



FAIR MARKET VALUE – ACCORDING TO WHOM?

APPRAISAL INSTITUTE SOUTHERN CALIFORNIA CHAPTER
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Better never settles

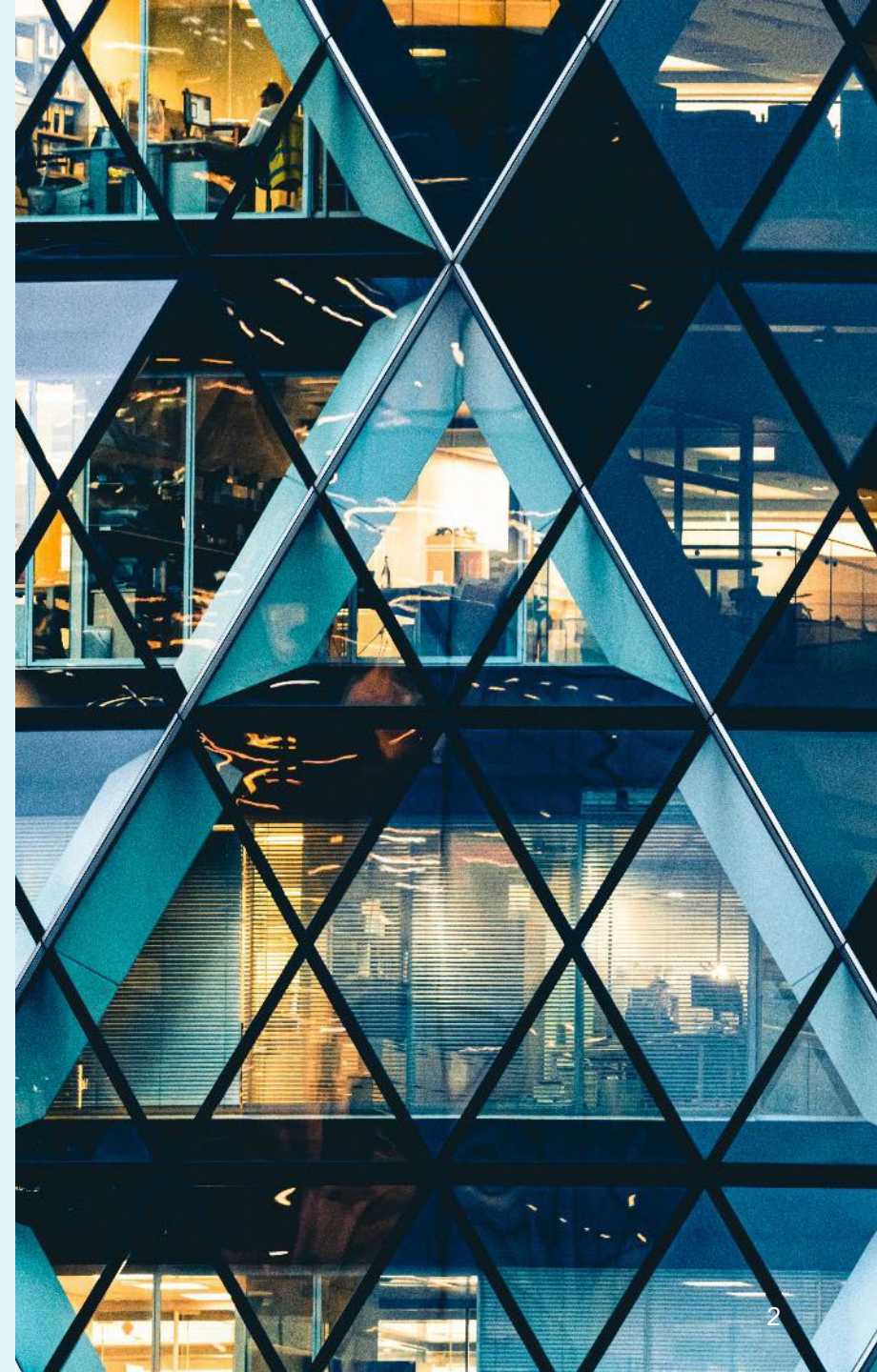
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01

INTRODUCTIONS

INTRODUCTIONS

Dispute Analysis & Litigation Group (DALs)



The DALs advisory service is a multi-disciplinary litigation support team experienced in providing professional experience in expert testimony, real property valuation, damages theory and calculations, arbitrations, business and shareholder disputes, bankruptcy, takings, machinery and equipment valuations, and partial interest and discount calculations.

