

# The Official Guide to Demonstration Appraisal Reporting: General

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# General Information

## **A. Demonstration Appraisal Report Defined**

A demonstration appraisal report is the most complete presentation of a property appraisal that an individual can produce given the limits of the individual's abilities and the market evidence available at the time. The term *most complete* simply means the most concise but thorough presentation of each section of the report demonstrating the Associate Member's level of knowledge and expertise.

A demonstration appraisal report and a well-prepared business report differ in one respect. The business report has a different function than the demonstration appraisal report and is written to satisfy its intended use. Therefore, some sections of a business report may be given less emphasis than other sections, and in some cases sections may be omitted or inapplicable. The demonstration appraisal report, on the other hand, is intended to test the ability of the Associate Member to assemble a complete appraisal report and to handle each section thoroughly and concisely. Therefore, each important element of the report is given weight in the grading process. When the demonstration appraisal report is completed, each section is linked with the other sections to provide a continuous narrative leading to a final value conclusion.

The purpose of preparing a demonstration appraisal report is to test the Associate Member's ability to gather the necessary data, analyze the data properly, support conclusions, and write an appraisal report setting forth the analysis and conclusions, which will lead the reader to concur with the opinion of value.

This guide is not intended to be a textbook. It is anticipated that the Associate Member has received a basic education in appraisal theory and application and has the requisite experience to prepare the report. Reference should be made to the latest edition of *The Appraisal of Real Estate* and to *The Dictionary of Real Estate Appraisal* for current definitions, techniques, and theoretical applications, and to the *Standards of Professional Appraisal Practice* and the *Supplemental Standards of Professional Appraisal Practice* of the Appraisal Institute for the most up to date appraisal requirements. Also review the Demonstration Appraisal Reports section of the Appraisal Institute's Regulation No. 1.

## **B. Selection of a Subject Property**

The most important step in preparing a demonstration appraisal report is the selection of a subject property. If a poor selection is made, it may not be possible to write a demonstration appraisal report that could receive a passing grade. Many properties do not lend themselves to demonstrating all that is required. For many properties in the market, sufficient comparable market data are not available.

If the right property is chosen, there will be ample data to prepare all segments of the report, and the work of the Associate Member will be significantly easier. The Associate Member can then concentrate on preparing the best demonstration appraisal report that the market data will permit.

It is suggested that the Associate Member select a property use (office, multifamily residential, warehouse, retail strip center, etc.) within a community where ample market data are available. Once the use is selected, all market data available to support that use should be accumulated and given a cursory analysis. From the data available, the Associate Member should select a subject property that best fits the data.

If the community in which the Associate Member works has limited market activity, the Associate Member may choose to investigate a nearby community that has a more active market. On the other hand, a well-supported opinion of value done on a property in a small market will be rated by the grader in that context.

The following elements must be present to qualify the demonstration appraisal report for grading:

- a. A fundamental market analysis must be developed.
- b. The property selected must suffer from incurable long-lived physical deterioration. If more forms of depreciation or obsolescence are present, they must be properly treated. The breakdown method of depreciation must be applied.
- c. The appraisal must analyze the effect of expenses on rents and total occupancy cost in the development of a net income stream, even if only net leases are involved.
- d. The report must allow the Associate Member to demonstrate appraisal techniques applicable to the three approaches to value.
- e. The effective date of value can be no more than five calendar years prior to the year of submission.
- f. "Market value" must be the type of value estimated.
- g. The report should pertain to an "as-is" valuation; extraordinary assumptions and hypothetical conditions may be inappropriate.

### **C. The Physical Report**

The demonstration appraisal report should be the best work of the Associate Member's career to this point. Therefore, the photographs, exhibits, grammar, spelling, overall presentation, and binding of the physical report should be as professional as the Associate Member can possibly produce. It is recommended that the demonstration appraisal report be prepared on 8 1/2-by-11 inch paper and bound securely to ensure that the report remains intact through shipping and grading. Bind so that the report lies flat for grading. Do not use a three-ring binder or Velobind.

The analytical sections of the report, which include everything after the introduction (i.e., property description and market analysis through the reconciliation and final value opinion), should provide adequate justification, support, and documentation.

**Justification** demands evidence that a statement is well founded. Justification is best provided by reference to market-extracted data. It is an explanation of how the supporting data and documentation have been interpreted to reach the conclusion.

**Support** means to verify or substantiate conclusions with as much factual data as possible. For example, a conclusion in the area analysis that there is an oversupply of office space in the community should be supported with market information and an explanation of how it was extracted and confirmed in the market.

**Documentation** is the process of providing evidence of a statement or fact. Reliable or authoritative sources should always be used and referenced. Examples of some areas of the report requiring extensive documentation are: comparable sales, income, expenses, vacancy, rate selection, cost new estimates, and depreciation.

## **D. Market Extraction**

One of the major objectives of the demonstration appraisal report is to demonstrate the process of extracting data from the market to support, document, and justify the conclusions presented throughout the report. Some examples of extracted support data follow.

In the sales comparison approach, all adjustments to comparable sales should be market supported. The method for extracting market support can vary significantly depending on the kind of data available. Examples of market extraction may include extracting depreciation from comparable sales, which could then be applied as an age/condition adjustment in the sales comparison approach. A location adjustment could be supported by demonstrating the differences in value from one property location to another. Other means of extracting market support could include paired sales analysis, linear regression, and examining differences in income caused by varying conditions.

In the cost approach, the cost new estimate could include estimates from the published cost services (segregated section, not calculator section) and a detailed cost breakdown prepared by a qualified building contractor. These costs can be further supported using cost comparables found in the market.

Depreciation must be supported by the breakdown method. An important part of the breakdown method is the estimate of economic life, which can be extracted from market sales. External and functional obsolescence can be demonstrated through comparisons with sales and rentals of properties with both similar and dissimilar functions and external characteristics.

In the income capitalization approach, market rent estimates can be supported with an appropriate analysis of comparable rentals. Vacancy loss estimates can be supported by conducting vacancy ratio studies of comparable properties in the area. Reference can be made to data included in the market analysis section for support.

Expense estimates can be supported with operating expenses from comparable properties. Overall capitalization rates and yield capitalization rates and can be supported by market extraction of comparable sales data.

## **E. Exhibits**

Exhibits should contribute to the clear understanding of your written description and discussion. Place illustrations within the report where they will be most helpful to the reader. Exhibits should include, but not be limited to, the following:

**Photographs:** Color photographs of the subject property, nearby properties, comparable improved sales, land sales, and rentals should be included along with any other scene that might be considered important to understanding the value conclusion. Photographs should be identified and dated, and the camera's orientation should be indicated. Photographs must be in color. Color digital images are acceptable if at least 3 ½ inches by 5 inches in size and of high resolution on quality paper.

**Maps:** Maps indicating the market area, neighborhood boundaries, the location of the subject property, the location of comparable sale properties (including land sales), and the location of rental properties should be included in the report. Be sure to include a directional arrow on each map. Other maps that may be helpful could include an area map locating the subject and subject neighborhood in relation to the central business district, work centers, competing neighborhoods, and other important locational considerations, which relate to the property being appraised. Exhibits appropriate to the fundamental market analysis should be included.

**Site Plan:** A site plan that shows lot and building dimensions, easements, the placement of the improvements on the site, and abutting rights of way is expected. The plan could also indicate the location of driveways, parking, traffic flow through the site, and any other characteristics, which would help the reader, better visualize the site. Examples of additional items to consider would be existing easements, topographical lines, and the location and identification of any excess land.

**Floor Plan:** Include a plan of each level of the principal building, showing all room partitions, doors, windows, and relevant dimensions. The floor plan should be to scale.

## **F. Agricultural Properties**

This guide does not include specific requirements for the submission of a demonstration appraisal report on an agricultural property. The Associate Member should contact the Associate Member Service Center at 312-335-4111 for additional guidelines if the desired subject property is agricultural.

## **G. Properties That Cannot Be the Subject of a Demonstration Appraisal Report**

- a. A property that is the subject of a demonstration appraisal report used in a real estate course, clinic, seminar, or other organized appraisal learning experience.
- b. A property that was involved in litigation at the time the report was submitted or at the date of valuation or likely to be in litigation during the grading process.
- c. A property that is one- to four-unit residential units.

## **H. Definition of “Without Assistance”**

The Demonstration Appraisal Grading Panel developed the following definition of “without assistance” as used in Regulation No. 1:

Assistance should be limited to verbal advice, suggestions, theoretical explanation, references to textbooks and techniques, available literature, etc., relating to existing appraisal practice. Assistance should not include review or commentary on a demonstration appraisal report.

## **PART ONE**

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# Introduction

The outline shown below is suggested for the demonstration appraisal report. It is highly recommended that this outline be followed closely. It is recommended, but not necessary, that the Associate Member follow the exact order of the outline. Each individual segment of each section of the outline should be addressed in the demonstration appraisal report.

