



U.S. Department of Agriculture  
Office of Inspector General  
Southwest Region  
Audit Report

Forest Service  
Forest Legacy Program -  
The Hancock Tract



Report No.  
08099-11-Te  
APRIL 2001



UNITED STATES DEPARTMENT OF AGRICULTURE

OFFICE OF INSPECTOR GENERAL

Washington D.C. 20250



DATE: April 27, 2001

REPLY TO  
ATTN OF: 08099-11-Te

SUBJECT: Forest Service – Forest Legacy Program: The Hancock Tract

TO: Dale Bosworth  
Chief  
Forest Service

ATTN: Linda Washington  
Audit Liaison

This report presents the results of our audit of the Forest Service – Forest Legacy Program: The Hancock Tract. Forest Service's (FS) written response to the draft report is included as exhibit B and FS's comments and OIG's position concerning the written response are set forth in the audit finding.

We agreed with FS's planned action in their response; however, additional conditions are needed to reach a management decision on the audit recommendation. The conditions needed to reach an agreement are set forth in the finding and recommendation section of the report.

In accordance with Department Regulation 1720-1, please furnish a reply within 60 days describing corrective actions taken or planned and the timeframe for implementing the recommendations for which management decisions have not yet been reached. Please note that the regulation requires management decisions to be reached on all findings and recommendations within a maximum of 6 months from report issuance. Please follow your internal agency procedures in forwarding final action to the Office of the Chief Financial Officer.

/s/ J. R. Ebbitt

JAMES R. EBBITT  
Assistant Inspector General  
for Audit

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# EXECUTIVE SUMMARY

## FOREST SERVICE FOREST LEGACY PROGRAM – THE HANCOCK TRACT

REPORT NO. 08099-11-Te

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### RESULTS IN BRIEF

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We performed this audit based on a hotline complaint. The objective was to determine why the State of Vermont paid more than the appraised value of \$1.4 million for a conservation easement. We found that the purchase of the conservation easement of the Hancock Tract in the State of Vermont did not meet a statutory requirement of the Forest Legacy Program (FLP). The appraisal of the property, which is the basis of the amount paid by the Forest Service (FS), did not meet Federal appraisal standards. This occurred because the FS, without adequate justification, accepted an appraisal of the property that appeared to more closely represent the price that the property owner desired. The FS own appraisal valued the property at \$1.1 million less than the subsequent appraisal accepted by the FS.

As a result of the FS actions, \$1.1 million was spent without adequate justification and the FS created an appearance of preferential treatment being given to the seller of the easement.

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### KEY RECOMMENDATIONS

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We recommend that the FS recover \$1.1 million from Vermont representing the difference between the \$2.5 million appraisal that was not in accordance with Federal appraisal standards and the \$1.4 million appraisal that was in accordance with Federal appraisal standards.

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### AGENCY RESPONSE

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The FS did not concur with our recommendation to recover \$1.1 million from the State of Vermont. Instead, they proposed that another qualified appraiser conduct a new appraisal to make a final determination of the value of the property rights acquired under this acquisition. The FS agreed that if the new appraisal determines a lower value than what FS paid (\$2.5 million), the agency would seek to recover the difference in these values.

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## **OIG POSITION**

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We agreed with the FS's planned action in their response; however, additional conditions are needed to reach a management decision on the audit recommendation. The conditions needed to reach an agreement are set forth in the findings and recommendations section of the report.

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# INTRODUCTION

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## BACKGROUND

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The Forest Legacy Program<sup>1</sup> (FLP) was enacted as part of the Cooperative Forestry Assistance Act for the purposes of ascertaining and protecting environmentally important forest areas that are threatened by conversion to nonforest uses and, through the use of conservation easements and other mechanisms, for promoting forest land protection and other conservation opportunities. Such purposes are also required to include the protection of important scenic, cultural, fish, wildlife, and recreational resources, riparian areas, and other ecological values. In 1996, the FLP was amended to authorize the Secretary to make grants to States to carry out the FLP, including the acquisition by the State of lands and interests in lands. In August 1996, the FS published implementation guidelines for the FLP; however, the guidelines were not codified in the Code of Federal Regulations (CFR) and, therefore, are not legally binding.