Trust and Estates Group (T&E)



The Trust and Estates advisory service works with our nationwide group of state-licensed real estate appraisers and our business valuation professionals to assist attorneys and accountants with estate, gifting (i.e., discount studies on minority LLC/LP or TIC interests) and succession plans for their clients. Our professionals also have significant tax-related valuation experience in appraisal of closely held businesses and commercial real estate, including non-cash charitable donation valuations of commercial real estate. Stakeholders include minority/majority shareholders, federal and state regulatory agencies, REITs, real property investors and partnerships. Cushman & Wakefield professionals have defended stakeholders' opinions against challenges by tax authorities and, when needed, have provided litigation support services in such situations.



02

HOW MANY DEFINITIONS?

WHICH MARKET VALUE DO YOU USE? – TEST 1



Who is the Intended User and What is the Intended Use?

USPAP states Market Value is:

MARKET VALUE: a type of value, stated as an opinion, that presumes the transfer of a property (i.e., a right of ownership or a bundle of such rights), as of a certain date, under specific conditions set forth in the value definition that is identified by the appraiser as applicable in an appraisal. ⁹	131
	132
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<u>Comment:</u> Appraisers are cautioned to identify the exact definition of market value, and its authority, applicable in each appraisal completed for the purpose of market value.	134
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Advisory Opinion 22 cites:

Importance of Identifying the Specific Definition of Market Value —The definition of the value to be developed in an appraisal establishes specific conditions. These conditions impose parameters on the appraisal assignment that are necessary to ensure that the results of the assignment are meaningful in the context of that definition of value.	81
	82
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WHICH MARKET VALUE DO YOU USE? – TEST 2



Are you using the accurate definition and is the source cited the most recent/up to date?

Advisory Opinion 22 cites:

Importance of Identifying the Source of a Market Value Definition—Definitions of market value from different sources 91
contain different conditions. Those differences can directly affect the scope of work that is necessary to develop 92
credible assignment results. Each definition is unique, with authority only in a specific jurisdiction or to a specific client 93
group. **Therefore, identification of the source for the definition of value to be applied in an assignment is essential.** 94
The source must be consistent with the jurisdiction having authority over the transaction in which the appraisal 95
is to be used. For example, using a definition of market value other than the definition specified in regulations 96
published pursuant to Title XI of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA) 97
may invalidate that appraisal for use in a federally related transaction. Likewise, if an appraisal is prepared for use 98
in litigation, using a definition of value other than the definition specified by the court having jurisdiction over the 99
matter being litigated may disqualify that appraisal for use in that court. 100

WHICH MARKET VALUE DO YOU USE?



Definitions in the Dictionary of Real Estate Appraisal – 7th Edition

Market Value:

. Market value is described, not defined, in the Uniform Standards of Professional Appraisal Practice (USPAP) as follows: A type of value, stated as an opinion, that presumes the transfer of a property (i.e., a right of ownership or a bundle of such rights), as of a certain date, under specific conditions set forth in the value definition that is identified by the appraiser as applicable in an appraisal.

Fair Market Value:

1. In nontechnical usage, a term that is generally synonymous with the contemporary usage of *market value*.
2. As used in condemnation, litigation, income tax, and property tax situations, a term that is similar in concept to market value but may be defined explicitly by the relevant agency or interpreted differently by court precedent. In some situations, the interpretation of fair market value is more directly comparable to the concept of fair value than to market value in exchange. *See also market value.*

WHICH MARKET VALUE DO YOU USE?



International Valuation Standards Council Definition (IVSC)

Market Value is defined as:

The estimated amount for which an asset or liability *should* exchange on the *valuation date* between a willing buyer and a willing seller in an arm's length transaction, after proper marketing and where the parties had each acted knowledgeably, prudently, and without compulsion.

IVSC Glossary 10.18



MARKET VALUE – USED IN APPRAISALS FOR LENDERS

The following definition of market value is used by agencies that regulate federally insured financial institutions in the United States:

The most probable price that a property should bring in a competitive and open market under all conditions requisite to a fair sale, the buyer and seller each acting prudently and knowledgeably, and assuming the price is not affected by undue stimulus.

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

- i) Buyer and seller are typically motivated;*
- ii) Both parties are well informed or well advised, and acting in what they consider their own best interests;*
- iii) A reasonable time is allowed for exposure in the open market;*
- iv) Payment is made in terms of cash in U.S. dollars or in terms of financial arrangements comparable thereto; and*
- v) 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.¹*



1 -"Interagency Appraisal and Evaluation Guidelines." Federal Register 75:237 (December 10, 2010) p. 77472.

REAL ESTATE VALUATION BEFORE COURTS & IRS

Fair Market Value in 2024

When appraisals are requested for estate planning/tax, Fair Market Value (FMV) is the definition of value required by the Department of the Treasury, Internal Revenue Service.

FMV varies (slightly) from definition of Market Value as defined by USPAP (Uniform Standards of Professional Appraisal Practice), but connotation is important.

Fair Market Value (FMV) is the price that property would sell for on the open market.

Price is agreed upon between willing **buyers** and willing **sellers**, with neither being required to act, and both having reasonable knowledge of the relevant facts.