## **A. Title Page**

The title page should include:

- Identification as an appraisal report
- Property type
- Property address
- Effective date of report
- Effective date of value
- Name and address of the appraiser
- Name and address of client and intended user (i.e., the Appraisal Institute)

## **B. Letter of Transmittal**

The letter of transmittal formally presents the appraisal report. It may be addressed to the Appraisal Institute or to a real client. A suitable letter of transmittal may include:

- Date of letter and salutation
- Street address or location of the property and a brief description, if necessary
- Property type
- Statement identifying the interest in the property being appraised
- Reference to client's request for appraisal
- Statement of appraisal's purpose, intended use/user
- Statement that inspection of the property and necessary investigation and analysis were performed by the appraiser
- Statement as to the type of appraisal and appraisal report format
- Reference that the letter is accompanied by a complete appraisal report
- Effective date of value opinion (The date must be within five calendar years of the year the demonstration report is submitted.)
- Reference to assumptions and limiting conditions
- Value opinion (written and numerical)
- Appraiser's signature, with certificate/license number if appropriate

## **C. Table of Contents**

The table of contents lists the major components of the report in sequence with page references. The numbering of pages normally begins after the table of contents. Use headings and subheadings to identify the major divisions of the report.

## **D. Photographs**

A good frontal photograph of the subject property at the beginning of the report is recommended to give the reader a mental picture of the property. All photographs must be in color.

## **E. Summary of Important Facts and Conclusions**

An outline of the report's major points and important conclusions is recommended. Such a statement provides the reader with a convenient summary and gives the appraiser an opportunity to stress points that were considered in reaching the final opinion. Examples of items to include are site size, building size and age, zoning designation, gross rentable area, net rentable area, estimate of land value, indicated value by the cost approach, indicated value by the sales comparison approach, indicated value by the income capitalization approach, and final opinion of market value.

## **F. Scope of Work**

Describe the extent of the process of collecting, confirming, and reporting data. This is required by the current *Standards of Professional Appraisal Practice*. The extent of the appraisal investigation could include details of the property inspection. In some cases, such as the appraisal of large apartment complexes, it may not be possible to inspect each individual unit. This section of the report could describe the extent of the inspection.

The appraiser should also describe the extent of the investigation such as the parameters for comparable sales and rental searches and the extent of the confirmation process.

## **G. Purpose of the Appraisal**

The purpose of the appraisal must be to arrive at a supportable opinion of market value of the property in its "as-is" condition.

## **H. Intended Use of Appraisal and Intended User**

The intended use of the appraisal should be to satisfy the requirements of the Appraisal Institute pertaining to demonstration appraisal reports. Intended users may include representatives of the Appraisal Institute.

## **I. Property Rights Appraised**

The property rights appraised should be clearly identified and defined. These rights should then be consistently valued throughout the remainder of the report. Most reports will value the fee simple

estate; however, in some cases the leased fee estate may be chosen. It is important to remember that the property rights appraised should be handled consistently throughout the report.

## **J. Date of Value Opinion**

The effective date of value is integral to the report. The effective date of value in a demonstration appraisal report must no more than five calendar years prior to the year that the report is submitted for credit.

## **K. Definition of Value**

The only suitable value for a demonstration appraisal report is market value. Therefore, the definition provided in the most recent edition of *The Appraisal of Real Estate* is recommended. Also, note that the *USPAP* requirement regarding exposure time must be considered. Exposure time support should appear in the appropriate section within the appraisal report pertaining to discussion and analysis of market conditions. It is also recommended that this discussion be referenced with the definition of value.

## **L. Identification of the Property**

The property should be identified by a complete address, legal description, owner, and type of ownership. Other identifying remarks may also be included.

## **M. History of the Property**

A detailed history of the property should be provided and analyzed. 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 the dates of transfers of ownership for at least the past three years. Prior or current listings, offers, and/or contracts should also be included.

## PART TWO

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# Descriptions, Analysis, and Value Conclusions

## A. Property Description and Productivity Analysis

### Site Data and Analysis

The site must be accurately described. A site plan should be inserted at this point. The site plan should include a site plan or survey copy with dimensions. Identify road frontages, curb cuts and interior traffic flow, the location of the building and possibly landscaping, parking, or any other characteristics that help describe the site and its present use. Other items to include could be information on easements, neighboring encroachments, or any other factor that helps graphically depict the site. This section should include the following as a minimum:

- a. Site dimensions, area, and shape
- b. Topography
- c. Drainage, soil, and subsoil conditions
- d. Access (Describe streets and their adequacy.)
- e. Type, size, and adequacy of utilities
- f. Man-made improvements such as walks, curbs, and drives
- g. Proximity to any nuisances, hazards, or detrimental influences
- h. Analysis of units of comparison
- i. Flood zone and the effect, if any, on site usability
- j. Easements and encroachments and analysis as to their effect on the site
- k. A final conclusion as to how the site conditions previously described ultimately affect the use of the site

### Improvement Analysis

The improvement analysis should contain a detailed description of all improvements on the site followed by an analysis of these improvements as to their age, condition, physical life, etc.

**Description Portion.** The description portion should include the current use, architectural style, type, building dimensions, area, interior layout, structural and construction details, mechanical equipment description, and any ancillary improvements such as building and site improvements. The improvement can be described in an abbreviated outline form, in a narrative form, or in combination of both. It is suggested that a floor plan be provided here showing the building layout with dimensions.

**Analysis Portion.** The analysis portion should include a discussion of the age and condition of the improvements. This analysis should include an age and condition evaluation of the short- and long-lived building components. Since the breakdown method of depreciation must be used in the cost approach, market support for the effective age, and economic life of the building should be included here. Functional utility or inutility should be discussed and analyzed. This analysis can be continued

later in the Highest and Best Use section where more specific conclusions must be developed regarding the property as improved.

## **B. Zoning and Land Use Plans**

- a. Zoning designation and its meaning
- b. Allowable uses under the zoning (including setbacks, parking, height, building coverage, etc.)
- c. A conclusion as to the conformity or nonconformity of the site or property as improved to public and/or private restrictions

## **C. Taxes and Assessment Analysis**

This section should present taxes and assessment information that might affect the valuation of the subject property. The subject's current taxes and assessed value should be presented. Any special assessments should also be discussed at this point. Taxing trends in the area of the subject property should be discussed and analyzed. A tax and assessment history of the subject property should be provided in support of that analysis. In addition, a comparison of the subject taxes and assessments with other, competing properties' taxes and assessments should be provided to assess and support future taxes for the subject.

This section should end with a conclusion regarding the subject tax load.

## **D. Fundamental Market Analysis**

Market analysis is defined as a study of market conditions for a specific type of property. A complete market analysis is used to screen alternative uses as well as provide the data to test financial feasibility and the use or uses that are maximally productive. A thorough fundamental (Level C/D) market analysis must be performed to support an acceptable highest and best use conclusion.

Market analysis is typically performed on four separate levels (Levels A through D). For most appraisal problems, Levels A and B are adequate. However, for the demonstration appraisal report, a fundamental market analysis performed at Level C, and possibly Level D, is required. Levels C and D are characterized by the depth of analysis and the requirement for primary research to be done by the appraiser. Reliance on secondary data is not sufficient for this section of the demonstration appraisal report.

Data collection and analyses traditionally used in the regional and city and neighborhood sections are to be provided within the Fundamental Market Analysis section. The six-step process for market analysis is developed in the course materials for General Appraiser Market Analysis and Highest & Best Use.

For additional information, refer to the course, *General Appraiser Market Analysis and Highest & Best Use*; the seminar, *Case Studies in Commercial Highest and Best Use*; and the book *Market Analysis for*

*Valuation Appraisals* by Stephen F. Fanning, MAI, Terry Grissom, MAI, Ph.D. and Thomas Pearson, MAI, Ph.D.

This section of the appraisal process should develop the foundation for the conclusions of highest and best use as though vacant and as improved, to be summarized in the Highest and Best Use section.

An overview of the Six-Step Fundamental Market Analysis process follows:

**Step 1. Define the property (Property Productivity Analysis)**

- a. Physical attributes
- b. Legal and regulatory attributes
- c. Location Attributes
  - (1) Identify economic attributes-the association between land uses and their linkages.
  - (2) Identify movement of demand in relation to the direction of urban growth.
    - Analyze urban growth structure
      - Pattern
      - Direction
      - Rate
    - Analyze factors influencing urban growth structure
      - Natural
      - Man-made (including adequacy and cost of utilities)
      - Political
  - (3) Identify competition and comparison of location advantages and disadvantages between competition and subject (Including detrimental influences, nuisances, and hazards).
- d. Market Appeal Attributes
  - (1) Identify specific features such as design or amenities that appeal to market participants.

**Step 2. Define the user of the property (Market Delineation)**

- a. Market area concepts
  - (1) Time-Distance Concepts
  - (2) Area over which equally desirable substitute properties tend to compete with the subject.
- b. Delineate Competitive Market Area Geographically
  - (3) Define and support boundaries
- c. Identify characteristics of most probable user (consumer profile)

**Step 3. Forecast demand factors**

- a. Major demand types (Demographics Analysis)
  - (1) Population creates households
  - (2) Income creates retail-buying power

- (3) Employment creates office and industrial users
- b. Tastes and preferences: behavioral, motivational, and psychological factors
- c. Demand Segmentation

Step 4. Inventory and forecast competitive supply

- a. Existing stock of competitive properties
  - (1) Predominate type of development and conformity
  - (2) History of the area
  - (3) Life stage and trends
- b. Potential competition
  - (1) Under construction
  - (2) Proposed competition
  - (3) Probable additional competition
- c. Factors influencing completion of potential competition
  - (1) Extent built-up
  - (2) Land availability and costs
  - (3) Interest rates and most probable sources of financing including loan ratios and available mortgage rates
  - (4) Materials and labor costs
  - (5) Entrepreneurship

Step 5. Analyze the interaction of supply and demand

- a. Competitive environment
  - (1) Range of sale prices, rents, and capitalization rates
  - (2) Vacancy and/or Occupancy rates
  - (3) Turnover in ownership/occupancy
- b. Residual demand concepts

Step 6. Forecast subject capture

- a. Capture rate and absorption period (specific time period)
- b. Risk analysis
- c. Reconciliation of market analysis conclusions for use in highest and best use analysis

In addition to all of the requirements for a Level C market analysis, this section of the report should provide the area background data pertinent to the valuation of the subject property. Consideration should be given to all significant factors in this analysis, but only data relevant to the subject property should be discussed, analyzed, and included in this section of the report.

