



Testimony

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Management, Committee on Energy and Natural
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FEDERAL LAND MANAGEMENT

Baca Ranch Appraisal Land Acquisition Issues

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G A O

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Mr. Chairman and Members of the Subcommittee:

We are pleased to be here today to present the results of our review of the appraisal for the Baca Location No. 1 (the Baca Ranch), a privately owned ranch covering almost 95,000 acres in northern New Mexico that the U.S. Department of Agriculture's Forest Service (the Service) wants to buy.¹ Our review was mandated by the Appropriations Act for the Department of the Interior and Related Agencies for fiscal year 2000.²

To establish a price for the ranch, the owners commissioned certified appraisers to appraise the property. Their appraisal, completed in September 1998, identified and evaluated sales of ranches considered to be comparable to the property and concluded that the fair market value of the Baca Ranch was \$1,061 per acre, or \$101 million in total. The Service reviewed the appraisal to assure that it complied with federal appraisal standards, which address the principles applicable to appraising property for federal acquisition.³ To facilitate its review of the appraisal, the Service commissioned a market study by another certified appraiser, completed in June 1998, that also identified and evaluated sales of ranches considered to be comparable to the Baca Ranch—although it was not an appraisal. Two Service appraisers used the market study when they reviewed the owner's appraisal and, in September 1999, found that the appraisal met federal standards and approved it. The Service and the owners signed a purchase agreement for the appraised value in October 1999. In November 1999, the Congress appropriated \$101 million for the purchase and required that authorizing legislation be enacted before the purchase can be completed.

Our review addressed (1) the extent to which the value established by the owner's appraisal was consistent with the comparable property sales data presented in the appraisal and in the Service's market study and (2) other key factors that influenced the appraisal's final outcome. In our review, we examined the owner's appraisal, the Service's appraisal review report, and the Service's market study. We also contracted with an independent and certified appraiser to

¹See *Federal Land Management: Land Acquisition Issues Related to the Baca Ranch Appraisal* (GAO/RCED-00-76, Mar. 2, 2000).

²P.L. 106-113 (Nov. 29, 1999).

³See *Uniform Appraisal Standards for Federal Land Acquisitions*, Interagency Land Acquisition Conference (1992). These standards were prepared to promote uniformity in the appraisal of real property among the various agencies acquiring property on behalf of the United States. The Interagency Land Acquisition Conference is chaired through the Department of Justice and composed of representatives of many federal agencies that acquire land.

conduct a desk review of the appraisal. Neither we nor the appraisal reviewer we contracted with attempted to reappraise the property. Because we were told by the owner's representative that the Baca Ranch was inaccessible due to winter conditions during the limited time available for our review, neither we nor the appraisal reviewer we contracted with visited it.

In summary, we found the following:

- Although the owner's appraisal of the Baca Ranch's value complied with federal appraisal standards, the appraised value is higher than supported solely by sales of comparable properties presented in the appraisal and in the Service's market study because it reflects a premium. In arriving at a value, the owner's appraisal identified sales of 16 large ranch properties located in New Mexico and Colorado that it considered comparable to the Baca Ranch in one or more ways, such as location, topographical features, and usage. On the basis of professional judgment, the owner's appraisers relied heavily on two higher-valued properties that they considered to be most comparable to estimate the Ranch's value of \$101 million. This value reflects a premium over what it would be if it were computed on the basis of all 16 comparable sales; for example, using a weighted average of these sales results in a value \$37 million lower than the appraised value. In reviewing the owner's appraisal, the Service's chief appraiser told us that he had questions about the value in the owner's appraisal until he made a visual inspection of the property, which led him to agree that a premium value was warranted because of the property's uniqueness.
- The Service's market study presents data on sales of 11 comparable properties (4 of which are also in the owner's appraisal) in New Mexico and southern Colorado that also support a range of lower values for the Baca Ranch—the high end of which is still \$37 million less than the appraised value. The appraisal reviewer we contracted with also found that the appraised value was higher than supported by information in the appraisal, which showed that some of the low-valued properties that the owner's appraisers did not use to calculate the Baca Ranch's value had similar characteristics and were comparable to the Baca Ranch. On the basis of our analysis of the comparable property sales data presented in the owner's appraisal and in the Service's market study, the government would pay a premium for the Baca Ranch if the value in the owner's appraisal is used to establish its price.

Mr. Chairman and Members of the Subcommittee, the appraised value of the Baca Ranch—as approved by the Forest Service—is higher than would be indicated if it were based solely on the sales prices of all the comparable properties. To develop this value, the appraisers applied their professional judgment and relied most heavily on two high-valued comparable properties, believing that the ranch would and should bring a premium price. As the Congress weighs its authorization decision, we believe it is important for you to be aware of this premium.

