industrial Realtors has maintained an industrial property inventory for the past four years, which was consulted for vacancy information.

EXHIBIT 3

GUIDE NOTE 1
To the Standards of Professional Practice

VALUATION OF REAL ESTATE INTERESTS INTENDED FOR SYNDICATION
AND
VALUATION OF REAL ESTATE PARTNERSHIP INTERESTS

GUIDE NOTE 1
To The Standards of Professional Practice

VALUATION OF REAL ESTATE INTERESTS INTENDED FOR SYNDICATION
AND
VALUATION OF REAL ESTATE PARTNERSHIP INTERESTS

Effective May 3, 1985

Introduction

The syndication of real estate has become an important element in the current real estate market. The process of syndication often begins when an individual or group (the syndicator) purchases interests in real estate for the purpose of transferring it to a limited partnership and then selling limited partnership interests to investors. Problems arise for an appraiser when he or she is asked to value the real estate interests at the time of their purchase by the syndicator because the syndicator frequently is buying more than real estate. Problems also arise when the syndicator sells limited partnership interests to investors because of the inherent difficulty involved in separating the value of the interests in real estate from the aggregate value of the limited partnership interests.

In the syndication industry the price of the interests in real estate at the time of acquisition by the syndicator is sometimes referred to as wholesale value; and the aggregate price of the individual partnership interests to be sold by the syndicator is sometimes referred to as aggregate market value, retail value, or syndication value. If these terms are used by an appraiser, however, they must be defined clearly and precisely so that the users of the report and the public will not be confused or misled.

Valuation problems often relate to non-real estate items or conditions involved in the sale and purchase transaction such as special financing and guarantees of occupancy or income. These items are difficult to isolate and evaluate even when all facts are known. In the context of syndication purchases, the problem of analyzing comparable sales is more difficult than usual because it is extremely difficult to obtain all relevant data.

When a syndicator sells the real estate partnership interests to investor purchasers, the sale price of a limited partnership interest includes a variety of items such as tax benefits, management services, and other benefits in addition to the interests in real estate.

The syndication of real estate involves the marketing of highly specialized interests, both real and personal, to a specifically defined group of purchasers with varying motivations. Unless extreme care is taken to distinguish the exact nature of the interests being appraised, valuation conclusions can be greatly distorted or misleading, and an appraiser may become liable to third parties under security and tax regulations that have often been described as punitive.

Basis for Proper Valuation

1. Acquisition by the Syndicator

All appropriate approaches should be used to estimate value. When analyzing comparable sales in the sales comparison approach, all transactions should be specifically analyzed to determine whether non-real estate items were included in the price. If non-real estate items were included, they should be separately identified and their effect on the sale price should be carefully considered.

A limited assignment should be accepted only in unusual circumstances.

2. Sale of Partnership Interests by the Syndicator

Syndicators frequently assert that the aggregate price they are paid by investors who purchase partnership interests establishes the market value of the interests in real estate that are the subject of the syndication. The market value of the interests in real estate is an important item in a syndication because the value of the improvements is used to establish the basis for depreciation which in turn creates substantial tax benefits. The appraiser, however, must carefully analyze the aggregate sale price of the partnership interests sold to investors and separate the value of the interests in real estate from the contributory value of the non-real estate interests sold. Rarely would the retail price of the individual partnership interests sold to investors equal the market value of the interests in real estate. It is essential that the appraiser understand that the partnership interests sold by the syndicator include many non-realty items such as tax shelter, potential capital appreciation, ability to invest in a major property that an investor might be incapable of investing in alone, and management services for the investment.

When valuing fractional interests in a real estate partnership, an appraiser must be certain that all market data is comparable and be acutely aware of what was included in each investment package utilized in the valuation process. In this connection an appraiser can appraise the partnership interest involved either by breaking it down into separate components or by considering it as a whole with all the components properly identified.

Unacceptable Practices

1. Failing to determine whether non-realty items were included in the price of comparable sales.
2. Using the retail price of the aggregate fractional interests in the partnership or the aggregate market value of the partnership as the market value of the real estate interests being appraised.
3. Combining the value of non-real estate items with the value of the real estate interests being appraised without proper identification and analysis.
4. Failing to describe and measure the effects of submarket or atypical financing on the value of the real estate interests being appraised.

EXHIBIT 4

APPRAISAL POLICIES AND PRACTICES OF INSURED
INSTITUTIONS AND SERVICE CORPORATIONS (R 41b)

an estimate of identifiable market demand and sales pace, cites data on competing projects showing size of project, sale price per model and per square foot and sales rates in each development, recaps the anticipated cost of development, and assesses probability of obtaining governmental approval of the proposed development.

(11) *Comprehensive Cash Flow Projection*

The file should contain a cash flow projection which contains data on the following matters projected over the life of the project at quarter-year intervals: sales; expenditures broken down as to land, overhead, development, taxes and interest, marketing, and maintenance; and a calculation of the internal rate of return or profitability analysis.

(12) *Accounting and Other Internal Controls*

The file should contain a description of the type and periodicity of accounting reports to be furnished to the management and directorate of both the service corporation and its parent association(s) together with a description of the controls to be maintained with respect to cash receipts and expenditures in the project. (3/2/77)

R 39 INSURANCE REGULATION 563.33

Paragraph (b) of Insurance Regulation 563.33 provides that any insured institution which agrees in writing with the Corporation to comply with all of the guidelines set forth in paragraph (a) of the section need no longer comply with any present condition of insurance or provision of its agreement for operating policies concerning the composition of its board of directors or the employment of its officers.

Institutions wishing to enter into such an agreement should submit a resolution of their board of directors to the Supervisory Agent. Such resolution should set forth the institution's agreement to comply with Section 563.33(a) recommended guidelines for composition of the board of directors of an insured institution. In the event the existing board of the insured institution is not in compliance with the guidelines, the resolution should include a proposed schedule for bringing the noncomforming directorate into compliance. Such proposed schedule should be for a short a period of time as is reasonably possible consistent with the remaining terms of the existing directorate, but in no event later than the third annual meeting following the date of submission to the Supervisory Agent.

Unless notified by the Supervisory Agent within 30 days after submission of its resolution that the agreement is not acceptable, an institution need no longer comply with any present condition of insurance or provision of its agreement for operating policies concerning the composition of its board of directors or the employment of its officers. (3/2/77)

R 40 [Rescinded]

R 41 [Rescinded]

R 41a [Rescinded]

R 41b APPRAISAL POLICIES AND PRACTICES OF INSURED INSTITUTIONS AND SERVICE CORPORATIONS

(Editor's Note: In addition to consolidating the provisions of Memoranda R 41a and R41a-1 into a single document and incorporating the content of T 15-1, the following significant revisions have been incorporated in the section entitled "Appraisal Procedures":

Item #4—expands and clarifies requirement that appraisals of development type properties reflect deductions and discounts by eliminating the 12 month sell-out/occupancy threshold formerly provided by R-41a.

Item #5—expands and clarifies expected use of market/economic feasibility assessments to include support of appraiser's conclusion of highest and best use as well as of probable success of the project.

Item #7—revises definition of "Market Value" to reflect terminology currently in use by leading professional appraisal organizations and, consistent with the collateral lending posture of the savings and loan industry, the need to obtain the most probable selling price should the property be placed on the market under the conditions herein specified.)

Introduction

The soundness of an association's or service corporation's mortgage loans and real estate investments depends to a great extent upon the adequacy of the appraisals of the real estate. This memorandum provides guidelines for appraisal management and procedures to assist in determining compliance with the appraisal requirements of Insurance Regulation 563.17-1(c)(1)(iii).

Appraisal Management

The lending policies established by the board of directors will determine the complexity and diversity of appraisal situations to be encountered and, therefore, the general requirements of the association or service corporation for appraisal staff and facilities. Management should ensure that appraisal services provided, whether by fee or staff appraisers, meet the current needs of the association or service corporation.

An appraisal should serve an underwriter's needs by providing a supported opinion of a property's market value as of a specified date sufficiently current so as to reduce the likelihood of material value fluctuations prior to the loan/investment decision. In addition to providing estimated market value, the appraisal should give the appraiser's opinion of the property's feasibility and marketability. An accurate and useful appraisal is most often produced by a

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Source: Federal Home Loan Bank of Chicago

capable and suitably equipped fee or staff appraiser who has ready access to current market information. Therefore, each association and service corporation should be able to demonstrate that its fee and staff appraisers are competent and knowledgeable of the relevant markets, and have the facilities necessary to perform adequate appraisals.

Appraisal skills and professional requirements are not static. Staff appraisers should continually increase their knowledge and skills through attendance at courses sponsored by universities, colleges, and/or professional organizations. Memberships in professional appraisal organizations should be encouraged. Attendance at courses and participation in the activities of professional organizations are also useful factors for management to consider in selecting independent fee appraisers.

Appraisal Procedures

The appraisal content shall follow generally accepted and established appraisal practices, as reflected in the standards of the nationally recognized professional appraisal organizations.

