MountainSeed General Guidelines for Financial Institutions

Commercial Appraisal Services

Introduction

These general guidelines are to be used by all appraisers engaged by MountainSeed Appraisal Management, LLC ("MountainSeed") in providing quality commercial appraisals. All engaged appraisals must conform to the following:

1. Title XI of the Financial Institutions Reform, Recovery and Enforcement Act of 1989 ("FIRREA") and all appraisal regulations promulgated thereunder, including, without limitation, Office of the Comptroller of the Currency ("OCC") Real Estate Lending and Appraisals Regulations, 12 C.F.R. § 34; Board of Governors of the Federal Reserve System ("FRB") Appraisal Standards for Federally Related Transactions, 12 C.F.R. § 225.61–67; Federal Deposit Insurance Corporation ("FDIC") Appraisal Regulations, 12 C.F.R. § 323; Office of Thrift Supervision ("OTS") Appraisals Regulations, 12 C.F.R. § 564, as may be enforced by the applicable federal agency; and the National Credit Union Administration ("NCUA") Appraisals Regulations, 12 C.F.R. § 722.

2. Guidelines issued in connection with the legislation and implementing regulations described above, including without limitation, the final Interagency Appraisal and Evaluation Guidelines issued on December 2, 2010 by the Office of the Comptroller of the Currency ("OCC"), Federal Reserve Board ("FRB"), Federal Deposit Insurance Corporation ("FDIC"), Office of Thrift Supervision ("OTS") and National Credit Union Administration ("NCUA"), the Interagency FAQs on the Agencies Appraisal Regulations and Interagency Statement on Independence of Appraisal and Evaluation Functions (see, for example, FRBs SR 18-9), and the Interagency FAQs on Residential Tract Development Lending (see, for example, FRBs SR 05–14).

3. Standards for real estate appraisals established by the state, territory, or district regulatory board with authority over the assignment.

4. MountainSeed General Guidelines for Financial Institutions – Commercial Appraisal Services (i.e., this document).

5. Special Instructions for certain property types referenced in the request for proposal.

6. Special Requirements specified in the engagement letter for the assignment.

These general guidelines are hereby incorporated by reference into, and shall be considered for all purposes a part of, any engagement letter entered by MountainSeed.

Appraisers should communicate all questions regarding these guidelines or the engaged assignment to MountainSeed.

Contents

Report Format

The Uniform Standards of Professional Appraisal Practice ("USPAP") identifies two report options: Appraisal Report and Restricted Appraisal Report. Unless otherwise noted in the engagement letter, MountainSeed requires an Appraisal Report. Appraisal Reports are the appropriate report option in most circumstances since the Interagency Appraisal and Evaluation Guidelines require all valuations to contain "*sufficient information and analysis to support the institution's decision to engage in the transaction.*" The Restricted Appraisal Report is not a good reporting format for Federally Related Transactions since USPAP allows all support to be contained in the appraiser's work file, not in the actual report delivered to the client. Regardless of the report format, all appraisals must comply with the reporting requirements indicated in Standard 2 of USPAP.

"As Is" Market Value

The Appraisal Report must estimate the market value of real property in its current physical condition, use, and zoning as of the appraisal's effective date. All appraisals involving Federally Related Transactions are required to include an "As Is" Market Value.

Property Rights

While the engagement letter identifies the property rights, the appraiser should check for accuracy and appropriateness. If at any time during the assignment the property rights are in question, immediately contact MountainSeed for guidance. Some examples that cause confusion are listed below.

- If the existing tenant is the buyer of the property (and the new borrower) then the lease will be extinguished at the time of sale and the appropriate property rights is fee simple.
- If the leases in place will not survive a sale, then fee simple is appropriate.
- Any real property with one or more arm's length leases should be valued as leased fee unless expressly instructed otherwise by MountainSeed. (An example of an exception is a property with month-to-month leases.)

Appraisal Content Requirements

The requirements outlined in the following pages correspond to sections of the Appraisal Report and are applicable for an Appraisal Report format. All Appraisal Reports should contain sufficient supporting documentation with all pertinent information reported so that the appraiser's logic, reasoning, judgment, and analysis in arriving at a conclusion demonstrates a credible assignment result.