In March 1998, we received a hotline complaint. The complainant believed that the State of Vermont used Federal FLP funds to pay \$2.9 million for a conservation easement appraised at \$1.4 million. The easement was on property owned by John Hancock Mutual Life Insurance Company (Hancock) consisting of 31,493 noncontiguous acres of timberland in 9 individual timber tracts that are comprised of 15 separate lot numbers (The Hancock Tract). The complainant also stated that the State of Vermont influenced the appraiser to come up with an appraisal to justify the amount the State had already agreed to pay Hancock.

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## OBJECTIVE

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The objective was to determine why the State of Vermont paid more than the appraised value of \$1.4 million for the conservation easement.

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## SCOPE

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The activity audited was the acquisition of a conservation easement on The Hancock Tract in Vermont for the FLP. The period of audit coverage was from February 1994 until December 1996. The audit fieldwork was performed at the offices of the FS Northeastern Area for State and Private Forestry in Newtown Square, Pennsylvania, and the Vermont Department of Forest and Parks, Waterbury, Vermont. The audit fieldwork was performed from March 1998 until October 2000. A delay in the performance of the audit occurred from August 1999 until February 2000 due to the reassignment of personnel.

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<sup>1</sup> Title 16, United States Code (USC), 2103c.

In fiscal year (FY) 1996, congressional appropriations for the nationwide FLP were \$3 million. The Hancock Tract acquisition used \$2.5 million of this appropriation.

This audit was performed in accordance with Government Auditing Standards issued by the Comptroller General of the United States.

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## **METHODOLOGY**

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We obtained documentary evidence, such as correspondence, memoranda, records of telephone conversations, and e-mails, of the actions of United States Department of Agriculture personnel from the FS files. We also obtained testimonial evidence from the FS and Office of the General Counsel personnel. We obtained additional testimonial evidence of the circumstances surrounding the contract appraisal for The Hancock Tract from Vermont officials, the contract appraiser, and the contract review appraiser. Auditors also developed analytical evidence during the audit.

The FS National Forest System Chief Appraiser performed an appraisal review, in accordance with Federal appraisal standards, and prepared a report on his professional opinion of whether the appraisal performed under contract from Vermont of The Hancock Tract met Federal appraisal standards. Also, although there are no provisions in the Federal appraisal standards for a second-party review of an appraisal review, we requested that a FS senior review appraiser from the Green Mountain National Forest in Vermont review the appraisal review to determine if it met the Uniform Standards for Professional Appraisal Practice (USPAP).

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# FINDINGS AND RECOMMENDATIONS

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## CHAPTER 1

### THE BASIS FOR CONSERVATION EASEMENT PURCHASE DID NOT MEET FEDERAL APPRAISAL STANDARDS

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#### FINDING NO. 1

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The State of Vermont used Federal funds to pay an amount in excess of fair market value for a conservation easement for the FLP. This occurred because the State used an appraisal that did not meet Federal appraisal standards, a statutory requirement of the FLP, after Hancock rejected an appraisal of \$1.4 million that met Federal appraisal standards. The rejection occurred because agency officials had made statements that gave Hancock the expectation that its value demands (\$2.5 million) would be met. As a result, the FS paid \$1.1 million in excess of the appraised value for the conservation easement.

The FLP statute<sup>2</sup> requires that compensation for conservation easements be paid in accordance with Federal appraisal standards.<sup>3</sup> Included in the Federal appraisal standards are Standards A-3, Highest and Best Use; A-9, Conjectural and Speculative Evidence; and C-8, Appraisal Review:

Standard A-3, Highest and Best Use. Fair market value is to be determined with reference to the property's "highest and best use," that is, the highest and most profitable use for which the property is adaptable and needed or likely to be needed in the near future. Ordinarily, the highest and best use of property is the use to which it is being subjected at the time of the taking;<sup>4</sup> however, if the property is clearly adaptable to a use other than the existing use, its marketable potential for such use should be considered in determining the property's fair market value.<sup>5</sup> However, just compensation cannot be predicated upon potential uses that are speculative and conjectural.

