

Review of New Evaluation guidelines, and help in selecting an AVM

The recently released report on **Interagency Appraisal and Evaluation Guidelines (IAEG)** including (OCC)¹; (FRB); (FDIC) (OTS); and (NCUA) (collectively, the Agencies), makes for excellent bedtime reading for insomniacs. However; for lenders it is an important redefinition of what can be used to support a loan under \$250,000. Historically, lenders used an evaluation, providing support for the lending. An Automated valuation Model (AVM) is sometimes used. Lenders like the evaluation product since it is less expensive than a full appraisal, and more importantly, it is faster. In busy times, appraisers can get backlogged with work sometimes adding weeks to the loan processing time.

IAEG Guidelines: The new guidelines redefine the definition of the evaluation. After studying the IAEG and in discussions with clients and appraisers we determined the new guidelines require a full appraisal, in most cases.

1. Market Value: The new IAEG requires a market value. AVMs are less precise and may or may not achieve the standard of a true market value.
2. Area and Neighborhood Analysis: The IAEG requires area and neighborhood analyses reflecting current local market conditions. These are not found in most AVMs available today.
3. Highest and Best Use: The evaluation must consider the property's current and projected use.
4. Property Inspection: While the IAEG does not require an inspection of the property the report must state how the evaluator supported the statement on the properties condition. To meet the intent of the guidelines we conclude a full inspection of the property would be called for in most instances.
5. As Is Value: The new IAEG guidelines require an AS IS value and states that no assumptions can be made that that the property (a) is in average condition, (b) complies with all zoning regulations and (c) is not affected by adverse market conditions. Most AVM's have disclaimers on these items.

¹ Office of the Comptroller of the Currency, Treasury; Board of Governors of the Federal Reserve System, Federal Deposit Insurance Corporation,); Office of Thrift Supervision, Treasury, National Credit Union Administration. See <http://www.ots.treas.gov/files/490054.pdf> for full report.

6. Valuation Approaches: The IAEG outlines valuation approaches and report format. While it does not say which approaches to value should be employed, it does state that the approach(s) used should be tailored to the subject property. These might include the Sales, Income, and Cost approaches to value. AVMs are not eliminated as an approach, but they have many caveats.
7. Report Format: The report format outlined in the IAEG contains most of the requirements of a full appraisal report. It includes the:
 - Location,
 - Property description,
 - Current and projected use,
 - Inspection description,
 - Approaches to value used,
 - Supplemental data, if an AVM,
 - Data sources used in the analysis,
 - Property specific data sources,
 - Evidence of property inspection, (sketch),
 - Subject photos,
 - Description of the neighborhood (neighborhood analysis),
 - Local market conditions (area analysis), and
 - The evaluation report signed by the evaluator.

Using AVM's in compliance with the guidelines. If you or your organization is interested in acquiring an AVM process for evaluations, there are a variety of software programs available in the marketplace. I've outlined some general guidelines for software selection based on my education and 15 years of experience as a software engineer and manager, as well as 20 years of appraisal experience.

1. Before beginning the selection process meet with your IT guru to gain a full understanding of the IAEG .
2. Meet with various stakeholders and then stratify your organizations needs into **Must Have, Should Have and Nice to have** capability. No piece of software will meet all your needs. You need a way to separate contenders from non-contenders.
3. Narrow the software field to no more than 3 vendors. Invite all stakeholders to be present at vendor presentations and make your selection based on your needs, each vendor's capability and service record.
4. Establish guidelines of when the AVM can be relied upon. A test of each market should

be undertaken to determine how well the AVM performs based on the software selected. An AVM may work well in market A but not market B. The AVM's confidence indicator is based on data provided. If the data is flawed, then the results and the confidence indicator will be flawed.

5. AVMs should not be used in periods of a national disaster or major economic change.
6. Ongoing testing of the AVM software should be undertaken to insure it continues to function as expected. Care should be taken not to rely on the vendor to provide these assurances.
7. The purchase of AVM software is an investment. You acquire it to provide a quick, accurate, inexpensive view of a property to establish a market value to support a lending decision. It is an alternative to the slower more accurate and more costly individual appraisal.
8. It is also prudent to test how the overall AVM program is meeting loan performance goals compared to other loan portfolios that did not use an AVM. The audited results of this testing can be used to tweak the policy guidelines and threshold setting.

Finally the decision to use an AVM must take into consideration the new IAEG guidelines which require the evaluation report to include most of the data found in a full appraisal report (See above).

For the licensed real estate appraiser: The IAEG requires “information on the preparer when an evaluation is performed by a person, such as the name and contact information, and signature (electronic or other legally permissible signature) of the preparer.” Some AVM providers now offer field inspections to augment the AVM value with the requisite inspection and subject property data. Since the evaluator does not have to be licensed the AVM provider may employ a broker or a licensed appraiser to undertake the field work.

The appraiser can attest to the portion he or she undertook, i.e. inspection, measurement, town hall data, area and neighborhood analysis, highest and best use. Unless the appraiser can verify the voracity of the AVM value he or she cannot imply that the value is the result of his or her findings, which is indicated by a signature.

This is a new Hybrid area of valuation and may or may not be covered by an appraiser or realtor's standard E&O insurance, especially if USPAP rules are violated. If the lenders guide lines require E&O coverage on all outside valuation assignments, they must be certain that the subcontractor has proper insurance; otherwise the lender will be purchasing an uninsured product and thus violating their own guide lines.

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