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DETERMINING FAIR MARKET VALUE


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One of the great challenges in a recessionary cycle is reconciling the apparent contradiction between property values disproportionately impacted by the short-term realities of a lean marketplace and a more balanced and nuanced assessment of long-term value. In a condemnation setting, the legal, practical and logistical difficulties of assessing value in a way that is fair and reasonable becomes particularly problematic.

Questions and concerns surrounding property valuation with regard to condemnation proceedings have become particularly relevant in the context of recent economic challenges. Residential values have fallen anywhere from 30 to 60 percent of the peak registered just a few years ago. While those values may have been somewhat inflated, the subsequent drops have been precipitous. Recently, the decline in residential values has spilled over into commercial properties. In the past 6 months, previously flat retail/commercial rental rates have fallen as much as 35 percent; the widening gap between fixed costs and decreasing rents has contributed to even more substantial losses in value.

Difficulty in assigning fair value in a condemnation setting arises as a result of existing procedures regarding how and when value is assigned. Because most jurisdictions identify a specific date for the transfer of title and property values are subsequently assessed based on that specific date, there is greater potential for an artificially low value assessment based on what may be an unfavorable “snapshot” in time.

By way of contrast, consider theAmerican Institute of Appraisers' definition of market value.The definition, which isrequired of U.S. lending institutions, isthe price that a property should bring in a competitive and open market under all conditions requisite to a fair sale, the buyer and seller each acting prudently and knowledgeably, and assuming the price is not affected by undue stimulus. This definition assumes that the buyer and seller are typically well-motivated, both parties are well-informed and acting in their best interests, and areasonable time is allowed for exposure in the open market. The market value guidelines also require that payment is made in U.S dollars or in comparable financialarrangements, and the price represents in unaffected bycreative financing or sales concessions.

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These underlying assumptions make sense in a stable and healthy economic environment, but they are less applicable in a recession or depression. The conditions are frequently compromised, absent or do not apply in an eminent domain dynamic. In such a position, sellers are clearly not "typically motivated," they are infrequently acting in their best interests, and financing options are much more likely to be limited. Fair market options are not available in a condemnation setting and are further compromised by a weak marketplace.

Eminent domain is perceived to be a harsh remedy in many jurisdictions; protections are often afforded to the owner who is dispossessed of his or her property.In these situations, the disconnect between the stated intention to deliver fair market value and the practical realities of doing so in a lean economy becomes even more noticeable. Since the landmark Kelo v. City of New London decision, dozens of states haveresponded byenacting state-specific legislative reforms that place significant limits on the power of municipalities to invoke eminent domain for economic development. Given that public sentiment and legislative momentum, the fact that there seems to be a disparity between legislative intent and the procedural and financial realities on the ground is even more worrying.

Concerns regarding the existing process for determining fair market value in a condemnation setting during a recession could be easily resolved. Straightforward legislative remedies, for example, could limit restrictions on loans or offer prospective lenders some type of guarantee. While preserving the integrity of market value that must be fundamentally based on supply and demand is a valid concern, any short-term interference in that balance would be quickly diluted by the tidal power of the marketplace. Of far greater concern to many is the obligation to provide fair valuations in a condemnation setting. Fundamentally, the underlying premise of fair market value is that property is sold without compulsion. To conclude that the sale must be made on a particular date could, for many owners, severely endanger the opportunity to receive just compensation, simply because they are not willing sellers in the marketplace.

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