Note that the Physical Attributes as well as the Legal and Regulatory Attributes under Step 1 should have been previously analyzed and presented prior to the beginning of this section of the report presentation (i.e., in the Site Description and the Improvement Description). The Fundamental Market

Analysis would therefore continue in this section with the Locational Attributes analysis portion of Step 1.

Fundamental Market Analysis identifies the interaction of the four forces on supply and demand, which in turn directly influences the value of real property. The four forces are categorized as follows:

- Economic
- Governmental
- Social
- Environmental

Identification of key points under these four major topics can help in organizing this section. Once the broad background features have been defined, narrow the analysis to the most pertinent points. Typical market behavior in the area should be the guide in determining the appropriateness of the information reported. This section should identify the economic basis for the value conclusion.

The conclusion should consist of a summary of pertinent factors affecting property values, including a forecast of future economic trends in the competitive market area. This analysis helps establish a framework for forecasting income projections, remaining economic life, and the existence of any external or functional obsolescence. This section should also include the price and rental levels of other properties that directly compete with the subject in the market area.

This section should include a map locating the relevant market area within the region or city and delineating the competitive market area boundaries. An additional map could also be helpful in graphically locating the subject property within the competitive market area. If possible, identify property uses on the map.

Avoid the canned material and flowery rhetoric found in some promotional materials. Exhibits in this section of the report can be very helpful in making relevant facts and trends clear.

This section must have a conclusion relative to the probable future of the area, general property values, and the relationship of these future conditions to the property appraised.

## **E. Highest and Best Use Analysis**

This section of the report must be complete and thorough. This should begin with a proper definition of highest and best use and include the source of the definition.

Two separate studies are mandatory for this section:

- A highest and best use analysis of the site as vacant
- A highest and best use analysis of the property as improved

**Highest and Best Use of the Land as Vacant.** This analysis should address four criteria. The highest and best use must be:

- a. Legally permissible
- b. Physically possible
- c. Financially feasible (should include mathematical analysis of alternative uses)
- d. Maximally productive (with support from market data)

This analysis should end with a conclusion as to the ideal highest and best use of the land if it were vacant. If externalities exist, this analysis should include an analysis of the ideal improvement without the presence of externalities.

**Highest and Best Use of the Property as Improved.** This section should describe the process of comparing and contrasting the ideal improvements for the site as if vacant (developed in “as vacant” analysis) with the improvements that actually exist on the site. The result of this analysis should identify and support property obsolescence. Note: Since the highest and best use of the site as if vacant would provide for new improvements, the existing improvements (not new) are not the highest and best use of the site as vacant.

All basic principles of real estate valuation should be considered. The conclusion should address not only the optimum use, but also timing (capture/absorption), and market participants (user of space/most probable buyer).

Mathematical support should be provided for conclusions as appropriate.

## **F. The Valuation Process**

Briefly explain the theory of each approach and outline how the approach will be handled in the appraisal process. The economic principles could be quoted with an explanation of how they apply to the appraisal process. The section should end with an explanation of the reconciliation process. Note: the introductory material may be included at the beginning of each approach rather than as a separate section.

## **G. Cost Approach**

The cost approach is divided into three segments: the land value opinion, the estimate of the cost new of the improvements, and the depreciation estimate. The cost approach is also known as the summation approach because at the end the three segments are brought together to derive an indication of value.

a. Site Valuation

The best method for estimating land value is via analysis of verified comparable vacant land sales. The sales should be reduced to appropriate units of comparison. The value of the land or site should be estimated as if the site were vacant and available for its highest and best use. Each comparable sale should be briefly described. The description must include the following data for each sale:

- Location
- Land area
- Dimensions
- Selling price
- Unit selling price
- Date
- Grantor (complete name)
- Grantee (complete name)
- Use at time of sale and current use
- Zoning
- Recording data
- Financing
- Name and phone number of person with whom sale was verified
- Other relevant data

The report should include a photograph of each sale and a map showing the location of the sales relative to each other and to the subject property.

Each sale should be analyzed with regard to the recognized elements of comparison:

- Property rights conveyed
- Financing terms
- Conditions of sale
- Market conditions
- Location
- Physical characteristics

All adjustments must be market supported and demonstrated, not just discussed narratively. Quantitative adjustments are required. A properly structured summary of the adjustment process is required.

This section should end with a reconciliation of the comparable sales into a final land value opinion.

b. Cost New Estimate (Current Construction Cost)

The cost new estimate should be developed from at least two independent sources. Current construction cost is required. If a cost service is used, the source material must be specifically identified and the process demonstrated. Remember that the calculator section of *The Marshall Valuation Guide* provides replacement costs, not reproduction costs. It is important to remember to include indirect costs of all types, entrepreneurial incentive, and the direct and indirect costs of all site improvements in the total cost new.

If cost estimators or contractors supplied cost figures, their expertise must be established. If reference is made to recently completed comparable structures, they must be photographed, identified, and analyzed with appropriate adjustments to the property being appraised.

c. Accrued Depreciation Estimate

The breakdown method must be used. For a property to qualify for grading as a demonstration appraisal report it must suffer from incurable physical deterioration (long-lived) and all forms of obsolescence that are present must be correctly identified and properly measured. If curable physical depreciation is present, it must be analyzed in the report. The report must demonstrate the appraiser's ability to estimate depreciation factually from market data. If more than one form of obsolescence is present, they must be treated factually based on market data. The estimate of depreciation must be substantiated with market support.

Finally, the computations in the cost approach must be shown. This includes an estimate of the total cost new of the improvements, an itemized breakdown of accrued depreciation and support there for, and deduction of total depreciation from the total cost new to indicate the depreciated improvements value. To this figure land value is added.

This section must end with an indication of value derived by the cost approach.

## **H. Sales Comparison Approach**

This section should begin with a brief discussion of the criteria used in the selection of comparable sales. The comparable sales should be described in detail. The description must include:

- Address/location of sale property
- Size of property (land and improvements)
- Other descriptive information
- Selling price
- Unit selling price (may be more than one)
- Grantor
- Grantee
- Recording data
- Date
- Financing

- Name and phone number of person with whom sale was verified
- Marketing time/history
- Other significant data also should be included, including the age and condition of the improvements, income, vacancies, and other verified facts such as past expenses, refurbishing costs, and land and building ratio.

The report must include a photograph of each sale and a map locating the sales relative to each other and to the subject property.

Sales should be presented on an adjustment grid that demonstrates all supportable adjustments. All adjustments should be market supported and computations leading to the concluded adjustment must be provided in the report, not just discussed. Each sale should be analyzed with consideration of the recognized elements of comparison:

- Property rights conveyed
- Financing terms
- Conditions of sale
- Market conditions
- Location
- Physical characteristics and economic characteristics

This approach should end with reconciliation of the value indications derived from the comparable sales after adjustment. The reconciliation should end with a final indication of value by the sales comparison approach. If the property suffers from curable physical deterioration or obsolescence, these losses must be properly and consistently handled without double-depreciating.

## **I. Income Capitalization Approach**

The first step in this approach is to present the property's actual income history. If possible, a three-year history of rents should be obtained along with the current rent roll. The amount of detail reported will depend on the property. Review and summarize existing leases. The details of existing leases could be placed in the addenda.

When reporting comparable rentals, the following information must be provided:

- Date of lease
- Term of lease
- Rental rate
- Size of space
- Rental unit of comparison
- Conditions of lease (expenses paid by landlord and those paid by tenant)
- Other significant conditions confirmed about the rental property

The rental data presented should include a photograph of each rent comparable and a rental map locating the rentals and the subject property.

Using units of rental comparison and actual rental transactions, estimate the current market rent for the property being appraised. This approach must be handled properly, recognizing the type of estate being valued (e.g., fee simple, lease fee) as stated in the introduction to the appraisal report. Using actual market rentals, adjust for major differences between the rentals and the property being appraised, based on market support. Rental comparisons must be presented in an adjustment grid summary. There is to be market support and justification for the adjustments and an adequate explanation. Project the subject's future gross income potential at market or contract rent depending on the type of estate being valued.

Vacancy and collection loss must be estimated. A survey of similar properties in the area should be conducted to estimate potential vacancy and rental losses. The results may be detailed here or summarized from the market analysis section. The subject property's past vacancy and collection losses should be presented. Background information developed in the area, region, and neighborhood sections should be used as additional support for the projected vacancy loss.

Show the itemized statements of past expenses for the property being appraised, if they are obtainable. The past expenses of the property being appraised should be compared item for item with the expenses incurred by similar properties in the area. From this information, project the stabilized fixed and operating expenses anticipated for the property being appraised.