Background

Federal appraisal standards require that property to be acquired by the federal government be appraised at fair market value, which is the amount for which a property would be sold by a willing and knowledgeable seller with no obligation to sell to a willing and knowledgeable buyer with no obligation to buy. Determining fair market value requires the appraiser to first identify the property’s “highest and best use,” defined as the use that is physically possible, legally permissible, financially feasible, and maximally profitable for the owner. Appraisers must then use an accepted valuation approach; the sales comparison approach is generally considered to be the most reliable when sufficient market data are available. This approach estimates a property’s value by comparing it with other properties that have been sold, considering various factors—such as the location, size and other physical characteristics, and uses of the properties—to estimate the extent of comparability. A property’s size is one of the physical characteristics considered when comparing the sales of similar properties; other things being equal, smaller parcels of land tend to have higher per-acre values than larger parcels.

Federal appraisal standards also require, among other things, that appraisers collect, verify, analyze, and reconcile available data; identify and consider appropriate market information; use all pertinent information in developing the appraised value; and report their analyses, opinions, and conclusions clearly and accurately in a manner that is not misleading and that contains sufficient information to allow the report’s users to understand it properly. The standards generally address appraisal procedures and documentation rather than outcomes; different appraisers can consider the same data and follow the same methodology but develop different estimates of appraised values, because they apply different professional judgments, and still comply with the standards. The federal standards also state that it is essential for appraisers to visually inspect the properties they are appraising and the properties used as comparisons.

Data on Comparable Sales Support a Lower Value for the Baca Ranch

While the September 1998 owner's appraisal is consistent with federal appraisal standards, it presents data on comparable ranch properties that support a value for the Baca Ranch that is lower than \$101 million. The appraisal used the sales comparison approach to value the property as a "trophy ranch" that is used primarily for recreation. The appraisers first considered over 50 sales of properties as possible comparable sales, then narrowed the number to 16 large ranch properties located in New Mexico and Colorado that were more comparable to the Baca Ranch. These 16 properties had per-acre prices (adjusted to account for changes in land prices over time) ranging from \$2,908 per acre for 5,800 acres to \$196 per acre for 90,000 acres (the only property of the 16 that is approximately the same size as the Baca Ranch).

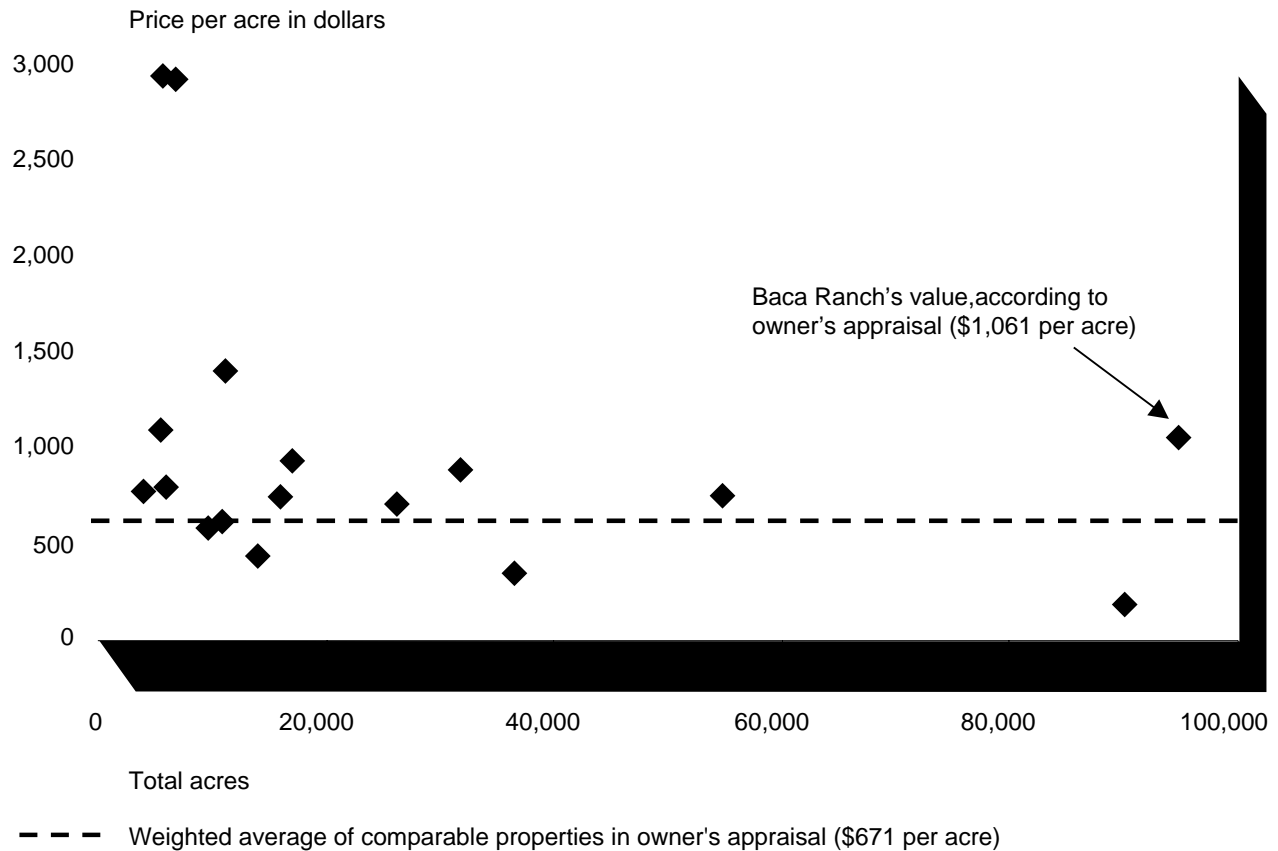
The appraisal further narrowed its consideration of comparable sales to five properties. Although these five properties were much smaller than the Baca Ranch (ranging from about 4,000 to 32,000 acres), they were considered to be the most relevant on the basis of other factors such as the date of sale, location, physical characteristics (other than size), and diversity of use. The appraisal estimated that the Baca Ranch's value fell between the values of two properties that it considered to be most comparable to the Baca Ranch in terms of location and usage: a property classified as superior at \$1,395 per acre for about 11,000 acres and a property classified as inferior at \$880 per acre for about 32,000 acres. The appraisal calculated the Baca Ranch's value by assigning 85 percent of the per-acre value to these two properties (40 percent and 45 percent, respectively) and the remaining 15 percent to the three lower-valued properties (5 percent each), resulting in the appraised value of \$1,061 per acre for the Baca Ranch.