Standard A-9, Conjectural and Speculative Evidence. In seeking to determine the fair market value, that is, the amount that in all probability would have been arrived at by fair negotiation between an owner willing to sell and a purchaser desiring to buy, there should be taken into account all

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<sup>2</sup> Title 16, USC, 2103c(j)(1).

<sup>3</sup> Uniform Appraisal Standards for Federal Land Acquisitions, published in March 1992 by the Interagency Land Acquisition Conference.

<sup>4</sup> United States v. Buhler, 305 F.2d 319, 328 (5<sup>th</sup> Cir. 1962). There is a presumption in favor of the existing use: United States v. 8.41 Acres of Land, Etc., 680 F.2d 388, 394 (5<sup>th</sup> Cir. 1982); United States v. 158.24 Acres of Land, Etc., 515 F.2d 230, 233 (5<sup>th</sup> Cir. C975).

<sup>5</sup> Olson v. United States, 292 U.S. 246, 255 (1934).

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considerations that fairly might be brought forward and reasonably be given substantial weight in such bargaining. However, in the words of the Supreme Court of the United States "Elements affecting value that depend upon events or combinations of occurrences which, while within the realm of possibility, are not fairly shown to be reasonably probable, should be excluded from consideration, for that would be to allow mere speculation and conjecture to become a guide for the ascertainment of value--a thing to be condemned in business transactions as well as in judicial ascertainment of truth \* \* \* ."6

Standard C-8, Appraisal Review. The review of appraisal reports by a qualified reviewing appraiser is required. The minimum requirements for an appraisal review process are found in 49 CFR 24.104. In addition, standards for appraisal review established by The Appraisal Foundation<sup>7</sup> should be considered a minimum requirement for reviewing an appraisal and reporting the results thereof. In accordance with the foregoing, prior to the adoption of an appraisal of property having more than token value, the reviewing appraiser should attach to the appraisal the written review report or review memorandum indicating the scope of his or her review and supporting the action recommended. It is the review appraiser's responsibility to determine whether the appraisal is adequately supported, whether it complies with recognized appraisal principles and practices, these standards, and whether it conforms to governing legal premises as prescribed by legal counsel.

The crux of the difference between the two easement amounts was the determination of the Highest and Best Use-Before Value (HBU-BV). The appraisal that met Federal appraisal standards stated the HBU-BV as timber production. However, the appraisal that did not meet Federal appraisal standards stated the HBU-BV was as a midterm investment or as a purchase to liquidate the timber. The Vermont contract appraiser made this decision even though long-term timber production was the purpose for which the land had been purchased by Hancock, and 7 of the 9 sales used by the Vermont contract appraiser, and all sales of over 9,000 acres, were for long-term timber production. This decision raised the appraised value of The Hancock Tract from \$6.5 million to \$7.907 million **before the application of the conservation easement**. This, in turn, raised the value of the conservation easement from \$1.4 million to \$3.051 million.

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<sup>6</sup> Olson v. United States, 292 U.S. 246, 257 (1934) (emphasis added). See also discussion in United States v. 320.0 Acres of Land, 605 F.2d 762, 814-820 (5th Cir. 1979).

Uniform Standards of Professional Appraisal Practice (The Appraisal Foundation, 1990), Standard 3.

After The Hancock Tract was appraised at \$1.4 million and Hancock refused an offer for the tract for \$1.4 million, the Vermont Governor contacted the Secretary of Agriculture. The Undersecretary for Natural Resources and Environment became involved to resolve the issue, and the FS allocated \$2.5 million (with plans for another \$300,000 from the State) for The Hancock Tract acquisition and entered into negotiations with Hancock designed to meet the price demanded by the company, which was \$2.75 million.