As noted on the first page of this document, Appraisal Reports prepared for MountainSeed must conform to USPAP and other regulatory requirements. The following requirements are included for emphasis.

Transmittal Letter

The transmittal letter should include:

- MountainSeed File ID
- The client name, consistent with the engagement letter, and all intended users (by name or type)
- The intended use of the appraisal

- A brief description of the subject property
- Clear statement of the real property interest appraised
- Date of the Appraisal Report
- Effective date(s) of the appraisal
- All extraordinary assumptions and hypothetical conditions
- All value conclusions
- Appraiser signature(s) and state license number(s)

Extraordinary Assumptions and Hypothetical Conditions

Any extraordinary assumptions and hypothetical conditions must be labeled accordingly and separated from the general assumptions and limiting conditions. The extraordinary assumptions and hypothetical conditions affecting the assignment should be clearly and conspicuously stated in the Appraisal Report and referenced in the transmittal letter. It is typically inappropriate to include an "As Is" Market Value that is subject to a hypothetical condition. An exception is when providing a Market Value "As If" Complete or a Market Value "As If" Stabilized. There is no such thing as a "hypothetical value," there is only a Market Value that is subject to a hypothetical condition.

Exposure Time

Provide an opinion of a reasonable exposure time linked to the value opinion for the subject property. The exposure time can be based on items such as statistical information about days on market, information gathered through sales verification, or interviews with market participants.

History of the Property

For all appraisals, a minimum of a three-year sales history preceding the date of value is required. The history section of the report may include the following: original assemblage, acquisition, construction cost information, capital additions or modernization expenditures, financial data, and transfers of ownership for the past three years. Report and analyze any prior sale and/or current agreement of sale, option, or listing (even if expired). Include and discuss items such as parties involved, sales date, sales price(s) and terms, marketing time and/or means of how the property was marketed (i.e., by owner, brokerage, auction, etc.).

Regional and Neighborhood Descriptions

These sections must be relevant to the property being appraised. Emphasis should be placed on how regional and neighborhood trends will affect real estate prices in the future. Neighborhood boundaries must be defined. This section should identify how the characteristics relate to the subject property. Land use and growth rates must be analyzed as well as the subject's market or sub-market areas. At a minimum, this section of the Appraisal Report should contain the following:

- Facts and statistics should be analyzed in relation to the subject and the specific assignment.
- The subject location should be adequately analyzed regarding linkages, land use, and the direction and rate of neighborhood and city growth.
- The subject's market and sub-market should be defined.
- Historical market trends should be provided and analyzed.
- Supply and demand should be discussed in the level of detail commensurate with the purpose of the appraisal and complexity of the assignment.

Site Description

This section of the report should address the following factors for the subject site:

- The site should be adequately described.

    - Legal description, address, size, shape, physical characteristics, tax parcel identification number, ingress/egress and visibility, functional adequacy, restrictions, relationship with surrounding properties, flood zone classification and description, exhibits such as survey, plat map, or tax map, and photos showing relevant features.

- The zoning must be provided and discussed. It must be clearly communicated whether the current or proposed use is conforming or non-conforming.

- The Appraisal Report should discuss relevant characteristics and summarize positive or negative factors that impact the site value.

Description of Improvements

At a minimum, this section of the report should address the following factors for the subject improvements.

- Functional utility or inutility of design/layout
- Presence or absence of deferred maintenance
- Current use and design; quality and type of construction
- Year built and effective age
- Interior/exterior construction details
- Current conditions – impact of proposed changes
- Synergy with surrounding properties
- Parking type and adequacy
- Structure drawings, plans, or assessor sketch (if unavailable, state the reason)
- Source(s) for improvement information
- Interior/exterior photographs
- Description of FF&E if applicable

If the existing or proposed improvements are non-conforming to the current zoning ordinance, discuss the consequences in the event the improvements should be destroyed by natural disaster or abandoned.

Property Tax and Assessment Analysis

The Appraisal Report must clearly describe the basis for the real estate tax assessment in the subject's taxing jurisdiction. Provide the current assessment and taxes for the property.

In states where the assessed value of the property is based on sales of comparable properties, a sufficient number of tax comparables must be used to estimate future taxes. For existing properties, a three-year history of both the assessment and the taxes should be included to support the tax estimate applied in the Income Capitalization Approach.