By relying on the two high-valued properties, the appraisal resulted in a per-acre value that reflects a premium over what it would have been, had it been computed on the basis of all 16 sales of comparable properties. We computed the weighted average per-acre price for all 16 comparable ranches presented in the appraisal to be about \$670 per acre.⁴ Although a weighted average does not reflect all of the factors affecting a property's value, it shows that, on average, the value of the comparable properties is about \$390 lower per acre—and \$37 million lower, in total—than the appraised value of the Baca Ranch. Figure 1 shows the time-adjusted price per

⁴For the properties that the appraiser had not already adjusted, we adjusted the sale prices to reflect an increase in land values of 4 percent per year so that these data would be more comparable to those presented in the appraisal.

acre and the total acres for each of the 16 comparable properties, the weighted average price per acre for the 16 properties, and the appraised value of the Baca Ranch.

Figure 1: Price per Acre v. Total Acres for All 16 Comparable Property Sales Included in the Owner's Appraisal, the Weighted Average Price per Acre for These Sales, and the Appraised Value of the Baca Ranch



In reviewing and approving the Baca Ranch appraisal and the appraised value, two review appraisers in the Service verified that it was complete and accurate, that its analysis and conclusions were logical, and that it met federal appraisal standards. As part of their review, the review appraisers visually inspected the Ranch as well as other properties discussed in the appraisal. The Service also used the market study to define the market and identify sales of properties that would be relevant to the sale of the Baca Ranch. The market study used the sales comparison approach, analyzing sales of 11 ranch properties located in New Mexico and southern Colorado (ranging from about 2,000 acres to about 95,000 acres) and comparing them to the Baca Ranch on the basis of several factors—such as the property's location and size, the

presence of buildings or other improvements, and amenities such as trees and water.⁵ Using a valuation technique similar to that used in the appraisal, the study placed the Baca Ranch's value between a property with a price of \$670 per acre (for about 16,000 acres) and another with a price of \$400 (for about 24,000 acres); a third property, priced at about \$580 per acre (for about 11,000 acres), was judged to be equal to the Baca Ranch. These values range from about \$390 to \$660 per acre lower than the appraised value of the Baca Ranch and suggest a total price about \$37 million to \$63 million lower than the appraised value.

The Service's chief appraiser said that the market study was useful and saved him substantial time in reviewing the subsequent Baca Ranch appraisal because it provided verified market information about the characteristics and sales prices of relatively large western ranch properties. Furthermore, he said the study allowed the Service's managers to make an early assessment that the agency would probably be able to approve an appraisal—which had not yet been submitted to the Service—that would meet the price expectations of the Baca Ranch's owners. However, he also said that he did not consider the market study's values to be relevant to the appraisal because they were not supported by physical inspections. We acknowledge the importance of physical inspections in appraising property; however, even without such inspections, the market study provided market data on comparable properties that indicate a lower range of value than estimated in the owner's appraisal.