Source: Publication 561 Determining the Value of Donated Property, Department of the Treasury, Internal Revenue Service Rev. April 2007 and Revenue Ruling 59-60.



WHAT THIS MEANS

The FMV definition requires a transaction on a specific date. A transaction **MUST** occur. Thus, with FMV, economic perceptions and fluctuations in interest rates have a direct impact on real estate values and discount studies.

WHEN FMV MATTERS...QUALIFIED APPRAISALS

According to **Section 1219 of the Pension Protection Act of 2006 (H.R. 4)**, a “Qualified Appraisal” by a “Qualified Appraiser” must be performed for a gift of non-cash property worth more than \$5,000. Per US Treasury Regulations, a “Qualified Appraisal” is defined as an appraisal document that;

- Is made **no earlier than 60 days prior** to the date of gift / **no later** than the due date of the donor’s tax return;
- Is prepared, signed, and dated by a “Qualified Appraiser”;
- Includes all required information;
- Must conform to generally accepted appraisal standards (USPAP); and
- Does not involve a prohibited appraisal fee.

Treasury Regulations continue to define a **“Qualified Appraiser”** as an individual that;

- Has earned an appraisal designation from a recognized professional appraiser organization or has otherwise met minimum educational and experience requirements as prescribed by US Treasury Regulations;
- Regularly performs appraisals for which the individual receives compensation;
- Can demonstrate verifiable education and experience in valuing the type of property subject to the appraisal;
- Has not been prohibited in practicing before the IRS anytime within a 3-year period prior to the appraisal date of value; and
- Meets other requirements as prescribed by US Treasury Regulations; including:
 1. Affirmation that the Qualified Appraisal will be used in connection with a Tax Return claim for refund;
 2. Affirmation that the Qualified Appraiser is responsible for gross valuation misstatement on the return and subject to penalty under § 6695A of the IRC.

REAL ESTATE VALUATION FOR ESTATE PLANNING

Impacts of the 2018 Tax Cuts and Jobs Act

The Estate Tax Exemption

What to Know:

Expires December 31, 2025 if Congress does not act to amend it.

- The federal estate and gift tax exemption amount is currently \$13.61M per individual and \$27.22M per married couple.
- 2024 Minimum Estate Tax Rate of 40% (\$0.40 on \$1.00).
- Without Congressional Action, the Exemption will repeal to \$7M per individual and \$14M per married couple on 1/1/26

Not taking full advantage of the gift tax exemption before it drops in two years could result in a far smaller estate for your heirs.

	Gift full 2024 exemption	Gift projected 2026 exemption
Current net worth	\$50 million	\$50 million
Gift in 2024	\$27.2 million	\$14 million
Taxable estate at death	\$22.8 million	\$36 million
Estate tax at 40%	\$9.1 million	\$14.4 million
Net to heirs	\$40.9 million	\$35.6 million

Note: Assumes both members of a couple make gifts; death of both spouses in 2026; and federal estate taxes only. The federal estate tax is calculated using a series of brackets with a maximum rate of 40%. For simplicity, these numbers were calculated using a 40% flat rate.

MARKET VALUE – FEDERAL LAND ACQUISITIONS

Federal Definition (except for leasehold acquisitions)

“Market Value is the amount in cash, or on terms reasonably equivalent to cash, for which in all probability the property would have sold on the effective date of value, after a reasonable exposure time on the open competitive market, from a willing and reasonably knowledgeable seller to a willing and reasonably knowledgeable buyer, with neither compelled to buy or sell, giving due consideration to all available economic uses of the property.”

Source: Section 4.2.1, Uniform Appraisal Standards for Federal Land Transactions



MARKET VALUE FOR EMINENT DOMAIN/CONDEMNATION

Federal Rules Definition

In addition to the definition for Federal Land Acquisitions, no consideration may be given to any physical changes (i.e. impact of the planned government construction) **as well as changes in market value that occur after the date of value.**

The date of value is generally determined by law (or a legal instruction) based on the nature of the acquisition.



MARKET VALUE FOR EMINENT DOMAIN/CONDEMNATION

CA State Rules Definition of Fair Market Value for Purposes of Determining Just Compensation

“The fair market value of the property taken is 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.”

Source: California Code of Civil Procedure (CCP) Article 4 Section 1263.320(a)



MARKET VALUE – CONTRACTUAL DEFINITION

Market value can be any of the prior definitions as cited with additional qualifiers that are agreed upon between two parties in a signed agreement/contract.





03

CASE STUDIES

CASE STUDY #1

Determination of the Fair Market Value for a Purchase Option by the Tenant

Background: The subject was ground leased for a 40 year term. The Lessee owned the existing improvements, which were a specialized (non-core) use and had a Purchase Option to buy the property from the Lessor

Per Section 44.3 of the current ground lease, “The purchase price for the Leased Premises shall be equal to the ‘fair market value’ (as defined below) of the Leased Premises as of the date of the Option Notice.”