In states where the assessor emphasizes the most recent sale of the subject property, future tax estimates must consider the appraised value in deriving the prospective tax amount. If the assessor typically applies the assessed value at less than the sales price of a property, the appraiser must discuss this and apply a similar reduction in assessed value/taxes. If available and appropriate, recently sold comparables should be used to support the tax estimate.

For all properties, the Appraisal Report should clearly state if an appeal is warranted (when the taxes are high) or if an increase is likely (when taxes are low). Unpaid real estate taxes and/or special assessments must be disclosed. If the subject property is involved in an appeal, the Appraisal Report must disclose details of the appeal.

Special assessments (if applicable) should be addressed and discussed separately.

Marketability Analysis

An opinion of market value requires a marketability analysis. MountainSeed has adopted the terms and methodology developed by Stephen F. Fanning, which is described in detail in his book "*Market Analysis for Real Estate: Concepts and Applications in Valuation and Highest and Best Use, Second Edition, 2014.*" This methodology is also used in the *Appraisal of Real Estate, 14th Edition*, published by the Appraisal Institute as well as several classes offered by the Appraisal Institute. Accordingly, MountainSeed will clearly communicate at the bidding stage and in the engagement letter one of three levels (or strata) of analysis: A, B, or C. The following table compares the three marketability study levels.

Comparison of Marketability Studies

Category	Level A	Level B	Level C
Property productivity Physical Legal Locational	 Descriptive only Basic General	 Descriptive + Critique Basic + Deed Research Linkages/urban growth	 Descriptive + Critique Basic + Deed research Linkages/urban growth + Rating grid
Market delineation	Macro: whole community	Concerned with direct competition	Concerned with source of demand (users)
Demand analysis	Comparable data + General regional/city/ neighborhood data	Comparable data + Published surveys + Trends	Comparable data + Published surveys + Forecasting
Timing/phasing of use	Timing not an issue	Timing could be minor issue	Timing an issue
Future market strength	Inferred from comparable data	Inferred through total demand	Calculated through marginal demand

Source: *The Appraisal of Real Estate*, 14th Edition (Chicago: Appraisal Institute, 2013), 315

As shown, Levels A and B employ general market information and market surveys. Inferred analysis (trend analysis) is applied to this historical information to make future projections. There is a marked shift in Level C analysis, which uses fundamental analysis for forecasting. In Level C analysis, general surveys are replaced with primary data obtained by the appraiser and a six-step process.

Six-Step Process Used in Level C Marketability Analysis

Step 1 – Define the Product (Productivity Analysis)
Step 2 – Determine the Market (Market Delineation)
Step 3 – Demand Analysis (Measure Demand)
Step 4 – Supply Analysis (Measure Competition)
Step 5 – Analyze the Interaction of Supply and Demand
Step 6 – Forecast Subject Capture

Source: *The Appraisal of Real Estate*, 14th Edition (Chicago: Appraisal Institute, 2013), 3

When determining the appropriate level of marketability analysis, MountainSeed Procurement will refer to the following reliability continuum. While the appraiser may decide to provide a more in-depth analysis than stated in the engagement letter (e.g., decide to perform a Level B analysis when a Level A analysis was required in the engagement letter), **the appraiser must obtain written approval from MountainSeed to lower the level of analysis stated at the bidding stage or in the engagement letter**.

Reliability Continuum

Level A		Level B		Level C	
Simple property Small property Stable market	} 3 of 3	Complex property Large property Volatile market	} 1 of 3	Complex property Large property Volatile market	} 2+ of 3
Timing is now.		Timing is probably now.		Timing is an issue.	

Source: *The Appraisal of Real Estate*, 14th Edition (Chicago: Appraisal Institute, 2013), 315

Highest and Best Use

The Appraisal Report should clearly evaluate the physically possible, legally permissible, financially feasible, and maximally productive uses of the subject property as vacant and as improved. **Immediately contact MountainSeed if you determine the Highest and Best Use is different than the property type stated in the engagement letter.**

The appraiser should analyze and report on current market and sub-market conditions and trends that will affect projected income or the absorption period, to the extent they affect the value of the subject property.

Proposed Properties
A brief feasibility analysis is required on all proposed properties. This analysis should compare the concluded costs of the development to the final value conclusion and discuss if the project is feasible. The timing for development must also be addressed.