Specifically, each appraisal report must:

1. be totally self-contained so that:
 - a. it is a useful tool for prudent underwriting, REO and/or LTF decisions.
 - b. when read by any third party, the appraiser's logic, reasoning, judgment and analysis in arriving at a final conclusion indicate to the reader the reasonableness of the market value reported.
 - c. it demonstrates professional competence, ethics and expertise.
2. be of a narrative style for major loans and/or investments made by the association or affiliates.
3. contain all recognized approaches to market value unless the appraiser fully explains and documents the rationale for eliminating one or more of the approaches to value.
4. take into consideration and make provision for all appropriate deductions and discounts for any development type property.
5. address itself to the market/economic feasibility prospects for any proposed major loan/investment real estate project, in sufficient detail to support the appraiser's forecast of the probable success and the conclusion(s) of highest and best use. If a market/economic feasibility report is prepared by other than the appraiser, the appraiser will set forth the reasoning and rationale for accepting or rejecting said report. All such market/economic feasibility studies will be made a permanent part of the appraisal report.
6. contain, if for major loan/investment properties (except for home type properties) located in highly speculative local market areas which have experienced dramatic price increases relative to regional norms, a sales history analysis

of the subject property covering the speculative time period. This analysis should reasonably disclose and verify:

- a. grantor(s)-grantee(s).
 - b. sale date(s).
 - c. sale price(s) and terms of financing, discounting the sale to a cash equivalent, where necessary.
 - d. any interrelated parties to each transaction.
7. address itself to "Market Value", as hereby defined and qualified:

The most probable price in terms of money which a property should bring in competitive and open market under all conditions requisite to a fair sale, the buyer and seller, each acting prudently, knowledgeably and assuming the price is not affected by undue stimulus.

Implicit in this definition is the consummation of a sale as of a specified date and the passing of title from seller to buyer under conditions whereby:

- a. buyer and seller are typically motivated.
- b. both parties are well informed or well advised, and each acting in what they consider their own best interest.
- c. a reasonable time is allowed for exposure in the open market.
- d. payment is made in cash or its equivalent.
- e. financing, if any, is on terms generally available in the community at the specified date and typical for the property type in its locale.
- f. the price represents a normal consideration for the property sold unaffected by special financing amounts and/or terms, services, fees, costs, or credits incurred in the transaction.

Market value as defined is applicable in all lending/investment circumstances for insured associations and affiliates, including special purpose properties and REO/LTF situations. In REO/LTF situations, defined market value estimates will be derived on an "as is" basis. Under no circumstances should the appraiser further qualify or, by assumptions, erode the impact of this definition. All market data inputs should be thoroughly analyzed and, where necessary, adjusted in terms of the above definition, as qualified.

As reflected in qualifications d, e and f of the above definition, all valuations must be couched in terms of "cash or its equivalent" and "typical financing" for that particular property type.

Any valuations which by assumption or qualification effectively utilize any form of specialized, unique and/or subsidized financing assumptions as surrogates for "typical financing" assumptions in the appraisal methodology are not considered to be acceptable. All properties, regardless of the specific nature of the particular financing arrangements then

existing and/or as proposed, must be evaluated in a market value context as defined and as qualified relative to "typical financing" and "cash equivalency."

For certain governmental subsidy programs, such as HUD Section 8 Programs, where the real estate project and the ultimate product user represent a distinct and readily identifiable separate market relative to those projects found in the typical market, the appraiser may consider the various subsidized income/vacancy guarantees and/or subsidized aspects of the specific financing/contractual programs. In no case, however, should the final value estimate exceed replacement cost. Replacement cost in this context refers to the sum of the following:

1. market value of the subject site ("value" conforming to the above referenced market value definition).
2. current reproduction cost less deterioration and obsolescence of all building and site improvements.
3. a reasonable, market-supportable, entrepreneurial profit.

Please note that the definition of "market value" contained in this memorandum supersedes all older definitions of "market value" or "fair market value" previously deemed acceptable to the Bank Board. Memorandum #T 13-1, which contains a now obsolete definition, is hereby rescinded. It should be understood, however, that the long-standing examining and supervisory policy described in #T 13-1 remains in effect. Substantial variations between the appraised "market value" of a property and its actual selling price (and/or book value in the case of REO) will continue to be carefully scrutinized during the examination process. (3/12/82)

R 42 REASONABLENESS OF COMPENSATION AND FEES

The Board of Directors of an insured institution or affiliated service corporation has the responsibility for the determination of compensation of officers of the institution which, in accordance with Insurance Regulation 563.17(b), must be reasonable and commensurate with their duties and responsibilities.

Such compensation generally includes: remuneration such as salary, bonus, profit sharing, and fees for serving as a director, advisory director, or member of an executive, loan or other committee; as well as annuities, options, pension or other retirement benefits.

In making the determination concerning institution officers, the Board of Directors should include at least the following in the factors to which consideration is given:

1. The qualifications and experiences of the person(s) concerned;

2. The compensation paid to other persons employed by the institution or service corporation;
3. The compensation paid to persons having similar duties and responsibilities in other insured institutions or service corporation affiliates;
4. The size of the institution or service corporation, and the complexity of its operations;
5. The financial condition, including income, of the institution or service corporation and the individual's contribution thereto;
6. Any amounts received, either directly or indirectly, by the officer whose principal occupation is with the institution or service corporation for other services performed for the institution or service corporation (i.e., fees for serving as appraiser, attorney, escrow agent, insurance agent, etc.);
7. The value of personal fringe benefits provided to the employee and also perquisites such as an automobile, club membership and expense account.

With respect to fees of outside appraisers or attorneys, the Board of Directors is responsible for a determination of whether those fees are reasonable and commensurate with the services being performed. The responsibility will not necessarily be satisfied by a determination that the fees (particularly if the outsider appraiser or attorney is an affiliated person) are comparable to those charged by other appraisers or attorneys performing similar services for other insured institutions in the same area. In exercising its responsibility, the Board should also consider the comparative advantages to be gained by the institution or service corporation by employing a staff appraiser or attorney to perform its appraisal and legal services.

In establishing fees to be paid to members of the board, each director should be keenly aware of his fiduciary responsibilities. Each should keep in mind that one of his primary responsibilities is to establish policies which will protect the assets of the association. Thus, directors should use similar factors in setting such fees as it does in setting officer's salaries. The minutes of the Board of Directors should include the record of deliberations concerning salaries for officers and fees for attorneys, appraisers and directors, and the records of the board should support the conclusions reached. (8/2/77)

R 43 CREDIT CARDS

The staff of the Bank Board has concluded that, under certain circumstances, Federal associations presently have the authority to issue credit cards. That conclusion is confirmed in a letter directed to California Federal Savings and Loan Association, a copy of which is attached to this memorandum. In arriving at that conclusion, the staff also recognized

EXHIBIT 5

GUIDANCE NOTES WITH BACKGROUND PAPERS
ON
THE VALUATION OF FIXED ASSETS

Documents in Exhibit 5 deleted; ownership unclear
and request for permission from International Asset Valuation
Standards Committee not returned

EXHIBIT 6

RICS Guidance Notes on the Valuation of Assets - 2nd Edition

Guidance Note No. GN 22

LAND AND BUILDINGS
DEFINITIONS OF 'OPEN MARKET VALUE' AND
'FORCED SALE VALUE'

Guidance Note No. GN 22

**LAND AND BUILDINGS
DEFINITIONS OF 'OPEN MARKET VALUE' AND
'FORCED SALE VALUE'****1. Open Market Value**

1.1 'Open Market Value' is intended to mean the best price at which an interest in a property might reasonably be expected to be sold by Private Treaty at the date of valuation assuming:

- (a) a willing seller;
- (b) a reasonable period within which to negotiate the sale taking into account the nature of the property and the state of the market;
- (c) values will remain static throughout the period;
- (b) the property will be freely exposed to the market;
- (e) no account is to be taken of an additional bid by a special purchaser.

1.2 The Institution stresses that if a valuer considers it appropriate to apply any qualifying words to 'Open Market Value', the meaning of those words should be discussed and agreed with the client before instructions are finally accepted. The Valuer should incorporate in his report the agreed meaning of the qualifying words.

1.3 It is emphasised that this definition can in no way override any statutory definition of market value which may have to be adopted for the purpose of valuations for Capital Gains Tax, compensation cases, etc.

2. Forced Sale Value

2.1 'Forced Sale Value' is the Open Market Value as defined above with the proviso that the vendor has imposed a time limit for completion which cannot be regarded as a 'reasonable period' as referred to in Para. 1.1.

2.2 If the term 'Forced Sale Value' is used members are advised that the time limit should be discussed and agreed with the client.

THE VALUATION OF PLANT AND MACHINERY ASSETS

1. General

1.1 The Companies Act 1967 requires that assets shall be classified in the balance sheet under headings appropriate to the company's business and further that fixed assets, current assets and assets that are neither fixed nor current be separately identified but the Act contains no definitions of these classes of assets, although it refers to investments, goodwill, patents and trademarks in terms which recognise the possibility that such assets may be so classified. It should be noted that the very word 'fixed' is somewhat of a misnomer; ships, motor vehicles, railway engines and heavy movable equipment including cranes will be included although some may be classified as 'neither fixed nor current'. Smaller items of plant and machinery, particularly where they are movable, are often classified, for accounting purposes, as neither fixed nor current.

1.2 As a matter of practicality, many companies use a minimum expenditure level to account for capital expenditure; thus any item costing less than a specified amount is written off to revenue in the year of purchase whereas strictly speaking such expenditure could be charged to a fixed asset account.

1.3 Current assets (which will include stocks and work in progress) are in general those assets which are expected to be consumed or realised in the ordinary course of business in the short term.

1.4 The precise nature of the asset is not the only criterion as regards classification. Assets considered to be 'fixed' in one business would not necessarily be so in another.

1.5 When Valuers are asked to make a valuation whether it be of land and buildings or plant and machinery for inclusion in a company's accounts (whether by incorporating the valuation in the accounts or by a reference in a note or in the directors' report) it is essential that there should be a clear understanding by all concerned of what is being valued and the date of the valuation. Valuation Reports and Certificates should clearly define inclusions and exclusions. It is also essential that there should be a clear understanding of the basis of valuation and the proposed treatment of that valuation in the accounts, etc., in order to ensure that there is a proper comparison between the valuation and the book amount of the same assets. Unless this understanding exists between the directors, the accountants and the valuers concerned, there is always the risk that misleading comparisons will be drawn.