Replacement reserves must be estimated for short-lived items. Show all computations (may be in this section or summarized from the cost approach). Reserves for the subject property, after computation, should be handled consistent with market practices for the subject property type in the relevant competitive market area. With the previously estimated figures, develop the estimated net income for the subject property.

If the property functions in a net lease market, all expenses must be properly estimated and allocated between landlord and tenant. The necessary expenses paid by the lessee must be discussed individually, in the same manner and with market support, as if the property were leased on a gross basis. Since a lessee can choose from any of a number of potential rental alternatives, the process of selection would include not only the net rental due but also the lessee's expense liability for each potential alternative location.

Outline a reconstructed operating statement for the subject property that includes total potential gross annual income, vacancy and collection loss allowances, effective gross income, all expenses, and net operating income.

The selection of a capitalization method depends on the appraisal problem. Direct capitalization is expected in demonstration appraisal reports; yield capitalization, if applicable to the subject property

valuation and well supported, is an acceptable alternative as an additional capitalization method. Direct capitalization rates must be developed from sale data. The summation method is not sufficient by itself, and the band-of-investment technique must be supported by market data. While other capitalization methods are not discouraged, selecting an appropriate property for a demonstration appraisal report will usually result in a value that can be supported by direct capitalization.

If there is surplus income because of excess lease rental or a lease percentage clause, this income must be explained and properly treated. If the income stream is below market level, it should be explained and properly treated in valuing a leased fee interest.

If income depends on capital expenditures, make the appropriate adjustment. If the income includes personal property, show and support value allocations to the real and personal property. If the property suffers from curable physical depreciation or functional obsolescence, make appropriate adjustments.

Derive a value estimate and justify capitalization method(s) and techniques selected. Include a discussion of why one or more techniques were used and others were not.

It is not acceptable to base the overall rate utilized in direct capitalization from an analysis of comparable sales for which the income and expense data are estimated by the appraiser. An additional data set of sales that are actually leased may be needed to provide data for an overall rate analysis, if the sales utilized in the Sales Comparison Approach are not leased.

## **J. Reconciliation and Final Value Opinion**

The purpose of reconciliation is to complete the process of correlation, which has taken place throughout the report, and to develop the value indications derived in the approaches into a final opinion of value. Reconciliation is a discussion that analyzes the quantity and quality of the data examined in each approach. This analysis includes examination of the strengths and weaknesses of the three approaches and the relevance they have to the property being appraised and the appraisal problem. It is not a restatement of methodology presented or analysis within the report.

Explain any wide discrepancies. It is not necessary for the results of the three approaches to be close numerically. Apply sound reasoning to the facts and interpretations that lead to the final opinion, keeping in mind the definition of value and the intended use and intended users of the report.

## **PART THREE**

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# **Certification and Addenda**

## **A. Certification of Value**

The certification of value in an appraisal report may follow the table of contents or be combined with the final value opinion. In a demonstration appraisal report, the certificate is appropriately placed after the final value opinion. The signature of the appraiser and the date are then added. The certification must conform to the wording set forth in the Appraisal Institute's *Standards of Professional Appraisal Practice* and *Supplemental Standards*.

## **B. Assumptions and Limiting Conditions**

Assumptions and limiting conditions in the demonstration appraisal report generally follow the certification of value. See the current edition of *The Appraisal of Real Estate* for suggested wording, appropriate standard conditions, and examples of general assumptions and limited conditions.

Any factors peculiar to the assignment in question should be fully explained. Extraordinary assumptions or hypothetical conditions may not be appropriate for demonstration report purposes.

## **C. Qualifications of the Appraiser**

The appraiser's qualifications may be placed in the introduction, after the reconciliation section of the report, or in the addenda. Qualifications should be listed in a brief and concise fashion. Qualifications may include:

- Educational background and training.
- Professional experience.
- Business, professional, and academic affiliations and activities.
- Some important clients and appraisal assignments.
- Identification of Associate Member status in accordance with the Appraisal Institute's *Standards of Professional Appraisal Practice*.

## **D. Statement of Candidacy**

Associate Members often ask how they may refer to their Appraisal Institute affiliation. For a detailed explanation, please refer to Article II, Part B of Regulation No. 1. This information also appears in the pledge and certification that is signed when an individual applies for Associate Membership.

Associate Members may refer to themselves with the terms "Associate Member," "general Associate Member" or "residential Associate Member" on letterhead, business cards, Web sites and other advertising materials and under a heading entitled "professional affiliations." Associate Members may use these terms only in conjunction with the name of an individual and not in connection with the name,

logo or signature of any firm, partnership or corporation. Associate Members may not abbreviate these terms or place these terms under a heading entitled “professional designations.”

**Correct:**

John Doe, Associate Member, Appraisal Institute  
Jane Doe, general Associate Member, Appraisal Institute

**Incorrect:**

John Doe, Member, Appraisal Institute  
John Doe, G.A.M.  
John Doe, SRA Associate Member, Appraisal Institute

**Why Incorrect:**

Must use “Associate Member”  
Cannot abbreviate  
Cannot use designation

If an Associate Member makes an improper reference to membership, the matter will be referred to the Appraisal Institute’s Ethics and Counseling Department for review. If a violation is found, the Associate Member will receive a letter concerning the violation.

## **E. Addenda**

Addenda are supplements to a report and may be used to avoid interrupting the narrative. Data that pertain directly to your narrative, such as comparable sales data, other market data, maps, and sketches, should be included in the body of the report unless they are overly lengthy. The addenda should include any necessary supplementary exhibits, such as:

- Additional photographs of the subject property. When possible, include pictures of items of curable depreciation, and interior views to help the reader visualize the property.
- Photographs of nearby properties referred to in the report.
- Maps of secondary importance.
- Statistical data, other similar study results, related to subject property.
- Any additional supporting data referred to in the body of the report.

## **F. Additional Important Information**

The rules pertaining to demonstration appraisal reports are set forth in Article III, Part E of Regulation No. 1. They include, but are not limited to, the following:

- The date of value in the report must be no more than five calendar years prior to the year the demonstration appraisal report is submitted for credit.
- The general demonstration appraisal report must relate to income-producing real estate. If a multi-family property is appraised, it must contain at least five units.
- The property chosen must allow the appraiser to demonstrate all three approaches to value and the property must suffer from incurable physical deterioration.
- All appraisal data contained in the report must be factual.

On the “Application for Demonstration Appraisal Report Credit,” you are required to certify that you personally and without assistance assembled all of the data used in preparing the appraisal, analyzed the data, formed the conclusions, and prepared the appraisal report. You must also certify that the appraisal and the appraisal report comply with the requirements of Regulation No. 1, the Standards of Professional Appraisal Practice of the Appraisal Institute, and the Code of Professional Ethics. If the demonstration appraisal report is found to be nonfactual or not the Associate Member’s own work, it will not receive credit. The Associate Member will then be required to submit another demonstration appraisal report on another subject.

The completed “Application for Demonstration Appraisal Report Credit” and a check for the grading fee must accompany the demonstration appraisal report. The package should be mailed to the Associate & Affiliate Member Service Center of the Appraisal Institute at 550 W. Van Buren St., Suite 1000, Chicago, IL 60607. For information regarding the amount of the grading fee, contact the Associate & Affiliate Member Service Center at 312-335-4111.

Send two copies of the demonstration appraisal report or one copy and a disk with the completed application. The demonstration appraisal report becomes the property of the Appraisal Institute and will not be returned to the Associate Member. For additional information and assistance, contact your chapter Admissions or Associate Member Guidance Chairs or the Associate & Affiliate Member Service Center.

## **G. Things to Do**

- Explain your reasoning completely, yet concisely. Conciseness is important. Too many Associate Members tend to write more lengthy reports than are actually needed.
- Put directional arrows indicating north on maps, plats, and aerial photos.
- Give sources of all definitions. Use current references.
- Prepare professional exhibits
- The body of the report may be double-spaced or 1.5 spaced. Please use a 10 font or larger.
- Explain any departure from normal procedure and consider the effects of any adverse conditions noted on the subject property.
- Remember that the factors affecting the property appraised in one approach must be considered in the other two approaches. Focus on consistency throughout the report. This includes appropriate treatment of all sources of losses in value.

## **H. Things Not to Do**

- Do not fabricate data.
- Do not rely on unsupported assumptions, conclusions, or opinions.

- Do not rely on outdated material.
- Do not use formats from demonstration appraisal reports prepared several years ago.
- Do not select a new, or almost new, property that will not give you an opportunity to measure incurable long-lived depreciation.
- Do not adjust gross rent multipliers.
- Do not fail to include a Level C market analysis (required as of August 1, 2001).
- Do not conclude that the present use is the highest and best use of the property simply because it conforms to other improvements in terms of zoning.
- Do not express opinions or conclusions based on estimates with an unrealistic degree of precision. Use good judgment and round appropriately.
- Do not use statements such as “Based on my experience and knowledge...” or “Knowledgeable people in the area say...” to support your adjustments. They are unacceptable.

**THIS GUIDE DOES NOT NULLIFY, AMEND, OR IN ANY WAY CHANGE THE REQUIREMENTS SET FORTH IN THE APPRAISAL INSTITUTE’S BYLAWS AND REGULATIONS.**

## **Conclusion**

Best wishes in successful completion of your demonstration appraisal report. If you have any questions or comments, please feel free to call the Associate & Affiliate Member Service Center. If necessary, staff will refer you to a grader to answer your questions.