Most Likely Buyer/Typical User
The Appraisal Report must form an opinion as to the most likely buyer and/or the typical user. Specifically, the Appraisal Report must address whether a sale to an owner-occupant or investor is the most likely scenario for the subject property. In addition, the analysis throughout the report must be consistent with this conclusion. For instance, if the typical buyer is an owner-occupant (versus an investor) then the sales comparison approach must primarily rely on sales of owner-occupied properties, not sales to investors. For most leased properties, the typical purchaser is an investor and the sales used would be of other leased properties, not owner-occupied sales.

Approaches to Value

The goal of the valuation process is to develop a well-supported value conclusion that reflects all pertinent factors that influence the market value of the property being appraised. To achieve this, the appraiser must consider the three approaches to value and employ and weigh the approach, or approaches, that are considered the most credible. If any approach is not utilized, the appraiser must explain the reason for the exclusion of that approach. In all cases, the scope of work must be understood prior to engagement.

Cost Approach

The type of cost (replacement or reproduction) must be clearly stated. The developer's budget must be included for proposed properties. The source(s) used to estimate costs must be disclosed.

Typical cost sources are as follows:

- Cost comparables, if available, are preferred. If used, there must be a sufficient number and be presented in sufficient detail to allow the reader to understand their comparability to the subject property. Details such as square footage and the relevant date applicable to the costs should be provided for comparison purposes.
- A cost index (such as *Marshall Valuation Service*) may also be used to estimate costs. The section, building class, and building quality must be clearly referenced so the reader can follow the appraisal's logic and calculations.
- For relatively new properties, the original costs should be obtained and trended forward to make a comparison to current cost comparables or the indicated cost using an index.

Soft costs must be accounted for and supported. Market-based entrepreneurial profit must be considered and applied if appropriate. All forms of depreciation must be considered and analyzed and, if present, incorporated into the analysis. The analysis must be consistent with the information and conclusions presented in the Subject Property Description.

For proposed or recent construction, the Cost Approach must be prepared unless the engagement letter indicates this approach is unnecessary.

The land value must be supported:

- An adequate number of sales should be analyzed to support the value conclusion. A minimum of three comparable sales are required. If the sale of the subject property is included as a comparable, three additional sales are required.
- Properties that are under contract may be included if sufficient information from reliable sources is available.
- The comparables must be confirmed with a party (or parties) directly involved in the transaction and cited in the report. If sales cannot be confirmed, the Appraisal Report must disclose this and provide the data source.
- The Appraisal Report should state if the comparables were inspected.
- Comparables must be presented in sufficient detail to understand the parties involved and relevant characteristics of the properties.
- Listings may be included for additional support.
- Comparables must be relevant for the assignment and distinguish inferior or superior elements.
- An adjustment grid is required with all significant elements of comparison considered. Either quantitative or qualitative adjustments may be used.
- Support and rationale for the adjustments must be provided in a narrative discussion. Restating the quantitative or qualitative adjustments used in the grid is not sufficient.

It is not acceptable to provide an Appraisal Report with the Cost Approach only. It is extremely unusual for MountainSeed to accept an Appraisal Report which includes only a Cost Approach. Contact MountainSeed if you have any questions related to this restriction prior to completing the assignment.

Sales Comparison Approach

A major premise of the Sales Comparison Approach is that an opinion of the market value can be supported by studying the market's reaction to comparable and competitive properties. Comparative analysis focuses on similarities and differences at the property and transaction level that affect value. Specific elements of comparison include property rights, financial terms, conditions of sale, expenditures made immediately after purchase, market conditions, location, physical characteristics, economic characteristics, legal characteristics, and non-realty components of value.

Sales Comparison Approach Comparable Sale Requirements

- An adequate number of sales should be analyzed to support the value conclusion. A minimum of three comparable sales are required. If the sale of the subject property is included as a comparable, three additional sales are required.
- Properties that are under contract may be included if sufficient information from reliable sources is available.
- The comparables must be confirmed with a party (or parties) directly involved in the transaction and cited in the report. If sales cannot be confirmed, the Appraisal Report must disclose this and provide the data source.
- Comparables must be presented in sufficient detail to understand the parties involved and relevant characteristics of the properties.
- Listings may be included for additional support.