2. Basis of Valuation

2.1 Basic accounting concepts postulate that accounts are on a going concern basis, that is to say that the enterprise will continue in operational existence for the foreseeable future. The normal basis of valuation of plant and machinery where the valuation is to be incorporated or referred to in the accounts, etc., of a company should therefore be its open market value on the assumption that the plant and machinery will continue in its present existing use in the business of the company. Normally this existing use basis of valuation will be depreciated replacement cost, i.e., the estimated cost as new at the date of the valuation including the cost of installation less an allowance for depreciation (i.e., wear and tear, age and obsolescence). Account should be taken in the valuation, however, of special factors such as scarcity value or the possible limitation of value caused by limited natural resources or the building housing the plant having a limited life or being held on a limited tenure or with limited planning consent. Further it is necessary to consider both individual and overall values of the plant.

See GN 11

2.2 In some cases an existing use basis of valuation will not be appropriate. It would almost certainly be inappropriate to use an existing use basis of valuation of plant and machinery where the plant and machinery are valued on an alternative basis.

See GN 1 and BP 2

the effect on the value of plant and machinery. In these circumstances the following alternatives would be available:

- (a) where the plant and machinery could be moved to and used by the company at another site, the valuation would be on a depreciated replacement cost basis, but making an allowance for the costs of removal and reinstallation;
- (b) where plant and machinery is to be disposed of rather than used in the company's business it would then be valued on an open market value basis. If there is a time limit on the disposal, forced sale value may be the proper basis of valuation.

2.3 Where the land and buildings have not been valued, then the plant and machinery should be valued on the basis that would have been appropriate had the land and buildings been valued.

See GN 24

2.4 Definitions of open market value and forced sale value are given in GN. 24. These definitions are to be used for the purpose of valuations which are to be used in company accounts, etc., and they cannot override any statutory definitions of market value which may have to be adopted for the purpose of valuation for capital gains tax, compensation cases, etc.

2.5 In all instances, it is essential that, in advance of the valuation being carried out, there should be a clear understanding with the company and its accountants (and probably its auditors) of what is to be valued, the reasons for the valuation, the use to be made of the valuation and all the surrounding circumstances so that the appropriate basis can be determined.

3. Plant and Machinery forming part of a Building

3.1 Problems have arisen when valuing land and buildings where there are items of plant and machinery which are regarded by the valuer as forming part of the building but which the accountant may wish to segregate for accounting purposes. Valuers when valuing premises will normally include all items of plant and machinery on the premises which provide the services to the land and buildings and which the open market regards as an integral part of the premises for letting or sale or as security for a loan.

See GN 25

3.2 A list of such items is given in GN 25 but it is stressed that the list is not comprehensive and merely indicates, as a general guide to valuers, those items that would usually fall to be included in the value of the premises.

3.3 Normally process plant and machinery should not be included in the valuation of the premises.

3.4 It is possible that some or all of these types of plant and machinery normally included in the valuation of the premises may be needed to be separated for accounting purposes, for instance when it is expected that they have a shorter useful life than the rest of the premises and depreciation is being provided accordingly.

3.5 An apportionment of a valuation as between:

- (i) land and buildings; and
- (ii) the plant and machinery element;

may also be necessary in order to correspond with the headings adopted by the company in its accounts.

3.6 In such circumstances Valuers will have to indicate clearly that their valuation is of the whole and that any apportionment is an allocation of their overall valuation between the different components. This should also be stated in the notes to the Company Accounts if the apportioned figures are referred to therein.

4. Dies, Moulds, Patterns and Spare Parts

4.1 As a general rule, dies, moulds, patterns, jigs, drawings, designs and similar items should be excluded from a valuation.

4.2 In the normal course of events, spare parts would not be valued as part of the unit as it is often the practice for these to be carried in stock, and only auxiliary items necessary

4.3 In both cases, Valuers should consult with the directors and auditors in order to take the appropriate action.

5. Plant and Machinery Register

5.1 It is recommended that all companies be encouraged to maintain an up-to-date plant and machinery register showing as a minimum, the location of each item of plant and machinery, its date of acquisition, original cost and any further capital expenditure as this assists considerably in a valuation and its reconciliation with the company accounts.

6. General

6.1 Valuers are advised to discuss with the Company Accountants and Auditors the requirements of the valuation before carrying out the detailed valuation.

6.2 Reports and Certificates should incorporate suitable savings clauses covering the treatment in the valuation of such items as assets on hire purchase, government grants and goodwill.

7. Consent

7.1 The Valuer's Certificate should state that his written consent to any reference to his valuation in company accounts and/or directors' reports or any company statement or circular must be obtained before such documents are published. All Valuation Certificates should, therefore, incorporate a paragraph to the effect that:

'Neither the whole nor any part of this Valuation Certificate or any reference thereto may be included in any published document, circular or statement nor published in any way without the Valuer's written approval of the form and context in which it may appear.'

**PLANT AND MACHINERY
DEFINITIONS OF 'OPEN MARKET VALUE' AND
'FORCED SALE VALUE'**

1. Open Market Value

1.1 'Open Market Value' is defined as the best price at which an interest in the plant and machinery might reasonably be expected to be sold at the date of valuation by either Private Treaty, Public Auction or Tender, as may be appropriate assuming:

- (a) a willing seller;
- (b) a reasonable period within which to negotiate the sale, taking into account the nature of the plant and machinery and the state of the market;
- (c) values will remain static throughout the period;
- (d) the plant and machinery will be freely exposed to the market;
- (e) no account is to be taken of an additional bid by a special purchaser;
- (f) the plant and machinery may be valued, either
 - (i) as a whole in its working place, or
 - (ii) as individual items for removal.

2. Forced Sale Value

2.1 'Forced Sale Value' is defined as the open market value as defined above with the proviso that the vendor has imposed a time limit for completion which cannot be regarded as a reasonable period as referred to in above.

2.2 If the term 'Forced Sale Value' is used members are advised that the time limit should be discussed and agreed with the client.

**PLANT AND MACHINERY
ITEMS OF PLANT AND MACHINERY NORMALLY INCLUDED
IN VALUATIONS OF LAND AND BUILDINGS**

1. The following observations are intended to apply in the valuation of assets comprised in the majority of industrial and commercial types of property. Factory premises of a specialised nature will often require individual treatment and segregation to meet particular circumstances. In the case of sale, fire insurance, rating, etc., different criteria may apply. The list which follows, however, whilst not comprehensive, indicates those items usually valued on the basis that they form part of the 'building' service installations as opposed to those provided as part of the industrial or commercial processes carried on by the occupier. It follows that the valuation of land and buildings would normally exclude all items of plant, machinery and equipment which may have been installed wholly or primarily in connection with the occupiers' industrial or commercial processes, furniture and furnishings, tenants' fixtures and fittings, vehicles, stock, moulds and loose tools. The excluded items may need to be separately valued for balance sheet or other purposes.

2. **Electricity**

Mains supply cables, transformer houses with transformers, sub-stations and their equipment, generating plant and associated equipment including standby plant, and all wiring and switchgear up to and including the main distribution board in each building, together with:-

(a) *In non-industrial buildings:*

Wiring for lighting and power from the distribution board to wall and ceiling points.

(b) *In industrial buildings:*

Wiring for lighting to wall and ceiling points.

Note: (power circuits from the distribution board would normally be excluded on the grounds that these are related to the processes).

(c) *Externally:*

Wiring and associated structures for lighting to roads and yards, etc.

3. **Gas**

Gas mains up to and including meter houses and piping from meter houses for non-process purposes. Where the property includes a gas producer plant this would normally be in connection with the occupier's industrial processes and would, therefore, be excluded.

4. **Water**

Wells, boreholes, pumps, pump houses, service pipes including those connected to Water Board's mains, water treatment plants, storage tanks and reservoirs and all structures required to contain, support or house such items.

5. **Space Heating and Hot Water**

5.1 Boilers and associated plant including fuel tanks, pipes and fittings (e.g., radiators and unit fan heaters) primarily supplying or using steam or hot water for space heating and other non-process purposes.

6. Air Conditioning and Ventilation

Air conditioning plant and trunking and fan extractors and ventilators except where forming part of a computer installation or primarily serving plant and machinery used in industrial or commercial processes.

7. Fire and Security

Hydrants, pumps and mains, sprinkler systems, smoke detectors and annexed fire and burglar alarm systems.

8. Drainage

8.1 Surface water and foul water drains and sewers.

8.2 Sewage disposal plants not primarily concerned with treating water and other liquids used in the processes of trade effluents.

9. Lifts and Gantries

9.1 Passenger and goods lifts, escalators and travelators designed to benefit the general occupation of a building.

9.2 Rails and supporting gantries for overhead travelling cranes where forming an integral part of the structure of a building.

Note:

Hoists, conveyors, elevators, overhead cranes, jib and derrick cranes would normally be excluded.

10. Structures

10.1 The decision upon which items should be included will, to some extent, depend upon general experience and the practice adopted by individual trades.

10.2 Among the criteria will be the degree of attachment, permanence and size. Structures which are necessary for the provision of the services or have been installed or erected other than for the industrial or commercial processes carried out on the property would normally be included in the valuation of land and buildings. Such items might include the following:

- Boiler houses, Chimneys (brick and steel) and Economiser Chambers;**
- Pits;**
- Stagings;**
- Internal Buildings;**
- Permanent Partitions;**
- Railways;**
- Bridges and Housings for Conveyors;**
- Fences;**
- Roads, Yards and Hard Standings.**

10.3 Structures which are ancillary to, or form a part of an item of Process Plant and Machinery, would normally be excluded.

