



2600 Virginia Ave. N.W.  
Suite 123  
Washington, DC 20037

T 202-298-6449  
F 202-298-5547  
www.appraisalinstitute.org

October 23, 2002

Mr. Ronald Bew  
Associate Deputy Administrator  
Office of Capital Access  
Small Business Administration  
409 3<sup>rd</sup> Street, SW, Room 8200  
Washington, D.C. 20416

Dear Mr. Bew,

On behalf of the nearly 25,000 members of the Appraisal Institute and the American Society of Appraisers, this will call your attention to two issues of concern for our members regarding appraisal guidelines of the Small Business Administration. A response to our concerns would be appreciated.

**Issue 1: Going Concern Values**

Many SBA-backed loans are used to acquire businesses which consist of real estate, furniture, fixtures and equipment and what is known as "ongoing business value." Properties with these features include: restaurants, motels, bowling alleys, golf courses, car washes, lube centers, and the like.

An appraisal of this type of property determines a "going concern value." Because "going concern value" may include the business' value as well as personal property assets it should be differentiated from the value solely of the real property. Unfortunately, SBA Standing Operating Procedure (SOP) 50-10 fails to address this very important issue. Nowhere in the SOP is the "going concern value" discussed and there is no procedure or directive on how to treat this type of property.

SBA is faced with a very serious problem -- appraisers are oftentimes hired to value this type of property, yet sometimes they incorrectly state that the appraised value is of the real property, when they have accounted for the business' value and personal property assets as well. Subsequently, the lender makes the loan believing that they have issued a loan on the real property only. If the business fails, another appraisal is ordered, and the value may be reported as much as 50% less than the original appraisal prepared by another appraiser because there is now no business or "going concern value" associated with the real property.

A key question SBA should address is whether or not it wants appraisals to reflect the going concern or just the real property? The SOP needs to clarify for both lenders and appraisers what value it requires. Once that is clarified, the SBA needs to ensure that qualified appraisers are used for these valuations. One way SBA might address this problem is to modify its appraiser qualifications to require appraisers who provide "going concern" appraisals to demonstrate experience and education relevant to such assignments.

The Appraisal Institute Course 800 currently deals with separating real and personal property assets. It provides the theoretical and analytical framework for separating the tangible and intangible assets of operating properties. Through discussion, lecture, readings, role-playing and case studies, participants actively solve problems related to “going concern value.” ASA also has practitioners specializing in personal property and business valuation that can be relied on for such assignments.

Additionally, SBA could place greater emphasis on holding lenders and appraisers accountable when they do not adhere to these guidelines. Recently, the SBA incurred losses on loans where the appraisals were significantly inflated, improperly underwritten or misunderstood by the lender. When a business fails, the only collateral left is the real estate, and that value appears significantly lower because of the going concern issue stated above. Situations like these can contribute to significant losses to SBA programs, and this issue warrants the attention of SBA.

### **Issue 2: SOP 50-10 Appraisal Guideline Inconsistencies**

We have a concern with language in SOP 50-10 which states that loans under \$1,000,000 require a “Limited Appraisal” while loans over \$1,000,000 must have a “Complete Appraisal.”

To an appraiser, the terms “limited appraisal” and “complete appraisal” do not fully explain the assignment absent further instructions. According to our members, the lack of guidance in this area causes confusion amongst appraisers regarding the kind of complete appraisal SBA requires. This problem is made worse by non-regulated lenders and small banks that do not have compliance departments experienced with the *Uniform Standards of Professional Appraisal Practice (USPAP)* and the appraisal process.

According to USPAP, there are three types of appraisal reports: *Self Contained*, *Summary* and *Restricted Use*. There are two types of *appraisals*, Complete and Limited. “Limited Appraisals” are appraisals that usually involve the elimination of one or more of the three traditional approaches to value. The key difference is that the term “Complete Appraisal” means that there are no such Departures from USPAP.

The issue to be addressed by the SBA is whether a “Complete Appraisal” means a Self Contained Report of a Complete Appraisal or a Summary Report of a Complete Appraisal (the Restricted Use option would not apply to SBA loans). Clarification is also needed on whether the reference to a “Limited Appraisal” means a Summary Report of a Limited Appraisal.

SBA might address this issue in two specific ways:

- 1) SBA could review the different types of appraisals and appraisal reports to determine which will provide sufficient detail for the SBA and other intended users in making sound lending decisions. SBA should then amend the SOP 50-10 to give lenders and appraisers further guidance on the new SBA complete appraisal requirement. One such policy could require a “Summary Report of a Complete Appraisal” appraisal for loans under \$1,000,000 and a “Self-Contained Report of a Complete Appraisal” for loans greater than \$1,000,000.
- 2) Another option would be for SBA to require strict compliance with USPAP and allow the appraiser and the client to decide the level of appraisal and type of report appropriate, doing

away with a loan-appraisal threshold entirely. Under these circumstances, the type of appraisal (complete or limited) would be based upon the purpose and intended use of the appraisal report. The appraiser's "scope of work" would subsequently define what is to be done in the development of the appraisal.

We hope that you consider these suggestions during the course of improving SBA lending programs, and we would very much like to work with you on this. In the coming weeks, our Washington office will contact you to arrange a meeting with you and your staff. Should you have any questions, please contact Donald Kelly, Vice President of Public Affairs, Appraisal Institute at 202-298-5583, [dkelly@appraisalinstitute.org](mailto:dkelly@appraisalinstitute.org) or Ted Baker, Executive Vice President, American Society of Appraisers at 703-733-2199, [tbaker@appraisers.org](mailto:tbaker@appraisers.org).

Sincerely,



Thomas A. Motta, MAI, SRA  
President  
Appraisal Institute



John Connolly, ASA  
President  
American Society of Appraisers

Cc: Representative Donald Manzullo, Chair, House Committee on Small Business  
Senator John F. Kerry, Chair, Senate Committee on Small Business  
Representative Nydia M. Velasquez, Ranking Member, House Committee on Small Business  
Senator Christopher "Kit" Bond, Ranking Member, Senate Committee on Small Business  
Mr. James Hammersley, Director, Loan Programs Division, SBA