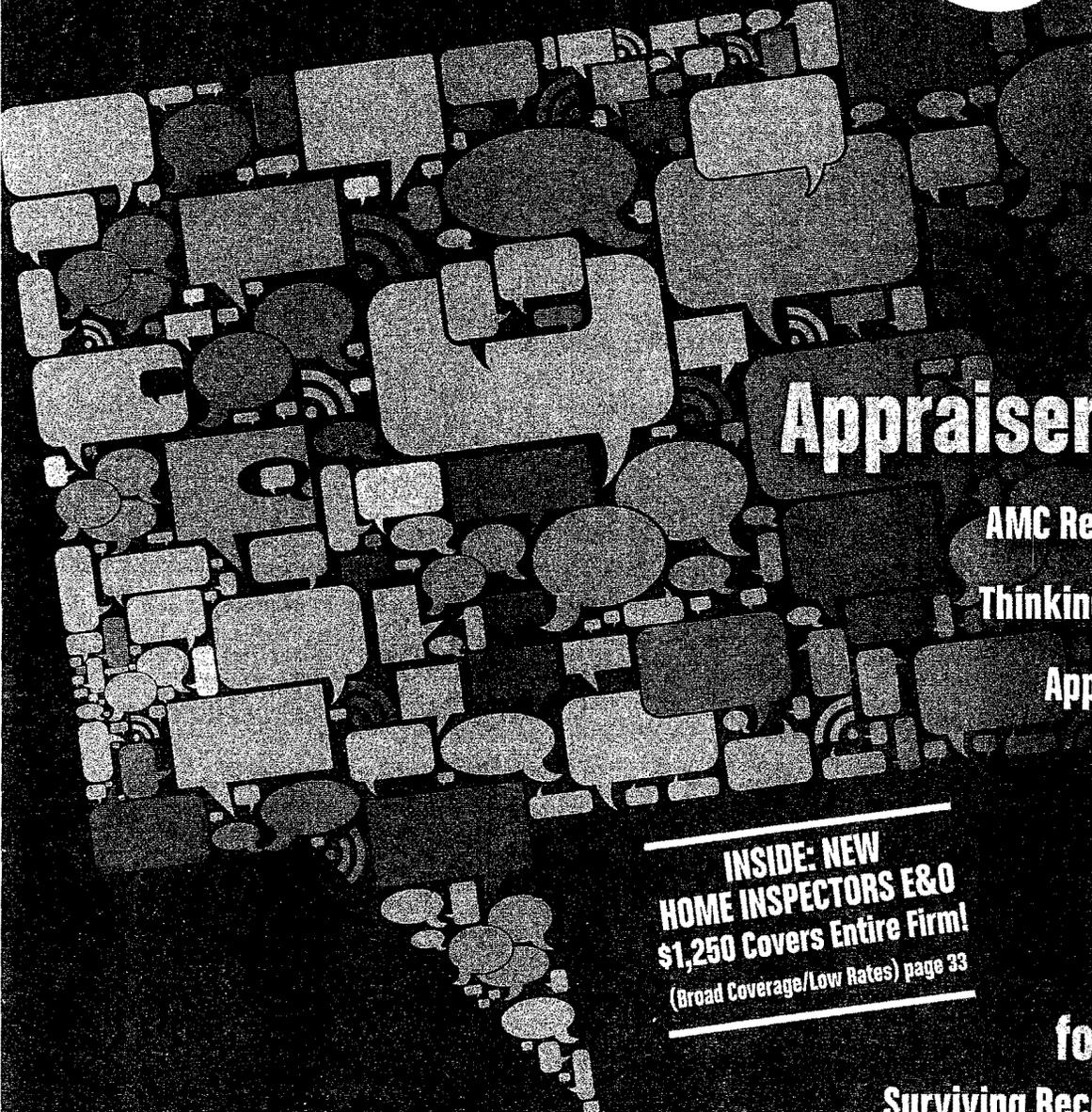


# Working RE

Real Estate Appraisers & Inspectors

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**Working RE**

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**Editor's Note:** Appraisers doing lender work are being squeezed for money and time, with the rise of low-fee AMCs work and recent requirements, such as those imposed by Fannie's 1004MC form. For these reasons, many appraisers are seeking more non-lender work. Here's some of what you need to know.

### **Appraising for Non-Lenders**

by Phil Spool, ASA

In order to continue in this profession with a decent income, residential appraisers have to begin looking for additional clients outside of the lending industry.