EXHIBIT 7

RICS Guidance Notes on the Valuation of Assets - 2nd Edition

Guidance Note No. GN 26

THE VALUATION OF PENSION FUND PROPERTY ASSETS

THE VALUATION OF PENSION FUND PROPERTY ASSETS

1. INTRODUCTION

1.1 The RICS draws the attention of members to the following guidance which should be observed when instructed to value the property assets owned by Pension and Superannuation Funds. This Note refers to a number of matters which should assist members but the general recommendations set out in the Guidance Notes Handbook should continue to be observed. It is recommended that the valuer should have discussions with the Trustees or the Fund Manager in order to establish the precise nature of the work required and to acquaint himself with the Fund's valuation policy and rules.

1.2 This Note applies equally to internal, external and independent valuers although, as indicated below, there can exist in certain specified circumstances special requirements which should be observed.

1.3 Funds may hold investments in companies, trusts or other entities, which in turn may own property assets. If valuers are instructed to provide a valuation of those property assets they should be valued and reported to the particular entity as separate valuations.

1.4 The term 'Trustees' includes any body of persons who have the ultimate responsibility for the investments and operation of the Fund.

1.5 The term 'Employer' refers to the body with whom the member of the fund has a contract of employment.

1.6 The term 'Fund Manager' refers to the individual to whom the Trustees may have delegated investment powers.

2. CATEGORIES OF PROPERTY

2.1 Properties owned by Funds should be categorised into four groups:—

- (a) Properties held as investments
- (b) Properties in course of development
- (c) Properties held for development
- (d) Properties in owner occupation.

2.2 Properties held as investments are those on which construction work has been completed and which are owned for the purpose of letting to produce a rental income which is negotiated at arm's length with third parties.

2.3 Properties in course of development include properties which have been acquired with vacant possession with the intention of seeking an early arm's length letting to a third party with or without works of repair or improvement being required. Apart from properties where work is in actual progress there should be included in this category any property where a start is imminent because all appropriate consents have been obtained and a building contract has been exchanged.

2.4 Properties held for development are those acquired with the intention to redevelop at some future date, with or without further properties not yet acquired, and which also do not fall within the other three categories.

2.5 Properties in owner occupation include any property which is subject to any form of intercompany leasing or licensing arrangement between the Fund and a subsidiary. Such arrangements should, therefore, be ignored. Properties which are partly occupied by the owner should only be included in this category if the occupation is substantial, say one-

3. BASIS OF VALUATION

3.1 The bases of valuation which should be adopted for each property category are:—

(a) Properties held as investments

Open Market Value.

(b) Properties in course of development

Cost, but if there is a permanent diminution in value to below cost, then at open market value, assuming the development is complete with the benefit of any contracted lettings less the estimated cost to complete. Properties should be valued on this basis until the earlier of either being fully let or a period, as may be appropriate, not exceeding twelve months from the date of practical completion.

(c) Properties held for development

Open Market Value.

(d) Properties in owner occupation

(i) Non-specialised properties—Open market value for existing use assuming vacant possession.

See GN11 and BP3

(ii) Specialised properties (See Guidance Note No. GN 11 and Background paper No. BP 3)—Depreciated replacement cost subject to adequate potential profitability.

Notes:

The Fund may occupy properties for its own administrative offices or a purpose such as farming or forestry either in hand or under some form of inter-company leasing or licensing arrangement between the Fund and a subsidiary, under which a business is either directly operated by a third party and/or the Fund.

See BP7

Certain properties like hotels and petrol filling stations are valued as fully operational business units (see Background Paper No. BP 7 on the subject of Open Market Valuations having regard to Trading Potential).

The Valuer should discuss with the Trustees or the Fund Manager whether it would be appropriate to undertake separate valuations of other items of fixed assets or current assets used in connection with the occupation of properties which come within this category.

In appropriate cases the valuer should draw attention to the existence of any material alternative use and the value attributable thereto where significantly different from the figure of open market value for existing use or depreciated replacement cost to be reported.

3.2 The valuer should enquire whether the valuation will be adopted for the purposes of an actuarial valuation and if so whether there are any specific requirements for the property valuation depending on whether the actuary is making a 'continuing' or (going concern) or a 'solvency' (or discontinuance valuation.)

3.3 The Fund should have a stated policy on the treatment of financial carrying charges. In the absence of such a policy if a valuer is requested to ascertain the figure of 'cost' for property in the course of development it would be usual to include a financial carrying charge. If a finance agreement exists with a third party the prescribed rate of interest should be adopted. If the property is a direct development of the Fund or no interest rate is stated in the agreement the valuer should adopt either an opportunity cost rate or a

4. THE VALUER

4.1 Valuers should meet the definition in Guidance Note No. GN 3 and can be internal, external or independent valuers, providing:— See GN3

- (a) If the Trustees should require an *independent valuation* the valuer must be *external* and also be able to comply with the requirement for an independent valuation in Guidance Note No. GN 3. An external valuer should always consider declining to accept instructions to carry out an independent valuation of certain properties if he considers that a conflict of interest could possibly arise. An external valuer who normally acts for the Fund in acquisitions and management would not generally be able to meet the requirements for an *independent valuation*.
- (b) If an internal valuer is not engaged wholtime on duties in connection with the properties of the Fund and also does not have a sole responsibility to the Trustees he may not meet the definition of a qualified internal asset valuer. It is for the internal valuer to satisfy himself as to where lies his responsibility.
- (c) If an external valuer is employed also by the Employer in respect of properties not owned by the Fund he may not meet the definition of an external asset valuer. It is for the external valuer to satisfy himself as to where lies his responsibility.
- (d) An external valuer responsible for the sale of a property to a Fund should not value the property for the Fund for a period of two years after the purchase.

4.2 The Employer and the Trustees should each be independently advised in any case relating to the transfer of any interest in a property between the Employer and the Fund, or in any matter affecting value, such as the disposal by way of sale/letting and rent reviews and where the Employer and the Fund have different legal interests in a property which could give rise to a conflict of interest. It follows that neither an internal nor an external valuer nor any RICS member should, therefore, act in such connection unless in the case of the last the RICS member had been appointed by both the Employer and the Trustees to act as an independent expert or arbitrator between the parties.

4.3 If the Fund wish to appoint an *independent valuer* he should conform to the definition contained in paragraph 3 of Guidance Note GN 19. See GN19

5. THE VALUATION CERTIFICATE

5.1 The Valuation Certificate should conform to Guidance Note GN 5 but in addition the valuer should provide the aggregate totals of the net rental income (after the deduction of all outgoings including ground and head rents but not amortization) passing at the date of valuation and at such other yearly anniversary dates in order to report reversionary increases/decreases based on market values current at the valuation date. The projection would not normally be for a period beyond ten years. See GN5

5.2 In normal circumstances the valuer should report to the Manager of the Fund but internal and external valuers must be prepared, if necessary and appropriate, to take steps to ensure that the Trustees individually have a sight of a copy of the Valuation Certificate but not necessarily copies of the schedules of properties.

5.3 It is emphasised that the Valuation Certificate should always contain a non-publication clause (see Guidance Note GN 5). See GN5

5.4 Internal, external and independent valuers should ensure that the following information is available in the Valuation Certificate to the Trustees:—

- (a) The total value of properties to be divided into:—
 - Freehold
 - Leasehold—long and short.
- (b) Para. (a) to be divided between:—
 - Completed investments
 - In course of development

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- (c) **Total gross rents**
 less Ground and Head rents
 Property expenses (but not amortization)
 Total net rental income.
- (d) **A projection of reversionary increases/decreases at yearly anniversary dates based on market values current at the valuation date, as set out in para. 5.1.**
- (e) **The percentage of the breakdown by capital value of the portfolio as between offices, retail, industrial, agricultural and others to be stated, differentiating between the U.K. and Overseas properties.**
- (f) **The date and basis of the valuation and the name and qualification of the valuer(s).**

5.5 It is the policy of The Royal Institution of Chartered Surveyors to encourage its members to request that the foregoing information is included in any published Report or Accounts to the extent that it is relevant and material to the valuation of the assets.

6. PLANT AND MACHINERY

See GN23

Any plant and machinery to be included in the valuation should be valued in accordance with Guidance Note GN 23.

7. FREQUENCY OF VALUATIONS

7.1 The Trustees have the responsibility for deciding the frequency at which valuations shall be made and whether by an internal, external or independent valuer. Nevertheless a member, who is engaged on duties which include those of an investment advisor and/or portfolio manager, will need from time to time to make capital and rental valuations. When such valuations are made he should draw to the attention of the Fund Manager or Trustees when appropriate any significant changes in the values of individual properties or in market conditions affecting the whole or part of the portfolio.

7.2 When a valuer is instructed he should recommend, in respect of any property falling within the category 'in course of development', where cost over-runs are a very real risk, that a valuation be made each year until the property is moved into another category in order to satisfy the Trustees that there has been no permanent diminution in value.

8. DISCUSSION PAPER

A discussion paper is being prepared by the Accounting Standards Committee. If this discussion paper is followed by an Accounting Standard it may be necessary to issue an amendment to this Guidance Note.

