

Liability of Appraising REOs & Foreclosures

By John Lifflander, ASA



What is the level of risk for these types of appraisals compared to purchases and refis?

Editor's Note: This is the inaugural installment of *Valuation Issues & Answers*. Your questions will be answered by John Lifflander, ASA, as a regular feature here in print. Look for additional installments in the bi-weekly e-mail edition of *WRE*. Send your appraisal questions to john@liffland.com. You can opt in for the free e-mail edition at WorkingRE.com.

Question: I have been performing a lot of exterior drive-by appraisals for REOs and pre-foreclosure purposes. The intended use is not for any type of financial transaction but for estimating market value purposes only. What is the level of risk for these types of appraisals compared to purchases and refis? Typically these appraisals are for people going into foreclosure and the bank wants to know an estimate of value in order to evaluate offers. Eventually, a new appraisal would have to be done by a different appraiser for the final purchase. Is my liability risk low or high? —Darrin Henry

Answer: I will answer to the best of my ability and suggest you also contact an attorney if you want a legal analysis. In the sense that these appraisals may not be used for lending purposes, it would seem that they would carry less liability than purchases or refinances. However, remember that a lending institution is making a value decision based on the appraisal. It might be the determining factor in the amount that they sell the property for, or how they deal with an owner who is trying to work out mortgage payment problems. So the appraisal is being used in a financial transaction. Moreover, you cannot be certain that they will not use the appraisal in some loan-related way, even though that is not the stated use.

That being said, your liability in a drive-by appraisal is high to the extent

that you must not accept an assignment if you do not have enough information to adequately perform the appraisal. This is up to you to determine, for USPAP puts the responsibility on you and not the client. In the 2008–2009 USPAP we read the following in the "Scope of Work Rule": *An appraiser must not allow assignment conditions to limit the scope of work to such a degree that the assignment results are not credible in the context of the intended use. Comment: If relevant information is not available because of assignment conditions that limit research opportunities (such as conditions that place limitations on inspection or information gathering), an appraiser must withdraw from the assignment unless the appraiser can: modify the assignment conditions to expand the scope of work to include gathering the information, or use an extraordinary assumption about such information, if credible assignment results can still be developed.*

One thing you should also consider is the value of the home you are appraising, especially if you are Certified. Certified appraisers are sometimes asked to perform drive-by appraisals on multi-million dollar homes. High-value houses are hard enough to appraise when the interior is accessed but the lack of interior inspection makes them far more difficult, which brings into question whether credible results can be obtained without one. Moreover, many appraisers carry a minimal amount of Errors and Omission insurance, which may be adequate for lower-priced homes. However, it is not unusual to see a \$2,000,000 home drop \$500,000 in value, particularly in the current market. So you can see that your liability, in terms of sheer monetary risk, increases with higher value homes.

John Lifflander, ASA, is a Certified General Appraiser in Washington and Oregon. He teaches appraisal courses and has been published numerous times, and is the author of "Fundamentals of Industrial Valuation," a textbook for industrial appraisers published by IAAO (International Association of Assessing Officers). He is a former administrative law judge for property tax appeals for the Oregon Department of Revenue and specializes in providing expert witness testimony and consultation for complex valuation litigation.

If the home is in a lower price range and you feel comfortable performing a drive-by appraisal, I suggest that you include a standard statement such as: "This appraisal is being performed under the extraordinary assumption that the interior of the subject property is in at least average condition for its age, and is in condition as good or better than the sale comparables that were used in this appraisal, if adjustments for condition are not made. The appraiser did not inspect the interior, so if this is not the case, the value could be substantially lower than estimated, and the appraiser will be held harmless due to this disclaimer."

Many appraisers have escaped potential litigation because of disclaimers such as this one. However, it will not alleviate you of your responsibility, for USPAP still requires that you must decide "if credible assignment results can still be developed."

Finally, I think it is important that every appraisal be done as if it is going to be critiqued in a courtroom, regardless of the stated use. Lenders are experiencing many losses today, and the underlying appraisal can become a target for recovery if they find flaws in it. I do not think that there is an absolute answer to your questions but hopefully this is helpful.

Question: A national lender has assigned an order to me, which is an REO property. However, they state that they do not want me to use other REO comparables sales in the appraisal, unless they dominate the market. I am wondering if they are correct in making that request because it seems to me that if I'm valuing an REO property, I should be able to use other REOs as comparables. What you think? —*Jeanne W.*

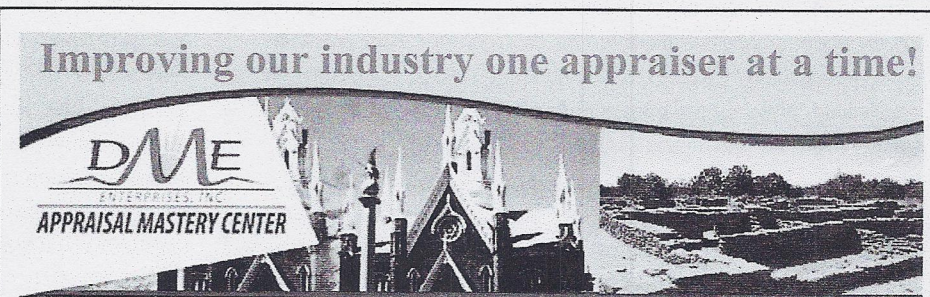
Question: First of all, the lender cannot tell the appraiser what types of comparable sales should be used. Lenders have tried to dictate how appraisals should be done for years and this is one reason we are experiencing the economic troubles we find ourselves in today. I won't print the name of the lender that

you mentioned in your question but it happens to be one of the largest, which is also currently under investigation for fraudulent lending activity.

Since you are being retained to determine market value, it is your decision whether or not to include or exclude comparable sales. The only exception to this would be if there are special conditions of the appraisal that are mutually agreed upon, which is not the case in this situation. By the way, even

if the property is not an REO property, and even if the market is not dominated by REO sales, an appraiser can use REO sales if he or she feels that they are valid in the valuation of the subject property.

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