

SKOLNIK REAL ESTATE CONSULTING SERVICES

Martin A. Skolnik, MAI

**Before Ordering an Appraisal...
After Receiving an Appraisal...**

A Lender's Guide to Real Estate Appraisals

Martin A. Skolnik, MAI

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Before Ordering an Appraisal

Before you start calling or faxing appraisers to bid on an appraisal for your latest loan or sales acquisition, ask yourself this: Are you asking for the appraiser's professional opinion of the market value of that property, or do you only want an appraisal to help you close the loan because FIRREA and the bank examiners tell you to? (I know that's a loaded question but I had to ask it or otherwise I wouldn't have an article to write!)

If you only want an appraisal to help you close the loan, do you know *why* you are asking for an appraisal? The appraiser is being hired to tell you -- the lender -- that you have adequate security for the loan in case the borrower defaults. The appraiser's fiduciary responsibility is to make sure that, in case you have to take the property back in foreclosure proceedings your company gets your money back. His/her job is not to confirm for the buyer that he/she/it paid the right price. The appraiser is working for *you!*

Martin A. Skolnik, MAI (Marty) has been involved with real estate valuation since 1979 and holds the MAI appraisal designation from the Appraisal Institute. He is President/Principal Appraiser for *Skolnik Real Estate Consulting Services*, specializing in commercial, industrial, retail, and non-residential property valuation and litigation support throughout Maryland, Pennsylvania and Northern Virginia. In addition, he performs independent appraisal reviews for lenders, attorneys, and government entities on properties throughout the United States, as either a desk reviewer or a field reviewer.

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So, that said, here’s some ideas of what you, the lender, can do to help facilitate the valuation process for the appraiser:

- Put in writing what you know about the property with documentation. The appraiser will need this information as a starting point in the appraisal process. This would include:
 - A copy of the pending loan documents
 - A copy of the sales contract (if this is a sale, not a refinancing)
 - Deed and/or Legal description
 - Survey
 - Brief description of the improvements
 - Address (for residences you should include the closest cross-street and closest major intersection)
 - Owner’s name, address, daytime and evening phone numbers
 - Contact’s name, address, daytime and evening phone numbers for access to the property
 - Rent roll and most recent 12-month income statement (if an income producing property)
 - A list of improvements or changes to the property over the past 3 years and their costs
- Tell the appraiser if you are getting a flood plain certification, building/home inspection, environmental study, or title report. *Share* this information with the appraiser -- don’t keep it a secret! If you or your client has pertinent data that may impact the appraiser’s analysis don’t withhold it until after the appraisal is finished! Provide it to the appraiser right up-front.
- Where will you get the names of appraisers to bid on your project? Does your company have an in-house roster of qualified appraisers? If so, is it updated regularly? Can *anyone* get on the roster? If your company does not have such a roster, will you use professional membership lists? Will you ask for recommendations from other lenders? Will you use the Internet for your search?
- Is the appraiser qualified/experienced to work on the project? This is a simple question but many times it is overlooked, especially by lenders that don’t keep an active, current roster of qualified appraisers. What types of projects has the appraiser worked on similar to yours?

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- Are you asking for bids from three appraisal companies only to satisfy an arcane management requirement? Do you know if there is there a reason you need three bids, or is that just “policy”? Do you *really* want to work with a low bidder on every project? Are the lowest bidders really the best suited for your project?
- If you regularly contract with the lowest appraisal bidder, do you realize that the amount of work you put into a project *after* you get the appraisal back is probably correlated to the low bid, especially if there is a wide discrepancy among the bidders? Could you avoid the post-appraisal follow-up, revisions, corrections, editing, and grief if you used someone other than the low bidder? How much is your time worth?
- Have you ever asked the higher bidders *why* they bid what they bid? Do you just ask for a fax bid, or do you talk to the appraisers about the project and get feedback? Perhaps the higher bidders realize that the project is more involved than the low bidder or than you think it is too! Maybe the low bidder does not realize the difficulty of your project or detail in analysis or data collection required to do a good job on your project.
- Once you contract with an appraisal firm, do you know *who* is going to actually do the fieldwork, the property inspection, the analysis, the research, and the report writing? As the client, you should know up-front if the appraisal firm has a trainee doing the bulk of your project’s work. Sure, the MAI or head of the company will probably be signing the report and taking “professional responsibility” but who actually is doing the work?
- As part of the bidding process discuss with the appraiser the scope of work that you will require for that particular project. Do you want a self-contained report, a summary report, or a restricted report? Will the project be a complete appraisal or do you only need a limited analysis (i.e., an income approach analysis or sales comparison approach only)? Do you want a discounted cash flow analysis or do you need an expanded supply and demand analysis? Put in writing (in the form of an engagement letter) your expectations as to what you and the appraiser agreed. Be precise about your reporting requirements, especially for commercial work.