July 1981

Background Paper No. BP 1

EXISTING USE VALUE

1. Fixed assets which are included in the balance sheet should, in accordance with existing law and accountancy practice, be stated on the basis of cost, or at a valuation (which may or may not be current). When assets are stated at a valuation it is assumed that the business will continue and in many cases the basis to be adopted is open market value for existing use with vacant possession.
2. Open market value for existing use as a basis for valuations to be incorporated into a Company's balance sheet, or for reference to in the notes, takes into account the RICS definition of open market value but with the added assumption that the property will continue as owner-occupied in its existing use, and thus ignores any possible alternative use of the property, any element of hope value, any value attributable to goodwill and any possible increase in value due to special investment or financial transactions such as sale and leaseback which would leave the company with a different interest from the one which is to be valued.
3. Open market value for existing use would, however, include the possibilities of extensions or further buildings on undeveloped land or redevelopment of existing buildings providing such construction can be undertaken without major interruption to the continuing business.
4. It is not unusual for the occupation of business premises to be subject to a planning consent which is personal to the occupier. Bearing in mind that accounts are normally prepared on the assumption that the business is to continue in operation for the foreseeable future, it is recommended that open market value for existing use should disregard any planning problems which may arise in the event of the owner vacating. It is, however, recommended where the occupation is subject to a personal planning consent (unless this limitation applies for a relatively short period only), the valuer should report in addition to open market value for existing use the open market value having regard to the particular planning situation. The latter figure will take account of possible alternative uses to the extent to which these would be reflected in the price obtainable on a sale.
5. Existing use for the valuation of land and buildings in company accounts does not carry the same meaning as in planning law, or as current use for D.L.T. purposes, nor does it necessarily mean the particular trade currently being undertaken on the property. Many buildings are general purpose structures suitable for a wide variety of different trades. Similar industrial buildings will probably have the same values irrespective of the different trades that are carried on, and this would also apply to shops. A factory is valued as a factory, not as a particular type of factory, and a shop as a shop, not as a particular type of shop (unless the market differentiates between the two).
6. There is a separate Background Paper "Adaptation Works and Costs" on the treatment of properties which have been adapted to meet the special requirements of the business in occupation. Likewise there is a further Background Paper "Depreciated Replacement Cost Basis of Valuation" applicable to properties which are of the type that are rarely, if ever, sold in the open market for their existing use except by way of a sale of the business in occupation.
7. There are certain types of property designed or adapted for particular uses, including hotels, public houses, cinemas and clubs. Such properties are normally valued having regard to trading potential and a separate Background Paper deals with this subject.

Background Paper No. BP 2

ALTERNATIVE USE VALUE

1. Land and buildings may possess a value differing from their existing use value when the prospective use of the property for some other purpose is reflected (i.e. 'alternative use value').
2. Normal accounting concepts assume an ongoing business and where properties are occupied for the purpose of the business an alternative use value, which could only be realised on liquidation or a closure or removal of the business to other premises, is not suitable for inclusion in the accounts.
3. Such alternative use value may, however, have relevance to an overall appraisal of the company's situation. Where it differs materially (either above or below) from existing use value it should be reported by the valuer, whether the existing use value is on an open market basis or by reference to depreciated replacement cost. In the case of property occupied by a business under a personal planning consent it is recommended that the valuer should always include in the Valuation Certificate, in addition to open market value for existing use, a reference to open market value without the benefit of the personal consent.
4. It is probable that the alternative use value will be referred to in the notes to the accounts or the Directors' Report if it is above the open market value for existing use.
5. Where land and buildings are declared by the Directors to be surplus to trading requirements, they will be assessed to open market value which takes into account any possible alternative use. Such properties will be shown separately in the Valuation Certificate to enable the company to make a deduction for the estimated expenses of sale to arrive at the recoverable amount.
6. Land and buildings held as investments or for development will also be valued on an open market basis, subject to relevant existing tenancies and this will take into account any alternative use if appropriate.
7. In all cases, alternative use value should be related to definite information as to statutory or other consents (e.g. superior landlord's approval) regarding change of use or other matters, and it would not be appropriate to make unfounded assumptions.
8. It may be noted that in exceptional circumstances, which are more likely to arise on leasehold land, an alternative use value may be negative.

EXHIBIT 8

RICS Guidance Notes on the Valuation of Assets - 2nd Edition

Guidance Note No. GN 19

NOTES FOR INDEPENDENT VALUERS OF
UNIT LINKED PROPERTY ASSETS OF LIFE INSURANCE COMPANIES

NOTES FOR INDEPENDENT VALUERS OF UNIT LINKED PROPERTY ASSETS OF LIFE INSURANCE COMPANIES

1. This Guidance Note is of particular interest to those concerned with the valuation of Property Funds of Life Insurance Companies and it is recommended that the principles and procedures set out should be generally followed unless the Valuer considers that there are special circumstances existing, which justify a deviation. Other Guidance Notes incorporate those principles which would normally be followed in making valuations but it is considered that there is a practical value in bringing them together with certain specifics applying to the valuation of properties within a Property Fund.

2. Introductory

2.1 It is stressed that the Fund Managers are solely responsible for the investment policy of the Property Fund, the selection of properties, the pricing of units and the management of the Fund and the independent Valuer plays no part in these functions.

2.2 The Valuer should arrange his appointment on terms which allow him to require the Fund Managers and others to give him the fullest co-operation.

3. Independence of Valuer

3.1 It is normal practice for firms and not individuals to be appointed as Independent Valuer to a Property Fund and this is felt to be in the best interests of all concerned as it is both practical and adds strength to the standing of the Valuer's appointment.

3.2 In accepting an appointment as an Independent Valuer to a Property Fund the firm or the individual should apply terms which ensure that they can be seen to act in an independent role free from any suggestion that their judgement might be influenced by other relationships with the Fund Managers or promoters.

3.3 To accord with this independent role the firm should follow these principles:

- (a) they should not be employed by the Property Fund in any other capacity;
- (b) they should neither act for the Property Fund in purchasing any property nor act for the Property Fund or a purchaser in the sale of any property owned by the Property Fund;
- (c) if they act for the vendor of a property bought by the Property Fund then another Valuer should value that property after its acquisition, but at the expiry of two years thereafter the Independent Valuer to the Property Fund should value the property;
- (d) they should have no direct financial interest in the management of the Property Fund or its promoters. This should not be regarded as a barrier to the Valuer holding a very minor interest, providing it could not influence or be affected by the Valuer's judgement.

4. Terms of Appointment

4.1 The appointment should be in writing and made by the Trustees or Fund Managers. The Valuer should satisfy himself that he will be free to follow, as appropriate, the contents of this and other Guidance Notes.

4.2 The Trustees or Fund Managers will have the right to call on the Valuer at any time to value the whole or any part of the portfolio and the Valuer should have a reciprocal right.

4.3 If the Valuer's appointment is terminated he should possess the right not only to value the whole or any part of the portfolio but to have his Valuation Certificate issued to the auditors and Unit holders. If the Valuer chooses to resign he should possess a

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4.4 Normally there should be only one Valuer to a Fund except when Para. 3.3(c) applies or when the portfolio includes:

- (a) overseas properties in areas where the Independent Valuer feels unable to value;
- (b) specialist properties outside the qualification and experience of the independent valuer, e.g. agricultural land.

4.5 The Valuer should have the right of direct access to the Fund's auditors.

5. Basis of Valuation

See GN 22 and BP 2

5.1 The basis of valuation should normally be open market value (thus reflecting any element recognised in the market generally for an alternative use) and the date of the valuation clearly stated.

5.2 Any assumptions made by the Valuer must be clearly set out and any qualifications to 'open market value' stated and their meaning explained.

5.3 Valuers should not include forward projections of value in their Valuation Certificates.

5.4 Valuers will normally place no additional reliance on 'buy-out' clauses arising on developments or rental guarantees unless the contracting party is of an 'undoubted' character and the contract is unconditional. Where in the rare case any reliance is so placed this should be made clear.

See GN 1

5.5 Valuations should make no allowance for taxation or expenses of realisation which may arise on a notional or actual disposal. The principles set out in Guidance Note GN1 concerning the valuation of contracts and options, should be followed.

5.6 The valuation of a Property portfolio will normally be the aggregate of the individual property values.

6. Frequency of Valuations

6.1 Where the Fund Managers calculate the price of the units of a Property Fund less frequently than once a month the Valuer should revalue immediately before each date on which the price is calculated and in any event at least once every twelve months, when he provides the Valuation Certificate for publication (see paragraphs 7 and 8).

6.2 If the price is calculated monthly or at more frequent intervals the Valuer should value all the properties once every month and only in the event of a material change would a shorter interval be appropriate. Every property should be valued immediately after purchase (but never before completion has taken place) and at any time when there has been a material change of facts or market conditions.

7. Publication of Valuations

7.1 The Annual Report and Accounts of the Property Fund should reproduce the year end Valuation Certificate/Certificates relating to all the properties in the Fund at the end of the accounting year.

7.2 The Fund Managers are responsible for acting on intermediate valuations made by the Valuer and these need not normally be published except when a Valuer's appointment ceases by termination or resignation (see para. 4.3).

8. Form of Valuation Certificate

See GN 5

8.1 The contents of the preamble to the Certificates are a matter for each Valuer but attention is drawn to Guidance Note No. GN 5.

8.2 The Certificate should state clearly the date of valuation, the basis of valuation, and any assumptions made (see para. 5). The Certificate should give the aggregate of the valuation of each of the properties and this total be sub-divided into the categories:

- (a) Properties held as Investments.

(c) Properties substantially vacant.

(d) Properties held for development in the future.

8.3 Each category should be sub-divided between freehold and leasehold. Overseas properties should be shown separately. The Valuer should draw attention to any significant holding in short leasehold interests. He should state the identity of the largest property and its proportion to the aggregate amount of all Fund properties he has valued.

8.4 It is not considered necessary that any details of the individual properties need be given in the Certificate. If the Certificate refers to all the properties in the Property Fund the Valuer should request the Auditors to check the accuracy of the identity of the properties he has valued.

8.5 If the Certificate applies to only certain properties (because e.g. another Valuer is valuing the remainder) it will be desirable to state this and indicate the properties included or excluded. The Certificate should contain a 'non-publication without consent' clause. See GN 5

8.6 If in the Valuer's opinion there has been a material change in the aggregate value due to market changes or factors affecting a particular property or properties between the date of valuation and the date of the Certificate the Valuer should make an appropriate reference.