— The Demonstration Appraisal Grading Panel

# Most Frequently Asked Questions Regarding the General Demonstration Appraisal Report

## General Considerations

### 1. Why are demonstration reports required?

Preparing a report demonstrates the Associate Member's ability to focus appraisal theory and principles on a specific appraisal problem and develop an acceptable solution. A report can determine whether an Associate Member has attained the level of performance necessary for designated membership in the Appraisal Institute.

### 2. May others help me prepare my demonstration appraisal report? To what extent?

Others may help by typing or word processing the report, and proofreading the copy for spelling or grammatical errors. All of the writing, analysis, numerical calculations, and conclusions must be your own. It is unethical for a Member or Associate Member of the Appraisal Institute to correct your demonstration report prior to submission.

### 3. What happens if the Appraisal Institute discovers that a demonstration report is entirely or partly the work of another? What if the facts have been fabricated?

By signing Form D-1, the Associate Member certifies that the report is his or her own work and that the report complies with the requirements of Regulation 1 and the *Code of Professional Ethics and Standards of Professional Appraisal Practice of the Appraisal Institute*. If this statement is untrue, credit will be rescinded, and the Member will not be allowed to base any new submission upon the same property. Fabricated data will also result in the loss of credit for the report.

### 4. When are reports sent back to a local representative for verification of the factual data?

When a demonstration appraisal report meets technical requirements, it is sent to a local representative appointed by the Chair of the Demonstration Appraisal Grading Panel (or delegate) for factual verification. The local representative does not regrade the report.

### 5. How old can the appraisal be?

The date of valuation of the demonstration appraisal report may be no more than five years prior to the year the report is received in the Chicago office. Members should not ask for special treatment. Bending the rules would be unfair to other Associate Members.

### 6. If I have written a passing demonstration report for another organization, will the Appraisal Institute accept it?

No, the Appraisal Institute does not grant reciprocal credit. To receive credit toward the SRA or MAI designation, the demonstration report must be prepared for, but not necessarily addressed to, the Appraisal Institute.

**7. May I submit a demonstration report on a property that I own?**

Yes, with proper disclosure and the ability to complete the assignment objectively and credibly.

**8. How can I ensure that my report qualifies for grading?**

Make sure that your report includes all three approaches to value, and that the report demonstrates the proper methods of handling physical incurable deterioration (long-lived); that is, the property cannot be new, and the report must contain a fundamental market analysis. A report can be disqualified if it is not signed, or if a required section is omitted.

**9. May I submit a demonstration appraisal report on a property subject to a net lease?**

Yes, you may value this property, but all applicable expenses must be analyzed because the income capitalization approach must account for the effect on net rent of all expenses, whether they are the responsibility of the owner or the tenant.

**10. Must I appraise the leased fee interest in a leased property?**

No, but the interest appraised must be clearly disclosed, and the specifics of the lease must be discussed along with a statement of the effect, if any, of the lease interest on the fee simple unencumbered value of the property. You may appraise any interest in the property that is appropriate, with disclosure.

**11. Must I follow the format suggested in *The Official Guide to Demonstration Appraisal Reporting: General*?**

No, you need not follow this format, but do refer to the form for content. You may use whatever format seems logical, e.g., it may be practical to put the approaches in a different order.

**12. How do I resolve the contradictory information on methods and techniques that I may have received from various texts, teachers, seminars, and other sources?**

No grader will dispute the authority of *The Appraisal of Real Estate*. If you think a method or technique used in your report may be controversial, help the grader by citing your source.

**13. How long should the report be?**

Most demonstration reports are too long. Understandably, Associate Members are reluctant to risk being downgraded for omissions or insufficient explanation. Although some people are able to write completely and succinctly, others find this very difficult.

Experience shows that reports often run long due to redundancy, the inclusion of extraneous material, and misunderstandings about what the problem is and how it should be solved. Most writers use too many words when they should strive for the best words.

In preparing a demonstration report, select a subject property that lends itself to the demonstration process (take-home examination). Build the report correctly, using only relevant information. Try to anticipate and satisfy the reader's questions, but do not repeat yourself. Search for the best ways to get your message across, which may involve exhibits and photographs.

Sharp editing and writing experience are needed to prepare a report. If you cannot structure the narrative logically, you are not ready to write a demonstration report. Remember, the skills needed to write a good demonstration report may lag behind the ability to appraise the property in question.

**14. Should a property in litigation or one that may be involved in litigation during the grading process be the subject of a demonstration appraisal report?**

No. There may be legal and confidentiality issues.

**15. Will an elaborate cover or binding earn me additional points?**

These factors are considered in the overall presentation of the report. They do make a report look professional and reflect positively on the appearance of the report. The grading process awards some points for presentation, but this is not the focus of the pass/fail decision. The binding method used should allow the report to lay flat for grading.

**16. How do I select a subject property or market area?**

Before selecting a property, gather market data and other information. Choose a property that will allow you to demonstrate your ability to make use of market data in applying all three approaches and arriving at a value conclusion.

**17. What advice would you offer to someone who is contemplating writing a demonstration appraisal report?**

First, read and follow *The Official Guide to Demonstration Appraisal Reporting: General*. Then, select a type of property with which you are familiar. Make sure you have the necessary experience and adequate market data. Next, select a specific subject, and define the appraisal problem to be solved. Finally, write and submit your appraisal report.

## **Technical Considerations**

**18. How should data previously included in regional, city, and neighborhood sections be presented?**

All of the items previously addressed in the regional, city, and neighborhood analyses should be in the market analysis section. This is in accordance with the demonstration report requirements in effect since August 1, 2001.

Be careful to avoid an abundance of disorganized data researched or compiled by others. Do not include a history of the area or detailed statistics that are not relevant to the problem at hand.

The conclusions presented in the market analysis section of the report should alert the reader to any potential economic or external problems or benefits that could affect the subject property. Often, the remaining economic life of the subject can be illustrated in this section.

**19. What is meant by the levels of market analysis?**

The primary distinction is in the depth and detail of the analysis and in the difference between primary and secondary data. Levels C and D require that the supply and demand data analyzed and presented in that section be derived by the appraiser, not summarized from studies done by others. Levels A and B refer to an inferred analysis (see material in manual).

Other specifications and requirements are provided in the materials for the Appraisal Institute's Course *General Appraiser Market Analysis and Highest & Best Use*.

**20. What problems do Associate Members have in estimating effective age and economic life?**

Too often, effective age and economic life are presented as unsupported conclusions or conclusions based on the statements of others.

Effective age is an observable judgment based on inspection and knowledge of property maintenance and the capital improvements made to the property. The conclusion of remaining economic life, however, can be supported using one or more techniques of market measurement. This fundamental statistic cannot be adopted from a cost manual of broad national averages; it is a function of the local market. If the property's remaining economic life is not carefully measured or reasoned, this weakness will permeate the rest of the report.

**21. If the property I am appraising is an office building in an office park, do I need to include a detailed discussion of highest and best use?**

Yes, it may seem obvious, but in a demonstration report, the obvious must be analyzed, reasoned and verified. The definition of highest and best use that is used dictates how the rest of the section is presented. First, the site use must be analyzed as *if vacant*. Then the property must be analyzed as *improved*. Economic, physical, and legal considerations that would affect the vacant site can be covered briefly. Site measurements can be presented, and the site's appropriateness for possible uses can be discussed. Alternative uses must be studied to provide specific support for the "ideal" use for the site as though vacant.

After concluding the proper type of use, the degree to which the actual improvements meet this ideal can be discussed and differences can be shown. Because of the requirements of the demonstration report, the existing improvements will not represent the optimum use of the land as though vacant.

**22. What problems may be encountered in the site value section?**

Use of an insufficient number of sales can hamper analysis. Also, using sales that are too similar to the subject site can hinder site valuation. Part of the answer, of course, lies in selecting a good subject property and using the best data available. If this section does not fully demonstrate your abilities, later sections surely will. Be thorough in relating the comparable sales to the subject property. It is imperative that you extract adjustments from the comparable sales to support the indicated site value for the subject site.

**23. Would an adjustment for market conditions be made before any other adjustments?**

Not necessarily. Sometimes an adjustment for financing or conditions of sale must be made before a time adjustment is logical or applicable. Refer to *The Appraisal of Real Estate* for more information.

**24. May I use a cost manual to estimate current construction cost?**

Reproduction cost is a requirement of the Traditional Demonstration Appraisal Report. Replacement cost may only be used in the TARA submission. When using a cost manual in a Traditional Demonstration Appraisal Report, be sure to use the section of the manual that provides reproduction cost new (current construction cost of an exact replica), not replacement cost. The Marshall Valuation Service calculator cost section is replacement cost; the segregated cost section can be helpful in developing an estimate of reproduction cost)

The graders strongly suggest supporting the estimate with an alternate source such as the cost of recent comparable properties, a contractor's bid, or updated actual costs. Whatever source(s) you use, be sure to explain what the estimate does and does not include, such as architect's fees and other indirect costs, entrepreneurial incentive, and site improvements costs.

