Appraisal Primer

Lead Office: HUD-MF

Participating Offices: USDA-RD, HUD-MF, HUD-PIH, HUD-CPD, HUD-OSHC, Treasury-IRS

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Issue Statement:

Federal law indirectly requires the use of the Uniform Standards of Professional Appraisal Practice (USPAP) as the basis for real estate appraisal work; however, Federal and State housing agencies' capabilities and methods for enforcement vary. In existence only since 1987, USPAP remains widely misunderstood and, in some cases, is even unknown to rental housing program staff and participants who are not themselves professional appraisers. In addition the specific ways in which USPAP applies to valuation of rental housing in various subsidy situations is frequently misunderstood or ignored.

Subject matter experts have pointed out that numerous variations exist among State housing agencies and Federal programs as to when an appraisal assignment is needed and the scope of work the particular agency requires. USPAP makes appraisers accountable to their clients to know and understand a correct scope of work for any particular assignment. But in many cases, the appraiser's client is a lender or an agency, not a property owner or developer. As a consequence, the appraiser is often not informed of the property owner/developer's intent to seek multiple financing sources that may trigger an expanded scope of work, or indeed, the decision to seek additional or alternative financing sources may occur after an initial appraisal assignment has been completed. Lack of communication with the appraiser about the prospective uses of the appraisal report and lack of user knowledge about how to describe an appropriate scope of work create situations where completed appraisals are not responsive to the demands of all funding sources engaged in a project. In addition, the passage of time from one funding application to another may exceed the acceptable shelf life of an initial appraisal.

These circumstances expose end users of rental housing programs to inconsistent use of appraisals among Federal and State offices and the periodic frustration of obtaining additional or updated appraisal work. Lack of knowledge about USPAP fundamentals among users and laypersons (non-appraisers, in and out of government) weakens USPAP as a tool intended to discipline and standardize appraisal practice.

Proposed Alignment:

Alignment Summary**:** To improve use and understanding of USPAP among rental housing professionals who are not appraisers, the Team proposes to develop and publish a primer (see attached draft specification) intended to be freely available, both in print and on the web, and widely distributed, and to promote this learning tool among agencies and industry participants. The primer should explicitly describe the general USPAP principles that apply to valuation of rental housing when public subsidies are provided. In addition the primer should either contain as an appendix, or reference as a source, a table setting out general lender and agency scope of work requirements for appraisals as well as their acceptable shelf life so that all users can make informed decisions when scoping an appraisal assignment. It should be noted that the primer represents an education strategy to solve a knowledge problem and to enable appraisal users to be more 'informed consumers' of appraisal products and hence reduce confusion and miscommunication. To the extent that informed consumers exert market discipline, appraiser carelessness or misconduct will also be reduced.

Creation of the primer does not require any Federal rule making, but it does involve some decision making and an actionable plan by certain participants**,** together with a potential need for modest funding and the allocation of some personnel resources.

Specific actions to effect appraisal alignment**:**

A. The Appraisal Institute has expressed an interest in publishing the proposed primer as a public service relying on expertise of its individual members obtained through an internal proposal process. The Appraisal Institute is the largest publisher of appraisal education resources and is well equipped to prepare and publish (in multiple formats/media) the envisioned primer. It is anticipated that the primary means of distribution will be electronic.

A. Should the Appraisal Institute not proceed with such a primer (or the primer not fully address the concerns identified), an alternate means of procurement or production must be selected which could be:
   (1) Writing and production by a competent subject matter expert or organization under a Federal procurement contract or grant.
   (2) Writing and production by agency staff, with lesser assistance in publication or web posting by contractors as needed.
   (3) In either event, funding must be found, although the amount should be relatively modest.

Resource Estimate for Implementation: Should it be necessary for the federal government to undertake writing and production of a primer, it is anticipated that at least one staff person from HUD and one from USDA-RD would commit significant time to coordinating the effort, soliciting the views and comments of subject matter experts, obtaining internal reviews and editing the document. Over the course of a year, it is reasonable to expect at least one to two person/months of time from each of these agency lead persons. There will be numerous contributions of hours by other agency staff as they are asked to review, comment or contribute to the drafting and editorial effort. A small procurement will be required and this will engage a greater allocation of staff time to manage the procurement process. In addition, funds will be necessary to compensate the successful contractor. Use of the procurement process will add significantly to the elapsed time before the primer can be completed. A reasonable estimate of the costs is $40,000 to $50,000.

Estimated Appraisal Costs: There are at least two ways to consider possible results from publication and wide distribution of the appraisal primer. The first is quantitative. Will the government or program users save money or time? How much? The second is qualitative. Will the quality of real estate decision making be improved and will this have any particular impacts?

