LITIGATION SUPPORT:
RUMINATIONS FROM A COMMERCIAL APPRAISER

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Here is a Pop Quiz. (See answers, below.) Answer True or False:

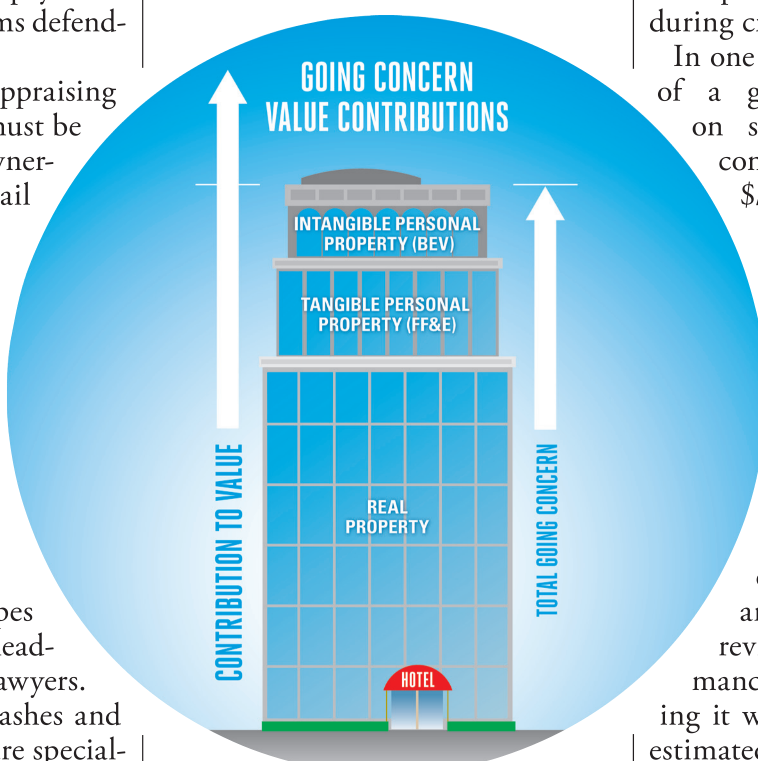
1. You have retained an appraiser in a Relief of Stay case. It is okay for that appraiser to be an advocate for his own value conclusion, even if he supports your desired outcome in the case.
2. In a partnership dispute, your appraiser came in with an opinion of going concern market value on a gas station at $3,000,000; the property generates net business income of $95,000 before mortgage payment. There should be no problems defending that opinion.
3. The methodology for appraising a gas station or car wash must be different than for an owner-user warehouse or retail building.

This article hopes to offer a few nuggets of information learned over several years of working closely with some excellent lawyers on a number of complex assignments.

Appraisal Concepts That Can Trip You Up

Certain property types have a tendency to cause headaches for appraisers and lawyers. Prime examples are car washes and gas stations because they are special-purpose properties that cannot be easily converted to a different use in the same way as general-purpose properties, like retail centers. Special-purpose properties often sell as "going concerns," with tangible real property (land, buildings, underground tanks, car wash tunnel fixtures), tangible personal property known as furniture, fixtures, and equipment (FF&E), and intangible personal property (business enterprise value (BEV) that may include goodwill, contracts in place, trained workforce, etc.).

The Appraisal Institute offers courses that deal with the intricacies of going concern properties, and they inevitably require a different valuation methodology than would apply to a simple warehouse or retail building. Whereas using the typical Sales Comparison Approach, with adjustments on the basis of dollars per square foot ($/SF), is very common for warehouse buildings, there are many reasons such an analysis will be highly problematic for many going concern appraisals (Quiz #3). Such properties are mainly bought for their ability to generate income as a business operation, so the valuation should look closely at the going concern operation; and this involves a careful income analysis. Once the total value is determined—the price a willing and experienced buyer would pay for the total assets of the business—then the total value is broken down into its component parts. Appraisers who are not familiar with this whole concept leave themselves vulnerable during cross-examination.



In one case, an opposing appraiser of a gas station relied mainly on sales of gas stations and compared them on the basis of $/SF of building area, just as if the subject were an industrial building, and did not consider the performance of the business operation. Hypothetically, let's say his conclusion, based on other gas stations in the region (about which he had no income information), supported a value of the real property in the amount of $3,000,000. After reviewing the actual performance of the facility, and assuming it was run reasonably well, we estimated net income from operations of around $95,000.

Imagine if the owner obtained a loan for, say, $2,100,000 (70% of $3,000,000), at an interest rate of 5.5%. The amount of net income needed to pay interest only on the loan would be $116,000. The mort-