**25. Should I use replacement or reproduction cost in my report?**

Reproduction cost is required in the Traditional Demonstration Appraisal Report. Replacement cost may only be used in the TARA submission. Remember, replacement cost reflects the cost to construct, at current prices, a building with utility equivalent to the building being appraised; whereas, reproduction cost is the cost to construct, at current prices, an exact duplicate, embodying all the subject's deficiencies, superadequacies, and obsolescence.

**26. Do I have to have two forms of depreciation?**

This depends upon which option has been chosen. Under the obsolescence option, the subject property must suffer from at least one form of depreciation (physical long-lived) and a form of obsolescence (functional or external, curable or incurable). Under the FMA option, the subject property must suffer from at least one form of depreciation (physical long-lived), and all forms of depreciation that are present in the property must be adequately identified and properly addressed.

## **27. What mistakes are commonly made in calculating depreciation?**

An Associate Member may fail to account for some form of functional or external deficiency that was clearly described or intimated in early sections of the report. Another individual may depreciate an item and then double depreciate it in the steps that follow. An error can be made by concluding that functional obsolescence is either curable or incurable when the data presented in the other two approaches contradicts this conclusion.

When age/life depreciation is derived from comparable sales, some appraisers fail to establish that the proportion of short-lived items to long-lived items in the comparable sales is similar to this proportion in the subject, or if the proportions are dissimilar, they fail to break down these items in the sales. When depreciation is supported by sales, some appraisers fail to account for similarity or dissimilarity in construction.

Sometimes an appraiser may report small amounts of deferred maintenance, which would be imperceptible in market transactions. Accrued depreciation is market-oriented in all categories. If the appraiser has penalized the subject property with a type of depreciation that the rest of the market data does not recognize, the property probably doesn't have it either.

## **28. May I use the depreciation schedules listed in cost manuals?**

No. Depreciation is a function of the market, and, therefore, it is reflected only by local market actions. Cost manuals deal with national averages, which may or may not apply in your subject area and are not acceptable in the demonstration report.

## **29. What mistakes are commonly made in the sales comparison approach?**

Some appraisers fail to extract adjustments from the comparables before comparing the sales to the subject. This almost always results in adjustments that are subjective rather than objective and that are not market-supported.

Appraisers need to measure differences using paired data analysis. It's important to use the unit or units of comparison that are actually used by participants in the market, e.g., dollars per square foot of building area or dollars per unit.

Appraisers should not adopt costs as the basis for adjustments unless they clearly establish that market participants would view the issue in this way. Adjustments must be abstracted from market data.

Appraisers may fail to account for the impact of nonconventional financing on the value of the comparables, considering only those factors that affect the seller or the buyer. Sometimes appraisers do not appropriately or adequately adjust the sales for depreciation, excessive vacancy, or income below market level, which exists in the subject property but not in the comparables, or vice versa.

**30. What are the most common oversights or deficiencies in using the income capitalization approach?**

Some reports may not show the causes of vacancies in rent comparables and the causes for the variations in rent. Other reports rely on estimated income and expense data. Actual data is required for the demonstration report. Sale comparables must be adjusted to include all the appropriate categories of expenses, so that capitalization rates can be more accurately measured.

Discounted cash flow procedures are best suited to leased fee valuations of properties that have multitenant leases with varying terms, rates, and conditions. The discount rates for these procedures and the overall rates used for reversionary values must be supported in the market.

If other capitalization techniques are used, all rates must be supported by market data.

The reasons for using one or more capitalization techniques should also be discussed.

**31. What should I address in the reconciliation and final opinion of value section of my report?**

Do not repeat the analysis presented in other sections of the report. Rather, explore the inherent strengths and weaknesses of the approaches, show how they are interrelated, and establish which is the strongest (best supported) and/or most recognized in the market. The conclusion should relate to the strongest approach, or if two approaches have equal weight, the conclusion should fall between the two approaches. Avoid the appearance of adopting an average as your conclusion.

## **PART FOUR**

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# Online General Demonstration Report Alternative

## **Introduction and Overview**

As an enhanced learning experience of the traditional demonstration report, a general Associate Member of the Appraisal Institute may select the alternative E-demo. The E-demo follows the same policies and procedures as the traditional demonstration report. The general Associate Member is paired with an adviser or advisers. Each section of the report is reviewed by the adviser prior to final submission of the demonstration report to assess strengths and weaknesses of the report.

## **Eligibility**

To be eligible for the Online General Demonstration Report Alternative, a general Associate Member would need to have completed

- Level I and Level II education requirements
- College degree requirement
- Demonstration appraisal seminar
- Current Standards and Ethics education cycle requirements

Before a general Associate Member would receive permission to work with an adviser, the general Associate Member would need to summarize initial research on the subject property that indicates the property is appropriate and that sufficient data exists.

Once the general Associate Member receives permission to proceed, the general Associate Member would then complete the various sections, which are listed on the next page.

## **Policies relating to the E-demo path to the general demonstration appraisal report**

The demonstration report must be prepared by the general Associate Member without appraisal assistance or revision by another person. The report is divided into six sections.

1. Section 1—Introduction (cover page through improvements)
  - a. Description analysis and conclusions

- b. Site data and analysis
  - c. Description and analysis of improvements
  - d. Zoning, taxes, and assessment analysis
2. Section 2—Market analysis and highest and best use analysis
  3. Section 3—Land valuation and cost approach
  4. Section 4—Sales comparison approach
  5. Section 5—Income capitalization approach
  6. Section 6—Reconciliation

Each section must be completed and submitted to the adviser to be reviewed in stages. The adviser assesses the strengths and weaknesses of each section and provides a review as well as access to resources for each section as needed. The adviser must determine that a section is “qualified to grade” before the general Associate Member can submit another section. A general Associate Member has six (6) months to complete the process and submit the final report.

### **Primary Responsibility**

Applicant must be the sole author of the reports submitted. Applicant must not have received assistance, review, or correction related to demographics, market analysis, descriptive information, data, analysis, and conclusions. Working with the e-demo adviser is not “significant real property appraisal assistance” as defined for this purpose.

### **Sole Signatory**

The general Associate Member must be the sole signatory to the completed demonstration report prepared as part of the E-demo process.

### **Grading Policy**

The E-demo report will be graded in the same manner as the traditional demonstration report to determine whether the general Associate Member has demonstrated the requisite level of knowledge, understanding, and application of appraisal principles and practices required in the demonstration appraisal report.

## **Guidelines**

The most concise and detailed guidance for completion of this option is provided in Appraisal Institute Regulation No. 1, Article III, Part F, Section 10, which is quoted below and on the following pages.

“Online General Demonstration Report Alternative. General Associate Members who meet the eligibility requirements may satisfy the demonstration appraisal report requirement by receiving credit for a demonstration report that meets the requirements of the Online General Demonstration Report Alternative as provided in this Regulation, the Code of Professional Ethics, the Standards of Professional Appraisal Practice and The Official Guide to Demonstration Appraisal Reporting published by the Appraisal Institute, as modified from time to time.

General Associate Members who have attended the required courses, received a passing grade on required examinations, received credit for the college degree requirement, are current with the USPAP and Ethics education requirements, and have attended the appropriate demonstration appraisal report seminar are eligible to participate in the Online General Demonstration Report Alternative.”

## **Responsibilities of Applicant**

“All appraisal data contained in the appraisal reports submitted for credit must be factual.”

- A. The general Associate Member must attest to his/her primary responsibility in the application for credit for
  - 1. Assembling the data
  - 2. Analyzing the data
  - 3. Forming the conclusions
  - 4. Preparing the appraisal reports submitted
  
- B. Assistance

In preparing the appraisal reports, the general Associate Member may receive assistance in matters: such as

- 1. Photography
- 2. Drawings

3. Typing, spell-checking, and word processing

C. Credit

“Appraisal reports that receive credit as an alternative to the demonstration appraisal report may be listed toward the required number of hours of experience, but (these reports) may not be selected by the general Associate Member or the Screener for review.”

## **Grading**

A. Procedures

The procedures for grading appraisal reports submitted under this section are as follows:

Under the E-demo option, each section is submitted to the adviser when completed for review and/or revision. When all of the sections have been completed, the final report will be graded in its entirety, and the report will be submitted for the factual verification process.

B. Field verification

After a grader determines that the appraisal reports meet the technical requirements, the report may be processed for “factual verification before a decision is made whether to grant credit.” Local representatives, appointed by the chair of the Demonstration Appraisal Grading Panel (or delegate), may conduct a “field verification of information contained in the appraisal reports” and in the general Associate Member’s application for credit.

If an application for credit is not factual, or if an appraisal report contains appraisal data that is not factual, then the general Associate Member may neither submit the appraisal report for regarding nor revise the appraisal report. “The general Associate Member may submit a substitute appraisal report for grading that was developed after the date of the grader’s critique.”

**Most Frequently Asked Questions Regarding**

# The Online General Demonstration Report Alternative (E-Demo Report)

**1. What is the time frame for completion of an appraisal report under the E-demo option?**

The general Associate Member must commit to completion of the assignment in six months. This can be extended for just cause by the Chair of the General Demonstration Reports Panel.

**2. How are the requirements for the report for the E-demo option different/similar to those for a traditional demonstration report?**

The requirements are essentially the same. The process for preparation of the report is different, and the grading procedures are different.