Appraisals are transactional due diligence documents normally prepared in association with the purchase, recapitalization or construction of a real estate asset. So, a key data item is the average number of transactions per year. Obtaining such a figure only for multifamily properties is not that easy. Activity varies widely with economic conditions, interest rates, employment and household growth and similar factors. But data suggest that in an average year:

1. About 2,600 new multifamily projects start construction.
2. The number of refinance and purchase transactions exceeds new starts by a factor of about 4 to 1, meaning that in an average year there may be 10,000 to 11,000 refinancing or sale transactions.
3. There are about 1,300 new tax credit transactions per year and of these about 900 are new constructions and 400 are acquisition and rehabilitation.
4. Of the other new construction starts, about 125 are FHA-insured starts. Historically, few FHA insured starts have LIHTCs. By contrast, 80% to 85% of USDA-RD transactions are LIHTC deals and there is an average of 130 USDA-RD multifamily transactions per year. All FHA and USDA-RD starts require appraisals. While many State agencies do not require appraisals for allocation of tax credits, some do, and most deals will encounter an appraisal requirement by either or both the lender and investor.
5. A significant and probably growing percentage of LIHTC transactions involve multiple funding sources that could trigger additional or duplicative requirements for appraisal work. If all additional sources required such documentation, the number of additional appraisal requirements would average about 1,400 appraisal assignments per year. However, it is reasonable to estimate that no more than half of supplementary funding sources require additional appraisal work and the preponderance of this would be revisions to an existing document rather than an entirely new appraisal report. Accordingly, an estimated 700 modified or additional appraisal assignments per year are generated by supplementary funding sources
6. Accordingly, a reasonable estimate of annual multifamily appraisal activity suggests that there are 14,000 appraisal assignments for transactions each year (2,600 new, 11,000

existing and 500 to 700 duplicates). At an average cost of $8,000 per appraisal the multifamily appraisal industry generates about $112,000,000 per annum.

Estimated Costs Savings to Owner/Developers: The maximum savings to developers by eliminating duplicates would be $5,600,000 (700 x $8,000). Although the primer will be helpful in eliminating some duplicates, it will not be 100% effective. The Team hopes that the primer will result in a 25% reduction in duplication costs or $1,400,000. Every instance where there are dollar savings will also represent a time savings as the time to discover a need for a new or amended appraisal as well as the time to prepare the actual document will be eliminated. Lenders and investors do not typically bear appraisal costs since they charge borrowers or owners for the costs of third party reports.

Estimated Cost Savings to state, local and Federal governments: There will be no direct savings in costs to governments. However, it is reasonable to expect that improved knowledge of appraisal practice, more accurate and more correctly written scopes of work and other qualitative improvements in the use and understanding of appraisal documents will improve real estate decision making and reduce waste of government staff time spent dealing with poor or inappropriate appraisal documents. More importantly, improved decisions should result in more efficient use of Federal rental housing dollar resources, reduced exposure to default risk for lenders as well as for the Federal mortgage insurance programs of HUD-FHA and USDA-RD.

Schedule for Alignment Implementation: Work on the primer can proceed promptly after approval and should be completed on a 12 month or shorter, schedule.

Challenges to effecting proposed solution(s):

If the Appraisal Institute does not proceed with a primer along the lines discussed above or if their product does not fully address the issues that this team has raised, then the following challenges will arise:

- Identifying a means of production and procurement for the primer which is modest in scale comparable to the nature of the endeavor.
- Securing the participation of non-governmental subject matter experts/authors who likely would require compensation.
- Identifying sources of funding, albeit modest.

Purpose

This document is part of an ongoing effort to better align Federal rental policy across the Administration and is sponsored by the Rental Policy Working Group. The Rental Policy Working Group is composed of the White House Domestic Policy Council (DPC), National Economic Council (NEC), Office of Management and Budget (OMB), and the U.S. Departments of Housing and Urban Development (HUD), Agriculture (USDA), and Treasury.

The specific areas of concern identified herein emerged from July 2010 stakeholders gathering at the White House on areas of Federal rental policy inconsistency across the administration. The revised conceptual proposals for alignment articulated within this report are preliminary in nature and have not been endorsed by any Federal agency or office.

With any questions, please contact the Rental Policy Working Group Agency Alignment Leads: Larry Anderson, Director of Multi-Family Housing Preservation and Direct Loans at USDA-Rural Development, Ben Metcalf, Senior Advisor at HUD's Office of Multifamily Housing Programs; or Michael Novey, Associate Tax Legislative Counsel in Treasury's Office of Tax Policy.