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- Use an engagement letter, drafted by either you or the appraiser. Agreeing to the appraisal of a piece of property between lender and appraiser is contractual arrangement and you should have the pertinent factors of this business contract in writing for the sake of both of you! Whether it is for a \$300 residential appraisal or a \$25,000 commercial appraisal there should be documentation about the amount of the fee, timing of the report delivery, any basic assumptions you want the appraiser to make, and when/how the appraiser gets paid.
- Be realistic about your reporting requirements. Do you *really* need to know the subject property’s census tract, especially for a commercial property? Also, if you have a tight budget, don’t ask for a self-contained complete appraisal and then berate the appraiser when you learn what the fee will be. You are paying for the appraiser’s time and expertise – if you want full documentation and every hoop jumped through, then the fee will reflect the time that the appraiser has to spend on your project.
- If you are using an appraiser for the first time, it is not uncommon to ask for a photocopy of the appraiser’s license for you files (or copies of the licenses for anyone working on your particular assignment from the appraiser’s company). In addition, you should ask for a complete listing of professional qualifications, too.
- If your company has specific appraisal requirements, include a copy of these requirements with any engagement letter you send to the appraiser. If your company doesn’t have written requirements and guidelines, *get some!* At the very least, make sure that every appraiser on your approved list gets an *annual* updated copy of your guidelines/requirements.
- If you are calling for a bid and you get the appraiser’s voice mail, please be clear about how you pronounce and spell your name, and *slowly* repeat your phone number or email address twice, just to be sure.
- If you typically request bids from a number of appraisers for each project, it would be nice to send a fax or email to the unsuccessful bidders and tell them the ranking of all the bids on a particular project. You don’t have to disclose the competition’s names, you can say Appraiser #1 bid \$XXXXXX, Appraiser #2 bid \$YYYYYY, etc. etc.

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After Receiving an Appraisal

You have been waiting a week, two weeks, four weeks or six for the final appraisal report -- the fate of your commission hangs in the balance. From your perspective, the appraiser will either hit your number or screw your deal. Some reports will be four to eight pages of fill-in-the-blank forms. Others will be up to 100 pages of narrative discussion. Whichever type of report you are getting, don’t just read the “number” and react. Get out a pad of paper and a pen to take notes. Go get some yellow sticky notes to mark places in the report that you want to reference later. Grab a yellow highlighter. Close the door to your office (if you don’t have a door, go find a quiet conference room where you can concentrate on the report in your hands). Pour yourself a cup or two of coffee and hit the vending machine for some peanut butter crackers. This might take a while! As you read the report, consider these bits of advice:

- Have realistic expectations and an open mind when you start reading. The appraisal should tell you the story of the valuation analysis of the subject. It might be written out in narrative paragraphs, displayed in tables with short phrases, or just fill-in-the-box format. In any style, there is a story in there that you should try to extract.
- Read the appraisal cover-to-cover.
- After you finish the report, ask your appraiser questions about anything you don’t understand or isn’t clear from the report.
- Ask yourself this question – did the appraiser analyze the subject property and its market, and report a valuation conclusion for the property, or did he/she only fill out an appraisal template?
- Did you get a feeling that the data that the appraiser used in the report is the best data available for the subject (given its size, location, condition, use, etc.) or did you get the feeling that the data and descriptions in the report was copied over from an appraisal on a similar property nearby?

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- Be aware that sometimes good comparable data (sales or rentals) can be unavailable for unique properties, rural markets, or slow markets. If that is the case for one of your projects, insist that the appraiser explain the scope of his/her research to find the best comparables and how they were analyzed.
- Re-read the report.
- Ask questions until you get answers that make sense. Ask questions even if the appraisal “hits” your number! The value conclusion may be what you are looking for, but if the analysis and data are garbage then your “number” is garbage, too.
- Question any assumptions or analysis that looks like a “leap of faith” or smoke and mirrors. If the appraiser implies or writes *anywhere* in the report, “such and such is based on my years of experience and knowledge of the area”, call him or her on it. Similarly, ask for specific detail when you see a statement similar to, “knowledgeable brokers report that...” or “market research concluded that...”
- If the appraiser’s value estimate does not match your expectations perhaps you know something about the property or the market that you haven’t conveyed to the appraiser yet. If you feel that he has omitted information critical to your project, provide him with whatever additional information you may have available to you. However, do not just say, “Mr. Appraiser, your comparable sales are not acceptable. We need three more comps.” Do you really think that the appraiser has purposely reported to you secondary comparables and kept the better ones in his files for future use?
- There isn’t an appraiser in existence that believes that his or her job is to screw your deal up. If he believes that his valuation is going to hurt your deal, he’ll typically go to great lengths to double check his market data and his calculations *before* he sends you the report. He’ll re-think his adjustments and perhaps even re-measure the property to make sure that the square footage of the subject is accurate. A good appraiser will call the lender in advance and verbally report the problem and what steps he or she has taken to ensure that his valuation is an accurate representation of the subject and the market data. True – our valuations are

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historically focused and we can’t always be in front of the curve in a rapidly appreciating market. That’s one of the restrictions on the mechanics of our profession. More than once appraisers have been told, “You don’t have any vision” when their value estimates come in short of a developer’s or lender’s expectations. That’s where a creative lender can help structure a transaction to make it work.

- If the appraiser doesn’t “hit the number” that doesn’t mean that you should blackball the appraiser. Perhaps he/she has done you a favor. Perhaps he/she sees something in the market, in the valuation or in the subject that you haven’t or that the owner hasn’t told you about “yet”.

These are just a few ideas that you can use in your daily lending practice to improve the appraisal ordering and appraisal review portion of job. If there is any way that I could be of more assistance in the appraisal review process, please email me at **Mskolnik@realestate-consulting.com**, or call me at **410-580-0168**, or go to **www.realestate-consulting.com** and click on the first link to *Order an Appraisal Review* to order a review or to see the fee schedule.

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