Sales Comparison Approach Analysis Requirements

The comparables must be analyzed using the appropriate unit of comparison, as indicated by the local market, for the specific property type (price/SF, price/unit, etc.).

- Comparables must be relevant for the assignment and distinguish inferior or superior elements.
- An adjustment grid is required with all significant elements of comparison considered. Either quantitative or qualitative adjustments may be used.
- Support and rationale for the adjustments must be provided in a narrative discussion. Restating the quantitative or qualitative adjustments used in the grid is not sufficient.
- Substantial adjustments must be supported in greater detail. If an adjustment is significantly larger, the sale may not be comparable to the subject. If substantial adjustments are applied to the sales, the report must address the research undertaken to find sales and indicate why more comparable sales were not available for analysis.

Income Capitalization Approach

The Income Capitalization Approach is typically the primary valuation tool for income-producing properties. As such, this approach is often the most scrutinized. The actual income and expenses (three-year history, if available) must be analyzed along with the owner's budget. If the appraisal's projections differ from the historical income and expenses, or from the owner's projections, the Appraisal Report should clearly explain the rationale. A current rent roll must be included in the body of the report or the Addendum. If a current rent roll or expense history is not provided or available, the appraiser must state the reason and details as to why it is not included in the Appraisal Report.

Rent Roll and Review of Leases

The rent roll must be analyzed and, when available, detailed lease abstracts should be cross-checked with the rent roll. If lease abstracts are not available, an acceptable alternative to reviewing all leases is to review all major leases and a sampling of minor leases. If significant discrepancies exist between the leases reviewed and abstracts, then all the leases must be reviewed. The Appraisal Report should state which lease review process was performed. Lease abstracts should contain the pertinent information necessary to properly model the cash flow such as lease area, commencement, expiration, term, initial rate, concessions, escalations within the term, expense stops, CAM charges, expenses paid by lessor, leasing commissions, and tenant improvements.

Income Capitalization Approach Market Rent Analysis

- An adequate number of rent comparables must be analyzed to support market rent conclusions; actual rents should be analyzed not just asking rents.
- The credit quality of the tenant must be discussed. The report should clearly communicate whether the tenant is investment grade or non-investment grade.
- Contract rent(s) must be analyzed to determine if existing leases are below, at, or above market.
- Rental concessions must be disclosed and considered when arriving at effective market rent. Examples of concessions include free rent, excessive tenant improvements, moving allowances, lease buyouts, cash allowances, or any other leasing incentives.
- For more complex properties, several types of comparables to estimate market rents must be provided (e.g., retail centers with anchors, in-line tenants, and pads).

- Lease terms should be specified (see preceding “Rent Roll and Review of Leases” section for specifics).
- Comparables must be converted to the same basis (net, gross, modified gross) when analyzed.
- Leases should be reviewed for co-tenancy clauses and other provisions with an analysis of the effects of these provisions on the on-going financial performance and marketability of the property.
- The comparables must be presented in sufficient detail to understand the parties involved and relevant characteristics of the properties.
- An analysis using multipliers (such as PGIM and/or EGIM) is acceptable if used by buyers and sellers in a given market. Certain intended users may also allow this type of analysis. If included, it is preferred that the multiplier analysis be included in the Income Capitalization Approach, not the Sales Comparison Approach.
- Report and analyze historical and current revenues, expenses, and vacancies for the subject property, if it is, and/or will, continue to be income-producing. A three-year history is expected, especially if the property has not transferred during this time.

Vacancy and Collection Loss

The estimate should consider the vacancies in the overall market, the sub-market, the rent comparables, as well as the historical vacancy rate of the subject property. Collection loss should be separately stated. The vacancy and collection loss estimate must be logical and consistent with the historical and future trends discussed in the marketabilty analysis. Market trends should be discussed as well as the subject’s vacancy history.

Absorption

For proposed properties, properties in lease-up, or non-stabilized properties, the rate of absorption must be supported with market information. The conclusion must be consistent with the historical and future trends discussed in the marketability analysis. The absorption forecast must clearly identify supply and demand interaction.

