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## **Valuation of assets with real estate and a business**

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Just what is the business component of an asset with real estate really worth? Some examples of properties that pose these valuation challenges are lodging facilities, restaurants, shopping malls, fitness clubs or other business enterprises with realty. Real estate appraisal and accounting methods are merging in this specialty that includes assets more complex than intuitively apparent.

Historically, real estate appraisers have often avoided dealing explicitly with the allocation of value into often called realty; furnishings, fixtures and equipment (FF & E); and goodwill. The words "inextricably intertwined" are sometimes used to glibly explain away the need to identify and value the parts comprising the whole. Estimating the value of "goodwill," "business value," "going concern value" and other semantically ambiguous and overlapping terms was left to the business appraisers and accountants or simply and implicitly included with the real estate. The result can be overvalued realty that does not reflect the contribution of high risk, tangible FF & E and even higher risk identified or unidentified intangibles that may be present.

Valuation models are evolving with the current Uniform Standards of Professional Appraisal Practice (USPAP), Interagency Guidelines and SBA requirements. They require an appraiser to identify any non-realty items and evaluate their impact on the "Total Assets of the Business." The explanation and dovetailing of the methods that accounting and appraisal professionals use are convincingly well-presented in a new Appraisal Institute course Separating Real Property, Personal Property and Intangible Business Assets. In my mind, some semantic overlaps and baffling ambiguity still exist with the terminology used by appraisers and accountants. But, the different appraiser and accountant methods for quantification of tangible personal property (FF & E) and intangible personal property (such as trained work force, trade names, non-realty contracts, innovations, and even tenant synergy, amongst others) are persuasive. They offer alternatives between the FASB standards of the accounting profession and the more economic, market based methods of appraisers.

What has historically been called "goodwill" is especially interesting, qualitatively and quantitatively. It has simplistically been a "catch all" for the value premium calculated by any difference between a cost approach threshold value and a higher income or sales comparison approach value. Now, however, we can refer to it as a final, residual, entrepreneurial value left after economic (market) returns to and of the real estate, tangible and any other intangible personal property have been "paid" by the enterprise. Goodwill and other intangibles are typically high risk, have limited life and require much higher discount rates than the real estate. It is easy to see the validity of that premise, but it can be a challenge to identify and evaluate the economic cost or return that those non-realty assets require.

A motivation for this dovetailing of accounting and appraisal valuation methods is the call for "mark to market" values on corporate balance sheets. Financial reporting usually reflects debt interest and

amortization, depreciation, and income taxes. The "marking" process for estimating balance sheet values at market value will provide a more real time and real world basis for corporate and lending community decisions and regulations.

Business and real estate valuation is becoming more sophisticated and interesting. USPAP, Interagency Guidelines and SBA appraisal requirements have enlarged the scope of research and analysis required for assets with real estate and business components. Appropriately educated and experienced real estate appraisers have a fine opportunity in this specialty. Working with accountants and experienced appraisers until comfortable and competent is a wise idea.

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