On December 17, 1998, the FS Chief Appraiser completed an appraisal review of the appraisal dated August 29, 1996, and supplemented October 10, 1996, of The Hancock Tract. The Chief Appraiser stated the purpose of his review was to determine whether the appraisal met the Uniform Appraisal Standards for Federal Land Acquisitions and the USPAP. The appraisal review reported the following:

- Valuation – Before, Highest and Best Use: The reviewer’s comment states the appraiser cites nine sales in his analysis of the subject property. These sales range in size from 4,351 acres to 58,800 acres. With the exception of sales 1 and 3, all of the properties were purchased for long-term timber production. Sales 1 and 3, at 7,040 acres and 9,000 acres, were, according to the appraiser, purchased for liquidation. All sales over 9,000 acres were purchased for long-term timber production. Further, the subject has been in use for industrial timberland for many years.<sup>8</sup> Finally, the last sale of the subject, as part of a 238,000-acre transaction (October 1993), was for long-term timber production. The appraiser does not present sufficient evidence to support his conclusion of highest and best use according to Federal standards. The sales presented indicated a highest and best use of long-term timber production.

The appraisal review also questioned the valuation analysis of the highest and best use that the appraiser had decided. In using the sales comparison approach of valuation, the reviewer stated that “Generally, the adjustments made to the several sales are inadequately supported by direct market evidence. \* \* \* The appraiser’s methodology is flawed, and could be misleading.”

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<sup>8</sup> “Ordinarily, the highest and best use of property is the use to which it is being subjected at the time of taking. However, if the property is clearly adaptable to a use other than the existing use, its marketable potential for such use should be considered in determining the property’s fair market value. However, just compensation cannot be predicated upon potential uses that are speculative and conjectural \* \* \*. A proposed highest and best use requires a showing of reasonable probability that the land is both physically adaptable for such use **and** that there is a need or demand for such use in the reasonably near future.” Interagency Land Acquisition Conference, *Uniform Appraisal Standards for Federal Land Acquisitions* (U.S. Government Printing Office, 1992), pages 8-9.

In his use of the income approach to valuing the highest and best use, the reviewer stated “The appraiser does not support his selection of 12% as an appropriate discount rate. \* \* \*To the reviewer’s knowledge, there is little indication of significant demand for Norton Pond lots. Further, the appraiser does not address land use control law, which would significantly hamper a developer of this waterfront. Similarly, the appraiser does not support his resale estimates for the various timberland parcels and the 12% discount rate is not based on market evidence.”

- Valuation – After the conservation easement. The reviewer analysis of the sales comparison approach states “As in the before condition, the adjustments are not generally supported by market data, but are based on the appraiser’s judgment.”

In the appraiser's use of the income approach, the reviewer states “The appraiser cited various bond rates and interviews with market participants, but no direct market evidence is presented to support the selected rate of 7.5%. Without better support for this rate, it is difficult to support a value conclusion by this method.”

The FS Chief Appraiser in the summary comments of his appraisal review stated that the crux of an appraisal problem, particularly an appraisal problem involving a before and after value for a conservation easement, is the analysis of highest and best use. According to the appraisal review, the appraiser concluded a highest and best use in the before condition of midterm investor or liquidation. However, the property’s past history and other sales in excess of 10,000 acres all suggest long-term timber production is the property’s highest and best use. According to the appraisal review, the appraiser should have utilized a similar income approach in the before condition as was applied in the after condition. Utilizing the appraiser’s numbers, and discounting the property’s timber income over the next 30 years to the present at 6 percent (the rate indicated by the appraiser for noneasement encumbered properties), a value of \$6,127,502 is indicated for the before condition. Comparison of this figure to the appraiser’s final value estimate in the after condition of \$4,856,252 indicates a conservation easement value of \$1,271,250.

The appraisal review by the FS Chief Appraiser concluded that the appraisal report did not meet Federal standards and did not adequately support the estimated value conclusions. The appraisal review also concluded that the appraiser’s assumption that the imposition of a conservation easement changes the highest and best use of the subject property from a midterm timber investment or liquidation to a long-term timber investment is not adequately supported in the before condition. Therefore, according to the appraisal review, the appraiser’s assumption falls and the analysis falls with it.

The review appraiser’s report stated that the appraisal was “\* \* \* prepared in accordance with the Federal and State regulations applicable to acquisitions of lands with Federal funds.” An initial review by a FS senior review appraiser of the contracted review appraiser’s report concluded that it did not meet the minimum requirements of the USPAP. On May 25, 2000, the contracted review appraiser

was provided with a copy of the comments and asked to respond. On June 14, 2000, the contracted review appraiser responded that it may be technically correct that he did not comply with all aspects of USPAP, but he used the same procedure and format that he had used for years in review of appraisals for right-of-way acquisitions for Federal highway projects. He was of the opinion that it substantially satisfied the State and Federal appraisal requirements.