9. Developments

9.1 Developments should be valued in the state in which they exist at the date of valuation and any assumptions should be stated and explained.

9.2 Where information which is not within the Valuer's direct knowledge (e.g. the cost of completing a development) is needed to arrive at a value, such information should be obtained from an examination of the relevant documentation or from the professional adviser concerned.

10. Vacant Properties

Properties which are entirely or substantially vacant should be valued in their existing state and not on the basis that lettings might be completed, with a deduction for voids and expenses.

11. Overseas Properties

The valuation figure to be certified by the Valuer will be on the same basis as in the U.K. (i.e. open market value). The general principles relating to overseas valuations set out in Guidance Note No. 5 should be followed. As valuations are carried out in local currency the Fund Managers should be asked to arrange for a Banker to provide a letter giving the exchange rate to be adopted for conversion to Sterling on the valuation date. See GN 5

12. Information on Property Assets and Changes

The publication of information on the property assets, changes and movements is the responsibility of the Fund Manager. The Valuer will need to compare any such published information with the facts known to him and as referred to in his Valuation Certificate to ensure that his valuation is based on correct advice.

13. Inspections

The frequency of physical inspections of the properties must be a discretionary matter for the Valuer. When properties are valued at short intervals it is not practical for inspections to be made to a similar timetable. It is recommended that the Valuer should have visited each property every year and that a full inspection should be made at least every three years. Arrangements should be made for the Property Managers to notify the

14. Sources of Information

The Valuer should wherever possible verify the facts relating to a property and not rely on others. On the other hand he should not accept responsibility for matters which are the province of others. It is important, therefore, to state in the Valuation Certificate the information which is relied upon and not verified and by whom it has been supplied. Where other sources of information are relied upon the facts should be confirmed in writing, e.g. a Banker's letter on currency exchange rates (see para. 11).

Guidance Note No. GN 20

ASSET VALUATIONS IN ACCORDANCE WITH THE INSURANCE COMPANIES ACT 1974

1. When valuing assets of Insurance Companies it is necessary to comply with the terms of The Insurance Companies (Valuation of Assets) Regulations 1976 (SI 1976 No. 87) made under Sections 78 and 86 of The Insurance Companies Act 1974. (See Footnote)

The Regulations are effective from 1st May, 1976, and revoke SI 1974 No. 2203.

The Regulations apply to all general business assets, and all long-term business assets but unit linked property assets are excluded and subject to separate requirements. The Regulations apply to nine categories of assets: those likely to be of direct concern to members are 'Land' and 'Debts'. 'Land' includes land and buildings and any interest in land. An option to purchase is considered to be an interest in land and consequently must be valued.

The Regulations apply to all insurance companies authorised to carry on any class of insurance business in the United Kingdom.

Whilst Valuers will wish to read the Regulations as a whole, the following are probably of principal interest:

2. **Regulation 3**

2.1 Para. (4) provides in effect that the most recent 'proper valuation' made under Regulation 7 is a maximum. If the Valuer makes a qualification to the valuation (e.g. the absence of HAC has not been verified or some other adverse factor) a lower value may have to be adopted by the insurance company. If there has been a change in circumstances since the last 'proper valuation' (e.g. a change in market conditions with rising yields) which make it likely that the valuation figure is not realisable, then the appropriate lesser amount is to be taken.

2.2 This could mean in practice that an up-to-date revaluation may have to be made or further advice obtained and insurance companies can be expected to consult with their valuers.

2.3 Similar considerations apply to certain other categories of assets including 'debts' valued under Regulation 6.

3. **Regulations 4 and 5**

3.1 These Regulations concern the valuation of assets of dependents (as defined in Regulation 2(2)). If members are instructed to value assets of this category of companies they should consult with their clients as to the advice and valuations required to comply with the Regulations in the particular circumstances.

4. **Regulation 6**

4.1 This prescribes the method of valuing 'debts' which include mortgages.

4.2 If due within twelve months the value is the amount which can reasonably be expected to be recovered. This will include a debt which would become due within twelve months if the insurance company exercised any right to require payment.

4.3 If due beyond twelve months the value is the amount which would reasonably be paid for an assignment of the debt with the benefit of the security. Thus in 1979, for example, a standing mortgage of £100,000 for 20 years fixed at 7½% in 1965 would have fallen to be valued at a discount; consideration must also be given to the other conditions of the debt,

Note: These regulations should be read in conjunction with SI 1976 No. 2039 (which freed from the admissibility limits investments by insurance companies in Government and public authorities and increased the limit of admissibility set to certain debts from individuals) and SI 1980 No. 5 which enables insurers to elect, subject

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the status of the mortgagor and the nature of the security and the strength of the cover provided by it for the debt. Where the security is land members may be asked to comment on its nature and/or the value of the land.

4.4 Members may be asked to advise on the value of a 'salvage right' where the insurance company have a right to possess or sell an asset.

5. Regulation 7

5.1 This deals with the valuation of 'land'. The value to the insurance company for the purposes of the Regulation will not be greater than the amount obtainable (after deducting reasonable sale expenses) if the land were sold at the most recent 'proper' valuation. This basis is governed by Regulation 3(4) upon which comments are made above.

5.2 A 'proper valuation' is defined in Regulation 2 and is the amount realisable by an open market sale and must have been made not more than three years before the relevant date. This valuation must have been made by a 'qualified valuer' (see Regulation 2) viz. a person who is a Fellow or a Professional Associate of the Royal Institution of Chartered Surveyors (or a Fellow or an Associate of the ISVA or the RVA) who must have knowledge and experience in the valuation of land or by any other person approved by the Secretary of State for the Department of Trade.

5.3 As a 'person' can include any body of persons corporate or unincorporate it follows that a firm may or may not be a 'qualified valuer'. Where one or more of the partners is not a 'qualified valuer' the valuation must be made by, and the valuation report signed by, a partner who is a 'qualified valuer'.

5.4 It is recommended that the Valuer should produce the figure for the 'proper valuation' leaving the insurance company to assess the deduction for reasonable expenses of sale (according to the latter's judgement of the appropriate method of disposal). Members are advised to make it quite clear when submitting a valuation that it takes no account of the expenses of sale. Members should be prepared, if requested, to advise on the amount of sale expenses according to the circumstances.

5.5 The relevant date of valuation must be given to the Valuer by the insurance company.

5.6 It is to be noted that valuations do not have to be made by independent persons so that if they are 'qualified valuers' both directors and employees of the insurance company can undertake the valuation.

5.7 Land not so valued is excluded from being taken account of for the purposes of the Regulations (see Regulation 3(1)). This allows a company, if it so wishes, to exclude relatively small holdings.

5.8 Land occupied by the company is to be valued as if with the benefit of vacant possession; it would be wrong to value it on the basis of a sale as an investment with an assumed lease to the company at a rent.

5.9 Land is to be valued as free and clear of any mortgage or charge.

5.10 The Regulations cover land in the UK and overseas.

6. Regulation 8

6.1 This applies special valuation rules to equipment which includes 'plant and machinery'. Valuers in this field should note that the rules are severe and apply percentage deductions to a strict time scale on computer equipment and for all other equipment a minimum of 50% deduction on cost in the financial year of acquisition and a complete write-off thereafter. As the rules apply also to dependent companies it is important that Valuers consult with their instructing clients (see comments on Regulations 4 and 5).

6.2 In valuing an 'in hand' agricultural holding the basis of valuation of the land will assume vacant possession and it would appear that the operating capital (except for any item of plant and machinery acquired during the financial year) would have to be ignored.

6.4 Reference should be made to Guidance Note No. GN 25 as to those items of plant and machinery which are normally valued as an integral part of land and buildings and it follows that such items do not fall within the scope of this Regulation. See GN 25

7. Regulation 13

This Regulation provides for life interests to be valued as the amount which would reasonably be paid for an immediate transfer; it also expressly provides for leases and reversions to be valued on the basis prescribed in Regulation 7. It should be noted that reference in this Regulation to property includes all forms of property.

8. Schedule 2

This Schedule prescribes permitted limits for certain categories of assets in relation to the general business amount or the long term business amount (as defined in Regulation 15(2)). In this connection paragraph 1 should be noted by Valuers. This deals with the position where a valuation of a piece of land (other than land held as security for a debt) or a number of pieces of such land is greater than the aggregate of the valuations of each piece of land valued separately. This will cover the situation for example where the insurance company owns a number of interests (but not all) in a block of property or an island site, which is being assembled for development. Valuers can be expected, therefore, to be asked to advise on the 'lotting' of a portfolio to produce the highest proper valuation in order that the permitted limits can be tested.

9. The Signing of Valuation Certificates under the Insurance Companies Regulations

9.1 It is recommended that members should confirm in their Valuation Certificate that it is a 'proper valuation' made in accordance with the Regulations and the signatory is a 'qualified valuer' (see Regulation 7 above).

9.2 Care must be taken to ensure that the valuation is only signed by a qualified valuer.

9.3 The Institution is advised that where a partnership consists entirely of persons having the specified qualifications or corporate membership then the Valuation Certificate may be signed in the name of the partnership but this should also include a statement to the effect that all the partners have the specified qualifications.

9.4 If one or more of the partners is, therefore, not a corporate member of the Royal Institution of Chartered Surveyors, or the Incorporated Society of Valuers and Auctioneers or the Rating & Valuation Association the Valuation Certificate must be signed by the qualified valuer who has actually made the valuation and a statement included to the effect that the signatory is a qualified valuer within the meaning of the Regulations.