The appraisal reviewer we contracted with found that the owner's appraisal complies with professional appraisal standards;⁶ however, he disagreed with the appraisal's conclusion regarding the appraised value. He said that the information on comparable sales presented in the appraisal indicate that the appraised value should be lower, but he did not estimate how much lower that value should be because he did not reappraise or visually inspect the property.

The Baca Ranch's Uniqueness Was Cited as a Key Factor in Assigning It a Premium Value

The key factor that was cited by the appraisers as influencing their ultimate assessment of the property's premium value—and by the Service's chief appraiser as influencing his decision to

⁵Four of the 11 comparable properties identified in the Service's market study were also included in the 5 comparable properties identified as most relevant in the owner's appraisal.

accept it—was the Baca Ranch’s uniqueness. Specifically, the owner’s appraisal said that the Baca Ranch is a unique property—because of characteristics such as its location, size, scenery, and pristine appearance—and that purchasers of such “trophy ranches” as the Baca Ranch are willing to pay premium prices for uniqueness. Furthermore, the appraisal asserted that properties such as the Baca Ranch that range in size from 10,000 to 100,000 acres do not follow the usual size-price relationship in land—that is, as the amount of acreage increases, the price per acre decreases. As a result, the owner’s appraisers believe that the Baca Ranch’s size does not matter as much as its location, usage, and other physical characteristics do and that the property should bring a premium price because of these other factors. According to the owner’s appraisal, no properties are truly comparable to the Baca Ranch; therefore, the appraisers applied professional judgment and used qualitative analysis to eliminate most of the larger and low-valued comparable properties and instead rely on two smaller comparable properties to compute the appraised value. The appraisal then used the per-acre prices of these two relatively high-priced properties to estimate the per-acre value of the Baca Ranch and calculated the total appraised value by multiplying the per-acre value by the ranch’s acreage—a calculation that assumes that the property’s total value is directly based on its size.

The Service’s chief appraiser agreed with the owner’s appraisal that the Baca Ranch is unique and said that professional judgment was a key factor in his review and approval of the appraisal. He said that the appraised value for the Baca Ranch lies within the parameters of the existing market—that is, it lies within the range of comparable sales data that are presented in the appraisal. However, he also said that in his review of the appraisal, he was initially very concerned that the appraised value appeared to be too high, but then he visually inspected the Baca Ranch and the comparable properties. In seeing the properties firsthand, he said that on the basis of his professional judgment, the relatively high value given to the Baca Ranch in the appraisal was warranted. He did not provide more specific information about the basis for his professional judgment, however, to support his approval of the appraised value. He noted that an appraised value is only an estimate and that the actual market value of a property can reasonably be expected to vary as much as 10 percent either way.

⁹See *Uniform Standards of Professional Appraisal Practice*, The Appraisal Foundation (1998). These standards are incorporated by reference into federal appraisal standards.

The appraisal reviewer we contracted with disagreed with the basic premise of the owner's appraisal, namely, that the Baca Ranch is unique and therefore exempt from the usual size-price relationship. He said that the information presented in the appraisal did not conclusively demonstrate to him that the Baca Ranch is unique. For example, he noted that the appraisal presented no clear evidence that the Baca Ranch property is the only large property with streams, timber, and other amenities. He said that the appraisal provides information showing that some of the lower-valued properties it identified have physical characteristics that make them comparable to the Baca Ranch. For example, some of the properties also reflect values associated with keeping them undeveloped. Furthermore, he said that the sales of these comparable properties clearly demonstrate the usual size-price relationship—size matters—and that the size of the Baca Ranch is a relevant factor to consider in estimating its appraised value. For these reasons, he said that the comparable sales support a lower appraised value.

In closing, Mr. Chairman and Members of the Subcommittee, the value placed on the Baca Ranch by the owner's appraisal and agreed to by the Forest Service is higher than would be indicated if it were based solely on the sales prices of all the comparable properties. In arriving at this value, the appraisers applied their professional judgment and relied most heavily on two high-valued comparable properties, believing that the Baca Ranch would and should bring a premium price. Ultimately, the Congress will decide whether the federal government should acquire this property and whether the property warrants a premium price. In weighing its authorization decision, we believe it is important for the Congress to be aware of the significance of this premium in determining the property's appraised value.

Mr. Chairman, this concludes our testimony, and we would be happy to respond to any questions that you and the Members of the Subcommittee may have.

Contacts and Acknowledgements

For further information, please contact Barry T. Hill at (202) 512-3841. Individuals making key contributions to this testimony were Jennifer L. Duncan and Sue Ellen Naiberk.

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