Additionally, we requested a response from the Vermont contract appraiser to address the appraisal review. He stated that his appraisal did not disclose that he relied upon confidential information provided by Hancock and that Hancock's investment horizons were midterm (3-10 years), even though publicly they maintained the investment model was long-term.

The FS did not concur with the conclusion that the appraisal did not meet Federal appraisal standards. Their response (exhibit B) stated that the difference in the value between the Federal appraisal and State appraisal was a result of "different assumptions" made by the appraisers. They concluded that there was adequate justification for the State to believe their value complied with Federal appraisal standards.

We agree that the reason for the difference in the valuation was a difference in assumptions of the highest and best use of the property being acquired. However, the reason for the different assumptions was the fact that market evidence presented in the State appraisal did not support the highest and best use conclusion used to obtain the higher valuation. The fact that the market evidence did not support this key assumption was the primary reason that valuation did not meet Federal appraisal standards. The determination of highest and best use is the single most important factor in making any determination of a property's value.

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## **RECOMMENDATION NO. 1**

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Recover \$1.1 million from Vermont representing the difference between the \$2.5 million appraisal that was not in accordance with Federal appraisal standards and the \$1.4 million appraisal that was in accordance with Federal appraisal standards.

### **ES Response**

The FS did not concur with our recommendation to recover \$1.1 million from the State of Vermont. Instead, they proposed that another qualified appraiser conduct a new appraisal to make a final determination of the value of the property rights acquired under this acquisition. The FS agreed that if the new appraisal determines a lower value than what FS paid (\$2.5 million), the agency would seek to recover the difference in these values. (See exhibit B for complete FS response.)

## **OIG Position**

We can accept management decision if the following conditions are met:

1. The instructions provided to the new appraiser must be reviewed and agreed to by both FS and the State of Vermont. A copy of the instructions (in draft) will be provided to the Office of Inspector General.
2. The instruction must ensure that property rights appraised are the same as those that were actually acquired.
3. The appraiser selected to conduct the new appraisal must be acceptable to both the State of Vermont and the current FS Chief Appraiser.
4. A copy of the prior appraisal, the FS review of the appraisal, and a copy of this report must be provided to the new appraiser.
5. A qualified review appraiser, agreeable to both the FS and the State of Vermont, must review the new appraisal to ensure it meets Federal appraisal standards.

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**EXHIBIT A – SUMMARY OF MONETARY RESULTS**

<b>FINDING NUMBER</b>	<b>REC. NUMBER</b>	<b>DESCRIPTION</b>	<b>AMOUNT</b>	<b>CATEGORY</b>
1	1	Difference between \$2.5 million appraisal not in accordance with Federal appraisal standards and \$1.4 million appraisal that was in accordance with Federal appraisal standards.	\$1,100,000	Unsupported Costs, Recovery Recommended
<b>TOTAL</b>			<b>\$1,100,000</b>	

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# EXHIBIT B – AUDITEE RESPONSE TO DRAFT REPORT



United States  
Department of  
Agriculture

Forest  
Service

Washington Office

14<sup>th</sup> & Independence SW  
P.O. Box 96090  
Washington, DC 20090-6090

File Code: 1430  
Route To: (3000/5100)

Date: MAR 30 2001

Subject: Office of Inspector General Discussion Draft Report, "Forest Service – Forest Legacy Program: The Hancock Tract," Report No. 08099-11-Te

To: James R. Ebbitt  
Assistant Inspector General for Audit  
Office of Inspector General

We have completed our review of the Office of Inspector General (OIG) Discussion Draft Report, "Forest Service – Forest Legacy Program: The Hancock Tract," Dated February 13, 2001, Report No. 08099-11-Te.

Enclosed is our response to the OIG report. If you have questions, please contact Linda Washington, the External Audit Liaison, on (202) 205-3761.