9.5 If the partnership consists entirely of corporate members of the Royal Institution of Chartered Surveyors or the Incorporated Society of Valuers and Auctioneers or the Rating & Valuation Association, the Valuation Certificate can still be signed in the firm's name, even though one or more of the partners may specialise in the valuation of categories of land other than that which is the subject of the valuation. In this event it must be understood that the actual valuation must have been made by a qualified valuer who has the appropriate knowledge and experience in valuing the subject land.

9.6 If the firm (and this may particularly apply in some overseas countries) is not a partnership but a corporate body then the signatory must be a qualified valuer, and a director or secretary, unless so qualified, may not sign the Valuation Certificate. In this case, it is also necessary for a statement to be made to the effect that the signatory is a qualified valuer within the meaning of the Regulations.

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9.8 It follows, therefore, that there should normally be only four forms of signature in accordance with the following examples:

(a) Smith, Jones and Robinson

(Where in this case every partner is a qualified valuer within the meaning of Regulation 7).

or

(b) (i) A. Smith or

**(ii) A. Smith
for Smith, Jones & Robinson, or**

**(iii) Smith, Jones & Robinson
A. Smith**

In cases (b) (i), (ii) and (iii) A. Smith being a qualified valuer within the meaning of the Regulations and the person fully responsible for the Valuation.

In both cases (a) and (b) The Valuation Certificate must include the statements as to qualifications referred to earlier.

It must not be overlooked that a partnership can contain as a partner a body of persons corporate or unincorporate and in that case the requirements will only be met by the application of examples (b) (i), (ii) or (iii).

REVIEWING OF VALUATIONS

1. Reviews of a Valuer's Previous Valuations

1.1 Valuers are often asked to carry out reviews of their previous valuations without undertaking a full reinspection of the properties. Valuers should be cautious in accepting such instructions and should have regard to the period of time that has elapsed since the last valuation. It would not normally be appropriate to accept such limited instructions where there has been a material alteration or change in the property portfolio, a material change in the property market, or a material change in the criteria previously adopted. Changes in rental income or other aspects of tenancies from investment properties would not normally be regarded as falling within the ambit of the foregoing circumstances.

1.2 Where such reviews are undertaken the Valuer is advised to obtain from the client a 'letter of comfort' stating that neither material alterations nor changes have taken place in the portfolio.

1.3 Where there have been material alterations or changes in the portfolio it will be necessary for the Valuer to undertake a valuation of those properties new to the portfolio or those where there have been alterations or changes.

1.4 When reporting the results of a review of a previous valuation the valuer is recommended not to refer to a 'desk study' or similar wording but to adopt the following, suitably amended to meet the particular circumstances:

'As instructed, we have reviewed our valuations of (date) without reinspecting (all) the properties and on the same criteria as previously used but under current market conditions we are of the opinion that the open market value as at (date) is of the order of £.....'

1.5 Where alterations and changes of a material or significant nature have occurred and a review has still been undertaken, these should be referred to in the review report.

2. Review of Valuations made by another party

2.1 A Valuer may be asked to review in whole or in part a valuation made by a director or internal valuer of the company which owns the property, or to undertake a review of a valuation by another external valuer.

2.2 A Valuer should not accept instructions to undertake a review of a valuation unless he made that valuation, in which case he should follow the recommendations above.

2.3 Unless the Valuer has already inspected the property concerned and is already familiar with the building and location or is afforded the opportunity of carrying out an inspection and has made all other relevant enquiries, or has been supplied with the information that would result from such enquiries, he is in no position to express an opinion as to value except on a restricted basis.

See GN 2

2.4 It is recommended that the Valuer should report his own valuation with such qualifications as may be appropriate. There should be no reference to any valuation prepared by another party as otherwise there may be implied criticism which would be unfair and possibly damaging to the other Valuer's reputation if he is afforded no right of reply.

See GN 17

2.5 Where a Valuer is instructed to carry out a valuation jointly with another Valuer, this would not be considered to be a review within the ambit of this Guidance Note, even though one of the Valuers may be an internal valuer.

See GN 3

EXHIBIT 9

FIRST ASSET REALTY ADVISORS
APPRAISAL ENGAGEMENT LETTER



Appraisal Engagement Letter - Preliminary Draft

TO:

RE: Property Identification

Dear _____:

On behalf of First Asset Realty Advisors (FARA), we would like to engage your services for the appraisal of the above property to determine the fair market value of the legal interests owned by a Commingled Fund as of (date of appraisal). To that end and before accepting the assignment, the appraiser should consider the following requirements as to definition and procedure:

1. Fair market value shall be defined as the most probable price at which the property would sell to a knowledgeable buyer on a given date if placed on the market for a reasonable length of time by a well informed seller assuming:
 - a. Cash to the seller or cash plus debt owed or assumed by the buyer, where appropriate.
 - b. Fee title will be encumbered by leases in place and possible other covenants. Appraiser must indicate remaining market value of these other leasehold or non-possessory interests.
 - c. The appropriate exposure on the market has occurred prior to the date of sale.
 - d. Buyer motivation is profiled as an assumption by the appraiser.

2. Fee title may be encumbered by leases, mortgages as well as possible conditional use permits and private covenants. FARA is obligated to provide access to all of the appropriate documents at the office of _____ located at _____ during normal business hours. The appraiser is expected to read the leases, mortgage instruments and other encumbrances and relate to them appropriately. If existing debt is assumable by another buyer, then the appraiser can value the sale as cash to the seller with the buyer accepting the mortgage(s) already in place if that would be consistent with the most probable buyers self interest. Otherwise the trustees of the Commingled Fund management (FARA) are interested in a value which is the most probable cash price to the seller and with the buyer accepting the existing encumbrances in terms of leases and covenants, etc.

3. When using the market comparison approach the appraiser must document each comparable sale as to grantor, grantee, public record, plot plan and photograph as well as basic details of construction and existing encumbrances, terms of sale, and seller motivation. All calculations necessary to adjust engineered prices to cash equivalencies must be documented and explained as well as any and all adjustments to relate the comparable price to the subject property must be itemized and explained so that the reader can repeat the mathematical adjustments possible.
4. The income approach must use discounted cash flow from a ten year forecast (and your own forecast if different) in which all major leases are detailed individually and minor leases classified into groups if appropriate. The rationale for roll-over vacancies, absorptions, and expense projections must be itemized with a series of footnotes in the manner of a fully detailed accounting income and balance sheet statement. Normalized income methods including investment bond, Ellwood, or net income multipliers are not acceptable.
5. The appraiser must document his opinion as to the appropriate discount rate applied to each segment of the cash throw-off and after tax cash flow as appropriate, together with financing terms assumed.
6. A cost approach by a responsible service or professional should be supplied with the initial appraisal. If it is not used in the final valuation, then a discussion on why it is not used is required. The appraiser is expected to carefully inspect the property and report his own independent views on the quality of maintenance, deferred maintenance, and tenant housekeeping.
7. The appraiser is regarded as the eyes and property inspector of FARA. To put the property in context the appraiser must supply and evaluate a list of projects which are competitive alternatives in the market areas of the appraiser and indicate rent structures, vacancy rates, turnover rates, and in the case of the new building, coming on stream or about to be built, some indication as to their rentup success and the source of their tenants. Wherever possible the appraiser is to indicate the ownership and character of investment position in these competitive properties and the property management or leasing term involved with each.

Following the initial appraisal at the time of acquisition, the appraiser will be asked to submit a letter of review 180 days after the date of the original appraisal indicating if he would modify any of his critical assumptions at that time, and if so, indicating how this might affect his original value estimate as a specific dollar adjustment, up or down.

At the end of 360 days the appraiser would be expected to perform a thorough review of his original appraisal, specifically focusing on the market approach (Item 3), adjustments indicated for the income approach (Item 4 & 5), and additions and amendments to

market data, (Item 7). Aside from the specific instructions provided in paragraphs 1-7 above, it is anticipated that all work will be done according to the standards of the American Institute of Real Estate Appraisers, and it is further understood that the client for whom the appraisal is done for purposes of professional accountability is both First Asset Realty Advisors, Inc. and its operations agent, The Center Companies of Minneapolis, Minnesota. Purpose of the appraisal is to meet the asset valuation requirements of an open-ended, commingled real estate fund suitable for investment by pension fund programs subject to ERISA.

Please return both copies of this letter together with an indication of your fee for the appraisal services above, with a separate quote for the initial appraisal, the 180 day review, and a 360 day reappraisal. If this is your first assignment for FARA, please include a sample of your work, preferably of a similar property, in which you have provided for the necessary cash flow projections.

NORTHWEST CENTER FOR PROFESSIONAL EDUCATION

SEMINAR ATTENDEE LIST
FOR 85168NYC

CONTEMPORARY APPRAISING/PENSION FUND
ST REGIS SHERATON
09/26/1985 THRU 09/27/1985

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November 10-13, 1985

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October 28, 1985

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Salt Lake City, UT

Dr. James Graaskamp
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Madison, Wisconsin 53705

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California Public Employees
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Sacramento, CA

Dear Jim:

The Pension Fund Conference in San Francisco, November 10-13, is now only two weeks away. Registrations are most encouraging -- we have 155 advisors and 121 sponsors registered, the largest response ever!

I am enclosing a Tape Release Form which gives us permission to record the audio segment of your presentation. Please sign and return this release to us at your earliest convenience. If you would like a complimentary tape of your presentation, check the box at the bottom of the form. We will be happy to send you a copy.

We would like to invite you to have lunch with Clem Laufenberg, Conference Manager, and the other Monday afternoon speakers in the Milan Room of the Hotel on Monday, November 11, at 12:30 p.m. We hope you will be able to attend.

Don't forget the tour and champagne party at the Embarcadero Center on Sunday afternoon. We are hoping for a large turnout for what we consider one of the highlights of the conference this year. If you are planning to attend, please call our Bellevue office at 1-800-426-5575 to RSVP. We need to know the number of people attending since we are providing transportation from the Ramada Renaissance to the Center.