Expenses

The depth of expense analysis should be based on the expense structure of the subject property and/or the expense structure that is typical for the market. For properties where the owner is responsible for most, or many, of the subject expenses (or the market rent estimate concludes this), the analysis must include more explanation and support. This should include:

- Actual subject property expenses (three-year history, if available) must be analyzed using generally accepted expense categories along with owner’s budget.
- Expense comparables should be included in the Appraisal Report and reconciled with actual expenses using generally accepted expense categories. Comparables should consist of similar properties from the local market or from national publications such as Building Owners and Manager Association (BOMA), Institute or Real Estate Management (IREM), and/or Dollars and Cents.
- If the appraisal’s estimates differ from the historical expenses, the report must explain the reason for the differences.

For properties where the tenant is responsible for most, or many, of the subject property expenses (or market rent estimate concludes this), the analysis must provide explanation and support for the tenant paid expenses. If the expense terms for the property impact the market rent estimate, this factor must be accounted for in the estimates applied in the Appraisal Report.

Income Capitalization Approach - Direct Capitalization

- Deriving capitalization rates from comparable sales is the preferred technique.
- Local investor or broker surveys are also encouraged for non-investment grade real estate. If used, the source and experience should be cited, along with the date of the survey.
- Published national investor surveys may provide additional support for investment grade real estate.
- Band of investment and debt coverage formulas are generally not necessary.

Income Capitalization Approach - Discounted Cash Flow Analysis

Unless otherwise stated in the engagement for the assignment, a discount cash flow ("DCF") analysis is required for properties with five (5) or more leases (excludes multi-family).

The assumptions and variables must be clearly stated and supported with market evidence. This applies to the length of the holding period, income and expense growth rates, rollover assumptions, as well as re-leasing expenses. The inherent risk of these projections must be considered when selecting the discount/yield rate. All supporting schedules must be included (preferably in the Addendum).

Other Valuation Issues

Properties Commonly Subject to Deductions and Discounts

When appraising proposed construction or renovation and/or partially leased buildings, the Appraisal Report should include consideration for the absorption of unleased space and make appropriate deductions for items such as leasing commissions, rent loss, tenant improvements and entrepreneurial profit. Deductions including, but not limited to, holding costs, marketing costs, entrepreneurial profit, and other costs specific to a property should also be considered when appraising raw land (development approach), proposed construction and sale of five (5) or more attached or detached single-family units in the same development, and proposed construction and sale of a condominium building with five (5) or more units. Further, if the highest and best use of a property is for development to a different use, the cost of demolition and site preparation should be considered.

Developed Lots

The appraisal should analyze and report appropriate deductions and discounts for existing or proposed developments of five (5) or more lots in a single development. Appropriate deductions and discounts should reflect holding costs, marketing costs, and entrepreneurial profit during the sales absorption period for the sale of the developed lots. The estimated sales absorption period should reflect the projected time-frame for the actual development and sale of the lots, starting on the effective date of value and ending as of the expected date of the last lot sale. Absorption should be based on market demand for lots considering current and expected competition for similar lots in the market area.

Owner-Occupied Property

Since the premise of market value assumes a sale, it is important to solve the appraisal problem by determining whether the subject property is best suited for owner-occupancy or if it is to be purchased by an investor.

Owner-occupied property should be valued as if vacant and available for sale or lease. This premise is consistent with the definition of market value which assumes “the consummation of a sale as of a specified date.” In these cases, the appraiser should consider whether lease-up costs (entrepreneurial profit, rent loss, leasing commissions, operating expenses during periods of vacancy, TI’s, etc.) should be deducted. That is, if the most likely buyer of the subject property is an owner-occupant, deductions for these factors would be unnecessary. On the other hand, if the most likely purchaser is an investor, then deductions for these factors must be considered.

Valuations Involving Going Concerns

When developing an opinion of value involving a going concern, (i.e., established and operating business with an indefinite future life) the Appraisal Report must identify any personal property (FF&E) or intangible items that are not real property but are included in the Appraisal Report. Allocations to the real property, personal property, and intangible property must be appropriately supported and clearly identified within each reported value premise.