VINCETTE L. GOERL  
Chief Financial Officer  
Deputy Chief, Office of Finance



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**United States Department of Agriculture  
Forest Service**

**Office of Inspector General (OIG)**

**Forest Service-Forest Legacy Program:  
The Hancock Tract**

**March 19, 2001**

**Forest Service (FS) Review Comments**

**GENERAL COMMENTS**

The final appraisal of the Hancock Tract by the State of Vermont was based on stipulations that differed from the original appraisal conducted by the USDA Forest Service. The final appraisal, accomplished under the "State Grant Option" for the Forest Legacy Program, was conducted using standard Federal Appraisal Guidelines. Accordingly, there was adequate justification, at least in the view of the State of Vermont, for the appraisal value of \$2.5 million.

The values for the two appraisals are based on different assumptions. Accordingly, it is not correct to draw conclusions that may be interpreted as negative.

The issue in this case must be based on whether or not the State of Vermont followed Federal Appraisal Guidelines. The narrative in the SF-424, Federal Financial Assistance, clearly states that these guides must be followed. However, because of perceived bias by the Forest Service toward the State of Vermont regarding this specific tract, the interpretation of whether or not the guidelines were followed would best be determined by an independent, neutral third party.

Thus, the agency proposes that conclusionary language that may be potentially negative, and in the final analysis not factual, be stricken from this section. Further, that an independent, neutral appraiser, agreed to by the State of Vermont and the USDA Forest Service, be appointed to review the adherence to Federal Appraisal Guidelines in the final appraisal of the Hancock Tract. Until this occurs the Forest does not agree with the Summary of Monetary Results.

If the findings of the independent, neutral appraiser conclude that the guidelines were followed, the case will be closed with a formal letter provided to the agency and the State of Vermont.

If the findings conclude that the guidelines were not adhered to, resulting in a different appraisal value, the USDA Forest Service will acknowledge these findings and seek to recover the difference between the final appraisal of the Hancock Tract (\$2.5 million) and the new appraisal from the independent, neutral appraiser.

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**OIG RECOMMENDATION NO. 1:**

Recover \$1.1 million from Vermont representing the difference between the \$2.5 million appraisal that was not in accordance with Federal appraisal standards and the \$1.4 million appraisal that was in accordance with Federal appraisal standards.

**FOREST SERVICE RESPONSE RECOMMENDATION NO. 1:**

Forest Service does not concur with this recommendation. For a variety of reasons, professional bias surfaced between the USDA Forest Service and the State of Vermont regarding the Hancock Tract. Accordingly, any results of the USDA Forest Service appraisers in determining whether the appraisal performed by Vermont met Federal Appraisal Guidelines will be viewed with suspicion. This has been stated many times over the past years. Thus, a critic may conclude that the methodologies in determining the recommendation of report No. 08099-11-Te may be flawed.

It is critical that this variable (perceived bias by the USDA Forest Service) be excluded from the basic analysis and that an independent, neutral appraiser provide the technical assistance required for a more clinical conclusion.

Two appraisals were conducted – one by the USDA Forest Service using a specific set of assumptions and one done by the State of Vermont, under the State Grant Option, using a different set of assumptions. Two values were determined. The second appraisal is the appraisal of record and the one the Federal financial assistance was based on.

The position of the agency remains the same. The Forest Service will contract for a neutral third party, skilled in appraisals of conservation easements using Federal Appraisal Guidelines to conduct another appraisal by June 30. The results of the review will be binding. The Forest Service will include the OIG in the initial process to assure appropriate questions will be answered in the appraisal.

If the findings conclude that the guidelines were not adhered to, resulting in a different appraisal value, the USDA Forest Service will acknowledge these finding and seek to recover the difference between the final appraisal of record for the Hancock Tract (\$2.5 million) and the new appraisal from the independent, neutral appraiser.

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## ABBREVIATIONS

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CFR	Code of Federal Regulations
FLP	Forest Legacy Program
FS	Forest Service
FY	Fiscal Year
Hancock	John Hancock Mutual Life Insurance Company
HBU-BV	Highest and Best Use–Before Value
USC	United States Code
USPAP	Uniform Standards for Professional Appraisal Practice