Non-lending clients are attorneys, accountants, agents, homeowners and insurance companies (for insurable value), among others. Attorneys need appraisals for marital assets for divorces; accountants need appraisals for estate purposes (retrospective market value); agents need appraisals to either set or adjust the asking price on a listing and a homeowner may want to hire an appraiser directly to determine how much their home is worth. While there are several other potential reasons why a residential appraisal is needed, the above are the most common sources for residential appraisals other than the sale of a house or a refinance of an existing mortgage. Additional types of properties include a condominium unit and two to four rental units, which State Certified Residential appraisers are allowed to appraise.

Now that you have decided to appraise for non-lenders don't begin rejoicing just yet; even though you no longer have to deal with those "pain in the neck" review appraisers- looking over your shoulder, telling you what you should or should not do, you now are your own reviewer and decision maker regarding comp selection and adjustments. You are responsible for your report and therefore should have someone there to review your work for factual, typographical and theoretical errors. Also, your work product now becomes available to more intended users than when the appraisal was for a single lender.

If you perform an appraisal for litigation, such as a divorce, there is a good chance the opposing party will have a skilled appraiser scrutinizing your appraisal report for any weaknesses. Nothing can be more embarrassing than mistakes brought to your attention during a deposition and/or court trial, not to mention an "attack" to your credibility. Remember, the opposing side is looking for any excuse to discredit you. This includes any USPAP violation you've made. If I emphasize the need to avoid USPAP violations, it is because other than careless errors, poor comp selection and the misapplication of appraisal theory, USPAP violations can lead to a suspension or worse, revocation of your appraisal license.

### **Using Good Forms**

Appraisals for non-lenders have one thing in common: the property can't be appraised using the current Fannie Mae 1004 or 1073 form, which states: "The intended use of this appraisal report is for the lender/client to evaluate the property that is the subject of this appraisal for a *mortgage finance transaction*." As the intended use is stated in the form, you cannot cross it out, ignore it or add another intended use. Forms without this pre-printed verbiage, that you might want to use for non-lender work, are not USPAP compliant unless they include certain elements that must

always be present. These include:

- (1) intended user - Standard Rule 2-2 (b) (i);;
- (2) intended use - Standard Rule 2-2 (b) (ii);
- (3) scope of work - Standard Rule 2-2 (b) (vii); and
- (4) summarization of the highest and best use of the subject - Standard Rule 2-2 (b) (ix).

**Using Text Addendums:** It is incumbent upon you to add the four previous items into any appraisal report you do. Some forms may already have a place to type in the intended user and intended use. Otherwise, the best location for adding these USPAP requirements is within a *Text* or *Supplemental Addendum*.

**Intended User:** The client is always your intended user but there may be others depending on the intended use. If you are doing an appraisal for estate tax purposes or for estate planning, intended users may include the client's attorney and accountant. Be sure to discuss with your client what other intended users should be included.

**Intended Use:** Too many appraisers get *intended use* and *purpose* mixed up. The *purpose* is to estimate the market value of the subject. The *intended use*, if not for a mortgage finance transaction, might be one of several, such as the disposition of the property (sale), internal asset management (value), potential purchase of the property (for a buyer), dissolution of marriage (divorce) or for estate tax purposes and estate planning (for an accountant). These represent only a portion of alternative intended uses other than for a mortgage finance transaction.

**Scope of Work:** Remember, appraisals on forms are considered a *Summary* Appraisal Report. Therefore, according to USPAP Standards Rule 2-2 (b) (vii), the appraiser must *summarize* the Scope of Work used to develop the appraisal, including (1) What methods employed; (2) What methods are not utilized and (3) Recognition that someone other than the signer(s) of the report who was significantly involved in preparation of the appraisal report.

(1) **What methods employed** means to state which of the approaches to value you use. If you are appraising an older single family residence, chances are you are using only the *Sales Comparison Approach*. There are mainly three reasons why you want to use the *Cost Approach* as well: (a) Appraising a proposed house; (b) Appraising a partially constructed house and (c) Appraising a relatively new house with adequate land sales or use of the abstraction method to properly support the site value.

For those using the *cost approach* for an older house because a lender requires it, please consider Fannie Mae's Announcement 08-30, dated November 14, 2008: *Appraisal-Related Policy Changes and Clarifications*, page 8 under the heading "Utilizing the Cost Approach to Value for Insurance Purposes" (*Selling Guide*, Part V, Section 302: Coverage for Home Mortgages; and Part XI, Section 407, Cost Approach to Value). This section states: "If a lender requires the cost approach to be completed in order to obtain a replacement cost estimate for the purpose of determining the level of hazard insurance coverage required for a one-unit property, the lender may rely on the appraiser's estimate of the replacement cost of the improvements."