Property types that typically include a going concern are: hospitality properties, senior housing facilities, surgical centers and/or hospitals, golf courses, country clubs, athletic clubs, quick serve restaurants, full-service car wash facilities, convenience stores and/or gasoline stations, and educational facilities.
It should be clearly understood at the bidding stage, and clearly communicated in the engagement letter, if the assignment involves a going concern. MountainSeed should be contacted immediately if questions arise pertaining to assignments involving going concerns, or if it is discovered (after accepting an assignment without a going concern) that a going concern premise may be appropriate.

Non-Realty Components

The Appraisal Report must identify all non-realty components and provide an allocation of real property, personal property (such as furniture, fixtures, and equipment), and intangible assets. The methods and logic used to arrive at the allocation should be explained and any sources used should be disclosed. The allocation of real property, personal property, and intangible assets should be included in each value premise (such as the “As Is” Market Value as well as the Prospective Market Value upon Stabilization).

Replacement Cost for Insurance Purposes (Insurable Value)

The value of an asset or assets covered by an insurance policy is often referred to as Insurable Value. However, since the concluded amount is an indication of cost, a more accurate term is “Replacement Cost for Insurance Purposes.”

In general, Replacement Cost for Insurance Purposes provides the loss settlement, in the event of damage by an insured peril, that will cover the cost of replacing damaged property without deducting for depreciation. Maximum reimbursements are limited by insurance contracts and laws vary from state-to-state. Thus, what is specifically included in the Replacement Cost for Insurance Purposes estimate is a matter of underwriting and not a matter of valuation. Unless instructed otherwise by the financial institution, the following methodology is suggested when estimating Replacement Cost for Insurance Purposes.

Methodology

1) The first step in developing Replacement Cost for Insurance Purposes is to estimate the Replacement Cost New (RCN) of all vertical construction improvements using a third-party source (such as Marshall & Swift Valuation Services). The RCN should include all direct construction costs, typical general contractor overhead and profit, indirect costs (such as architecture and engineering fees), and building permits.

   Note that the RCN excludes land value, site improvements, entrepreneurial profit, and depreciation.
2) Insurable exclusions should then be deducted from the RCN. Exclusions include below ground improvements (foundations, below ground piping, etc.) that would not normally be destroyed by catastrophic events, such as a fire, wind, or flood.

Photographs, Maps, and Exhibits

If available/applicable or unless otherwise noted in the engagement, the following exhibits must be included in the report:

- Interior and exterior photographs of the subject property
- Exterior photographs of comparable sales and rental properties
- Regional and neighborhood maps
- Location maps of comparable land sales, improved sales, and rent comparables
- Assessor’s plat map with subject property noted
- Site plan or survey with subject property noted
- Reduced floor plans or sketch of building area (assessor or tax records are acceptable)
- Detailed construction budget, plans, and specifications for proposed properties or those undergoing renovation
- Flood zone map (including panel number) with subject property noted
- Legal Description (if in the unusual situation that it is not available, then an adequate description must be provided)
- Rent roll and/or operating statements in the Addendum
- Operating data and budget (proforma for proposed properties)
- Any other pertinent information needed to support or understand the report analysis
- Copies of current and valid state certifications or licenses for all signatories
- Appraiser’s qualification
- Signed engagement letter

Definitions

"As Is" Market Value – The estimate of the market value of real property in its current physical condition, use, and zoning as of the appraisal's effective date.[1]

Extraordinary Assumption – An assignment-specific assumption as of the effective date regarding uncertain information used in the analysis, which, if found to be false, could alter the appraiser's opinions or conclusions.[2]

Going Concern – An established and operating business having an indefinite future life.[3]

Going-Concern Value – An outdated label for the market value of all the tangible and intangible assets of an established and operating business with an indefinite life, as if sold in aggregate; more accurately termed the market value of the going concern or market value of the total assets of the business.[4]

Hypothetical Condition – A condition, directly related to a specific assignment, which is contrary to what is known by the appraiser to exist on the effective date of the assignment results, but is used for the purpose of the analysis.[5]

Insurable Value – The value of an asset or asset group that is covered by an insurance policy.[6] The amount is more accurately an indication of cost (see the definition for "Replacement Cost for Insurance Purposes" which is the term used in the Dictionary of Real Estate, 6th Edition).