Section 44.6 of the current ground lease defines the Fair Market Value as follows:

“For the purposes of this Article 44, the term ‘fair market value’ shall be determined based on the following assumptions:

- (a) So long as there is at least one (1) unexpired Extension Term, the arbitrators shall assume that the Tenant will not terminate this Lease under Section 2.2 and that the Term of the Lease shall extend for a period of ten (10) years from the date of the Option Notice.
- (b) The fair market value shall be the fair market value of the Landlord’s interest in this Lease, including its reversionary interest in the Leased Premises (**but excluding any value attributable to the Improvements**).

CASE STUDY #1 (CONT.)

Determination of the Fair Market Value for a Purchase Option by the Tenant

(c) Notwithstanding any other provision of Article 44 to the contrary, **in no event shall the fair market value exceed the fair market value which the Arbitrators determine would be paid by a willing third party purchaser for Landlord's interest in the Lease (including its reversionary interest in the Leased Premises and the Improvements)** without regard to the assumptions set forth in Subsection 44.6(a) and (b) above and with full regard to Tenant's termination rights under Section 2.2, above.”

It should be noted that Section 2.2 of the ground lease provides the Tenant the right to terminate the lease one year in advance. However, the requirements of Section 44.6(a) assume that this Right to Terminate is not exercised by the Tenant.

CASE STUDY #2

Determination of the Offer Amount for an Option to Purchase agreement in a Master-Lease

Background: The subject property consisted of 4 individual properties located in 4 different states that were encumbered by a 20-year Master-Lease that commenced in 2002 with two 10-year renewals.

Included in the master-lease agreement was an Option to Purchase the entire portfolio (no less than all of the 4 properties) for a purchase price equal to an "Offer Amount". The Offer Amount as defined in the master-lease was to be:

"Offer Amount" shall mean the greater of (a) the sum of the Fair Market Value of the Leased Premises or Sale Premises as of the Relevant Date and the applicable Prepayment Premium which Landlord will be required to pay in prepaying any Loan with proceeds of any such Offer Amount or (b) the sum of the Acquisition Cost and the applicable Prepayment Premium which Landlord will be required to pay in prepaying any Loan with proceeds of any such Offer Amount.

CASE STUDY #2 (CONT.)

Determination of the Offer Amount for an Option to Purchase agreement in a Master-Lease

The Fair Market Value was defined in Section 2 of the master-lease as:

"Fair Market Value" of either the Leased Premises or any Related Premises, as the case may be, and the context may require, shall mean the higher of (a) the fair market value of the Leased Premises or any Related Premises, as the case may be, as of the Relevant Date as if unaffected and unencumbered by this Lease or (b) the fair market value of the Leased Premises or Related Premises, as the case may be, as of the Relevant Date as affected and encumbered by this Lease and assuming that the Term has been extended for all extension periods provided for herein.

Finally, the definition of Acquisition Cost is provided in the lease as follows:

"Acquisition Cost" of each of the Related Premises shall mean the amount set forth opposite such premises on Exhibit "E" hereto.

CASE STUDY #2 (CONT.)

Determination of the Offer Amount for an Option to Purchase agreement in a Master-Lease

Methodologies used:

- Market Value As-If Unencumbered (No master-lease in place)
- Market Value with Master-Lease and defined terms in effect
- Consideration of Acquisition Costs plus Prepayment Premium for any outstanding loans (figures agreed upon by Clients) – there were no prepayment premiums remaining as of the date of value and so the requirements under Paragraph 2, Section (b) of the master-lease was to be just the Acquisition Cost.

The above methodologies were applied to each of the 4 individual properties with the highest resulting aggregate value under the 3 methodologies resulting the Fair Market Value as defined by the Contractual Definition.



04

Q&A



MELISSA BACH, MAI, CRE

Executive Managing Director
National Practice Lead - Dispute Analysis & Litigation Support
melissa.bach@cushwake.com
415.659.3698

ERIC B. GARFIELD, MAI, CCIM, CRE

Executive Managing Director
National Practice Lead, - Trust & Estates Valuation Services
eric.garfield@cushwake.com

ABOUT CUSHMAN & WAKEFIELD

Cushman & Wakefield (NYSE: CWK) is a leading global commercial real estate services firm for property owners and occupiers with approximately 52,000 employees in nearly 400 offices and 60 countries. In 2023, the firm reported revenue of \$9.5 billion across its core services of property, facilities and project management, leasing, capital markets, and valuation and other services. It also receives numerous industry and business accolades for its award-winning culture and commitment to Diversity, Equity and Inclusion (DEI), sustainability and more. For additional information, visit www.cushmanwakefield.com.

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