So guess what? You now are liable for the *replacement cost new* amount that you indicated. Not

only that, if you cannot support your Site Value, Replacement Cost New or the Accrued Depreciation within the report or work file or within retrievable access or arrangements, you are in violation of the Record Keeping portion of USPAP. So let me repeat myself, stop doing the Cost Approach unless the house you are appraising is proposed, under construction or relatively brand new.

(2) **What methods are not utilized** means which of the approaches to value you *did not* use. Most appraisers overlook this USPAP requirement, Standards Rule 2-2 (b) (viii) that states: “Exclusion of the sales comparison approach, cost approach, or income approach must be explained.” There are three reasons why you would not want to use the Cost Approach: (a) Lack of adequate land sales to develop the site value: (b) Inadequate improved sales to effectively utilize the abstraction (extraction) method to develop the site value or (c) The effective age of the subject improvements is such that estimating accrued depreciation would be too subjective. The main reason why you would not want to use the Income Approach is due to the lack of houses that are sold which were rented in order to arrive at a Gross Rent Multiplier. You need to indicate which methods you did not use and why.

(3) **You must give recognition of someone other than the signer(s) of the report** who was significantly involved in preparation of the appraisal report. The Scope of Work should indicate the name(s) of those who provide assistance and the extent of the assistance. Standard Rule 2-3 requires the name(s) of those providing the significant real property appraisal assistance in the certification. Therefore, it is my suggestion that somewhere in your Text or Supplemental Addendum, state the name(s) of those who provide significant appraisal assistance and explain what they did. In the *Certification* section of the appraisal report, you can just state their name and license number. Explaining what they did is for their benefit too, when they want to get credit for the hours spent on the report toward getting certified. This explanation supports the hours they log in.

### **Highest and Best Use**

USPAP Standards Rule 2-2 (b) (ix) states that the appraiser must *summarize* the support and rationale for the opinion of the highest and best use. Most appraisers conveniently check the box that indicates that the subject’s highest and best use as improved is its current use. On occasion the appraiser checks the box that the subject is a legal non-conforming use. All of this is fine but what is missing is the appraiser’s summarization in the appraisal report that the subject is or is not its highest and best use or that it is a legal non-conforming use. This summarization must be made in the narrative portion of your appraisal report, specifically in the Text or Supplemental Addendum.

If the subject’s highest and best use is its current use as improved, then explain why it is its highest and best use. I use the following statement in my Text Addendum to support my highest and best use decision: “The subject as improved is a legally permissible use based on its current zoning. Also, the lot size, shape, physical condition and land-to-building ratio allow the present structure and indicate a good utilization of the improvements. Based on current market conditions, the present use and structure as a single family residence is its financially feasible and maximally productive use.”

The previous statement satisfies the four criteria in determining the highest and best use “as improved,” which is (1) Legally permissible; (2) Physically possible; (3) Financially feasible; and (4) Maximally productive. Many appraisers just quote the definition of Highest and Best Use and think that is sufficient, not realizing that USPAP wants the appraiser to *summarize* the support and rationale for the opinion of the highest and best use. If you like my statement you may use it or expand on it. Of course, if your highest and best use is something other than its present use, such as a legal non-conforming use, then it should be modified.

**Text or Supplemental Addendums** are an excellent place to discuss any discrepancies between what you indicate in the appraisal report versus what is indicated in public records, survey, deed or anywhere else. For example, if your calculations of the gross living area are different from public records or any other data source, a statement should be made within the Addendum explaining how you arrived at your gross living area and that it is different from the source that is usually relied upon, such as the public records. Perhaps there was a mistake in the survey- the Addendum is the place to explain the discrepancy. The same holds true on any other difference from what you indicate in the appraisal report versus what the intended user, appraiser peer or a review appraiser would rely on. Remember, USPAP's Scope of Work Acceptability indicates what is acceptable, which is: "what an appraiser's peers' actions would be in performing the same or a similar assignment."

#### **About the Author**

Philip G. Spool, ASA, is a State-Certified General in Florida, appraising over 36 years. Formerly the Chief Appraisal of Flagler Federal Savings and Loan Association, he has been self-employed for the past 17 years. In addition to appraising, he is an instructor with Miami-Dade College, teaching beginning and advanced residential appraisal classes as well as continuing education. He can be reached at [pgspool@bellsouth.net](mailto:pgspool@bellsouth.net).