Intangible Property – Nonphysical assets, including but not limited to franchises, trademarks, patents, copyrights, goodwill, equities, securities, and contracts as distinguished from physical assets such as facilities and equipment.[7]

Market Analysis – The study of supply and demand in a specific area for a specific type of property.[8]

Marketability Analysis – The study of how a specific property is expected to perform in a specific market. A marketability analysis expands on a market analysis by addressing a specific property.[9]

Market Value – The most probable price which a property should bring in a competitive and open market under all conditions requisite to a fair sale, buyer and seller each acting prudently and 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 form the seller to buyer under conditions whereby:

1. Buyer and seller are typically motivated;
2. Both parties are well informed or well advised, and acting in what they consider their own best interests;
3. A reasonable time is allowed for exposure in the open market;

---

[1] *Interagency Appraisal and Evaluation Guidelines,* December 2010, Appendix D
[2] *Uniform Standards of Professional Appraisal Practice*, 2018-2019 Edition, (Washington, D.C: The Appraisal Foundation), Definitions, 4
[3] *The Dictionary of Real Estate Appraisal*, 6th Edition, (Chicago: Appraisal Institute), s.v. "going concern."
[4] Ibid., s.v. "going-concern value."
[5] *USPAP 2018-2019 Edition*, Definitions, 4
[6] *The Appraisal of Real Estate*, 14th Edition, (Chicago: Appraisal Institute), 65
[7] *USPAP 2018-2019 Edition,* Definitions, page 5, s.v. "intangible property."
[8] *The Dictionary of Real Estate Appraisal*, 6th Edition, (Chicago: Appraisal Institute), s.v. "market analysis."
[9] Ibid., s.v. "marketability analysis."

4. Payment is made in terms of cash in the U.S. dollars or in terms of financial arrangements comparable thereto; and
5. The price represents the normal consideration for the property sold, unaffected by special or creative financing or sales concessions granted by anyone associated with the sale.[10]

Personal Property – Identifiable tangible objects that are considered by the general public as being "personal" – for example, furnishing, artwork, antiques, gems and jewelry, collectibles, machinery and equipment; all tangible property that is not classified as real estate.[11]

Prospective Market Value Upon Completion – The market value of property as of a future date when all construction is expected to be completed. It is based on market conditions forecasted to exist as of the completion date. This value premise assumes the project is complete and ready to lease to individual tenants.[12]

Prospective Market Value Upon Stabilization – The market value of a property as of a future date when all construction is expected to be complete and the property has been leased to its stabilized level of long-term occupancy. At this point, capital expenses for tenant improvements, leasing commissions, marketing costs, and other carrying costs are assumed to have been absorbed.[13]

Prospective Opinion of Value – A value opinion effective as of a specified future date. The term does not define a type of value. Instead, it identifies a value opinion as being effective at some specified future date. An opinion of value as of a prospective date is frequently sought in connection with projects that are proposed, under construction, or under conversion to a new use, or those that have not yet achieved sell-out or a stabilized level of long-term occupancy.[14]

Replacement Cost – The estimated cost to construct, at current prices as of a specific date, a substitute for a building or other improvements, using modern materials and current standards, design, and layout.[15]

Replacement Cost for Insurance Purposes – The estimated cost, at current prices as of the effective date of valuation, of a substitute for the building being valued, using modern materials and current standards, design, and layout for insurance coverage purposes guaranteeing that damaged property is replaced with new property (i.e., depreciation is not deducted).[16]

Reproduction Cost – The estimated cost to construct, at current prices as of the effective date of the appraisal, an exact duplicate or replica of the building being appraised, using the same materials, construction standards, design, layout, and quality of workmanship and embodying all the deficiencies, superadequacies, and obsolescence of the subject building.[17]

---

[10] Federal Register, Volume 55, 12 C.F.R Part 34.42(g), Page 34696, August 24, 1990, as amended at Federal Register 57 Page 12202, April 9, 1992; Federal Register, Volume 59, Page 29499, June 7, 1994.
[11] *USPAP 2018-2019 Edition*, Definitions, 5
[12] Compiled and summarized from several industry sources.
[13] Compiled and summarized from several industry sources.
[14] *The Dictionary of Real Estate Appraisal*, 6th Edition, (Chicago: Appraisal Institute), s.v. "prospective opinion of value."
[15] Ibid., s.v. "replacement cost."
[16] Ibid., s.v. "replacement cost for insurance purposes."
[17] Ibid., s.v. "reproduction cost."