We will be in touch with you again shortly before the conference.

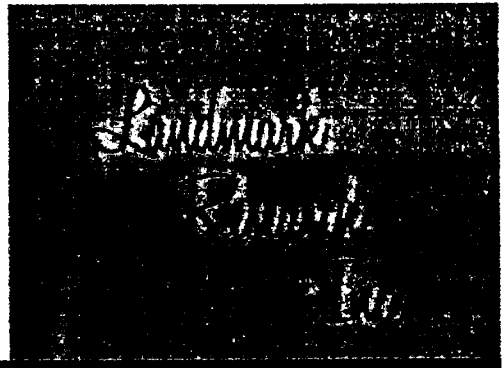
Sincerely,



Darlene Carlson
Program Manager

DC:d
Enc.

CONFERENCE MANAGER
CLEMENS J. LAUFENBERG
Northwest Center for
Professional Education
Portland, OR
(503) 223-3921



*James A. Graaskamp, Ph.D., S.R.E.A., C.R.E.
Jean B. Davis, M.S.*

May 13, 1985

Norman P. Swent, Executive Director
Northwest Center for Professional Education
13555 Bel-Red Road
C-96870
Bellevue, WA 98009

Dear Paul:

Here are the two one-day course outlines I promised. Let me know if there is more detail required.

Please send a note confirming the various dates for the fall-winter road show as I seem to have misplaced your note.

Best regards,

JAMES A. GRAASKAMP

The Emerging Role of Consulting Appraising in a Changing Real Estate Marketplace

The commercial real estate industry is undergoing tremendous change. Tax reform, lower inflation, overbuilding, longer term lease-ups, the securitization of real estate, and the growth in pension fund assets invested in real estate are major forces causing restructuring of commercial property values.

These market and economic factors have dramatic, and often misleading, effects on real property values. This places greater demands on the appraisal community. The role of the appraiser as counselor and advisor has never been so important. This provides appraisers with an opportunity for greater professionalism and profit if they are willing to shift from only traditional approaches and to add innovative thinking and new appraisal practices.

Today's real estate market requires a fresh and broad approach to real property valuation, utilizing contemporary appraisal techniques and emphasizing

identification of the issues and problems to be solved. Spend one or two days with Dr. Jim Graaskamp, the nation's foremost authority on appraisal methods, to broaden your perspective and improve your appraising skills.

The first day, **Contemporary Issues and Methods for Appraising Commercial Properties** focuses on appraisal methods. The second day, **Real Estate Valuation Issues for Pension Funds**, deals with the practical and ethical approaches to using appraisals in the valuing of pension fund assets.

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Contemporary Issues and Methods for Appraising Commercial Properties

Thursday, January 16, 1986

Day One

8:30am - 10:00am

1. Defining the appraisal problem with the client, his attorney, and the accountant

- The issues for which the appraisal is required as a benchmark
- The exact "sticks" in the bundle of rights to be appraised
- The perspective in time, viewpoint, and going concern assumption controlling the appraisal
- The definition of value to be applied
- Responsibility for engineering, marketing or legal/political data and assumptions
- Special enhancements or encumbrances to be valued as components
- Specification as to methods, data sources and controls on use through letter of engagement

BREAK

10:15am - 12:00pm

2. Decision theory and improved methods for the market comparison approach

- The three approaches to the contemporary method
- Market inference by means of proxy patterns

- Why regression pricing is discredited
- Developing a pricing algorithm for comparable properties
- Selecting the proper unit of comparison
- The price per point per unit of comparison
- Developing a weighting system for the attribute scores
- Testing the price weighting system for best estimate of the comparables by hand or by computer
- Variations on the theme by Dilmore

COMPLIMENTARY LUNCHEON

1:00pm - 2:45pm

3. Professionalizing the income approach or investment stimulation approach

- Recognizing the significance for allocating income to real estate, personality, intangible assets or management, depending upon the issue for which the appraisal is sought as a benchmark
- Perspective and accounting: cash or accrual, normalized or simulated
- Revenue classification and projection
- Operating expense classification and projection

- Income from operations vs. cash for distribution
- Projecting increases, leakages and concessions
- Formatting the pro forma real estate operating statement
- Financial footnotes in lieu of a narrative report

BREAK

3:00pm - 5:00pm

4. Case examples of defining the issue, the method, and the accounting relevant to litigation

- Real estate tax appeal for subsidized houses
- Credit enhanced elderly housing with HODAG and income from providing support services
- Right-of-way for a power transmission line
- Partnership values in dissolution

5:00pm - 5:30pm

5. Professional status for the appraisers in litigation matters

- The vested interest of the attorney
- Counseling vs. advocacy
- Compensation relative to value of service

Seminar Instructor

James A. Graaskamp, Ph.D., SREA, CRE, CPCU, is one of the most popular and dynamic real estate instructors in the U.S. today. His presentations reflect the rare combination of real world experience and academic achievement that has characterized him as one of the industry's "original thinkers."

He has served as Chairman of the Department of Real Estate and Urban Land Economics at the University of Wisconsin for over ten years. He is currently teaching advanced appraising techniques and advanced feasibility studies.

In addition to his academic work, Dr. Graaskamp is President and founder of Landmark Research, Inc. He is also co-founder of a general contracting firm, a land development company

Dr. James Graaskamp

and a real estate investment corporation. He serves on the Board and Executive Committee of First Asset Realty Advisors, a subsidiary of First Bank Minneapolis, and is a member of the American Real Estate and Urban Economics Association.

Dr. Graaskamp is the co-designer and instructor of the EDUCARE teaching program for computer applications in the real estate industry. His work also includes substantial and varied consulting and valuation assignments such as investment counseling to insurance companies, banks and other lenders and feasibility and financial analysis of nationally known real estate development projects for a wide variety of clients.

Pension Fund Real Estate Valuation Issues

Friday, January 17, 1986

8:30am - 12:00noon

1. The case for greater standardization of appraisal and accounting reporting for asset valuation and performance measurement

- Appraisal process must respond to issues for which appraisal is required as a benchmark
 - Adequacy of pension funding
 - Entry/exit unit values of co-mingled shares in real estate pools
 - Performance of asset managers
- Traditional presumptions of appraisal standardization
 - Appraisal format imposed by U.S. professional societies
 - Appraisal format used in the Common Market
 - Appraisal format under development for imposition by American intermediary banking institutions, i.e. FHLB, FDIC, and FNMA
 - Guidelines for pension managers by NCREIF
- Current research progress of actual appraisal practices of pension real estate managers and their methodology
 - Formal pension policy, regarding appraisals
 - Selection criteria for appraisers
 - Control of appraisals for asset measurement
 - Pattern of practice revealed in actual paired appraisals from 1983 and 1984
 - Procedures and controls on internal appraisal values by asset managers between anniversary appraisals

BREAK

2. Suggested requirements for developing consistent appraisal quality and consistent performance by appraisers

- Basic components of standardization process
 - Standards promulgated by industry association
 - Written policy statement by pension fund sponsor
 - Written appraisal method statement to implement policy by asset manager
 - Letter of engagement to the appraiser
 - Explicit methodology and terminology from appraisal association

Day Two

- Standards promulgated by industry association
 - FASB and MAIs
 - Consistency with NCREIF guidelines
 - Objectives of ERISA
 - Total fee income and substantial economic ties constituting conflict of interest
 - A vacuum of appraisal standards or white paper methods
- Valuation controls imposed by pension sponsor
 - Frequency, quality, and independence
 - Parameters for projection and financial simulation
 - Responsibility for structural and mechanical engineering integrity
 - Permissible level of aggregate simulation, e.g. financial details of leases
 - Segregated accounts vs. co-mingled accounts
 - Accounting issues vs. appraisal issues: How to handle lease concessions
 - Issues of ethics and fiduciary responsibility
- Suggested formats to accomplish desired objectives

COMPLIMENTARY LUNCHEON

1:00pm - 5:00pm

3. Pitfalls to look for when reviewing an appraisal using the market approach to value

- Failure to establish the best unit of comparison between properties
- Failure to report terms of sale or quantitative adjustments for cash equivalency
- Failure to establish rules for selection and quantification of accounting patterns
- Failure to explain adjustments for differences
- Failure to report addresses and transaction details of comparables
- Other problems

BREAK

4. Need for standardized accounting formats, accounting rules, and assumptions for financial projections

- Inconsistency of discounted cash flow

concepts and appraisal pro forma accounting

- Establishing standardized financial models to handle amortizable assets and expenses such as tenant improvements, lease renewal commissions and financing charges
 - Providing the appraiser with receipt and expenditure models pre-built by asset manager for market review by appraiser. Is this an ethical issue?
 - How to integrate accounting/budgeting and appraisal forecasting while maintaining the independence of the appraiser
 - Reconciliation of appraisal and accounting issues
 - How pension fund and asset managers exercise control over appraisal valuations: Actual case examples from national study
- ### 5. Philosophies and practices of asset managers relative to internal appraisal procedures
- Alternative internal procedures and controls
 - Justification of quarterly adjustments to independent appraisals
 - Integration of capital expenditures during interim period with independent appraisers
 - Reallocation of values relative to leasehold value and investment value due to passage of time and perceived changes in discount rates
 - Should quarterly sequence of appraised value changes and source of change be indicated for each property for fund investors?
- ### 6. Suggested new ways for the pension fund industry to operate
- Establish valuation reserves reflecting potential appraisal bias to high side
 - Dollar-cost-average commitments to invest or disinvest over six quarters so that two independent appraisals of total portfolio could have occurred
 - Prohibit quarterly internal adjustments to value except for adjustments due to capital expenditures