JAMES A. GRAASKAMP COLLECTION OF TEACHING MATERIALS

V. INDUSTRY SEMINARS AND SPEECHES - SHORT TERM

I. Other Presentations In Which Either The Date And / Or Sponsoring Organization Is Missing

2. Appraisal Topics

v. "Appraisal Procurement Seminar", no date

Index

APPRAISAL PROCUREMENT SEMINAR

I. The traditional approaches as a simple , idealistic logic and economic rationale are based on the principle of substitution--specifically that buyers and sellers have alternatives of nearly equal acceptability, or sentiment, not to mention access to cash capital and freedom from irritation and duress.

A. MARKET COMPARISON methods are preferred, but the appraisal profession has found it difficult to develop objective methods for neutralizing differences and selecting properties objectively. Moreover, prices on investment properties are engineered to accomplish accounting objectives of the parties.

B. The INCOME APPROACH is schizophrenic as to whether it is measuring economic productivity, the sum of liability, or the change in spendable cash for ownership through control of property rights.

C. The COST APPROACH has moved from unethical according to the National Association of Realtors (NAR) in 1925, to pivotal in 1935, to embarrassing in 1985 since no one is sure if fiduciary responsibility requires a cost approach to avoid a sin of omission in the event of unforeseen disputes about value.

II. However, none of these methodologies as logic systems structure the behavioral process required of the appraiser and his client. The client assumes that the task is defined when you ask for an appraisal and the appraiser assumes the client understands the rationale and appropriate application of fair market value or probable price. Both are more concerned with form than the substance of careful recognition of the problem for which the appraisal will serve as a benchmark.

A. Objective appraisal

1. Validate purchase price as appropriate.
2. Identify change in price over time, if any.
3. Independent inspection of property and review of property management effectiveness.
4. Liquidating value of asset currently.
5. Future value of present assets.
6. Historical return on investment or future return on investment, real or nominal.

B. Definition of value to be sought

1. Alternative definitions of value and related assumptions.
2. Which definition of value is to be applied to which problem.
3. Market value vs. probable price.

C. Definition of assets to be valued

1. Property rights to be appraised
2. Accounting rules to defining assets, collectively (going concern) or individually (liquidating).

D. Definition of methods to be used

1. What constitutes comparative market data?
2. What constitutes objective market comparisons?
3. What constitutes an income approach to value?
4. Relevance of the cost approach to appraisal and appraisal adjustments?
5. Which appraisal methods are appropriate to which appraisal functions?

E. Definition of elements income approach

1. Cash or accrual accounting.
2. Going concern value or value attributed to land and buildings.
3. Accounting rules for income.
4. Forecasting rules for changing income and expenses.
5. Estimating rules for changing income and expenses.
6. Provision for resale cost.
7. Conformity with historical pattern and leases in place for project.

F. Definition of appraiser/client relationship

1. Who is considered an independent participant for preparation of financial data, asset management plans, and engineering disclosure?
2. Frequency of appraisal and volume of business as source of bias.
3. Who is the arbiter of methods for integrating information into cohesive standardized formats suitable for measuring comparative performance?

III. Ironically, quality control of the appraisal process is in the hands of the customers for appraisal services, specifically those who stand to lose by permitting current conditions to continue. Historically, reform of the appraisal process has always been in the control of the customer who invests or guarantees real estate capital.

A. Historical origins of the three approaches

1. The cost approach and the life insurance industry.
2. The income approach, academia, and the FHA.
3. The market approach and the National Association of Realtors.

B. Standardized reporting requirements of the American Institute of Real Estate Appraisers begin with Canon 5 of their Code of Ethics.

1. The Institute has never issued white papers on specific appraisal problems to standardize professional response to changing issues of common interest.

2. Recently the Institute has tried to issue white papers as guidelines.

C. More recent efforts at quality control include:

1. The Home Loan Bank redirecting appraisal attention to R-41-b.

2. FNMA and FHLBMC and requirements for appraising multi-family development.

3. Residential form appraisal for FNMA, VA, FHA, and FHLBMC.

D. The Royal Institute of Chartered Surveyors and the European Common Market Accountants have been developing a standardized language and procedure for the valuation of and reporting balance sheet assets.

E. Development of consistent appraisal performance standards for pension programs requires a six-step process:

1. Development of written policy statement by pension fund trustees relative to reporting of real estate asset values by money managers responsible for real estate.

2. A written appraisal standard followed by a specific real estate fund manager's report covering both minimum standards shared with an association of managers and unique features believed to provide better communication to fund trustees of important underlying facts and assumptions inherent in the appraisals.

3. A standard letter of engagement when contracting for appraisal services implementing the written policies of sponsor and money manager.

4. A standard procedure for in-house appraisal reviews in the interim between independent outside appraisal reviews, including tolerance for variance before reporting changed values.

5. Auditing and monitoring of appraisal reports by specially trained, CPA reviewers as part of the accounting audit process.

6. Spot checking of appraisal procedures and a review process for disapproval of appraisal firms found to be likely of misinformation or misapplication of technique by ERISA.

F. An early effort at appraisal control was a Letter of Engagement used at First Asset Realty Advisors (FARA) together with knowledgeable efforts to select the best local assessors.

1. The best appraisers are difficult to pick by reputation as the big names delegate their work to apprentices.

2. Some appraisers admit to being intimidated and avoiding the assignment or charging extra for the assignment, anticipating that FARA will be more demanding.

3. On balance, we are getting better appraisals than most of the funds we have seen in our research but at a higher average cost.

G. The FARA letter was followed by an effort by the National Council of Real Estate Investment Fiduciaries (NCREIF) to develop guidelines.

IV. Appraisal procurement must address three major areas of concern:

A. Policy directs from board of directors resolution controlling

1. decisions for which appraisal data will be a bench mark,

2. selection of appraisers to eliminate business bias, and

3. priority of appraised value by independents relative to inside appraisal procedures.

B. Protocol for providing professional information to the appraiser and production of data sources within appraisal.

1. Accounting for revenues and expenses.

2. Role of property management program.

3. Details for future appraisal budgets.

4. Disclosure of negative data on tenant, toxic materials, life safety systems, or engineering issues.

C. Control of content and quality of appraisal reports through purchasing policies.