**3. Is it true that a section can be revised several times until it is approved by the adviser?**

This is true; however, there is a fixed time frame for the process, and the report will be graded in its entirety to ensure internal consistency upon completion.

**4. Is there a required order for submission of the report sections?**

Approval of the order of submissions is agreed upon by the adviser and the Associate Member.

## **PART FIVE**

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# **Three Appraisal Reports Alternative**

## **Introduction and Overview**

As an alternative to the traditional demonstration report detailed in Section II, a general Associate Member of the Appraisal Institute may submit three full narrative appraisal reports which in the aggregate demonstrate the same level of knowledge, understanding and application of appraisal principles and practices required in the demonstration appraisal report. Provided below is the policy regarding this alternative.

## **POLICIES RELATING TO THE THREE APPRAISAL REPORTS ALTERNATIVE TO THE GENERAL DEMONSTRATION APPRAISAL REPORT**

The three appraisal reports must be prepared by the general Associate Member without appraisal assistance or revision by another person. If the Associate Member plans to submit a draft appraisal report to another appraiser for possible approval or revision, the Associate Member must save a copy of the draft report. The Associate Member may enhance the draft report to expand the analyses, reconciliation, or other aspects to meet the requirements listed for the three appraisal reports.

### **Primary Responsibility**

Applicant must be the sole author of the reports submitted. Applicant must not have received assistance, review, or correction related to demographics, market analysis, descriptive information, data, analysis, or conclusions.

### **Sole Signatory**

It is intended that the applicant submit reports essentially in a finished form as submitted to a principal for review. The Associate Member may enhance his or her draft reports by expanding the analyses, reconciliation sections, or other aspects of the reports to meet the requirements for the three appraisal reports.

### **Grading Policy**

The three appraisal reports are graded to determine whether, in the aggregate, the general Associate Member has demonstrated the same level of knowledge, understanding, and application of appraisal principles and practices required in the demonstration appraisal report. If an applicant's reports fail to meet the technical requirements, they may be revised and submitted for re-grading one time.

## **GUIDELINES**

The most concise and detailed guidance for completion of this option is provided in Appraisal Institute Regulation No. 1, excerpted below:

Effective January 1, 2002, general Associate Members may satisfy the demonstration appraisal report requirement by receiving credit for three (3) appraisal reports developed in the normal course of business that:

- A. relate to real estate other than one-to-four-family residential real estate;
- B. are communicated in a full narrative format;
- C. are dated no more than five (5) calendar years prior to the year of submission to the Appraisal Institute;
- D. meet the applicable appraisal standards; and
- E. contain the types of analyses listed below:
  - 1. At least one of the reports must include all three approaches to value.
  - 2. At least one must include a fundamental market analysis.
  - 3. At least one must include a yield capitalization analysis.
  - 4. At least one must include a direct capitalization analysis.
  - 5. Each report must contain a reconciliation as outlined in The Official Guide to Demonstration Appraisal Reporting: General.

All appraisal data contained in the appraisal reports submitted for credit must be factual. The general Associate Member must have had primary responsibility for assembling the data, analyzing the data, forming the conclusions, and preparing the appraisal reports submitted, and must so attest in the application for credit. In preparing the appraisal reports, the general Associate Member may receive assistance in matters such as photography, drawings, typing, and word processing. The reports shall be signed only by the general Associate Member. The general Associate Member may enhance such reports delivered to clients and submit the enhanced reports for grading.

Appraisal reports that receive credit as an alternative to the demonstration appraisal report may be listed toward the required number of hours of experience, but may not be selected by the general Associate Member or the Screener for review.

The three reports will be graded to determine whether, in the aggregate, the general Associate Member has demonstrated the same level of knowledge, understanding and application of appraisal principles and practices required in the demonstration appraisal report.

The procedures for grading appraisal reports submitted under this section are as follows:

- A. Upon receipt of a general Associate Member's appraisal reports and application for credit from the Admissions Division, a grader(s) will be assigned to grade the reports to determine whether they meet the technical requirements;
- B. If the grader(s) determine(s) that the general Associate Member's appraisal reports meet the technical requirements, the grader(s) shall notify the Admissions Division in writing; and
- C. If the grader(s) determine(s) that the appraisal reports fail to meet the technical requirements, the grader(s) shall prepare a critique explaining the reasons for the failing grade. The grader shall forward the critique to the Admissions Division, which shall in turn transmit the critique to the general Associate Member.

Appraisal reports that meet the technical requirements after grading may be processed for factual verification before a decision is made whether to grant credit. Field verification of information contained in appraisal reports and in general Associate Members' applications for credit shall be conducted by Local Representatives pursuant to procedures contained in the Procedure Manual, substituting the words "appraisal reports" for the words "demonstration appraisal report."

If an application for credit is not factual or if an appraisal report contains appraisal data that is not factual, then the general Associate Member may not submit the appraisal report for re-grading nor revise the appraisal report. The general Associate Member may submit a substitute appraisal report for grading that was developed after the date of the grader's critique.

# Frequently Asked Questions Regarding the Three Appraisal Reports Alternative

## General Considerations

### 1. Why was this alternative provided?

Until recently, a general Associate Member had one alternative, which was the traditional demonstration appraisal report. There are now several alternatives to the traditional demonstration report to provide enhanced flexibility for general Associate Members.

### Summary of the three appraisal reports alternative

In the aggregate, the three reports have to be equivalent to the traditional demonstration report. When the reports are submitted, the Associate Member must direct the grader to the various sections of the report that fulfill the requirements as outlined in Regulation No. 1. The graders will review those sections of the report using a grading sheet that is identical to the one used for a traditional demonstration appraisal report. For those Associate Members who choose this alternative, it is likely that more extensive analysis will be required than is typically required in a report submitted to a client. In fact, Associate Members are strongly encouraged to enhance the reports. Attending the General Demonstration Report Seminar is also recommended.

### 2. Can I just submit three appraisals off the shelf?

That depends on the quality of work you have been performing. You need to recognize that this alternative will be graded with the same standards as those used for the traditional demonstration appraisal report. Likely, enhancement of the reports will be necessary to demonstrate an understanding of the appraisal techniques and theories reviewed for a demonstration appraisal report.

### 3. I work for a company, and all of my reports are cosigned. Can I still use this alternative?

Proper planning may allow you to use this alternative. The reports submitted for grading must reflect your sole work. As such, a cosigned report does not qualify; however, you can keep a copy of the work product prior to submission to the reviewer in your company. It is likely that the report submitted for grading may be substantially different from the report eventually submitted to the client. The graders strongly encourage enhancement of the reports when necessary to comply with the requirements outlined in *The Official Guide to Demonstration Appraisal Reporting: General*. The issue of whether a report was cosigned will be scrutinized during the factual verification process.

**4. Can I submit one report that meets all of the requirements and two single approach appraisals?**

No. At least one report must have all three approaches to value, and the remaining reports must have a reconciliation as outlined in *The Official Guide to Demonstration Appraisal Reporting: General*. As such, all of the reports have to have a minimum of two approaches to value.

**5. Can any of the appraisals be on proposed construction?**

Yes, but at least one of the reports must contain all three approaches to value. Since the requirements for the cost approach require at least one form of depreciation, use of proposed projects may create difficulties unless the property as proposed will suffer from some form of functional or external obsolescence.

**6. Do I have to have two forms of depreciation?**

This depends upon which option has been chosen. Under the obsolescence option, the subject property must suffer from at least one form of depreciation (physical long-lived) and a form of obsolescence (functional or external, curable or incurable). Under the FMA option, the subject property must suffer from at least one form of depreciation (physical long-lived), and all forms of depreciation that are present in the property must be adequately identified and properly addressed.

**7. Can I use a subdivision analysis in one of the reports?**

No, all demonstration reports for MAI designation credit must relate to the valuation of income-producing real estate improved with a building or buildings.

**8. What does full narrative format mean?**

A full narrative format means the appraisal report contains: (a) the relevant factual data assembled in the course of the work, (b) the appraiser's analysis of the relevant factual data; (c) the reasoning that led to the appraiser's conclusions; and (d) the opinion or conclusion of the author of the report.

**9. Do I still have to develop and report reproduction costs or can I use replacement cost for the three appraisal report alternative to the general demonstration report?**

If your property suffers from some form of functional obsolescence, the use of the replacement cost may not allow you to adequately demonstrate the measurement as would be possible if you used reproduction cost. You should carefully consider this issue when developing the appraisals and enhancing them for grading. There is not a specific requirement to use reproduction cost under this alternative; however, the report will be reviewed and graded based upon your ability to properly identify and measure any obsolescence that is present.

**10. I received a non-passing grade on my submission and wish to substitute another report for one or more of the reports. Can I do this?**

If your reports fail to meet technical requirements, you are allowed to revise and submit the same reports for regarding one time, addressing the areas outlined in the “Report to the Associate Member.” If you want to start over, you may submit three new reports.

**11. Why do I have to do yield capitalization under this alternative, yet it is not required under the traditional demonstration appraisal report alternative?**

The approval of this alternative by the board of directors was specifically linked to the general guidelines developed by the white paper group. This specific guideline was included to measure an Associate Member’s ability to apply current and appropriate techniques to the valuation of an income-producing property. Since many investors use yield capitalization, it is important for Associate Members to be able to demonstrate its appropriate use.

