

# Acquisition in the Public Interest

by Norman H. Lee

Public real estate acquisitions are only undertaken in "the public interest." It is the intent of the appraisal assignment to arrive at a value that is "just compensation" to the landowner and is also fair to the public at large.

Unless otherwise stated, the purpose of an appraisal used to determine value for a public acquisition is to determine "market value," not the "value in use" to the acquiring agency. The proposed use of the land by the agency cannot be considered as its highest and best use, unless it can be clearly demonstrated that there is a competitive demand in the open market for that use.

## Highest and Best Use

The issue of highest and best use is addressed in federal and state appraisal policies and regulations, by appraisal industry standards and practices, and by Uniform Standards of Profession Appraisal Practice.

*Highest and best use cannot be predicated on a demand created solely by the project for which the property is taken ([for example, a] rock quarry, when [the] only market is [a] highway project for which [the] property was taken). A proposed highest and best use cannot be the use for which the government is acquiring the property ([such as a] missile test range, [or]*

*airfield park), unless there is a prospect and demand for that use by others than the government.<sup>1</sup>*

*The analysis and interpretation of highest and best use is an economic study of market forces focused on the subject property. The benefit a real estate development produces for a community or the amenity contribution provided by a planned project ([like] the public space in a park-like area) are not considered in the appraiser's analysis of highest and best use.<sup>2</sup>*

*In determining which uses are legally permissible and physically possible, an appraiser eliminates some uses from consideration. Then, the uses that meet the first two criteria are analyzed further to determine which are likely to produce an income, or return, equal to or greater than the amount needed to satisfy operating expenses, financial obligations and capital amortization. All uses that are expected to produce a positive return are regarded as financially feasible. Analyses of supply and demand and of location are needed to identify those uses that are financially feasible as well as the use that is maximally productive.*

*To determine financial feasibility, an appraiser estimates the future gross income that can be expected from each potential highest and best use.<sup>3</sup>*

*Of the financially feasible uses, the uses that produce the highest residual land value consistent with the rate of return warranted by the market for that use is the highest and best use.<sup>4</sup>*

The real estate market recognizes, and common sense dictates, that the lower the intensity of use for a property, the lower the value of the property. Yet, appraisers who attempt to arrive at a public interest or natural land value say that a property's value increases because of its low utility. This

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logic is not supported by the economic realities of the open real estate market.

### *Market Value*

The Uniform Appraisal Standards for Federal Land Acquisitions has existed for decades and is well grounded in case law. Case law and federal and state regulations have been the guiding factors in the real estate appraisal profession. This applies to all federal land acquisition practices, not just condemnation.<sup>5</sup> The UASFLA also requires an appraisal to be consistent with USPAP and 49 CFR 24.103,<sup>6</sup> which states:

*... (b) Influence of the project on just compensation. To the extent permitted by applicable law, the appraiser shall disregard any decrease or increase in the fair market value of the real property caused by the project for which the property is to be acquired, or by the likelihood that the property would be acquired for the project.*

The UASFLA also addresses comparable sales. The use of "forced sales" (made under some form of legal, as distinguished from economic) compulsion<sup>7</sup> is disallowed, as is the use of transactions involving the threat of condemnation. Transactions involving exchanges or a "typical motivation" (coercion sui generis) are unreliable. They should not be used unless they can be accurately weighed or adjusted to reflect the conditions of sale.<sup>8</sup>

The interpretation of "buyer and seller are typically motivated" raises some questions. It is very doubtful that a legislated purchase by a government agency could constitute a "typical motivation." That would be similar to saying that an acquisition for a highway project should be based on the sales of highways. Yet, some appraisers are using the sales of lands with very high intensity alternative uses as comparable sales, because the motivation of the buyer is to keep the property in a natural condition. The buyer of this property was most likely purchasing the property at its economic value. If the buyer has paid more for a tract than is reflected by the economic market value, it is the appraiser's job to determine if there was any duress. Normally sales to government entities would be precluded from use as market indicators because of the duress typically applied by threat of condemnation, pressure from lobbyists, or lack of exposure in the open market. When using sales to a governmental entity as comparable transactions, the presence of these factors would render the transaction suspect under the Standards.

A good example of duress is the Kachemak Bay acquisition by the state of Alaska. The seller had asked its corporate shareholders to write to the legislatures in support of the project. The seller also provided financial support to local environmental groups to lobby for the acquisition. The seller also threatened to close access to a fishery and to clear-cut a portion of the property if the state did not make the purchase.

All comparable sales data used in a market value determination for federal and state acquisitions shall meet the

*Please see Public Interest p. 31*



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definition of market value. Since the purpose of the appraisal is to determine market value of the subject, as reflected by open market transactions, the only acceptable comparable sales are those exposed to the open real estate market and meeting the definition of market value.

### *Public Interest*

All acquisitions by governmental agencies are driven by public interest. Without the motivation of public interest, there would not be any highways, water and sewer systems, electric and telephone utilities. It is not an appraiser's job to determine the need (public interest) of a project. Rather, it is the job of the appraiser to determine the value of the property as if it would sell on the open market.

Federal laws and policies have provision for the administrative branch to determine a public interest value. This is not the responsibility of the appraiser. For example, Section 1302(h)

of the Alaska National Interest Lands Conservation Act of 1980 states:

*... Exchanges shall be on the basis of equal value, either party to the exchange may pay or accept cash in order to equalize the value of the property exchanged, except that if the parties agree to an exchange and the Secretary determines it is in the public interest, such exchanges may be made for other than equal value.*

To reiterate and conclude, appraisals based on a premise of "public interest value" will not be accepted by federal agencies and the Exxon Valdez oil spill trustee council. It is not the appraiser's job to determine what an agency might pay for a property. It is the appraiser's job to determine what a property would sell for in the open real estate market. These standards also apply to appraisals submitted by property owners. Public interest value, if any, will be determined by the appropriate agency officer or legislative body, not

by the appraiser. Appraisers who follow these guidelines will not be in violation of USPAP. (See Jurisdictional Exception and Supplemental Standards in USPAP Section I, Introduction.)

1. Uniform Appraisal Standards for Federal Land Acquisition, 1992 (UASFLA), page 9
2. The Appraisal of Real Estate, Tenth Edition, page 276
3. *ibid.*, page 282
4. *ibid.*, page 282
5. UASFLA, *ibid.*, page 1
6. *ibid.*, page 64
7. *ibid.*, page 12
8. *ibid.*, page 13

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