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*Professionals Providing  
Real Estate Solutions*

550 W. Van Buren St.  
Suite 1000  
Chicago, IL 60607

T 312-335-4100  
F 312-335-4400  
[www.appraisalinstitute.org](http://www.appraisalinstitute.org)

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Working Group 1-CAC's  
c/o Paula Douglas Seidel  
The Appraisal Foundation  
1155 15th Street NW, Suite 1111  
Washington, D.C. 20005  
Email: [commentsCACs@appraisalfoundation.org](mailto:commentsCACs@appraisalfoundation.org)

**Re: Appraisal Institute Comments on “The Identification of Contributory Assets and the Calculation of Economic Rents” Exposure Draft**

Ladies and Gentlemen:

On behalf of the 25,000 members of the Appraisal Institute (AI), and particularly AI's Valuation for Financial Reporting (VFR) Project Team, thank you for the opportunity to provide comment on the February 25, 2009 Exposure Draft of “The Identification of Contributory Assets and the Calculation of Economic Rents”. The Intangible Asset Working Group is to be commended for the quality and quantity of the research and discussion provided. As the largest organization representing professional real estate appraisers, we are best qualified to comment on best practices for valuations of real property tangible (fixed) assets and the calculation of economic rents.

Within the last two years, the Appraisal Institute has spent a significant amount of time and resources in developing programs for real estate appraisers in the emerging area of Valuation for Financial Reporting. Our new 7-hour “Introduction to Valuation for Financial Reporting” seminar will be presented for the first time on May 14, 2009 in Chicago, and this seminar is scheduled to be presented in five locations around the country over the next two months. An “advanced” version of this VFR seminar is currently in development and will likely be released in early 2010. It is likely that the Institute will also offer a new certificate program for those that can demonstrate expertise on this important topic through successful completion of a rigorous training program. Lastly, the AI has a 76-year body of knowledge dealing with market-based economic rent support for real property fixed assets.

In a separate letter sent to you on April 9, 2009, James D. Vernor, Ph. D, MAI, Chair Emeritus of the Real Estate Department at Georgia State University wrote, "This document ("Best Practices" Exposure Document) takes a company approach and discusses the valuation of assets commonly found in an operating company with staff and the usual assets. What is lacking is a perspective for appraisers who must value operating properties, (perhaps owned within those companies or perhaps not) where the going concern is a package of assets including

traditionally recognized real property assets such as site and improvements, but also other intangible personal property”.

In layman's terms, Dr. Vernor is arguing that the Exposure Draft should recognize that the valuation of real property tangible assets should be performed by real property valuation experts who have an abundance of market data to support their value conclusions, including:

- 1) Real land values at the valuation date, which is emphasized in Section 3.3 Land, lines 251 through 255 where the exposure draft states, "Special consideration should be given to the appropriate market participant level of land values, serving as the basis for the calculation of the Contributory Asset Charge (CAC), as land values over time may move independently from entity of subject intangible property asset values";
- 2) Real Property Market Discount Rates for return "on" land and return "on" and "of" tangible real property assets; and
- 3) Real Property Market Economic Rents for real property fixed assets.

Importantly, when there is a business component in special real property fixed assets such as nursing homes, restaurants, golf courses, billboards, etc., real property valuation experts are also well suited to value those business value components as a residual, after all market-based returns and costs are applied to the real property fixed assets. On the other hand, specialists in business valuation who take the “company” approach consider the values of all intangible assets and personal property assets with real property components as a residual, which is variable according to the values assigned to intangible assets. Of course, we believe that the first approach results in more accurate and reliable opinions of value.

In the present economic and political climate, where the underlying value of real property fixed assets has become an international issue, there is a need to exercise extreme caution in allocating non-market based, unsupportable values to real property fixed assets, contributory asset charges, and economic rents. It is no longer acceptable to assign hypothetical values and CAC for real property fixed assets based on going rates and costs "of working capital" (Lines 251 and 252). The report cites a "paucity of data on asset specific returns" (Lines 483-484). However, there is an abundance of data available from real estate professionals to support those charges.

"Close counts only in horse-shoes!" A little bit off here, and a little bit off there, then a compounding of the partially flawed values for sale as investment packages, and pretty soon you have the present financial breakdown. The last thing TAF and its supporting professional valuation organizations want to be accused of is a continuation of the status quo.

In order to prevent such a problem, the Appraisal Institute recommends the following guidelines:

- a) Fixed Asset Land Market Values should be provided by competent real estate valuation experts with a minimum qualification of State Certified General Real Estate Appraiser at least once annually (FASB and IAVSC are advocating for quarterly), and the value opinions should be provided in Financial Reports as "Additional Notes" or "Footnotes" citing the market values as of a specific date.

In the Exposure Draft paragraph 3.4, "Fixed Assets (not including land)", it is pointed out that accounting depreciation is a non-cash expense that decreases taxable income and is added back to the after-tax income to arrive at free cash flow, and the net effect is to account for the tax benefit of accounting depreciation embedded in fixed assets.

- b) Support for opinions of Remaining Economic Life and Accrued Depreciation for real property fixed assets (not including land) should be shown in Financial Reports as "Additional Notes", or "Footnotes", citing the depreciated improvement asset values as of a specific date.
- c) Opinions of Economic Rent for real property fixed assets, which includes market returns on the asset and appropriate return of the asset, should be provided by competent real estate valuation specialists, with a minimum qualification of State Certified General Real Estate Appraiser at least once per year; and the opinion of market economic rent be shown in Financial Reports as "Additional Notes" or "Footnotes" citing the economic rent as of a specified date.

Current accounting regulations for financial reporting using Fair Value concepts allow for considerable latitude in interpreting real property market factors by those performing financial reports. Accuracy, credibility, and transparency is enhanced by utilizing best available sources of information to support the final report value of all assets. There is no "paucity" of available real estate valuation expertise within the pool of existing General Certified Appraisers.

We appreciate the opportunity to provide comments on the Exposure Draft. If you should have any questions, or if you need additional information, please do not hesitate to contact me at (954) 583-2116 or via e-mail at [vanceval@comcast.net](mailto:vanceval@comcast.net), or the Appraisal Institute's Scott DiBiasio at (202) 298-5593 or via e-mail at [sdibiasio@appraisalinstitute.org](mailto:sdibiasio@appraisalinstitute.org).

Respectfully,

Appraisal Institute Valuation for Financial Reporting Project Team