## **PART SIX**

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# Research Project Alternative

## **Introduction and Overview**

As an alternative to the traditional demonstration report detailed in Section II, a general Associate Member of the Appraisal Institute may submit a research project to meet the requirements of Regulation No. 1. If you want to submit a proposal for a research project, start by reading the rules for such a project in Regulation No. 1, Article III, Part E.

You must have sole professional responsibility for the development of the Research Project. You must personally and without assistance define the problem, develop the analysis, formulate the conclusions, and prepare the Research Project.

### **The Research Project Proposal: Documentation and Procedures**

Applications should provide a great deal of detailed information. Much of the work on the total project should go into the proposal.

*In those instances where the proposed Research Project is intended to expand the Body of Knowledge, the application should include, at a minimum:*

1. An exploration of why the proposed topic/hypothesis is important, what might be the implications of the findings, and what applications there might be for the results
2. Complete consideration of the processes of discovery, application and integration of the results of the research
3. Preliminary analysis and research into available resources including a thorough review of what work has previously been done by others in the particular area of research
4. Literature review

*In those instances where the proposed Research Project is a consultation prepared in accordance with Standards 4 and 5 of the current version of the Uniform Standards of Professional Appraisal Practice, the application should include, at a minimum:*

1. A detailed description of the property or properties that are the subject of the consultation
2. The nature of the consultation assignment
3. The scope and intended use of the consultation
4. The methodology proposed to accomplish the consultation

### **Research Project Proposal Submission Requirements**

1. The proposal must be written in standard business English such that it can be understood by the grader, using terminology from the current versions of *The Appraisal of Real Estate* and *The Dictionary of Real Estate Appraisal*.
2. The proposed Research Project must involve a practical real estate economics related topic/problem (not including one- to four-family properties).
3. The proposal must identify in sufficient detail the topic/thesis to be researched such that the project will demonstrate a thorough understanding of real estate economics.
4. The proposal must identify in detail the proposed methodology.
5. The proposal must identify in detail proposed resources and any possible applicable source literature. A bibliography should be included.
6. The proposal must outline the independent/original or primary research to be done. The Research Project Proposal may be supported by secondary research to assist in documentation of the proposal.
7. The proposal must set forth the proposed time frame for completion of the Research Project, not to exceed one year from the date the Associate Member is notified of the approval of the proposal.
8. The applicant shall submit three paper copies of the proposal together with a copy in digital format.

### **Initial Responsibilities of Grader upon Receipt of Topic Proposal**

1. The grader has 30 days after receipt of the proposal to provide a response on the topic proposal to Appraisal Institute staff, which in turn informs the Associate Member.
2. The grader is strongly advised to seek academic or specialty advice if the proposal is intended to expand the body of knowledge.
3. The grader will make one of the following recommendations:
  - a. Accept the proposed topic
  - b. Decline the proposed topic
  - c. Recommend modification and resubmission of the proposed topic

### **Research Project Requirements**

1. The Research Project must be written in standard business English such that it can be understood by the grader, using terminology from the current versions of *The Appraisal of Real Estate* and *The Dictionary of Real Estate Appraisal*.
2. Research Project must be “self-contained” that is, complete and thorough. The document must include the entire body of research data and analyses utilized to support the conclusions.
3. The Research Project report must be consistent with approved methodology of the Research Project proposal and be submitted within the approved time frame.
4. The Research Project report must contain, at a minimum:
  - a) An introduction/overview
  - b) A definition of the problem
  - c) Research methodology
  - d) Presentation of data
  - e) Discussion of analyses and findings
  - f) Conclusions
5. Two hard copies of the Research Project must be submitted to the Appraisal Institute along with a digital copy.
6. Submission of the Research Project to the Appraisal Institute for publication is optional at the discretion of the author, upon receipt of a passing grade as an alternative to the general demonstration report. If the project is published, the Associate Member may make no representations of acceptance by the Appraisal Institute and may not mention the Appraisal Institute’s acceptance of the report as a part of the general admissions requirements.

### **Procedures for Review of Research Project**

7. One copy is sent to a grader.
8. The grader’s decision to accept or revise is based on standard demonstration report grading process.
9. If the Research Project must be revised, the grader will provide a written summary of issues and deficiencies to be addressed in the revision.
10. The Associate Member has one year in which to revise and resubmit the Research Project. The Associate Member can revise the Research Project one time.
11. The review process for revised and resubmitted Research Project reports will follow the same procedure outlined above for the initial submission.
12. The grader has 30 days in which to complete each review and notify Appraisal Institute in writing of final results.

# Frequently Asked Questions Regarding The Research Project Alternative

## **1. What is the research project alternative?**

There are currently three alternatives available to Associate Members with respect to receiving credit for the demonstration report. The traditional demonstration appraisal report is still in place with two options; the three appraisal report alternative (TARA) and the research project alternative provide two remaining options.

The research project alternative was designed for Associate Members from the academic world as well as Associate Members from other parts of the world who live in countries where the economies make it impossible to do the traditional demonstration appraisal report or TARA. In addition, the research project alternative was developed to recognize the broader scope of analytical practices.

The research project alternative allows an Associate Member to receive credit for the demonstration report requirement by developing a research project under one of two essential types of projects—a consultation research project and an original research project. The consultation research project is a project developed and communicated in the style outlined in STANDARDS 4 and 5 of the current version of the *Uniform Standards of Professional Appraisal Practice*. The original research project is a project that expands the overall body of knowledge of the appraisal profession. In both cases, the proposed research project is to be of sufficient scope and complexity to demonstrate that the Associate Member has a thorough understanding of the principles, theories, techniques, and applications of real estate economics.

## **2. What type of topic can I chose?**

The focus of the project should be one that addresses a practical real estate economics topic or problem.

## **3. Are there any pre-approved topics?**

There are no currently pre-approved topics; however, the research project must not focus on one-to four-unit properties.

## **4. What is the process?**

First, the Associate Member must submit an application and topic proposal to the Appraisal Institute. After the topic proposal is accepted, the research project can be submitted for grading.

## **5. Why must I submit a proposal first?**

The foundation of this requirement is firmly entrenched in the academic world. The Appraisal Institute wants to be sure that your topic is meaningful and can adequately demonstrate a

thorough understanding of the principles, theories, techniques, and applications of real estate economics. The proposal will be initially reviewed by a grader who will either accept the proposal or offer feedback for possible changes. Once the proposal is accepted, the grader will give you final approval to complete and submit the research project.

**6. What must my consultation research project proposal contain?**

1. A detailed description of the property or properties that are the subject of the consultation
2. The nature of the consultation assignment
3. The scope and intended use of the consultation
4. The methodology proposed to accomplish the consultation

**7. What must my body of knowledge research project proposal contain?**

1. An exploration of why the proposed topic/hypothesis is important, the possible implications of the findings, and the possible applications of the results.
2. Complete consideration of the processes of discovery, application, and integration of the results of the research.
3. Preliminary analysis and research into available resources; what has already been done in the field?
4. Literature review

**8. How long should my proposal and research project be?**

There is not a specific requirement. The proposal and research project that follows must be described in sufficient detail for the grader to make an informed decision about its appropriateness. The proposal is a measurable component of the overall research project alternative. Your concern should be to present your proposal and research project in a way that communicates clearly and effectively. Clear communication allows the grader to have a pleasant experience. Poor presentation can interfere in the process of communication and lead to lower marks. Good presentation makes the most of the hard work that you put into your research.

**9. Can I get assistance with my research project?**

No. The Associate Member must have sole professional responsibility for the development of the research project. The research project may include work that is performed in the course of the Associate Member's business practice if the Associate Member personally, and without assistance, defined the problem, developed the analysis, formulated the conclusions, and prepared the project.

**10. Do I have to defend my research project?**

The term *research project* as used in this document and the Appraisal Institute literature should not be confused with a doctoral dissertation. The research project prepared by the Associate

Member is a rigorous and thorough analysis presented in a written document. The Associate Member will not be required to defend the research project orally.

**11. Is there a recommended format for the proposal and research project?**

The form and presentation of the proposal and the research project is left to the Associate Member. There are several publications and books available that could provide a meaningful outline. When developing a consultation research project, care should be taken to meet the requirements of the current edition of the *Uniform Standards of Professional Appraisal Practice* as well as the *Certification Standard* of the Appraisal Institute. International Valuation Standards may also be applicable.

**12. Can you give me some guidance as to what to include in my proposal?**

There is not one correct way to develop your proposal. Items to consider might be a statement of the problem and its setting, a review of related literature, the data, treatment of the data and its interpretation, the qualifications of the researcher, the outline of the proposed study, and a selected bibliography. In outlining the problem and its setting, it is important to give a clear statement of the problem and its potential subproblems. It is also important to state a clear hypothesis, the limitations of the study, any definitions pertinent to the assignment, a list of assumptions, and the importance of the study. The data should be outlined with both the primary and secondary data summarized. The research methodology and the specific treatment of each problem would be helpful as well.

**13. Why are proposals rejected or sent back for revisions?**

Generally, proposals have been sent back for revisions when the objectives are ill-defined, or the topic doesn't appear to be one in which the Associate Member could demonstrate a thorough understanding of the principles, theories, techniques, and applications of real estate economics.

**14. My proposal was accepted by the grader, but I have decided to select a different topic. Can I do this?**

Yes, however, a new proposal must be submitted and approved before continuing with the research project.

**15. Can I submit a research project that has already been published?**

No.