

Reviewing appraisals: Art and science - Part 1

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To those occasionally dependent on appraisals, "mystifying" sometimes describes the process. Whether appraisals are the product of tried and true academic methods or some vague art form has long been debated in real estate venues. The simple answer to this cliché is that it is both. The same is true of the appraisal review function, which has grown in importance in this "sea changed" economy. Appraising complex assets with meager transaction data in a persistently challenging real estate market has raised the bar for "appraisers" and "review appraisers" in the provision of reliable valuation services. In my career as an appraiser, review appraiser and counselor, several observations come to mind about the contribution of review appraisers. This article summarizes some of the obvious and also less obvious functions and benefits of the process beyond peer review, quality control and regulatory compliance. The reader is directed to an excellent Appraisal Institute publication titled *Appraising the Appraisal*, by Richard Sorenson, MAI, for a thorough presentation of the technical and practical nature of the review process. Some reader knowledge of the appraisal process is presumed in this article.

The 1980's recession again revealed inconsistency in the quality and reliability of appraisals. This time it led to the creation of the Uniform Standards of Professional Appraisal Practice ("USPAP") in 1987; FIRREA in 1989 with Interagency Guidelines; and the formalizing of additional appraisal guidelines by IRS, transportation authorities, the U.S. government for federal land acquisitions, and others. USPAP Standards 1 and 2 relate to appraisals and Standard 3 relates to appraisal reviews, explaining the detailed requirements of each.

How does appraisal review contribute to the real estate investment process and what do reviewers actually do? The extent of an appraisal review can be limited or broad depending on the nature of the assignment and complexity of subject property appraisal issues. There are several terms used to describe the different functions and level of detail available in that process. These terms are not clearly defined or consistently used by appraisers or clients. For example, an abbreviated "desk" or "administrative" review can mean a limited check for compliance with client or USPAP requirements, and does not penetrate far into appraisal "issues". A "technical" review of an appraisal report, with or without a reviewer field inspection, usually involves a thorough and constructive critique of the appraiser's description of the subject property, market data selected for analysis, highest and best use analysis, appropriate use of valuation methods, and the value conclusion. A reviewer can also evaluate an oral appraisal report, file memoranda, or portions of an appraisal. Individual or portfolio assets can be reviewed in different geographical locations far from the reviewer's base.

Since there are so many types and levels of an appraisal review, the review appraiser and client must agree in advance on a USPAP required "Scope of Work." It discloses the nature, extent, and detail of the review process for the subject appraisal and must lead to a credible reviewer conclusion that is not misleading. An appraisal review can be required as a simple bureaucratic compliance

checklist, at one extreme, or as a critical part of a financial transaction, asset management, disposition or litigation, at the other. The technical methods, analytical requirements and judgment required in an appraisal review contribute obvious value to the process by completing due diligence and supporting clients or employers in carrying out their fiduciary responsibilities.

Part 2 will appear in the March 9th edition of NEREJ in the Appraisal & Consulting section.

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